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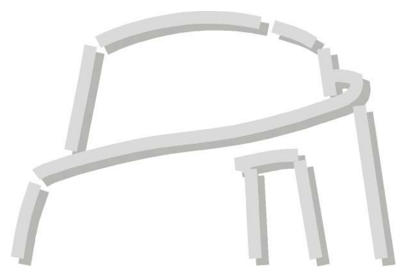
Globalization and development



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Explanatory notes

The following symbols have been used in this Study:

Three dots (...) indicate that data are not available or are not separately reported.
A minus sign (-) indicates a deficit or decrease, unless otherwise indicated.
A full stop (.) is used to indicate decimals.
Use of a hyphen between years, e.g., 1960-1970, signifies an annual average for the calendar years involved, including the beginning and the end years.
The word “dollars” refers to United States dollars, unless otherwise specified.
Figures and percentages in tables may not necessarily add up to the corresponding totals, because of rounding.

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Introduction

The process that has come to be known as globalization —i.e., the progressively greater influence being exerted by worldwide economic, social and cultural processes over national or regional ones— is clearly leaving its mark on the world of today. This is not a new process. Its historical roots run deep. Yet the dramatic changes in terms of space and time being brought about by the communications and information revolution represent a qualitative break with the past. In the light of these changes, the countries of the region have requested the secretariat to focus the deliberations of the twenty-ninth session of ECLAC on the issue of globalization and development.

Globalization clearly opens up opportunities for development. We are all aware —and rightfully so— that national strategies should be designed to take advantage of the potential and meet the requirements associated with greater integration into the world economy. This process also, however, entails risks: risk generated by new sources of instability in trade flows and, especially, finance; the risk that countries unprepared for the formidable demands of competitiveness in today's world may be excluded from the process; and the risk of an exacerbation of the structural heterogeneity existing among social sectors and regions within countries whose linkages with the world economy are segmented and marginal in nature. Many of these risks are associated with two disturbing aspects of the globalization process. The first is the bias in the current form of market globalization created by the fact that the mobility of capital and the mobility of goods and services exist alongside severe restrictions on the mobility of labour. This is reflected in the asymmetric, incomplete nature of the international agenda that accompanies the globalization process. This agenda does not, for example, includelabour mobility. Nor does it include mechanisms for ensuring the global coherence of the central economies' macroeconomic policies, international standards for the appropriate taxation of capital, or agreements regarding the mobilization of resources to relieve the distributional tensions generated by globalization between and within countries.

These shortcomings are the reflection of an even more disturbing problem: the absence of a suitable form of governance in the contemporary world, not only in economic terms (as has become particularly evident in the financial sector) but in many other areas as well. This lack of governance can be attributed, in its turn, to the sharp divergence between global problems and political processes that continue to be pursued within national and, increasingly, local frameworks.

An important dimension of the globalization process —but certainly not one of the main focuses of attention in discussions on the subject— is the gradual spread of ideas and values with regard to civil and political rights, on the one hand, and economic, social and cultural rights, on the other. These ideas and values are gradually laying the foundations for the concept of global citizenship. No one entity embodies this aspect of the globalization process more fully than the United Nations. Under its founding Charter, ever since its inception the United Nations has reaffirmed global ideas and values regarding these rights. These ideas and values have subsequently been ratified by the Governments at a series of world summits.

The first part of this study analyses globalization from an integral standpoint. As part of an exploration of the multidimensional nature of globalization, chapter 1 places the current phase of this process within the historical context of the world economy's progressive internationalization and explores its social, political and cultural components. Chapter 2 reviews the economic facets of the globalization process, including trade and investment, finance and macroeconomic regimes, and international labour mobility. Trends in income inequality and the fundamental asymmetries of the global order are examined in chapter 3. The fourth and final chapter of part one contains a proposal for a positive agenda for Latin America and the Caribbean in the global era. Based on a number of essential principles —such as shared objectives; global institutions that respect diversity; the complementarity of global, regional and national institutions; and equitable participation in accordance with suitable rules of governance— it outlines the steps to be taken at the national, regional and global levels to achieve three priority objectives of the new international order: the provision of global public goods, the correction of international asymmetries and the pursuit of a rights-based social agenda.

The second part of the study focuses on specific issues: external vulnerability and macroeconomic policy (chapter 5), the integration of Latin America and the Caribbean in global trade and production circuits (chapter 6), strengthening innovation systems and technological development (chapter 7), international migration and globalization (chapter 8), globalization and environmental sustainability (chapter 9), globalization and social development (chapter 10) and the effects of globalization on the Caribbean economies (chapter 11). Following a brief diagnosis of the main problems in each of these areas, recommendations are made in these chapters concerning a series of measures that can be taken at the national, regional and international levels in order to implement the proposals put forward in chapter 4.

Part I: Global outlook

Chapter 1

Globalization: a historical and multidimensional perspective

In the past decade the concept of globalization has been employed widely in academic and political debate, but the meanings attributed to the term are far from consistent. In this document it is used to refer to the growing influence exerted at the local, national and regional levels by financial, economic, environmental, political, social and cultural processes that are global in scope. This definition of the term highlights the multidimensional nature of globalization. Indeed, although the economic facet of globalization is the most commonly referred to, it acts concomitantly with non-economic processes, which have their own momentum and therefore are not determined by economic factors. In addition, the tension that is generated between the different dimensions is a pivotal element of the process. In the economic sphere but also —and especially— in the broadest sense of the term, the current process of globalization is incomplete and asymmetric, and is marked by major shortcomings in the area of governance.

The dynamics of the globalization process are shaped, to a large extent, by the fact that the actors involved are on an unequal footing. Developed-country governments, together with transnational corporations, exert the strongest influence, while developing-country governments and civil society organizations hold much less sway. Moreover, these actors, particularly developed-country governments, reserve and exercise the right to take unilateral and bilateral action and to participate in regional processes, concurrently with their participation in debates and negotiations of global scope.

The meaning of the term "globalization" as used in this document is positively couched and is intended to serve the purposes of analysis. It does not embrace the normative use of the concept as referring to the only possible road to the full liberalization and integration of world markets, which is seen as the inevitable and desirable fate of all humankind.[1] The history of the twentieth century refutes such a view, as the period between the world wars was marked by a long and conflictive reversal of the internationalization process. The development of multilateral institutions which has accompanied this process over the last two centuries and the current debate on global governance show that there is not just one possible international order, nor is there a single way of dividing responsibilities among global, regional and national institutions and agencies. Moreover, the course of events in developed and developing countries has revealed that there are many ways to carve out a position in the global economy (ECLAC, 2000; Albert, 1991; Rodrik, 2001a). The differences are a reflection of each country's history and its perception of the opportunities and risks involved in becoming integrated into the world economy.

This chapter presents an initial approach to the process of globalization as a whole. The first section gives a general description of the history and economic dimensions of the process, and the following section analyses the main non-economic factors (ethical, cultural and political principles). The chapter concludes with an analysis of the opportunities and risks inherent in globalization.

I. The globalization process

The contemporary process of internationalization dates back to the emergence of capitalism in Europe in the late Middle Ages, the new scientific and cultural thinking embodied by the Renaissance and the establishment of the great European nations and their empires. The expansion of capitalism is the only historical phenomenon to have been truly global, albeit incomplete, in scope. To a greater extent than other parts of the developing world, the history of Latin America and the Caribbean has been strongly influenced by this phenomenon ever since the late fifteenth century.

Modern historians distinguish a number of stages[2] in the last 130 years of globalization which, with a few adaptations, will be employed here. The first phase, from 1870 to 1913, was marked by great capital and labour mobility, together with a trade boom which was the result of dramatically reduced transport costs rather than of free trade. This phase of globalization was cut short by the First World War. As a result, in the 1920s it was impossible to resume the trend of previous years, and in the 1930s the globalization process was openly reversed.

After the Second World War, a new stage of global integration began. This period consisted of two entirely different phases. The watershed events of the early 1970s that marked the changeover from the first to the second included the disintegration of the macroeconomic regulation regime established in 1944 in Bretton Woods, the first oil crisis, the increasing mobility of private capital —intensified by the first two phenomena— and the end of the "golden age" of growth in the industrialized countries (Marglin and Schor, 1990). If the early 1970s are taken as the turning point, then an earlier phase of globalization can be identified, which lasted from 1945 to 1973. This period was characterized by a major effort to develop international institutions for financial and trade cooperation and by a significant expansion of trade in manufactures between developed countries. It was also marked by widely varying models of economic organization and limitations on the

[1] Helleiner (2000) presents a comparison of these two visions.

[2] See Maddison (1991, 1995 and 2001); O'Rourke and Williamson (1999); Dowrich and DeLong (2001); Lindert and Williamson (2001) and O'Rourke (2001). The starting point, set at around 1870, is somewhat arbitrary, but it reflects the incipient and still limited integration at the international level (and even at the domestic level, in large countries) of goods, capital and labour markets up to that time, as well as the restricted scope of the industrialization process in most of the countries that formed the nucleus of the world economy.

mobility of capital and labour. The final quarter of the twentieth century ushered in a third phase of globalization, with the gradual spread of free trade, the growing presence on the international scene of transnational corporations operating as integrated production systems, the expansion and notable mobility of capital and a shift towards the standardization of development models. At the same time, restrictions on the movement of labour persisted.

This long process has been fuelled by successive technological revolutions and —most of all— by advances that have cut the costs of transportation, information and communications.[3] The shortening of distances, in the economic sense of the term, is a cumulative effect of cost reductions and of the development of new means of transport, in combination with the capacity for the "real time" transmission of information, starting with the invention of the telegraph and expanding with the telephone and the television. Access to information on a mass scale, however, became possible only with the development of information and communications technologies in recent years. These technologies have drastically reduced the cost of access to information, though not, obviously, the cost of processing it or, therefore, of making effective use of it.

Advances in transportation, information and communications are part of a wider range of technological innovations which have resulted in unprecedented leaps in productivity, economic expansion and increased international trade. In the European countries, the large capital cities have been engaged in international trade since inception of modern capitalism (Braudel, 1994). The internationalization of corporate production dates back to the late nineteenth century, when it emerged as a by-product of economic concentration in the industrialized countries. In fact, this is the phenomenon that marked the birth of transnational corporations. From the 1970s on, it became increasingly common for labour-intensive tasks, such as assembly or *maquila* activities, to be outsourced in other countries, in a trend facilitated by the reduction in transport costs and the trade regulations established by the industrialized countries. This was the first step towards the development of integrated production systems, in which production can be divided into various stages ("dismemberment of the value chain"). In such systems, the outsourcing plants or firms in different countries can then specialize in the production of certain components, in particular phases of production, or in the assembly of specific models.

These changes in the structure of production and trade have made major players of large corporations and business conglomerates. In fact, the development of integrated production systems and increased flows of trade and foreign direct investment go hand in hand with the growing influence of transnational corporations. The key factor has undoubtedly been the liberalization of trade, financial flows and investment in developing countries, whose pace has increased in the last two decades. These phenomena are partly to account for the huge wave of foreign investment and the marked concentration of production at the world level which were a hallmark of the final decade of the twentieth century.

As in the case of trade, international financial transactions originated in Europe at about the same time as modern capitalism (Kindleberger, 1984; Braudel, 1994). In the nineteenth century, London was the main international financial centre and presided over the consolidation of the gold standard as a system of international payments and macroeconomic regulation. Paris and —by the early twentieth century— New York were its closest competitors. The subscription of capital for large-scale projects, especially in infrastructure and natural resources, and the creation of an international market in public debt bonds were the predominant modalities of long-term international capital movements during the first phase of globalization. These developments were then joined by systems for financing international trade, with the emergence of an incipient

[3] In fact, globalization could not have come about without the railway, the steamship and the telegraph in the nineteenth century; the construction of canals connecting oceans (Suez in 1869 and Panama in 1903); automobiles, aeroplanes, telephones and television in the twentieth century; and, of course, the revolution in information and communication technologies in the final decades of the twentieth century.

international banking network. Long-term financing arrangements were then hit by a series of crises, however, and nearly disappeared as a result of the worldwide depression of the 1930s, the collapse of the gold standard and the massive moratoriums that ensued. As a response to this situation, the Bretton Woods agreements were adopted in 1944 with a view to creating a multilateral system of macroeconomic regulation based on fixed but adjustable exchange rates and on financial support for countries threatened with balance-of-payments crises. Another response was the establishment of an official international banking system at both the national level (export and import banks) and the multilateral level (World Bank and, later, Inter-American Development Bank and other regional banks).

In the 1960s, long-term international private flows reappeared, thanks in part to a new phase of global economic stability, but also to other factors: the surplus of dollars that built up in the 1960s and of petrodollars in the 1970s; the abandonment of the Bretton Woods system of fixed rates and the flotation of the main currencies in the early 1970s; the rapid development of institutional saving in the 1980s, led by the United States and the United Kingdom; and the emergence of an increasingly large financial derivatives market in the last decade of the twentieth century, which made it possible to hedge the risks associated with different financial assets and liabilities.

Globalization has proceeded at a faster pace in the financial sphere than in trade and production, and it can reasonably be argued that we live in an era in which the financial sphere holds sway over the real sector of the economy (ECLAC, 2001a). Both processes are taking place within a framework of profound institutional restructuring at the global level. And the essence of that process has been the liberalization of international current and capital transactions. The design of new global economic rules continues to be inadequate, however, and clearly suffers from institutional gaps.

On the other hand, there has been no corresponding liberalization of labour flows, which are subject to strict regulation by national authorities (except among the member countries of the European Union). This is one of the major differences between the first and current phases of globalization. The first was marked by two major migration flows: of European labour to temperate zones and of largely Asian labour to tropical areas. Together, these two migrations encompassed around 10% of the world population of the time (World Bank, 2002a).

In addition, the regulation of migratory flows is biased against unskilled labour, which consequently tends to seek out irregular channels. This exposes immigrants to abusive practices by traffickers, heightens their defencelessness against the authorities and generates further downward pressure on wages for unskilled labour in the receiving countries. The existing modalities for regulating migration absorb the most highly qualified —and relatively scarce— human resources from developing countries. The segmentation of labour mobility therefore exacerbates income disparities between workers with different skill levels in both their home and their host countries.

A number of other factors that are closely associated with economic activity have taken on great importance at the world level. One of these is the extent of global environmental problems. In the past three decades it has become clear —and has been scientifically documented— that the planet is facing an unprecedented situation as a result of the increasing scale and cumulative effect of human activity. The impacts are worldwide and include global warming, the thinning of the ozone layer, the decline in biodiversity and the spread of desertification and drought, which have taken on the perverse dimension of “global public ills”. This has highlighted the increasing ecological interdependence among countries, which has made the current moment in history unique (ECLAC/UNEP, 2001). The need to reverse these processes has given rise to new imperatives and opportunities for international cooperation, and the threat they pose to the sustainability of economic growth has been debated widely and at length. The responses that have been developed thus far, however, are clearly inadequate given the magnitude of these problems.

Another variety of “global public ills”, also linked to economic activity, is the spread of international crime: the production, trade and consumption of narcotics, and their close linkage with terrorist financing, arms trafficking and the international circulation of illicit capital generated by drug trafficking and by the different forms of corruption that transcend national boundaries. The system has been slow to recognize need to control the circulation of illicit capital in both developing and developed countries as well as in offshore financial centres because special mechanisms to monitor the circulation of illicit funds require existing bank secrecy arrangements to be scaled back. Unfortunately, the systems that have been developed thus far do not include measures to combat corruption.

II. Non-economic dimensions

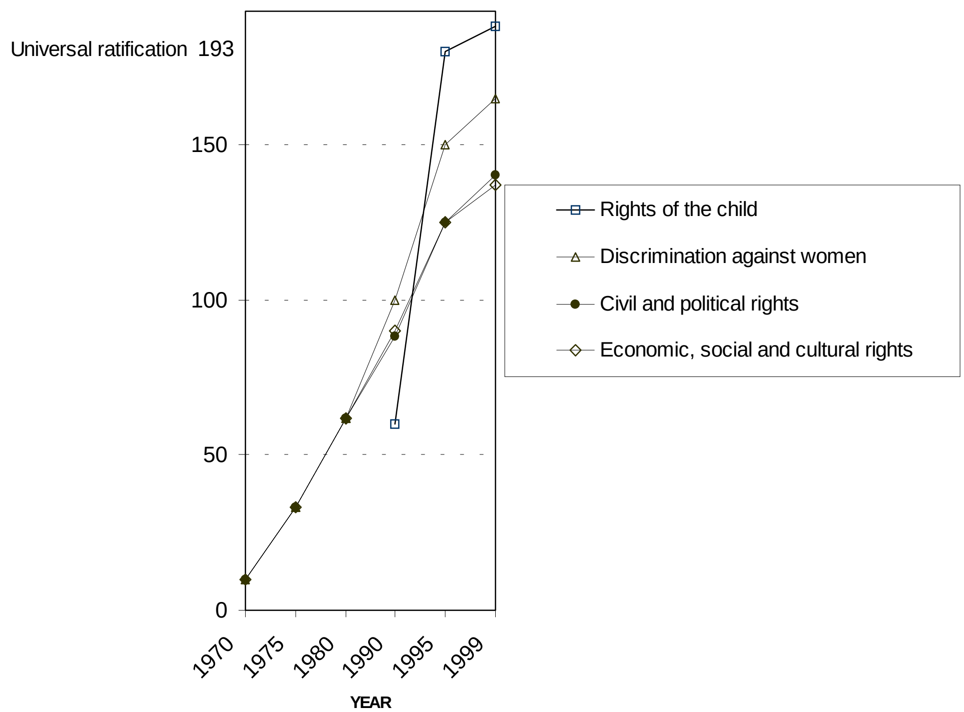
1. Ethical and cultural dimensions

Economic globalization is taking place alongside other processes that have a dynamic of their own. One of the most positive of these processes is what ECLAC has termed the “globalization of values”. This concept refers to the gradual spread of shared ethical principles (ECLAC, 2000a) and is manifested most clearly in declarations on human rights. The two main dimensions of concern here are: (i) civil and political rights, by virtue of which individuals have autonomy from the power of the State and are entitled to participate in public decision-making; and (ii) economic, social and cultural rights, which reflect the values of economic and social equality, solidarity and non-discrimination. This process has also found expression in the accession to United Nations human rights conventions by a growing number of governments (see figure 1.1). This phenomenon is reflected in the declarations issued by the participants in world summits held under United Nations auspices on the environment, social development, population, women and the rights of the child, among others. The Millennium Declaration (United Nations, 2000) is one of the most comprehensive expressions of the principles agreed upon at those summits.

It is important to note that, like economic globalization, this “globalization of values” has a long history linked to the aspirations of international civil society. Its most recent manifestation is the formation of a “global civil society” whose capacity for mobilization and the exchange of information has been multiplied by the new information and communications technologies. The history of this society dates back to the liberal internationalism that emerged in the wake of the American and French revolutions in the late eighteenth century, which was spelled out most clearly in the French revolution’s Declaration of the Rights of Man and of the Citizen. As is well known, these values strongly influenced the independence movements in Latin America and the Caribbean, which began when the Haitian revolution broke out in 1791 as a direct consequence of the French revolution.

Whereas the civil and political rights enshrined in the Universal Declaration of Human Rights adopted within the United Nations are rooted in the liberal movements of the late eighteenth century, the International Covenant on Economic, Social and Cultural Rights is a product of the social movements of the nineteenth and twentieth centuries; their chief political manifestation has been the International Socialist Organization in its successive forms. In addition, feminist internationalism had a decisive influence, throughout the twentieth century, on the recognition of women’s equal rights, while environmental internationalism has played a major role since the 1960s in incorporating sustainable development principles into national and international agendas (from Stockholm in 1972 to the United Nations Conference on Environment and Development, held in Rio de Janeiro in 1992, and the subsequent series of global environmental conventions). The emergence of ethnic internationalism in recent decades is the latest chapter in this long history of international civil society movements.

Figure 1.1
RATIFICATION OF HUMAN RIGHTS CONVENTIONS
(Total countries)



Source: United Nations, *Treaty Series. Cumulative Index*, No. 25, New York, 1999.

At the same time, it is important to note that this "globalization of values" sometimes comes into conflict with a diametrically opposed type of globalization that reflects the penetration of market-economy values into social relations (in the areas of production, culture and even the family). The tension generated between these shared ethical principles and the extension of market relations into the sphere of values, which is implicit in the concept of a "market society", is another distinctive feature of the globalization process. This tension sometimes reaches the level of conflict because the international market lacks the mediation mechanisms which the political sphere has traditionally provided at the national level.

In recent years, the long history of social movements has taken on a new dimension: the effort to preserve the identity of peoples and social groups that feel threatened by the tendency towards cultural homogeneity imposed by globalization. This "right to be different" is interrelated in various ways with human rights in the traditional sense, which highlight the equality of citizens, both among themselves and with the State. Thus at the global level, equality and identity are interrelated in quite complex ways.

Globalization simultaneously undermines and fosters cultural diversity. Indeed, whole segments of the world population feel that their unique histories and the values that govern their communities are under threat. At the same time, however, globalization builds closer relationships among different cultural traditions and ways of life, and promotes a plurality of interpretations of the global order.

The speed of this process poses unprecedented challenges. On the one hand, it threatens to turn the enriching dialogue of cultures into a monologue. On the other, interaction opens up cultural opportunities, including those related to the mixture of different cultures, to new and varied groups and individuals. This process of incorporation through participatory and exclusionary mechanisms has given rise to new forms of organization. New networks, including virtual ones, are replacing the traditional forms of organization of protest movements.

Box 1.1
INCLUSION AND IDENTITY: THE ISSUE OF ETHNICITY

Latin America and the Caribbean is a melting pot of cultures in which diversity and universality are mixed and blended. The region is home to over 400 indigenous peoples comprising 50 million individuals who have gradually been strengthening their ability to organize politically, to assert their ethnic identity and to defend their culture.—Five countries account for nearly 90% of the region's indigenous population: Peru (27%), Mexico (26%), Guatemala (15%), Bolivia (12%) and Ecuador (8%). The Afro-Latin and Afro-Caribbean population totals almost 150 million persons, most of whom live in Brazil (51%), Colombia (21%), the Caribbean subregion (16%) or Venezuela (12%).

At the start of this new millennium, the indigenous, Afro-Latin and Afro-Caribbean peoples of the region have the worst economic and social indicators, enjoy very little cultural recognition and lack access to public decision-making circles. Latin America and the Caribbean are faced with a formidable challenge in this respect. Social integration requires recognition and appreciation of cultural diversity, and this means that States, governments and societies must recognize the rights of the different ethnic groups, incorporate those rights into their legislation and provide the necessary means of exercising those rights. Development policy must also provide opportunities for these populations to develop their potentials and share in the basic codes of modern-day life without losing their identities.

The unprecedented development of the communications media has strongly influenced these processes and has also given rise to new problems. First, it has widened the gap between the cultural norms most broadly disseminated through global channels and the cultural and artistic roots of countries and regions. Second, control of the media, at the national and international levels, is concentrated in the hands of a few. This situation threatens the ideal of cultural diversity, since the control of symbolic exchanges affects identity-building and the formation of opinions and beliefs.[4] Third, the development of audiovisual media has led to greatly heightened personal expectations. Access to information is not always in balance with opportunities for steady employment and incomes, and, accordingly, for well-being and consumption. Today, more than ever before, the demonstration effect cuts across national boundaries. Lastly, participation in or exclusion from the electronic exchange of information has become a crucial factor for the exercise of citizenship, thereby posing the basic problem of how to prevent the emergence of a gap between those with access to information technology and those who suffer from "electronic invisibility".

2. The political dimension

International political relations have also undergone far-reaching changes in recent decades. The end of the cold war produced a dramatic change in the climate prevailing among sovereign States, while the exacerbation and increased visibility of a number of local conflicts generated international tensions of a very different nature than those seen before. While these trends had been in evidence since the 1970s, they became consolidated in the closing decade of the twentieth century, particularly as a result of the profound changes that took place after the fall of the Berlin Wall. The heightened predominance of the United States, European efforts to form a bloc capable

[4] None of the world's 20 largest multimedia groups is Ibero-American, and four of the five largest conglomerates are from the Anglo-Saxon world. In 1999, just four agencies controlled the international flow of news in print. If there is a correlation between these figures and the degree of symbolic influence, it may well be wondered how audible and visible the Latin American and Caribbean region is in the world of today.

of playing a leading role in global economic and political life, the setbacks suffered by Japan, the increased prominence of China and India, and the sudden transition experienced in the former socialist countries were the most salient features of this period.

These sweeping political changes have placed representative democracy in a position of unparalleled predominance. Political discourse is being shaped by an acceptance of the principles of pluralism, alternation of power, division of the powers of the State, election of authorities as a basis for legitimacy and recognition of the majority and respect for minorities, and these principles have begun to be applied much more widely.

Nevertheless, the transformations now under way have raised questions with respect to the functioning of all democratic institutions in societies where information, “image” and the power of money play a fundamental role. These criticisms extend to political parties, legislatures, the relationship between voters and representatives, and even the very meaning of politics, especially, though not exclusively, in the parts of the developing world that suffer from exclusion and poverty. Although democracy is the choice of the majority, there is certainly no scarcity of negative views regarding its workings and its effectiveness in meeting the population’s needs. Since the peace dividend resulting from the end of the cold war has not yielded significant benefits, it has not yet been possible to cash in on the “democracy bonus”.

Despite these difficulties, it is recognized that democracy is the best means of setting a development agenda (Sen, 1999) and that good governance is characterized by a focus on improving the design, management and evaluation of public policy, understood as the analytical and operational unit of government (Lahera, 1999). Nonetheless, government authorities and political leaders are under pressure to win broad local support and, at the same time, to respect the rigid rules deriving from specific forms of globalization. In this connection, it may be categorically stated that the promotion of democracy as a universal value is meaningless if national processes to provide for representation and participation are not allowed to influence the definition of economic and social development strategies or to mediate the tensions inherent in the globalization process.

The reduced capacity of the State has a bearing on the role which the public sector can play in reducing the cost of the “creative destruction” associated with rapid structural change and may exacerbate the difficulties involved in the modernization of the State. However, it is less than realistic to sing the praises of both globalization and the disintegration of the State at one and the same time. The role of the social State as a generator of technological and institutional externalities is and will remain very important. In a world of global risks, the claim that economic forces can and should take the place of public policy and the State is less and less convincing. It is helpful, in this connection, to recall the categorical warning issued by Polanyi (1957) in his analysis of the collapse of the first phase of globalization: if the market seeks to take precedence over society, it will end up destroying its own foundations.

III. Opportunities and risks

In the area of access to new technologies, as in the area of trade, the globalization of markets offers developing countries ample opportunity to integrate themselves more fully into the world economy. The sustained growth of international trade and the strengthening of multilateral rules and dispute settlement mechanisms within the framework of the World Trade Organization (WTO) are promising signs in this regard, as is regionalism when understood in the positive sense of open regionalism proposed by ECLAC (1994). However, the inroads being made in these directions run up against the incomplete liberalization of developed-country economies. The partial nature of this process is itself a reflection of the protectionist practices that still predominate in the world today, as well as the oversupply of certain goods in international trade, particularly raw materials. In addition, the developing countries face the challenge of adapting their policies to the institutional mechanisms required by WTO. This task has not been easy, and it may even have consequences that are more restrictive than desired. In fact, as will be shown later on in this study, global standards only generate greater disparities in the absence of genuine equality of opportunity at the international level.

The explosive pace of global financial development has created opportunities for financing and for hedging financial risk, but it has also revealed the enormous problems caused by the asymmetry existing between the strength of market forces and the weakness of the institutional frameworks that regulate them.[5] The coexistence of financial globalization and national macroeconomic policies, which are still formulated on the basis of domestic interests and contexts, creates considerable tension for developing countries. Their governments are subject to the uncertainty generated by the macroeconomic policies of developed countries, which do not adequately internalize their effects on the rest of the world and lack coordination mechanisms to ensure global coherence. These difficulties are compounded by the problems inherent in the financial market, particularly those of volatility and contagion, which have strongly affected the Latin American and Caribbean countries in recent decades. These phenomena are related to the market's inability to distinguish properly between different groups of borrowers, which elicits herd behaviour in the financial market during both booms and busts. The developing countries are also threatened by the globalization of financial volatility, which can have adverse effects on economic growth and social equity (Ffrench-Davis and Ocampo, 2001; Rodrik, 2001b).

Financial instability is the clearest, but not the only, manifestation of the progressive asymmetry between the power of the market and the lack of adequate economic governance. Other manifestations include the considerable economic concentration in evidence throughout the world and the multiple distributive tensions caused by the globalization process both between and within countries.[6] These phenomena reflect, among other factors, the stringent educational and knowledge requirements imposed by global technologies and markets, which threaten to marginalize those who are not fully prepared and to further confine the availability of these technologies and of new knowledge to just a few countries, social groups and enterprises. This process is part of a whole series of old and new threats to the economic and social security of the population, whose position is being made all the more precarious by a progressive weakening of the entire range of social safety nets, starting with those provided by the family and ending with those furnished by the State.

Globalization can also promote the emergence and appraisal of environmental comparative advantages, including the sustainable use of natural capital having economic value (forests, fisheries, tourist attractions), ecological value (natural sinks for the absorption of carbon and other pollutants) or aesthetic, historical or scientific value. This can give rise to countless policies on the development of ecotourism, research on new medicines, the use of empirical knowledge concerning natural resources management and the economic properties of local biological diversity, the use of the regional ecological supply (such as biomass and natural resources), the productive utilization of unique ecological niches and international negotiations on regional ecological services of global interest. At the national level, globalization can promote the improvement of public policies by raising the cost of implementing unsustainable strategies that adversely affect long-term development. One of the risks that arises in this connection, however, is the possibility that traditional comparative advantages may be lost without necessarily being replaced by new ones.

By definition, global environmental processes affect all countries, but small tropical countries, particularly island States, are especially vulnerable to global environmental changes, as is demonstrated by the increasing frequency and intensity of natural disasters. Indeed, unless specific national and international policies are adopted, the trend towards the overexploitation of certain

5 See United Nations (1999a), UNCTAD (1998, 2001a) and ECLAC (2001).
6 See UNCTAD (1997), UNDP (1999), Cornia (1999a), Rodrik (1997), Bourguignon and Morrison (2002) and chapter 3 of this report.

natural resources, the underutilization of others and the transfer of ecological costs from major polluting countries to the region can be expected to intensify.

Globalization also provides unprecedented opportunities in non-economic areas. As noted earlier, the spread of global values, the struggle for the right to be different and the establishment of international mechanisms to defend the exercise of citizenship are notable advances that are reflected in the consolidation, insufficient though it may be, of respect for human rights, democracy, gender equality and ethnic diversity. The breakdown of archaic structures of domination and the control of abuses of power at the country level are some of the advances of this new global era. Nonetheless, this has not done away with the tensions created by the lack of channels, in some cases, for the legitimization of international actions and the reduction of the enormous imbalances of power existing at the global level. The globalization of the communications media and their concentration in the hands of a few also pose new problems. One of these problems is the strong tensions this generates between homogeneity and cultural diversity. Another is the enormous distance between symbolic integration into the globalized world and the insufficient capacity for actual integration owing to the sharp inequalities that exist in today’s world.

Many of these problems stem from the incomplete and asymmetrical nature of the policy agenda associated with the current phase of the globalization process. This is largely because of the disparities, in terms of power and organization, found among the international players influencing the formulation and implementation of that agenda. In the terms used in the financial debates of recent years, all of this underscores the need for a new “international architecture” for the era of globalization based on a wide-ranging agenda and a representative and pluralistic negotiation process.

Such a global agenda should encompass both the provision of global public goods and the correction of major international inequalities and asymmetries. The international structure reveals, first, a contrast between the rapid development of markets and the slow development of global governance, which has resulted in a suboptimal supply of global public goods (Kaul, Grunberg and Stern, 1999). A second category of problems has to do with the lack of effective international instruments for guaranteeing the achievement of the development goals that have been reiterated so often, most recently in the United Nations Millennium Declaration. A third category is related to the correction of the asymmetries faced by developing countries in the global order in the areas of production, technology, finance and macroeconomics as a result of the contrast between the high international mobility of capital and the tight restrictions imposed on the mobility of labour (Ocampo, 2001a).

In the first decades following the Second World War, the need to correct the asymmetries of the international economic system was expressly acknowledged. The commitments entered into in relation to official development assistance and preferential treatment for developing countries in international trade were some of the partial, albeit relatively unsatisfactory, results of this effort to build a “new international economic order”. This vision has been radically eroded in recent decades and has been replaced with an alternative paradigm whereby the basic objective of changes in the international economic order should be to provide a “level playing field” for the efficient operation of free market forces. The evidence of a further exacerbation of inequalities over the past half century, which represents a continuation of more long-standing trends, shows that both approaches have fallen short.

The lack of global governance, which encompasses all these issues, reflects another deep-rooted conflict: the contrast between global problems and local political processes. This discrepancy basically means that there are no decision-making mechanisms at the global level to ensure that the interests of the least powerful countries and social sectors are adequately represented. Obviously, this situation gives rise to tensions because the exercise of citizenship and democracy remains confined to the national and local spheres.[7] In fact, in today's world, this is still the most important meaning attached to the concept of a nation, although globalization has also heightened the tensions between the demands of citizenship, which have been increased by democracy, and the limitations which globalization has imposed on the ability of governments to take action.

[7] Certainly, there are areas in which a form of "global citizenship" is emerging, as manifested in civil-society participation in United Nations world summits and in global debates on the environment and trade. This was demonstrated very clearly by the civil society event that took place in parallel with the Ministerial Meeting on Trade of the Summit of the Americas (Toronto, 1999) and by the clashes surrounding the WTO Ministerial Conference in Seattle (1999), the annual meeting of the International Monetary Fund and the World Bank in Prague (2000), the meeting of the Group of Eight in Genoa (2001) and the World Social Forum in Porto Alegre (2001 and 2002), among others.

Chapter 2

The economic dimensions of globalization

While the globalization process is a complex and multidimensional phenomenon, some of its most visible and influential aspects are economic in nature. This chapter contains an analysis, from a global standpoint, of major trends in trade, investment, finance, macroeconomic regimes and international labour mobility. This analysis covers a long period in history, from the last quarter of the nineteenth century to the present, and is structured according to the successive phases of globalization identified in the preceding chapter.

The first section focuses on the development of trade and investment flows among the principal regions of the world, with emphasis on the variable relationship between the expansion of trade and economic growth, the emergence of integrated production systems underpinning the operations of transnational corporations, the primary challenges faced by developing countries as a result of these global trends and the creation of an international institutional framework in the area of trade. The second section contains an analysis of the most important changes that have taken place in international finance and macroeconomic regimes. After reviewing major historical developments in this area, the study focuses on the volatility and contagion which have characterized capital flows in the third phase of globalization, and finally analyses the magnitude and composition of capital flows to developing countries.

The last section presents an overview of the phenomenon of international labour migration. It includes a comparison of the relative magnitude of migratory flows and the regulatory environment in which they took place during the different phases of globalization, as well as the various global patterns of origin and destination of migrants.

I. International trade and investment

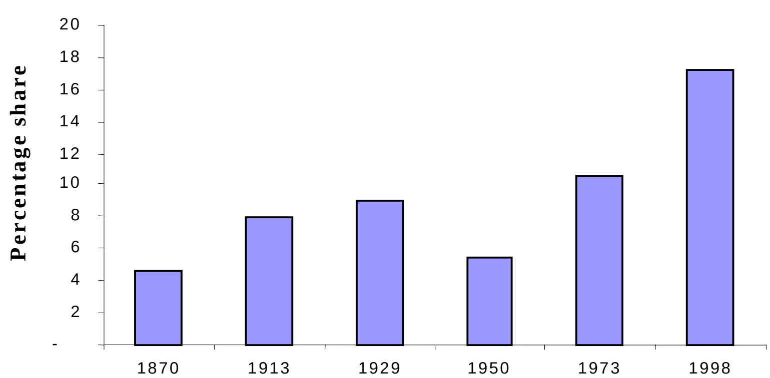
1. International trade and economic growth: a variable historical relationship

Throughout the nineteenth century, world trade expanded rapidly, outpacing world GDP, which also grew briskly (see figure 2.1). This expansion can be traced to a number of factors, including the first industrial revolutions and the consequent drop in transport costs, the "*pax Britannica*" imposed at the end of the Napoleonic wars and the replacement of the principles of mercantilist regulation with those of free enterprise.

Figure 2.1
TRADE AND GLOBAL OUTPUT, 1870-1998

A. Growth in world output and exports of goods

B. Ratio of exports to world GDP



Source: Angus Maddison, *The World Economy. A Millennial Perspective*, Paris, Organisation for Economic Co-operation and Development (OECD), 2001.

This period and, in particular, what was referred to in the preceding chapter as the first phase of globalization (1870-1913) was marked by considerable international mobility of capital and labour and by the spread of the gold standard, beginning in 1870, as a system of international payments and macroeconomic regulation. However, contrary to what is widely believed, the period also witnessed the emergence of new forms of State regulation in relation to the economy (currency and financial system) and social well-being (principles of worker protection and social security) and, especially, the maintenance of numerous restrictions on the free trade of goods.

In fact, except in the European powers committed to free trade (England and the Netherlands, in particular), in colonies whose economic relations with their respective ruling powers were governed by this system and in some independent powers on which similar requirements were imposed (Japan, which did not regain tariff autonomy until 1911, China and the Ottoman Empire, among others), and apart from a more widespread trend towards this form of trade in the 1860s and 1870s,[1] trade protectionism was the norm or, more specifically, the rule prevailing in all nations that maintained their tariff autonomy. Protectionism was the predominant practice in continental Europe, the United States, the self-governing territories of the British Empire that kept their autonomy (Canada and Australia) and many Latin American countries.[2] Bairoch (1993) has rightly argued that, in this period, it was economic growth that fuelled the expansion of international trade, and not vice versa. Accordingly, the idea that free trade was the primary engine of world economic growth between the mid-nineteenth century and the First World War is one of the great myths of history.

Table 2.1
GLOBAL EXPORTS, BY ORIGIN
(Percentage share at current exchange rate, 56 countries)

	1870	**1913**	**1929**	**1950**	**1950**	**1973**	**1990**	**1998**
				Excluding Africa	**Including Africa**			
Western Europe	65.7	56.3	47.4	40.8	38.6	50.3	51.9	47.4
United Kingdom	21.7	15.0	12.1	12.7	12.0	5.8	6.1	5.6
Continent	44.1	41.3	35.3	28.1	26.6	44.6	45.8	41.7
Central and Eastern Europe	5.8	6.0	6.6	8.3	7.8	9.2	5.4	4.9
United States and Canada	10.3	16.4	21.4	26.7	25.3	19.1	17.0	18.6
Other industrialized countries	2.8	4.7	6.2	6.0	5.7	9.6	11.0	9.5
Latin America and the Caribbean								
Asian developing countries	10.6	9.3	10.5	8.4	7.9	5.1	9.5	13.1
Africa					5.4	2.9	1.7	1.5
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Calculated by ECLAC on the basis of Angus Maddison, *The World Economy. A Millennial Perspective*, Paris, Organisation for Economic Co-operation and Development (OECD), 2001.

The rapid growth of international trade was interrupted between the two world wars. Contributing to this break in the trend were global political instability, the deceleration of economic growth in the developed countries, the inability to restore the gold standard and, in particular, the frequent use of protectionist measures (exchange and import controls) and the widespread breakdown of the multilateral payments system during the depression of the 1930s. This explains the importance attached, after the Second World War, to standard-setting and the establishment of international organizations, which evidently were shaped by the unequal power structure of the

[1] The most notable exception was the United States, which adopted highly protectionist principles after the victory of the northern states in the civil war.

[2] The Latin American countries concerned include Brazil, Chile, Colombia and Mexico (Bairoch, 1993, part I; Maddison, 1989, chap. 4; Cárdenas, Ocampo and Thorp, 2000a).

players that took part in the process. The development of this institutional framework will be analysed later in this document.

As a reflection of the manner in which the international trading system was structured in the post-war period, the most dynamic trade flows were originally centred in the two large European trading blocs. Subsequent developments in the two blocs were dissimilar, since the European Community, now the European Union, succeeded in consolidating itself, while the Council for Mutual Economic Assistance (CMEA), consisting of the socialist countries of Central and Eastern Europe, entered a period of decline and later disappeared. Japan and the first generation of “Asian tigers” also began to increase their share of world trade shortly after the end of the war, as a result of planning systems in which the conquest of foreign markets was a central component of development strategy. All the other regions of the world experienced a decline in their share of world trade between 1950 and 1973 (see table 2.2).

The emergence of a highly dynamic trading bloc in East Asia became the most striking feature of world trade beginning in the mid-1970s. Japan lost its lead in the last decade of the twentieth century, while China emerged as the most dynamic international trade hub. Other major changes also took place in the 1990s, in particular the renewed vigour of exports from the United States.

Latin America’s share of world exports fell drastically between 1950 and 1973, stabilized between 1973 and 1990 and then began to increase. Most of the increase is attributable to the upsurge in Mexican exports under the North American Free Trade Agreement. However, accelerated growth in exports from small economies, as compared to the growth of aggregate output, can be observed starting as early as the mid-1950s, while exports from large and medium-sized economies began to speed up shortly thereafter (see figure 2.2).[3] It was then that the countries of the region implemented various combinations of import substitution and export promotion measures, including a number of subregional integration arrangements, the first of which was that of Central America in the 1950s. This “mixed model”, rather than import substitution alone, as is often claimed, was the arrangement most commonly adopted in the region beginning in the 1960s (Cárdenas, Ocampo and Thorp, 2000b), and, in reality, the one advocated by ECLAC since the late 1950s (ECLAC, 1998b; Bielschowsky, 1998; Rosenthal, 2001). As early as the mid-1970s, the growth of exports began to surpass that of GDP in the region as a whole. This trend intensified during the “lost decade”, but more as a result of the sudden drop in GDP than of growth in exports, and, in the last decade of the twentieth century, as a consequence of their expansion.

Thus, the relationship between trade and economic growth has been variable, not only in the course of the century that preceded the Second World War, but also in more recent phases of globalization. As shown in figure 2.1, world trade and world growth accelerated simultaneously between 1950 and 1973, but the upswing in world trade was largely due to the reversal of the trend toward national isolationism observed between 1913 and 1950. The slowdown of the world economy between 1973 and 1990 was also due to the more sluggish growth of world trade, but the latter’s great dynamism in the last decade of the twentieth century **was not accompanied** by further global economic expansion.

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[3] Venezuela was not included in figure 2.2 because its development diverges radically from the regional average and, in fact, alters it significantly. It should be recalled that Venezuelan oil exports were very robust in terms of volume in the first decades after the Second World War, but that this trend was reversed beginning in the 1970s, partly as a result of the commitments entered into within the Organization of Petroleum Exporting Countries (OPEC).

Table 2.2
STRUCTURE OF WORLD IMPORTS, BY ORIGIN AND DESTINATION, 1985 AND 2000
(*Percentages of total world imports*)

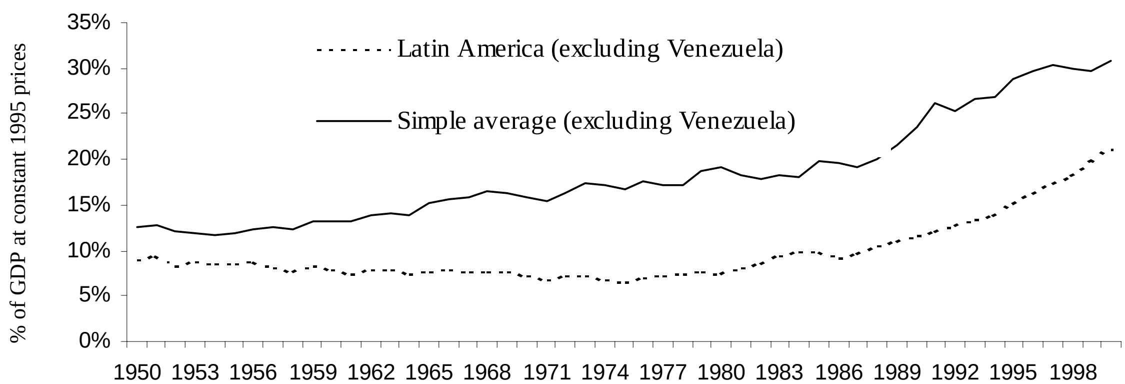
Region of origin \ Region of destination	Western Europe	United States	Other industrialized	Total industrialized	Latin America and the Caribbean	Asian developing	Africa	Total developing countries	Total by origin
A. 1985									
Western Europe	30.0	5.2	1.6	*36.8*	0.8	2.5	1.2	*4.6*	41.4
United States and Canada	3.8	7.1	2.4	*13.3*	1.1	1.8	0.3	*3.2*	16.4
Other industrialized	2.3	4.8	1.0	*8.1*	0.3	2.6	0.2	*3.0*	11.1
Total industrialized	***36.1***	***17.1***	***5.0***	***58.1***	***2.2***	***6.9***	***1.7***	***10.8***	***68.9***
Latin America and the Caribbean	1.5	2.9	0.4	*4.8*	0.7	0.2	0.1	*0.9*	5.8
Asian developing countries	3.5	4.2	4.1	*11.7*	0.3	3.8	0.2	*4.3*	16.1
Africa	2.9	0.8	0.2	*3.9*	0.1	0.2	0.1	*0.4*	4.3
Total developing countries	***7.9***	***7.9***	***4.7***	***20.5***	***1.1***	***4.3***	***0.4***	***5.7***	***26.2***
Rest of world	3.3	0.2	0.3	3.8	0.1	0.8	0.3	*1.1*	4.9
Total by destination	**47.3**	**25.2**	**10.0**	**82.4**	**3.4**	**12.0**	**2.3**	**17.6**	**100.0**
B. 2000									
Western Europe	25.5	4.6	1.5	*31.7*	1.0	2.9	0.6	*4.5*	36.1
United States and Canada	3.7	6.6	1.9	*12.2*	3.2	2.4	0.1	*5.7*	17.9
Other industrialized	2.0	3.1	0.6	*5.7*	0.3	3.4	0.1	*3.7*	9.4
Total industrialized	***31.2***	***14.3***	***4.0***	***49.5***	***4.4***	***8.7***	***0.8***	***13.9***	***63.5***
Latin America and the Caribbean	0.8	3.7	0.2	*4.7*	1.0	0.3	0.0	*1.3*	6.0
Asian developing countries	4.7	5.9	3.8	*14.4*	0.5	8.2	0.2	*8.9*	23.3
Africa	1.1	0.4	0.1	*1.7*	0.1	0.4	0.1	*0.5*	2.2
Total developing countries	***6.6***	***10.0***	***4.1***	***20.7***	***1.6***	***8.8***	***0.3***	***10.7***	***31.4***
Rest of world	3.7	0.5	0.2	4.4	0.1	0.5	0.1	*0.7*	5.1
Total by destination	**41.6**	**24.8**	**8.3**	**74.7**	**6.1**	**18.0**	**1.2**	**25.3**	**100.0**

Source: ECLAC, TradeCAN 2002, on the basis of the International Commodity Trade Data Base (COMTRADE) data.

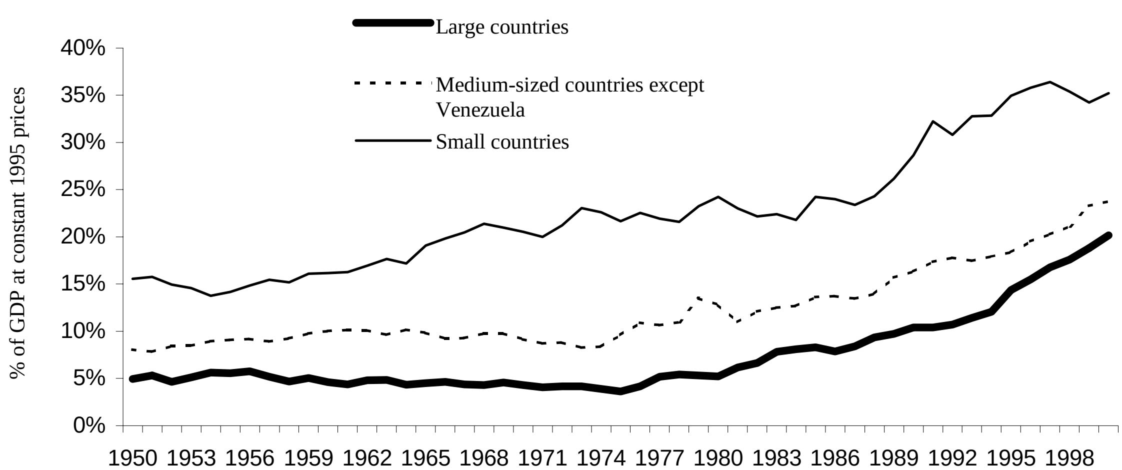
Note: The data on world imports refer to the total imports of 82 reporting countries, corresponding to approximately 90% of world trade. 1985 refers to the annual average for the period 1984-1986. 2000 refers to the annual average for 1999-2000. The countries not included as reporting countries are primarily those with economies in transition. Western Europe: European Union plus Switzerland, Norway and Iceland. Other industrialized: Japan, Australia, New Zealand and Israel. “Rest of world” is not included as a destination for lack of information. Asian origin, “Rest of world” refers to economies in transition, Oceania except Australia and New Zealand, free zones, etc.

Figure 2.2
EXPORTS FROM LATIN AMERICA

A. Percentages of GDP



B. Percentages of GDP by size of countries (simple averages)

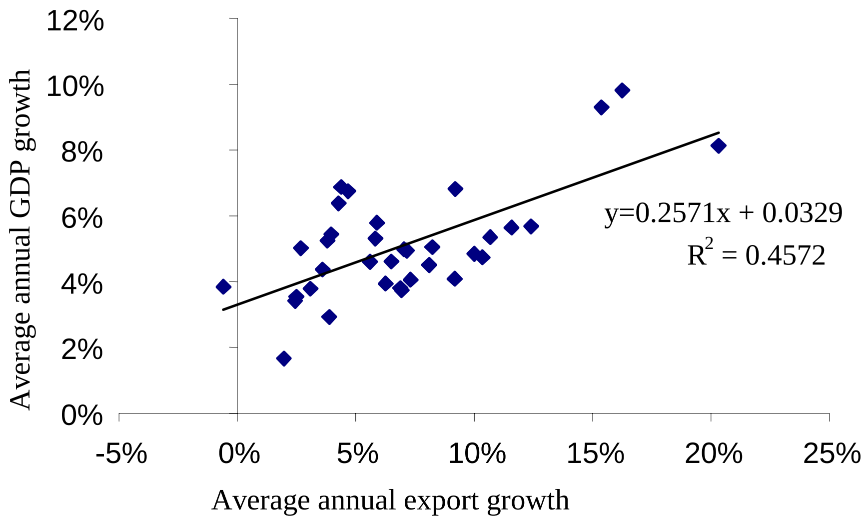


Source: ECLAC, on the basis of official figures.

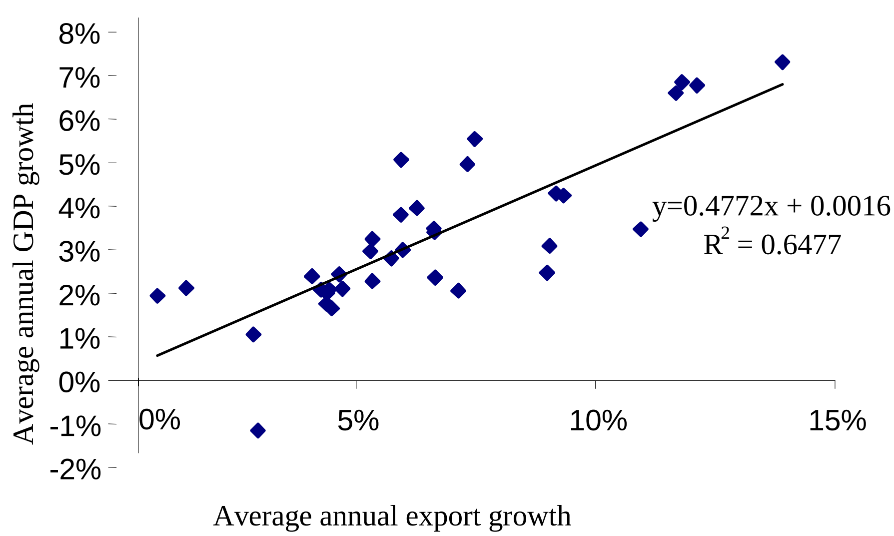
This variable relationship is confirmed by the data shown in figure 2.3. The period between 1950 and 1973 was marked by both faster GDP growth and widely varying patterns of integration into the world economy. Accordingly, the second phase of globalization was not characterized by a strong positive correlation between export growth and GDP growth in the different countries, although some of the fastest-growing economies in that period, particularly the Republic of Korea, Japan and Taiwan Province of China, were also very successful exporting economies. This correlation was, however, strengthened in the third phase of globalization. Thus, even though the liberalization and expansion of world trade **did not translate** into faster world economic growth in the third phase of globalization, the success achieved by individual countries **was** closely linked to their active participation in international trade flows.

Figure 2.3
EXPORT GROWTH AND GDP GROWTH BY COUNTRY
(*35 countries*)

A. 1950-1973



B. 1973-1998



Source: Angus Maddison, *The World Economy. A Millennial Perspective*, Paris, Organisation for Economic Co-operation and Development (OECD), 2001.

In the developing world, the relationship between development strategy, external trade and economic growth undoubtedly has varied since the end of the Second World War. Comparative analyses (see, for example, Helleiner, 1994) categorically demonstrate that trade policy has played an important role in development strategies, but also that there is no simple correlation applicable to all countries in all time periods or to a given country in different periods. The import substitution strategy yielded benefits in terms of rapid economic growth at certain stages, and was even, as noted by Chenery, Robinson and Syrquin (1986), a prerequisite for the export of manufactures at a later stage. Nonetheless, the effects of protectionist policies tended to weaken over time. As was reflected in the global relations referred to above, in more recent decades rapid economic growth has been increasingly linked to success in the area of exports, although this has been achieved under widely varying trade policy strategies. In reality, there is no close linkage between export growth and a liberal trade regime (UNCTAD and Rodríguez and Rodrik). Moreover, as indicated in the extensive literature on East Asia (see, for example, Akyüz, 1998; Amsden, 1989 on the Republic of Korea and 2001; Chang, 1994; Wade, 1990), instances of strong economic growth have been accompanied by mechanisms for State intervention in external trade, the financial sector and technology. According to Rodrik (1999a, 2001a), rapid growth in developing countries has coincided with various combinations of economic orthodoxy and “local heresies”.

In view of the increasing importance of export strength for countries’ economic growth, it is essential to identify precisely the patterns which have promoted export strength in recent decades. Accordingly, table 2.2 illustrates the changes in the network of international trade flows, by origin and destination, between 1985 and 1999; the notes to the table provide detailed information on the subject. The most striking trend that can be observed is the marked increase in the Asian developing countries’ share of world trade. This was achieved largely at the expense of the relative weight of trade between developed countries, which, in any case, still represents more than half of world trade. North America’s share also increased as a result of the considerable expansion of its exports to Latin America and the Caribbean. Trade between developing countries also rose steadily in Latin America and the Caribbean and, even more, in the Asian bloc. In contrast, the weighted share of Africa and the rest of the world (essentially the countries of Central and Eastern Europe) continued to fall. Latin America’s share of exports rose, but to a much lesser extent than its share of imports, with the result that the high positive trade balance of 1985 had become a deficit by 1999, sharply contrasting with the large trade surplus of the Asian developing countries.

The composition of world trade by category of goods has changed substantially over the past 15 years. Table 2.3 classifies products as dynamic or stagnant and indicates their relative importance in two categories of international trade: that involving the intensive use of natural resources and technology, as identified by ECLAC,[4] and the Standard International Trade Classification, known as SITC. The slow growth of trade in commodities and natural resource-based manufactures is one of the most striking phenomena in this regard. Moreover, increasing market competition has resulted in a severe deterioration of raw material prices, in a continuation of a more long-standing trend (see box 2.1). Among manufactures, those based on the use of advanced technology show a much higher growth rate than manufactures as a whole. At the same time, the share of agricultural products, non-food raw materials and, especially, fuel is declining. Lastly, the largest increases are found in the category of machinery and equipment, especially electrical equipment and equipment related to the information and communications industry, whose share increased by nine percentage points.

An analysis of the growth of international trade can be combined with an analysis of the “revealed competitiveness” of various regions, as reflected in their share of different types of products. This gives rise to four categories: (i) dynamic products in which a given region’s share of trade is increasing (“rising stars”); (ii) dynamic products in which its share is falling (“missed opportunities”); (iii) stagnant products in which the region’s market share is increasing (“falling stars”); and (iv) products that combine low growth with a loss of market share (“retreat products”).

4 ECLAC (1993) presents a system of classification by technology-intensiveness, in line with the SITC four-digit classification system.

Table 2.3
DYNAMIC AND STAGNANT PRODUCTS IN WORLD IMPORTS, 1985-2000
Four-digit SITC, Rev. 2 Weighted
(*% of total imports*)

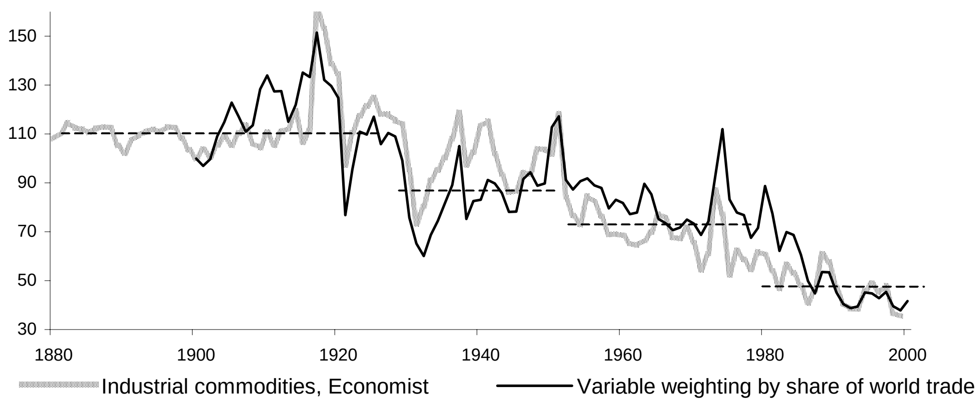
	Dynamic products				Stagnant products				
	Number of items	1985	2000	Increase	Number of items	1985	2000	Loss	Net increase or reduction
A. By technological category									
Commodities	15	0.7	0.8	0.1	132	22.5	11.6	-10.9	12.3
Natural resource-based manufactures	65	5.3	6.8	1.6	134	14.3	8.9	-5.4	14.1
Low-technology manufactures	71	7.3	10.8	3.5	90	7.1	4.9	-2.2	12.2
Mid-level technology manufactures	91	16.7	21.1	4.4	111	11.8	8.6	-3.3	25.2
High-technology manufactures	45	9.5	21.6	12.2	21	2.2	1.3	-0.9	10.8
Unclassified products	4	1.4	2.8	1.4	7	1.4	0.9	-0.5	2.3
Total	291	40.8	63.9	23.1	495	59.2	36.1	-23.1	76.9
B. By SITC classification									
Food and live animals for food	17	1.1	1.4	0.3	77	7.5	4.3	-3.2	-2.9
Beverages and tobacco	4	0.3	0.3	0.1	7	0.7	0.6	-0.2	-0.1
Crude materials, inedible, except fuels	8	0.1	0.1	0.0	96	6.1	3.4	-2.7	-2.6
Mineral fuels, lubricants and related materials	2	0.1	0.1	0.0	18	17.2	8.6	-8.6	-8.6
Animal and vegetable oils, fats and waxes	3	0.0	0.1	0.0	15	0.6	0.3	-0.3	-0.3
Chemicals and related products	39	3.6	6.0	2.4	56	4.5	3.3	-1.2	1.3
Manufactured goods classified by material	76	6.5	7.9	1.4	115	9.1	6.1	-3.1	-1.6
Machinery and transport equipment	89	22.0	35.6	13.6	70	7.9	5.6	-2.3	11.3
Power generating machinery and equipment	9	1.6	2.3	0.7	10	0.5	0.4	-0.2	0.5
Machinery specialized for particular industries	6	0.9	1.1	0.2	22	1.9	1.3	-0.6	-0.4
Metalworking machinery	4	0.3	0.3	0.0	4	0.4	0.3	-0.1	0.0
General industrial machinery and equipment	16	1.9	2.6	0.7	11	1.2	1.0	-0.2	0.6
Office machines and automatic data processing equipment	7	2.4	6.0	3.6	4	0.4	0.3	-0.2	3.4
Telecommunications and sound recording apparatus	6	1.6	3.7	2.1	6	1.2	0.8	-0.3	1.8
Electrical machinery, apparatus and appliances	25	4.7	9.8	5.1	0			0.0	5.1
Road vehicles, including air cushion vehicles	8	7.6	8.1	0.6	5	1.5	1.1	-0.4	0.2
Other transport equipment	8	1.1	1.6	0.6	8	0.7	0.3	-0.3	0.2
Miscellaneous manufactured articles	52	5.8	9.6	3.9	36	4.7	3.6	-1.1	2.8
Commodities and transactions not elsewhere classified	2	1.3	2.7	1.3	4	1.0	0.5	-0.6	0.8

Source: ECLAC, TradeCAN 2001, on the basis of the International Commodity Trade Data Base (COMTRADE) data.

Box 2.1
THE LONG-TERM DETERIORATION OF RAW MATERIAL PRICES

The terms of trade between commodities and manufactures have a crucial effect on both short-term macroeconomic performance and the developing countries' growth prospects, owing to the importance of commodities in these countries' export structures. In the 1950s, Prebisch and Singer formulated the hypothesis of a secular trend towards a decline in the commodity terms of trade. This hypothesis has been studied in depth since then, and both its theoretical and empirical bases have been called into question. Price data for 24 commodities in the period between 1900 and 2000 show that the terms of trade for non-oil commodities have deteriorated to such an extent that they now represent less than a third of their pre-1920 levels. This is equivalent to an annual decrease of 1.5% for the past 80 years, which is evidently a significant decline.

REAL COMMODITY PRICE INDEXES, 1900=100



However, a time series analysis does not reveal a persistent downward trend, but rather three structural changes: one around 1920, when commodity prices lost nearly a third of their relative value; another at the end of the Second World War; and the last in 1980, which set off a very negative trend that has resulted in a cumulative decline of nearly 30% over the past 20 years.

Historical analyses indicate that the First World War ushered in a period of slow economic expansion in the industrialized countries, particularly the United Kingdom and other European countries, that interrupted the brisk growth which had characterized the first phase of globalization. The initial decline coincided with the severe post-war crisis of 1920 and 1921, when real raw material prices plummeted by 45%. As a consequence of overproduction in both developed and developing countries, the terms of trade improved over the rest of the decade but never again reached their pre-war levels, despite the fleeting growth spurt in the world economy and especially the United States economy. The global economic collapse of 1929 triggered another slide in the prices of raw materials, which remained low until the end of the 1940s.

Economic growth rose sharply throughout the world after the Second World War, except in the period of tension generated by the Korean War, but commodity prices stayed low. The expansion of supply hindered their recovery, despite increased demand. The 1973 oil shock marked the only time when commodity prices regained the level they had reached before the First World War, as well as the onset of a new period of slower growth worldwide.

The real turning point, however, came in 1979, when the United States economic authorities decided to raise interest rates to curb inflation and protect the value of the dollar. Since then, despite the temporary recovery of the United States in the 1990s, world economic growth has been sluggish and the developed countries have stepped up their policies of instituting protectionist measures and providing agricultural subsidies. The deterioration of the commodity terms of trade, which accelerated in this period, has not been reversed. Currently, the oversupply of commodities and the slowdown in the world economy hold out little hope for a recovery in the near future.

Source: José Antonio Ocampo and María Ángela Parra, "El retorno de un eterno debate: los términos de intercambio de los productos básicos", Santiago, Chile, Economic Commission for Latin America and the Caribbean (ECLAC), 2002, unpublished.

Export growth in the Asian developing countries, and especially in North America, in the 1990s was associated with the first group of products (see table 2.4). Conversely, Europe's exports reveal the increasing weight of low-growth products in which the region is losing its market share. In the group of other industrialized countries (dominated by Japan), dynamic products prevail, though with a loss of market share. The export situation of Africa is characterized by the enormous weight of stagnant products in which the region is losing its market share, and that of the rest of the world (basically Central and Eastern Europe), by the loss of market share in dynamic products.

Within these parameters, Latin America and the Caribbean is characterized primarily by the importance of less dynamic products, which, in fact, represent the largest proportion of its exports (more than three fourths in the 1990s). As will be discussed in detail in chapter 6, there are actually two dominant patterns of specialization. One is characterized by the increasing weight of exports of dynamic products (Mexico and some Central American and Caribbean countries) and the other, by the predominance of natural resource-intensive products, whose share of world trade is growing slowly (South America). The most notable change between the periods 1985-1990 and 1990-1999 was the increased market share of stagnant products, as reflected in the relatively lesser importance of "retreat" products in relation to "falling stars". In addition, as the region also increased its market share in dynamic products, the weight of the "rising stars" increased in relation to the products classified as "missed opportunities". From this standpoint, the factor which has contributed most to the growth of regional exports has not been their reorientation towards the fastest-growing products in international trade, but rather the enhancement of competitiveness within the existing export structure.

2. The emergence of internationally integrated production systems

The close relationship between international trade and FDI has been another salient feature of recent decades. The participation of developed-country firms in international trade is hardly new, but this phenomenon, which dates back at least as far as the nineteenth century, took on greater relevance after the Second World War. Historically, transnational corporations have focused on the exploitation of natural resources, sometimes coming into conflict with nationalist interests in developing countries; on the construction and management of key segments of the infrastructure supporting agriculture- and mining-based export complexes; on the provision of home services in rapidly growing urban areas; and on capturing protected industrial markets under national import substitution strategies and, in some cases, also taking advantage of incipient subregional integration arrangements.

There is evidence that the growth of international trade in recent decades, the expansion of transnational corporations and the emergence of international integrated production systems are closely related. In the literature on the subject, four factors have been proposed as determinants of the recent growth in international trade: the first two are the reduction of transport costs and trade barriers; the third is the increased demand for different brands of the same products among countries with similar income levels; and the fourth is the break-up of production chains (value chains), which has generated trade flows in intermediate products that cross national boundaries several times in the process of manufacturing a single product (Feenstra, 1998). Some recent studies have highlighted, in particular, the increased trade in intermediate products and services as part of a deepening of the international division of labour between industrialized and developing countries (Feenstra, 1998; Baldwin and Martin, 1999; and Feenstra and Hanson, 2001).

Table 2.4
EXPORT STRUCTURE BY COMPETITIVE POSITION
(*Percentage of exports in the base year and in the final year*)

	Rising stars	Missed opportunities	Falling stars	Retreat	Variation total market share
A. 1985-1990					
Western Europe					
Base year	30.7	36.7	20.5	12.1	3.3
Final year	36.5	38.9	16.7	7.9	
United States and Canada					
Base year	15.3	44.5	13.3	26.9	-0.6
Final year	22.9	47.2	11.8	18.0	
Other industrialized					
Base year	21.0	47.0	11.2	20.9	-0.1
Final year	30.9	44.1	12.4	12.6	
Latin America and the Caribbean					
Base year	11.4	20.8	23.9	43.8	-1.1
Final year	22.6	24.3	24.5	28.6	
Africa					
Base year	5.2	11.0	14.3	69.5	-1.4
Final year	13.0	18.8	20.5	47.7	-0.7
B. 1990-2000					
Western Europe					
Base year	2.7	37.9	4.8	54.5	-8.6
Final year	5.7	44.8	5.7	43.8	
United States and Canada					
Base year	31.3	13.3	32.3	23.2	2.1
Final year	43.2	14.7	28.9	13.2	
Other industrialized					
Base year	6.4	48.8	19.5	25.3	-1.5
Final year	10.4	51.3	22.0	16.3	
Latin America and the Caribbean					
Base year	18.1	2.7	57.2	22.0	1.3
Final year	37.0	2.2	49.8	11.0	
Africa					
Base year	2.5	8.6	19.8	69.1	-0.8
Final year	6.6	9.1	23.9	60.4	
Asian developing countries					
Base year	31.4	3.9	37.0	27.6	6.0
Final year	50.1	3.0	31.7	15.2	

Source: ECLAC, TradeCAN 2001, on the basis of the International Commodity Trade Data Base (COMTRADE) data.

The restructuring of the international economy has reflected, on the one hand, the extension of the logic of business and industry to all sectors of the economy, and, on the other, the development of labour specialization in business and the growth strategies adopted over time (Chandler, 1977; 1990). In business, the progressive autonomy of the components of the labour process after a given stage of production, conditions of market competition and the costs of verticalization of the production process within a single firm, together with changes in demand, have fostered the relative growth of independent suppliers of intermediate goods and services. The trend towards globalization in some industries and the establishment of “global factories” represent an attempt to reproduce, at the world level, the specialization and outsourcing practised by individual firms in local markets (Grunwald and Flamm, 1985).

The fragmentation of the production process is a form of internationalization that depends on the characteristics of the product concerned and its market. In fact, the earliest definitions of global firms referred to those in which a product was produced simultaneously, in a similar manner, in different parts of the world (Levitt, 1983; Hammel and Prahalad, 1985). Some global industries, such as foodstuffs and personal care products, are characterized by the homogeneity of their products, which are produced by similar processes in plants located in different regions. These trends have been intensified by the increasing homogenization of consumer preferences, technologies and products traded on world markets (Levitt, 1983).

Moreover, there is an interaction between the growth strategies of transnational corporations and patterns of production and competition in specific sectors, which, in turn, combine with localization factors to determine the characteristics of trade flows in products, parts and components (Dunning, 1993a). One study by OECD (1996) concluded that trade in the most science-intensive sectors (such as the pharmaceuticals industry) tends to take place within firms, whereas trade in large-scale and technologically advanced industries (automobiles and consumer electronics, among others) primarily reflects assembly operations and intraregional trade. Natural resource-intensive products show low levels of intrafirm trade, and international integration is usually horizontal, meaning that it involves trade in similar products. In the garment industry, trade flows may involve either products assembled in different parts of the world (vertical specialization) or finished products (horizontal specialization). Both types of specialization generate intra-industry trade flows, which may or may not take place within the same firm.[5]

It is important to ensure that the mobility afforded by technological progress turns subsidiaries of transnational corporations, which used to operate in a geographically dispersed manner but with self-contained production processes, into integrated production and distribution networks at the regional and global levels. Within these networks, firms can purchase the inputs they need locally and produce for the local or regional market, or they can integrate economic activities scattered among different regions. From this standpoint, the regionalization of the world economy is, paradoxically, a corollary of globalization.[6]

In trade based on the segmentation of the value chain (Krugman, 1995), countries specialize, according to their absolute advantages, in productive activities and not in industries, as suggested in international trade studies (Feenstra, 1998; Knetter and Slaughter, 1999; Rayment, 1983). Consequently, countries with a large supply of low-skilled labour do not necessarily specialize in labour-intensive industries or branches of industry, but rather in the most labour-intensive activities, which, owing to the scale of production or distribution, are under the coordination of global firms. Therefore, each stage in the manufacture of a product, such as the sewing of a garment, for example, which used to be carried out as part of a factory assembly line, has now become a manufacturing activity that takes place in plants located in countries with a large supply of unskilled labour.[7]

Changes in international trade patterns have been closely linked, therefore, to the restructuring of transnational corporations and to the upswing in foreign direct investment (FDI). The links between FDI and free trade have also been facilitated by changes in the regulatory

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5 The practice of producing and assembling a product in one country for subsequent re-export to the country in which the firm is based began in the late 1960s as a strategy adopted by United States firms in Asian countries. In 1966, these operations represented about 10% of the sales of subsidiaries of United States-owned firms in those countries; in 1977, they represented 25% (Grunwald and Flamm, 1985).

6 Robert Feenstra (1998) has referred to this as the “integration of trade and disintegration of production”. See also Burda and Dulosch (2000).

7 These differences are not reflected in trade statistics, which are organized by industry. This means that they are not very useful for characterizing countries’ areas of international specialization. Moreover, the same product may appear in the customs records of different exporting countries, each of which specializes in a different stage of processing the product.

frameworks governing trade and investment[8] and by other factors related to the ongoing technological and managerial revolution. The lower cost of information management, communications and transport and the use of sophisticated techniques for synchronizing production with demand ("just-in-time") have turned worldwide production, marketing and research and development into profitable undertakings (Turner and Hodges, 1992). These changes have been considerably reliant on economies of scale and environment and, ultimately, on the predominance of large firms. Likewise, agglomeration economies have encouraged the concentration of enterprises in areas that afford them easy access to global markets and factors of production, as well as innovation capacity, suppliers and appropriate institutions.[9]

Furthermore, the increasing competition faced by enterprises, the technological advances that have made it possible to establish real-time long-distance linkages and the liberalization of external trade policies have resulted in greater geographical dispersion of all business functions, even essential ones such as design, research and development and financial management. Some important manifestations of this phenomenon are the establishment of subsidiaries to serve regional markets (such as those in Singapore for the Asian market) and the international division of labour among various regions (as in the automobile sector) and continents (as in the case of semiconductors). In these complex systems, the reassigned functions encompass a wide range of activities; the simplest tasks, such as assembly, are assigned to less industrialized areas, while functions requiring specialized know-how and technology are transferred to more industrially advanced areas.

In terms of the development of business strategies, cross-border mergers and acquisitions are one of the most visible signs of globalization, especially when they involve large firms, and require considerable amounts of financial resources and wide-ranging organizational restructuring. These operations, which intensified in the second half of the 1990s (see table 2.5a), enable firms to rapidly acquire a portfolio of localized assets, which are essential for strengthening its competitive position in the local, regional or world economy. In many cases, the firm's survival is the primary strategic incentive for these operations, especially since firms that are reluctant to engage in them may run a serious risk of being absorbed or of being placed at a competitive disadvantage by the merging of rival firms.[10] There is an intense and dynamic interaction between changes in the global economic environment and the factors that induce firms to engage in cross-border mergers and acquisitions; this explains the steady increase in such operations.[11]

The combination of all these factors has resulted in a rapid increase in foreign direct investment, with a consequent increase in the weight of international production in the world economy. In the 1990s, FDI flows grew considerably, particularly in the second half of the decade, rising from an annual average of about US$ 200 million between 1989 and 1994 to more than US$ 1.3 billion in 2000. Nonetheless, in 2001, for the first time since 1991, worldwide FDI flows declined significantly, dropping to around US$ 760 million.[12] In any event, this level is equivalent

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8 Between 1991 and 2000, a total of 1,185 changes were introduced into national laws on FDI; 1,121 (95%) of these changes were aimed at creating more favourable conditions for FDI.

9 Agglomerations of innovative activities, such as Silicon Valley in California (United States), Silicon Fen in Cambridge (United Kingdom), Wireless Valley in Stockholm (Sweden) and Zhong Guancum in Beijing (China), have evident advantages for attracting high-value FDI. Bangalore, India, has become a magnet for the development of computer programs, as have Penang, Malaysia, in the electronics industry and Singapore and the Special Administrative Region of Hong Kong, China, in the financial services industry.

10 One of the most interesting examples in this regard is the strategy adopted by Spanish firms to expand their operations in a number of Latin American countries.

11 Changes in the environment are associated with technological innovations, changes in the regulatory frameworks that influence a firm's operations and the development of capital markets. The primary strategic objectives are access to new markets, an increased share of such markets or a dominant position in them, ownership of natural resources, particularly non-renewable ones, enhancement of efficiency through the utilization of synergies, achievement of economies of scale through the firm's enlargement, hedging of risks through the diversification of activities and financial considerations (UNCTAD, 2001).

12 The sudden drop that occurred in 2001 is attributable to a number of factors, including the reduced number of cross-border mergers and acquisitions, the slowdown in the world economy and the steep decline in stock prices, the heightened uncertainty that prevailed

to just under four times the annual average for the period 1989-1994 and exceeds the values for each year of the 1990s, with the exception of 1999 and 2000 (see table 2.5b).

Thus, between 1982 and 1999, the percentage of worldwide gross fixed capital formation represented by FDI rose from 2% to 14%, and the value added by transnational corporations rose from 5% to 10% of world GDP. In addition, sales of subsidiaries of transnational corporations grew much faster than global exports (UNCTAD, 2000). As early as the mid-1990s, it was estimated that two thirds of world trade in goods and non-factor services was derived, in some way, from the international production structure of transnational corporations.[13]

This global expansion is driven by the operations of more than 60,000 transnational corporations with nearly 800,000 foreign subsidiaries. Developed countries remain the primary source and destination of FDI flows; in 2000, 71% of total FDI came from such countries and 82% was directed to them. FDI flows have also increased significantly in developing countries, quadrupling, in 2000, their average level for the period 1989-1994 (see table 2.4). The primary recipients were Hong Kong, China and India in Asia, and Mexico, Brazil and Argentina in Latin America.

A comparison of the global distribution of inflows and outflows in 1985 and 2000 shows that FDI has become more important to more countries than in the past. FDI inflows of over US$ 10 billion are now concentrated in more than 50 countries (including 24 developing countries), compared to only 17 countries (including seven developing countries) 15 years ago. The pattern of investment abroad is similar: the number of countries with more than US$ 10 billion in investments abroad rose from 10 to 33, and currently includes 12 developing countries, compared to eight in 1985.

While FDI has expanded geographically, its distribution remains highly asymmetrical. The head offices of 90 out of the 100 largest non-financial transnational corporations, classified as such by the amount of their assets abroad, are located in the United States, the European Union and Japan. In 1999, for the first time, three developing-country firms were among the world's 100 largest (Hutchison Whampoa of Hong Kong, Petróleos de Venezuela and CEMEX of Mexico). The 50 largest developing-country firms, the biggest of which are hardly comparable to the smallest of the 100 largest in the world, are scattered among 13 newly industrialized economies in Asia and Latin America. They include firms in Hong Kong, Venezuela, Mexico, Malaysia and the Republic of Korea.

In terms of major sectors of economic activity, the most striking feature is the significant growth in services. The share of services in FDI inflows between 1988 and 1999 rose by more than six percentage points worldwide, representing over half of cumulative FDI at the end of that period (see table 2.6). This important change is essentially attributable to two factors. First, the liberalization and privatization policies adopted by developing countries in the past decade have prompted a copious inflow of FDI in financial services, telecommunications and other components of infrastructure. Second, the emergence of new marketable services (including the production of computer programs, data processing, telephone calling centres and business support services) has enabled developing countries to take advantage of localization. Moreover, organizational innovations such as "just-in-time" production require logistical and inventory management solutions that are supplied largely by independent service firms.

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towards the end of the year and the strong impact of the telecommunications sector, which suffered as a result of the limited success of the introduction of the third generation of mobile telephones in Europe.

13 According to this estimate, one third of world trade in goods and non-factor services consisted of operations between the head offices, subsidiaries and associates of transnational conglomerates, valued at transfer prices, while another third consisted of exports by transnational corporations to non-associated firms (UNCTAD, 1995).

Table 2.5
FOREIGN DIRECT INVESTMENT
(Billions of dollars)

	Average 1989-1994	1995	1996	1997	1998	1999	2000	2001
A. Cross-border mergers and acquisitions								
Total	**110.2**	**186.6**	**227.0**	**304.8**	**531.6**	**766.0**	**1 143.8**	
Sales, by region of sale								
Developed countries	94.2	164.7	188.7	234.7	445.1	681.1	1057.1	
Developing countries	10.5	16.1	34.7	64.6	80.7	73.6	70.0	
Economies in transition	5.5	5.7	3.6	5.5	5.1	9.1	16.7	
Multinational a/	-	0.1	-	-	0.7	2.2	-	
Purchases, by region of purchase								
Developed countries	103.3	173.8	198.3	272.1	511.4	706.5	1 094.0	
Developing countries	6.6	12.8	28.1	32.5	19.2	57.7	42.1	
Economies in transition	0.3	-	0.5	0.2	1.0	1.5	1.7	
Multinational a/	-	-	0.1	-	-	0.3	6.0	
B. Regional distribution of inflows and outflows								
Total FDI inflows	**200.1**	**331.1**	**384.9**	**477.9**	**692.6**	**1 075.0**	**1 270.8**	**760.1**
Developed countries	137.1	203.5	219.7	271.4	483.2	829.8	1 005.2	5 10.1
Developing countries	59.6	113.3	152.5	187.4	188.4	222.0	240.2	2 24.9
Economies in transition	3.4	14.3	12.7	19.1	21.0	23.2	25.4	25.1
Total FDI outflows	**228.2**	**355.3**	**391.6**	**466.0**	**711.9**	**1 005.8**	**1 149.9**	-
Developed countries	203.2	305.8	332.9	396.9	672.0	945.7	1 046.3	-
Developing countries	24.9	49.0	57.6	65.7	37.7	58.0	99.5	-
Economies in transition	0.1	0.5	1.1	3.4	2.1	2.1	4.1	-

Source: The author, on the basis of United Nations Conference on Trade and Development (UNCTAD), *World Investment Report, 2001* (UNCTAD/WIR/(2001)), Geneva, 2001. United Nations publication, Sales No. E.01.II.D.12.

a/ Sales (purchases) involving more than two countries.
A: Tables B7 and B8
B: Tables B1 and B2

Table 2.6
FDI INFLOWS
(Millions of dollars and percentages)

Sector	Developed countries		Developing countries		World	
	1988	1999	1988	1999	1988	1999
Primary	10.3	5.7	13.7	5.4	10.7	5.6
Secondary	39.4	36.4	65.0	54.5	42.4	41.6
Tertiary	46.9	55.5	20.7	37.3	43.9	50.3
Unspecified	3.4	2.4	0.6	2.8	3.0	2.5
Total	890,456.0	2,520,194.0	119,016.0	1,014,657.0	1,009,472.0	3,534,851.0

Source: United Nations Conference on Trade and Development (UNCTAD), *World Investment Report, 2001* (UNCTAD/WIR/(2001)), tables A.II.3 and A.II.4, Geneva, 2001. United Nations publication, Sales No. E.01.II.D.12.

Note: The data are for 47 countries in 1988 and 57 countries in 1999, which represent more than 80% of FDI inflows in both years. Eastern Europe is excluded for both years.

This process has taken place alongside the restructuring of the industrialized economies, as a result of which the relative share of services has increased to represent more than two thirds of value added in the OECD countries (OECD, 2000). Meanwhile, the share of manufacturing activities as such has declined, representing less than a quarter of the final price of goods, while the rest is made up of the service activities that come into play from the product's conception to its final marketing (Giarini, 1999). The earnings of firms classified as manufacturing firms come mainly from sales of services; this has prompted some authors to speak of an "encapsulation" of services in manufactures.[14]

Alongside the growth in the share of the service sector and the decline in the relative share of the manufacturing sector, a pattern of high geographical concentration of technology-intensive industrial production has proliferated. Table 2.7 shows indicators of geographical concentration for a number of industries, grouped according to whether their technological level is high (semiconductors and biotechnology), intermediate (automobiles, radios and television sets) or low (food, beverages and textiles). The resulting picture is very clear: the more advanced the industry's technology, the greater its geographical concentration in a small number of countries and at the national level. This is the case of biotechnology, which is highly concentrated in certain areas of developed countries, and of the semiconductors industry, which is concentrated in those same countries and in some South-East Asian countries. The manufacture of radios and television sets is somewhat less concentrated geographically and also extends to some developing countries; this pattern is accentuated in the case of the automobile industry. Lastly, textiles and, particularly, the food and beverage industries are less concentrated in developed countries.

The predominance of developed countries as recipients of FDI flows is still based on industries with high and intermediate levels of technological advancement, but has also increased in low-technology industries, which, in 1988, were more geographically dispersed than in 1999. This trend shows that the availability of low-skilled, low-cost labour holds less attraction today for the manufacturing industry, as do opportunities for access to protected markets. In this industry, flows from some developing countries, especially in Asia but also in Latin America and the Caribbean, have increased significantly. In contrast, many countries rich in natural resources have only a marginal share in such flows, indicating that an abundance of natural resources is, by itself, insufficient for the development of enterprises that are competitive at the international level.

Table 2.7

GEOGRAPHICAL CONCENTRATION OF FOREIGN SUBSIDIARIES IN SELECTED MANUFACTURING INDUSTRIES, BY TECHNOLOGY-INTENSIVENESS, 1999

(*Share of total number of subsidiaries*)

Share of total industry	High technology		Mid-level technology		Low technology	
	Semi-conductors	Bio-technology	Auto-mobiles	Radio and television receivers	Food and beverages	Textiles
First 3 recipient countries	0.496	0.627	0.294	0.356	0.237	0.287
First 5 recipient countries	0.629	0.71	0.44	0.502	0.353	0.401
First 10 recipient countries	0.787	0.852	0.71	0.696	0.561	0.601
First 20 recipient countries	0.945	0.953	0.884	0.893	0.747	0.795
Memorandum:						
Total number of foreign subsidiaries b/	272	169	1 296	253	2 250	1 445
Total number of recipient countries	31	28	55	36	101	77

Source: United Nations Conference on Trade and Development (UNCTAD), *World Investment Report, 2001* (UNCTAD/WIR/(2001)), tables II.6, Geneva, 2001. United Nations publication, Sales No. E.01.II.D.12.

a/ Calculated as a proportion of the total number of each industry's foreign subsidiaries throughout the world.
b/ Only subsidiaries identified as primarily foreign-owned.

14 According to the relevant data, more than 50% of the earnings of IBM and Siemens come from service activities (Howells, 2000).

3. Outstanding challenges posed by the relationship between trade and economic growth

In the last 15 years the relationship between export performance and economic growth has raised a number of issues for developing countries. The countries' possible responses to these represent major challenges for the future, of which three are discussed here. First is the question of how to translate export competitiveness into rapid economic growth more effectively. Historically, the periods of greatest export expansion have tended to coincide with lacklustre economic growth, especially in Latin America and the Caribbean (see figure 2.4). In fact, export and output growth is more asymmetric in the region than in the world as a whole. This is largely attributable to the combined effects of rapid trade liberalization and the pursuit of macroeconomic policies based on a concept of stability that is limited to control of inflation and of the public deficit, which do not take account of significant repercussions for the real economy (see chapter 5). One of the consequences of this combination has been a structural deterioration in the economic growth/trade balance ratio (see figure 2.4). This trend is exhibited by virtually all developing countries, as discussed in Trade and development report, 1999 (UNCTAD), and largely accounts for the fact that trade growth has not yet provided these countries with the expected economic growth.

Aside from the fact that an inadequate macroeconomy is at the root of many of the problems linked to poor economic growth, a second challenge is to overcome the restrictions inherent in the production structure, in order to achieve high and sustained rates of economic expansion. Although the region has increased its share of world markets and of foreign investment flows, the production linkages associated with these have been weak. Furthermore, growing use of imported intermediate and capital goods —a typical feature of integrated production systems in globalized sectors of the economy— has resulted in the disintegration of production chains and of domestic systems of innovation that were established during the previous stage of development. These have not been replaced, or at least not at a comparable pace. In addition, the region has only a small stake in sectors associated with expanding international trade, especially those involving a large technological component (see chapters 6 and 7).

Consequently, dynamic activities have acted as only weak and intermittent multipliers and generators of technological externalities. In turn, poor trade balances have helped to keep external borrowing requirements high, even in times of recession. In a context in which expanding sectors generate an inadequate knock-on effect and world economic growth is sluggish, the structural heterogeneity (economic dualism) of production sectors has become more marked: there are now many more "world-class" firms, many of which are subsidiaries of transnational corporations, while a growing proportion of employment is concentrated in low-productivity informal-sector activities, which account for seven of every 10 new jobs created in Latin American urban areas in the last decade.[15]

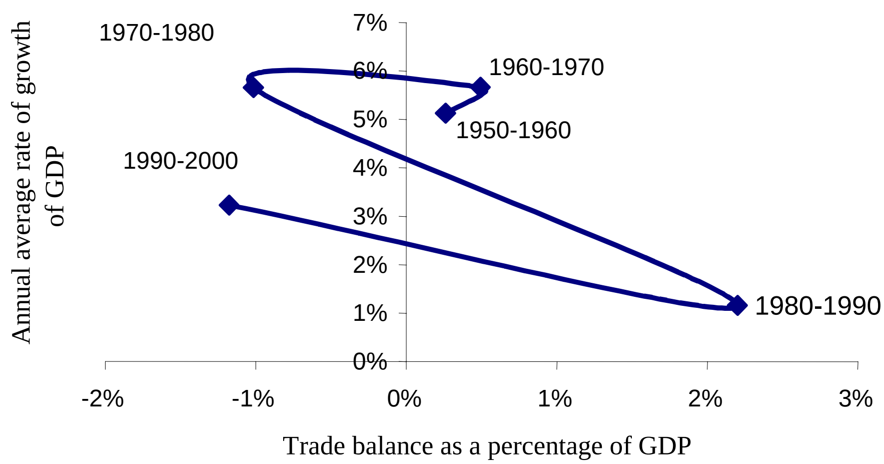
Indeed, the third challenge facing the region's countries concerns recent employment trends. There is no question that the structure of employment undergoes substantial changes in the course of the development process. In the manufacturing sector, it first tends to increase, then stabilizes and finally trends downward as per capita income rises. This pattern is consistent with the "inverted U" propounded by Rowthorn (1999).

[15] Chapters 6, 7 and 10 of this publication and ECLAC (2001a), Katz (2000) and Mortimore and Peres (2001) analyse these issues in greater depth.

Figure 2.4
TRADE AND GDP IN LATIN AMERICA, 1870-1998

A. Growth rates

B. Trade balance and GDP growth



Source: Angus Maddison, *The World Economy. A Millennial Perspective*, Paris, Centro de Estudios de Desarrollo, Organisation for Economic Co-operation and Development (OECD), 2001.

Palma's analysis (2002), which is based on a wide sample of countries, not only confirms this trend, but also introduces three striking new elements, two of which are illustrated in figure 2.5a. One of these is the continuous downward curve seen over the last four decades, which indicates a decrease in the share of manufacturing in total employment at all levels of per capita income. The author attributes this trend to the fact that productivity has increased more rapidly than GDP, which implies that employment in manufacturing has expanded at a slower pace and, in some cases, has contracted in absolute terms.[16] The second interesting element is a shift in the point of inflection to

[16] For example, in the European Union manufacturing employment decreased by almost a third in just three decades, from 1970 to 2000, while in the United Kingdom it fell by half in the same period.

lower levels of per capita income from 1980 onward. This means that the point at which the share of manufacturing in total employment begins to decrease is located at progressively lower levels of per capita income. In 1990, more than 30 countries recorded per capita income that was higher than the level at which manufacturing employment began to decrease. The services sector exhibits a very different trend, with productivity growing much more slowly than GDP, with the result that employment in the sector has increased its share of the total.[17]

The third new element points to the need to consider the phenomenon of "Dutch disease" from a fresh perspective.[18] First, the point must be made that the ratio between the share of manufacturing in total employment and per capita income is a function of the international trade pattern. Both developed- and developing-country exporters of raw materials or services, especially financial services and tourism, thus exhibit a lower ratio than exporters of manufactures at all levels of per capita income (see figure 2.5b).

Second, although these countries are usually less industrialized than exporters of manufactures, this does not alter the general trend towards de-industrialization in either group. In fact, as figure 2.5c shows, from 1960 to 1998 manufacturing employment as a proportion of the total decreased by half in both groups of countries: from 39% to 21% in exporters of manufactures and from 29% to 16% in exporters of natural resource-based goods or services. The point of inflection on the respective curves also shifted to a level of per capita income equivalent to half (from US$ 18,000 to US$ 9,000 in that period).

"Dutch disease" should thus be understood as an "excess of de-industrialization" owing to a change in the reference group. This occurred in the Netherlands, the United Kingdom and Norway, as well as Greece, Cyprus and Malta (tourism) and Switzerland, Luxembourg and Hong Kong (financial services). Lastly, none of these considerations give substance to the proposition that has been denominated the "curse of natural resources". In fact, a number of countries such as Finland, Malaysia and other Asian countries, all of which have a large endowment of natural resources, have been able to avert this phenomenon, either by carrying forward the industrialization process using the resources available or by developing a complementary manufacturing industry for the domestic market and for export. This shows that, although opportunities exist, there are apparently increasingly fewer countries prepared to take advantage of them.

One of the striking features of Latin America and the Caribbean is that whereas before the economic reforms the ratio of manufacturing to total employment was similar in most of the countries of the region, marked divergences emerged subsequently (see figure 2.5d). Brazil and the three Southern Cone countries (Argentina, Chile and Uruguay) exhibit the highest degree of de-industrialization following economic reform; they conform to the typical pattern of raw-materials exporters, of which Venezuela is a classic example. The second pattern corresponds to a number of Central American and Caribbean countries (El Salvador, Honduras and the Dominican Republic), in which manufacturing employment has increased considerably as a result of their active involvement in assembly activities. Lastly, in Mexico, Costa Rica and the other Andean countries (Bolivia, Colombia, Ecuador and Peru), economic reform did not significantly alter the share of manufacturing employment in the total, which implies that these countries have not been affected by either "Dutch disease" or the assembly activities which have had a heavy impact on other economies.

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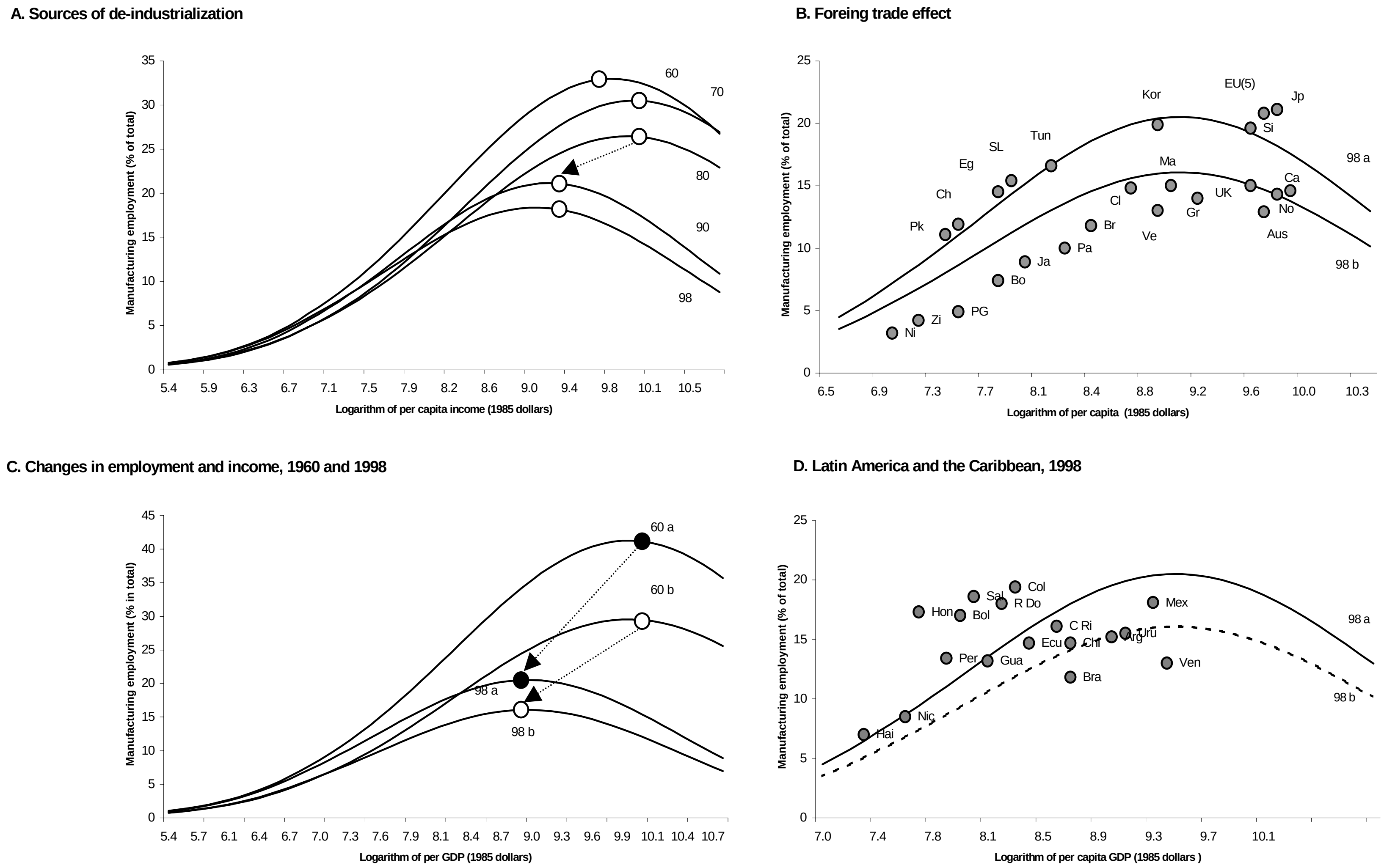
17 This is also true of the European Union, in which the productivity of the services sector has increased at less than half the rate of GDP growth (1.1% and 2.6%, respectively), since 1973.

18 "Dutch disease" usually refers to a sharp appreciation of the local currency as a result of the discovery of internationally tradable natural resources.

Figure 2.5
DE-INDUSTRIALISATION, FOREIGN TRADE, EMPLOYMENT AND INCOME



Source: Gabriel Palma, *Three Sources of 'De-industrialisation' and a New Concept of the Dutch Disease*, 2002.

4. Development of the institutional framework for international trade

Such was the scale of the new international institutional framework that grew up after the Second World War that it marked a turning point in trade and financial history. Economic transactions had obviously begun to expand and bring about changes in international relations in the nineteenth century, including the principle of "most favoured nation" in trade agreements —which was widely transgressed in the 1930s— and recourse to international arbitration to settle disputes between States. This was followed by the adoption of the gold standard by an increasing number of countries, although this reflected gradual adherence to a system headed by the leading international power of the time, rather than the implementation of principles of international cooperation. The process was restricted to weak forms of cooperation between the main central banks of the industrialized countries (Eichengreen, 1996, chap. 2). In the nineteenth century, a number of conventions were signed and specialized agencies established, including the World Health Organization and Pan American Health Organization, the Universal Postal Union and the Paris Convention on patents for inventions, but the most significant step in terms of international cooperation came later with the creation of the League of Nations in 1919. None of these processes, however, matched the scope of the international cooperation seen after the Second World War.

The period in which the international institutional framework developed most prolifically —the final years of the war and those immediately following— was characterized by a vision reflected, firstly, in the founding of the United Nations. In the economic domain, this led to the establishment of three key institutions: the International Monetary Fund (IMF), which was to restore multilateralism in current operations and provide financial support in times of crisis; the International Trade Organization, which was to oversee the development of multilateral trade principles; and the International Bank for Reconstruction and Development or World Bank, which was to facilitate the reconstruction of countries devastated by war. When the attempt to create the International Trade Organization failed, following the Havana Conference of 1948, the role it was intended to perform passed to the General Agreement on Tariffs and Trade (GATT), which had fewer members.

With respect to trade, there were two major counterweights to the strengthening of multilateralism. The first was the formation of regional blocs, within whose borders trade expanded rapidly. The European Economic Community was the most striking example, and a number of agreements were established on a smaller scale, including several in Latin America. The former Council for Mutual Economic Assistance (CMEA) also served to boost trade among the centrally planned economies.

The second counterweight to multilateralism was widespread recourse to protectionism in the developing world. This took the form not only of high tariffs, but also of quantitative restrictions, domestic content requirements for assembly industries and minimum export requirements for firms and industrial sectors with foreign exchange shortages. For newly independent countries, protectionism amounted to an expression of autonomy, as the colonial past was perceived as an era of economic failure that had to be overcome by means of deliberate action on the part of the State. By contrast, in Latin America the increasing use of interventionism and protection represented something that was perceived as a success. In fact, in the early stages of the import substitution period, between the two world wars, the region had achieved rapid economic growth, which facilitated a relatively easy transition from export-based development to "inward development" (see table 2.8).

Table 2.8
GDP GROWTH: WORLD AND LARGEST REGIONS, 1820-1998
(Weighted average annual growth rates)

	1820-1870	1870-1913	1913-1950	1950-1973	1973-1998
Western Europe	1.65	2.1	1.19	4.81	2.11
United States, Australia, New Zealand and Canada	4.33	3.92	2.81	4.03	2.98
Japan	0.41	2.44	2.21	9.29	2.97
Asia (not including Japan)	0.03	0.94	0.9	5.18	5.46
Latin America and the Caribbean	1.37	3.48	3.43	5.33	3.02
Eastern Europe and the former Soviet Union	1.52	2.37	1.84	4.84	-0.56
Africa	0.52	1.4	2.69	4.45	2.74
World	0.93	2.11	1.85	4.91	3.01

Source: ECLAC, calculations based on Angus Maddison, *The World Economy. A Millennial Perspective*, Paris, Organisation for Economic Co-operation and Development (OECD), 2001.

In addition, in the period between the two wars, development and industrialization were considered to be one and the same, and interventionism and State planning were standard practice worldwide, with few exceptions. In several cases, this represented an extension of the strict public control imposed during periods of conflict. Consequently, in the developing world the choice that was perceived were not between State planning and free markets, but rather between central planning and the weaker forms of planning typical of mixed economies.

There were also some notable exceptions to trade liberalization in the framework of GATT. In fact, the first six rounds of negotiations promoted the liberalization of intra-industrial trade in the developed economies, while the areas requiring internal adjustments on the part of the industrialized countries —including the agricultural and textile sectors— remained outside the multilateral trade rules. These rounds reduced levies on imports of non-agricultural products from developed countries to a low average level.[19] From the late 1960s on, and in parallel with the lowering of tariffs, the multilateral trade agenda focused on other public policies affecting competition between domestic and imported goods, such as administrative barriers, technical standards and contingent protection measures (safeguards) and trade protection (anti-dumping and subsidies), many of which came to be used for openly protectionist purposes. Voluntary export restraints, which became more widespread in the 1970s and 1980s, added to the use of protectionist instruments employed outside the GATT framework.

The Uruguay Round (1986-1994) was unquestionably the most comprehensive of all the rounds of multilateral trade negotiations. The countries agreed to lower the effective average level of industrial tariffs even further. In addition, the number of duty-free tariff lines was increased, virtually all the tariff structures were bound and stricter trade remedies were adopted. With respect to issues that had previously remained outside the GATT framework, commitments were established for the agricultural sector, not only to protect trade but also in relation to export and production subsidies; agreement was reached on the gradual dismantling of the Multifibre Arrangement; voluntary export restraints were prohibited; and it was agreed to eliminate trade-related investment measures (domestic content or export requirements), which were used liberally by many developing countries. In addition, the mandate of the World Trade Organization, the successor of GATT, included two new areas: liberalization of services and international rules on the protection of intellectual property. Moreover, a new dispute settlement mechanism was created.

[19] The Kennedy Round (1963-1967) was the first in which an agreement was reached on effective tariff reductions, covering nearly 35% of overall reductions for non-agricultural products, which represented 80% of dutiable trade (Winham, 1986).

More than seven years after the entry into force of the Marrakesh Agreement establishing the World Trade Organization, there is a broad consensus among the member countries that the proper functioning of WTO is important for the orderly conduct of international economic relations. WTO has fostered the settlement of trade disputes through mutually beneficial cooperation between countries and, as a result, has helped to create a framework of trade regulations that is more reliable and predictable than those of the past. The fact that developing countries have made increasing use of the WTO dispute settlement mechanism demonstrates the importance of the Organization's active role in upholding the system of standards as an arbiter in trade conflicts.

There is a serious imbalance, however, in the distribution of the benefits deriving from the Agreement. The developed countries have continued to gain the most from the liberalization of trade in goods and services.[20] First, these countries were able to reduce the costs of adjusting their agricultural and textile sectors, since they obtained generous transition periods to more open and competitive markets. In addition, they introduced varying degrees of flexibility into the regulations that impinged on their policies on agriculture and on certain industries. They extended the GATT rules, which originally referred only to products, to cover the rights of private agents (firms), and brought into the multilateral trading system those areas in which they enjoy a solid technological predominance, including the protection of intellectual property rights. Although there are no specific agreements on investment and the protection of competition, the industrialized countries obtained national treatment for transnational corporations through the commitments on investments, subsidies and trade in services. Furthermore, they achieved a firm legal basis for the liberalization of some sectors and modalities of service provision, such as financial services, basic telecommunications, electronic commerce and information technology products. By contrast, despite the commitments undertaken, those sectors that are of interest for the exports of developing countries have not only been slow to liberalize, but have often done so in conjunction with measures that undermine existing obligations. This has been exacerbated by new forms of protectionism, such as anti-dumping measures.

This asymmetry in the distribution of benefits and the slow progress made since the 1960s in terms of special and differential treatment prompted the developing countries to seek a new round of trade negotiations would focus on areas of particular interest to them (chapter 3 analyses this issue in greater depth). The commitment to develop measures to address this situation forms the basis of the Doha Declaration, which was adopted at the Fourth World Trade Organization Ministerial Conference (Qatar, November 2001), and lays out the work programme of WTO. This programme covers several areas of interest for the multilateral trading system.[21] A process of study and negotiation lasting until 2005 will be conducted to review, broaden or alter the rules established at the Uruguay Round.

II. International finance and the macroeconomic regime

1. Historic transformations in the international financial system

The expansion of international trade in the nineteenth and early twentieth centuries was accompanied by growth in international finance and the consolidation of the gold standard as a system of international payments and macroeconomic regulation. This expansion required the development of a system of financing instruments and payment instruments for commercial transactions (bills of exchange and suchlike), and an international network of branches of large

[20] See, among others, Finger and Schuknecht (1999), François, McDonald and Nordström (1996), Thomas and Whalley (1998) and UNCTAD/WTO (1996).

[21] This agreement was reached after the failure of the Third Ministerial Conference (Seattle, 1999). The work programme established is set forth in the "Ministerial Declaration" (WT/MIN(01)/DEC/1 of 14 November 2001). This text and other declarations and final decisions of the Fourth Conference are available for consultation on the WTO web site (www.wto.org).

European and United States banks grew up around this system. Long-term financing instruments developed at the same time, including both public debt bond issues and private financing instruments. One of the main types of private financing was the floating in financial centres of shares in infrastructure projects, especially railway and mining ventures. These modalities of private financing were conducted by newly created corporations that dealt in capital in an international financial centre, but operated beyond its borders. The first transnational corporations, especially in the natural resources sector, emerged a little later but developed rapidly, and by the early twentieth century were a well-established feature of the international scene.

The gold standard was consolidated by a process of voluntary adherence in the last three decades of the nineteenth century, on the basis of pre-existing monetary systems that were based on other metals. The key element of the expansion of the monetary base was the fiduciary money issued by central banks, which were generally fully or largely privately-owned and acquired monopolies over the issue of currency (sometimes after a period of unrestricted issues) in exchange for services rendered to the State. The system therefore consisted of convertible paper money backed only partially by gold reserves and, further away from the financial centres, by holdings of foreign currency; that is, the currency issued by these centres. The stability of the system relied on the maintenance of the currency's convertibility into gold. This was necessary to avoid a run on the central bank's reserves, which would obviously be insufficient. In addition, a banking system began to operate with minimum legal reserve requirements that provided only partial backing for deposits, and for notes in economies and periods in which free stipulation was permitted. This could pose the risk of a domestic financial crisis, in the event that problems experienced by one entity triggered loss of confidence in others, or even throughout the banking system. The systemic effects of such "contagion" led to the belated assignment of another function to the central banks: as lenders of last resort to commercial banks (Eichengreen, 1996).

In order to sustain confidence in convertibility, the "rules of the game" of the gold standard required a procyclical approach to macroeconomic policy in times of difficulty: in the event of a balance-of-payments shortfall, central banks were obliged to raise discount rates to generate contractionary pressures; if the misalignment persisted the outflow of gold eroded the monetary base, which had to be translated into a smaller volume of money and therefore lower demand; lastly, fiscal deficits were limited to the financing available and governments were therefore forced to pursue austerity policies in response to lower levels of financing and a likely decrease in tax receipts in periods of crisis. As indicated by Triffin (1968) and further substantiated by more recent studies (Aceña and Reis, 2000), this system operated in an asymmetric manner, to the detriment of countries on the periphery of the system, which were both exporters of raw materials, whose prices tended to fall in times of economic turmoil, and importers of capital, whose inflows behaved in a procyclical manner. The "rules of the game" thus generated strong pressures in these cases, which explain the frequent periods of inconvertibility seen in the peripheral countries, including several Latin American economies, during the crises of the late nineteenth and early twentieth centuries.

The European countries themselves abandoned the gold standard en masse during the First World War. It proved difficult to reinstate in the 1920s and was finally abandoned during the depression of the 1930s. The dual tensions generated between austerity policies and social pressure in the countries during difficult times, on the one hand, and between the central banks' responsibilities as monetary regulators and as lenders of last resort, on the other, finally spelled the end of this system in the developed countries.

The collapse of the gold standard was followed by an episode of genuine macroeconomic anarchy at the international level, marked by exchange-rate instability and, especially, by widespread and discriminatory exchange controls. This was exacerbated by the breakdown of international financing. The First World War had raised the profile of New York as a new international financial centre. The centre's expansion in the 1920s and subsequent collapse in 1929, in combination with widespread moratoria in the 1930s, caused long-term international financing to disappear almost completely. This was followed by the economic impact of the Second World War and, in particular, by sharp structural imbalances between the United States and Western Europe, which gave rise to a chronic "dollar shortage".

This was the context of the international cooperation efforts that began with the Bretton Woods agreements adopted in 1944. These efforts were channelled in two directions. First, notwithstanding the rejection of the ambitious proposals of Lord Keynes, a new international system of macroeconomic regulation was established. This was intended to surmount the problems of both the gold standard and the chaotic period following its demise. The new system was built on three pillars. The first was a system of fixed but adjustable parities with respect to an international standard (known as the gold-dollar, as the parity between the two was fixed). The second pillar was the provision of exceptional financing for countries that slipped into deficit in times of crisis, on the condition that they made commitments to economic adjustment, which could include exchange rate variations. This unprecedented combination of adjustment and international support was intended to prevent economic turmoil from spreading to the rest of the world through reduced demand for imports, excessive devaluation, increased protectionism and, in particular, the current payments restrictions that would likely ensue. The third pillar was a return to the principle of convertibility and non-discrimination in current payments, although no commitments were made on capital convertibility, and control of capital movements was accepted as legitimate international practice.[22] This element of the system released domestic policies, especially monetary policy, from the limitations that the free movement of capital could place on the pursuit of full employment. The resources used by IMF to fund its exceptional financing programmes came initially from the contributions of member countries, in addition to credit lines that were granted to some developed countries from 1962 on (General Arrangements to Borrow) and issues of a strictly international reserve currency, special drawing rights, in 1969; these issues have been repeated twice, the last time in 1981.

Secondly, the post-war financial reforms gave rise to new forms of long-term international financing. In response to the scarcity of private financing, official banking came to perform this role, through both the World Bank and later the regional development banks and domestic export-import banks. The Marshall Plan and, subsequently, official aid for developing countries acted as complementary means of long-term financing.

Although the official banks played a key role in financing for trade, private banks continued to perform this role even in the most fraught periods of the international payments system. The dollar surpluses generated by the United States' persistent external deficits in the 1960s —which succeeded the initial "dollar shortage" more quickly than expected— and by the petrodollars of the 1970s were recycled to provide the resources for a new phase of expansion in private international financing. The privileged position they had acquired afforded private banks a key role in this recycling process.

It is widely accepted that the dollar surplus also undermined the applicability of the Bretton Woods agreements. The dollar-gold parity was abandoned in 1971 and the major currencies were floated, which rendered the first pillar of the agreement obsolete and profoundly altered the third. The new principles were not the result of explicit international agreements, but a consequence of the facts, and they were certainly not established by means of broad negotiations like the Bretton Woods accords. The first pillar was replaced by a provision giving countries the autonomy to define their exchange regimes. The countries took very different approaches to managing the new risks posed by exchange-rate instability. The European Community attempted to reduce fluctuations

[22] Article VI of the IMF Articles of Agreement provides that: "Members may exercise such controls as are necessary to regulate international capital movements, but no member may exercise these controls in a manner which will restrict payments for current transactions".

among its members' currencies by affording priority to economic integration above all other objectives. This marked the beginning of a process which lasted a quarter of a century and culminated in monetary union among most of its members, the final stage of which was the replacement of national currencies with the euro on 1 January 2002. The developing countries espoused a number of strategies, often adopting one of the major currencies as a reference, or diversifying risks by linking their exchange rate to a currency basket.

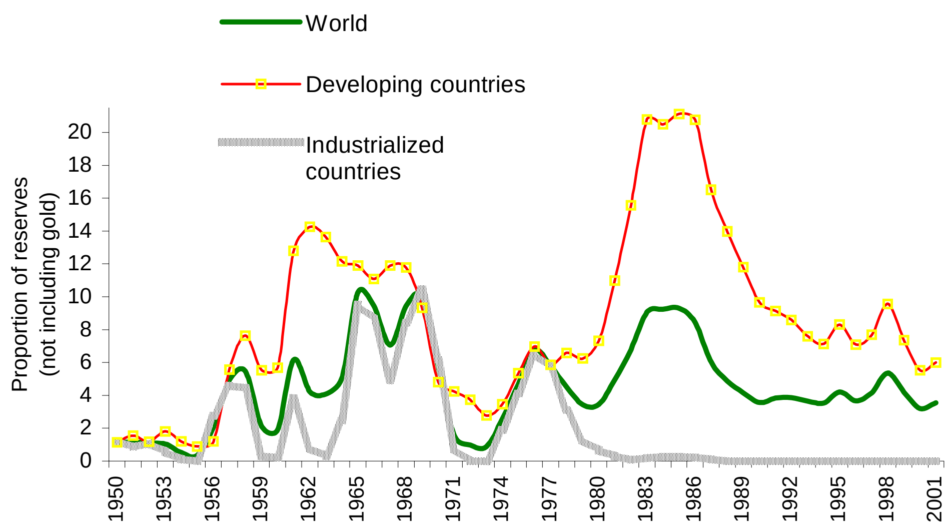
The floating of the major currencies represented a genuine "privatization of exchange risk", which generated a need for financial instruments to cover this risk and multiplied currency transactions. The ratio of currency transactions to the value of international trade increased sharply: from 2:1 in 1973 to 10:1 in 1980 and 70:1 in 1995 (Eatwell and Taylor, 2000). This, in combination with the strong expansion of international banking, profoundly altered the third pillar of the Bretton Woods accords. In practice, the liberalization of capital flows became the norm in the developed countries, which one by one eliminated controls of capital transfers in the 1970s and 1980s. A number of developing countries followed suit. The convertibility of the capital account was, in fact, meant to be enshrined at the 1997 annual meeting of IMF in Hong Kong. The explicit formulation of this principle was postponed, however, following a series of financial crises in a number of Asian countries, which have not yet come to an end. The principle of capital account convertibility has given way to the gradual liberalization of the capital account and of domestic financial sectors, in a process that has been conducted in a sequential manner, in conjunction with the development of a parallel institutional structure, in an attempt to ensure domestic financial stability. As will be discussed later, this has resulted in the emergence of new responsibilities for the Bretton Woods institutions.

The second pillar of the Bretton Woods agreement also saw substantial changes, for two reasons. First, IMF financing to developed countries, which has been very significant, was suspended at the end of the 1970s (see figure 2.6). The Fund's operations therefore came to target mainly developing countries and, increasingly, countries in which they were likely to have "systemic effects". Second, demand for resources grew, owing both to the structural nature of certain balance-of-payments problems which emerged during the crises caused by sharp hikes in petroleum prices and exacerbated during the debt crisis of the 1980s, and to capital account volatility in the 1990s. The need for larger volumes of funding for longer periods of time led to the establishment of new lines of IMF financing in the final two decades of the century. In 1979, the World Bank embarked on its structural adjustment programmes. These came to take precedence over the traditional lines of financing for projects financing which had previously been the focus of its credit strategy.

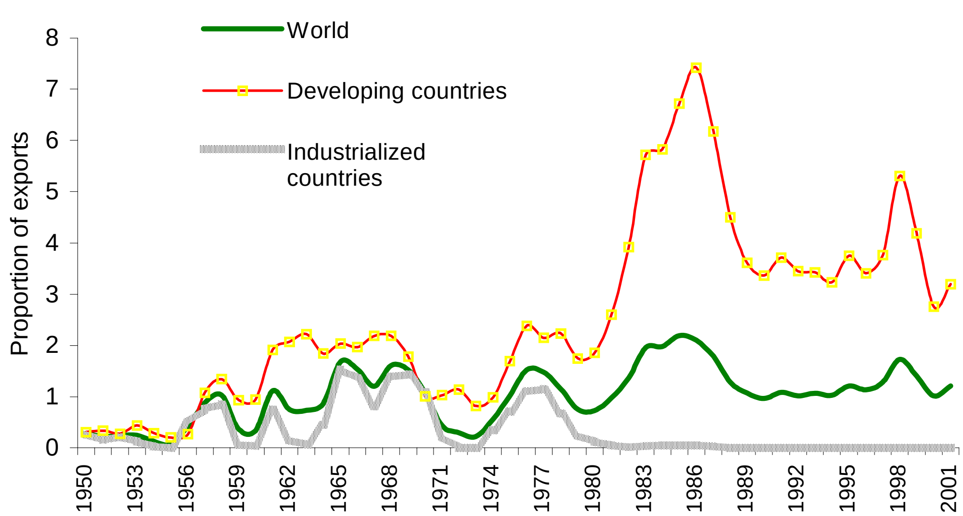
New conditionalities grew up around these changes and generated, in practice, a new function which was not contemplated in the Bretton Woods accords, and which was undertaken jointly by IMF and the World Bank from the 1980s on: the promotion of economic liberalization in the developing world, on the assumption that structural rigidities were caused by over-intervention on the part of the State. Like others before it, this new shift in the responsibilities of the Bretton Woods agencies did not arise from an explicit negotiation; clearly, it was a response to the ideological conditions and power relationships that were prevalent at the global level.

Figure 2.6
INTERNATIONAL MONETARY FUND: TOTAL CREDITS AND OUTSTANDING LOANS, 1950-2001

A. Proportion of international reserves



B. Proportion of exports



Source: International Monetary Fund (IMF), *International Financial Statistics*, Washington, D.C., CD-ROM version, December 2001.

It has been acknowledged since the 1970s that the growing internationalization of finances has generated a need for new regulatory standards. In response, in 1975 the Basel Committee on Banking Supervision was established under the auspices of the Bank for International Settlements. The most significant achievement of this initiative was the adoption in 1988 of the Basel principles on the regulation and supervision of banks. A number of reform proposals have been made since 1999, aimed at bringing the Basel principles into line with developments in the global banking industry and the shortcomings that were identified in the previous system.[23] In practice, the definition of minimum regulatory principles has extended to a much wider range of issues, including rules on debt issues in financial markets, the insurance industry and financial accounting. One of the elements of this reform, which has been broadly backed in recent years, is the creation of a programme to strengthen financial systems in developing countries, including the adoption of these international standards, and of principles for the management of external and public debt and international reserves. This new function of the Bretton Woods institutions has not been clearly differentiated from the responsibilities of other agencies, particularly the Bank for International Settlements.

2. Changes and recent episodes of volatility in financial markets

Developments in the macroeconomic environment have been accompanied by profound alterations in the financial systems of industrialized countries, which began in the 1980s and were consolidated in the 1990s.[24] This process may be summarized in terms of three basic trends. The first is the concentration of financial systems in the developed economies.[25] In the 1990s the world's main private financial institutions embarked on an intensive process of mergers and acquisitions, which became the hallmark of the decade, increasing in pace as the decade drew to a close.[26] Banking institutions therefore declined in number in almost all countries and banking concentration, calculated on the basis of the proportion of deposits controlled by the largest banks, tended to increase. In fact, this trend would be even more marked if operations off the balance sheet could be calculated.

Second, there has been a widespread trend towards banking disintermediation and an "institutionalization of savings", which is associated with the emergence of non-bank financial intermediaries, such as mutual and pension funds, investment banks and insurance companies (see table 2.9). Competition from these agents has chipped away at the predominance in international financial intermediation enjoyed by the banks in the 1960s and 1970s. It has also obliged traditional banking institutions to become conglomerates offering an ever broader range of financial services. As a result, the distinction between bank and non-bank roles has become increasingly blurred.

The activities of non-bank intermediaries were deregulated in the 1980s and this, in combination with the elimination of capital controls in developed countries, allowed these institutions to claim a growing stake in the international financial markets and a role in their expansion. This translated into considerable growth of secondary markets for debt instruments. In common with stock markets, the secondary debt markets appreciated in value thanks to the increased participation of institutional investors and of a large number of individual financial agents. This generated a virtuous circle which helped to generate new sources of financing for a relatively long period, until the trend was broken by the outbreak of international turmoil in 2000.

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[23] Criticism has been levelled at the procyclical effects of regulation, which the new proposals tend to accentuate, and their adverse effects on risk markets, including emerging countries. See Reisen (2001a) and Griffith-Jones and Spratt (2001).

[24] See, among others, Franklin (1993), Feeney (1994), Bloomstein (1995), Culpeper (1995), D'Arista and Griffith-Jones (2001) and Group of Ten (2001) for a more detailed account of the changes in the financial systems of the main industrialized economies.

[25] Group of Ten (2001) contains a comprehensive analysis of the causes and consequences of this process.

[26] Most of these mergers and acquisitions —70% in fact— correspond to banking institutions. In addition, joint ventures and strategic alliances between institutions increased significantly.

Table 2.9
FINANCIAL HOLDINGS BY INSTITUTIONAL INVESTORS a/
SELECTED OECD COUNTRIES
(*Percentage of GDP*)

	1992	1994	1996	1999	2000
Australia	61.6	65.9	92.4	127.9	131.2
Canada	68.6	80.2	92.1	112.7	111.3
France	61.9	71.8	86.6	125.4	133.3
Germany	34	41.3	50.6	76.8	79.7
Hungary	2.5	3.9	6.1	10.7	12.8
Iceland	55.3	66.7	79.6	111.3	110.1
Italy	21.8	32.2	39	96.9	
Japan	78	81.6	89.3	100.5	
Republic of Korea	51.8	53.7	57.3	88.5	72.6
Luxembourg	1,574.3	1,945.6	2,057	4,172.3	
Netherlands	131.5	144.5	167.6	212.8	209.6
Spain	21.9	32.3	44.3	65.4	62.1
United Kingdom	131.3	143.8	173.4	226.7	
United States	127.2	135.9	162.9	207.3	195.2

Source: Organisation for Economic Co-operation and Development (OECD), *Institutional Investors Statistical Yearbook, 2001*, Paris, 2001.

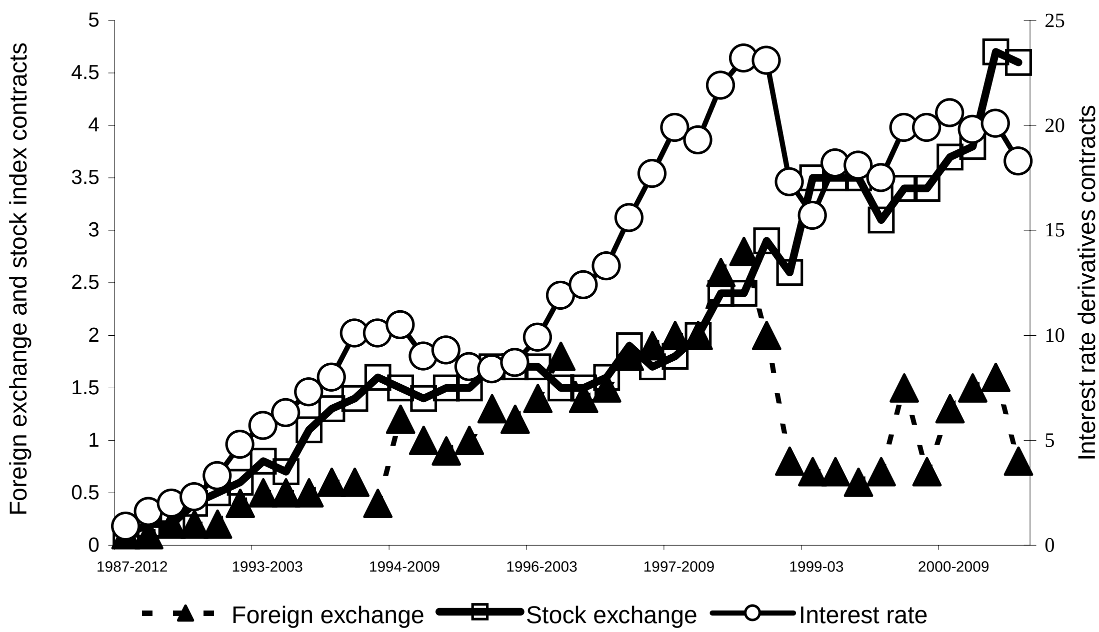
a/ Insurance companies, investment firms, pension funds and other forms of institutional saving. Netherlands 2000: insurance companies include life insurance only.

The expansion of secondary markets also aided financial deepening in developed countries (Fornari and Levy, 1999) and facilitated the emergence of new sources of corporate financing. One result of this was that the volume of bond issues in developed country markets, headed by the United States and Japan, more than doubled in the 1990s and also extended to a number of Latin American countries. The depth and liquidity of this well-developed secondary market, particularly in the United States, helped to finance the new high-technology sectors which led the economic expansion of the 1990s. Another recent innovation, the creation of risk capital funds, contributed to the growth of these activities, but this branch of activity appears to have come to an abrupt halt in the latest episode of economic turmoil.

Another result of the development of these markets is that the role of credit rating agencies has broadened considerably, as they provide information to investors and are consulted increasingly for regulatory purposes. A number of institutional investors, for example, will now accept nothing below an investiment-grade rating, and the Basel Committee recently put forward a proposal to use agency ratings in the regulation of the banking sector. There has been widespread criticism of the procyclical behaviour of agency ratings, in particular its impact on financing for developing countries (Reisen, 2001a and 2001b).

Lastly, the rapid growth of financial holdings by institutional investors effectively swelled demand for tools of risk diversification. Hence the development of specialized markets for particular instruments, such as the securitization of assets (including mortgage-backed assets), “junk bonds”, bonds issued by emerging economies and the securitization of assets based on shares in foreign firms, such as ADRs and GDRs. This phenomenon, in combination with the privatization of exchange risk, explains the demand for financial derivatives, which serve to hedge risk (see figure 2.7). The Asian crisis has severely affected the volume of exchange risk hedging contracts being concluded, however.

Figure 2.7
FINANCIAL DERIVATIVES TRADED ON ORGANIZED MARKETS
(*Millions of contracts*)



Source: Bank for International Settlements (BIS).

These trends have had both positive and negative effects on the industrialized economies. On the positive side, financing opportunities for production enterprises have expanded considerably, with both high-technology and medium-sized firms reaping the benefits. On the negative side, however, these trends have heightened financial fragility which, moreover, does not fall within the sphere of governance of the regulatory mechanisms of traditional banking activities. In fact, the activities that entail the highest risks and the greatest degrees of leverage —those associated with the derivatives market— remain outside the existing regulatory frameworks and there are as yet no proposals to extend regulatory standards to this domain. The regulations fall significantly short even with respect to institutional investors (D'Arista and Griffith-Jones, 2001).

There is, of course, nothing new in the volatile nature of financial markets, as economic history amply demonstrates (Kindleberger, Manias, Panics and Crashes) —even in recent times (BIS, 2001). This volatility was clearly reflected in the marked frequency of financial crises in both industrialized and developing countries in the last quarter of the twentieth century (IMF, 1998). Given that the majority of transactions on financial markets are conducted on an intertemporal basis, the lack of accurate information about the future constitutes the essential "market failure" to which its volatility may be attributed (Keynes, 1945; Eatwell and Taylor, 2000). Markets are thus vulnerable to changes of opinion and expectations that shift continually between optimism and pessimism as investors' "appetite for risk" varies. The impact of this is magnified by the effects of "contagion" of opinion and expectations from one market to another. These externalities constitute another basic market failure, since they can give rise to multiple equilibria and "self-fulfilling prophecies" when the expectations of a majority of agents point in the same direction.

Information asymmetries between debtors and creditors (Stiglitz, 1994) represent another market failure, as these translate into a bias in favour of debtors considered to be low-risk, and render markets strongly inclined to rely on the flawed information held by creditors on their debtors, especially the highest-risk ones. Given that this market confidence also behaves in a procyclical manner, the spreads on the market's highest-risk loans are procyclical too, which generates alternate periods of "appetite" for high-risk activities and "flight to quality assets". This also accounts for the fact that secondary markets display much greater liquidity in times of abundance, as they too depend on the market's confidence in the information available to buyers. For this same reason, derivatives markets also tend to behave in a procyclical manner, with those operations that are considered to entail excessive risk even coming to a complete standstill in times of crisis.

Contemporary financial markets have a number of features that have tended to exacerbate their volatility.[27] These are: (i) inadequate regulation of the activities of both the banking sector and institutional investors and agents in the derivatives market, in addition to the procyclical bias of the existing regulations;[28] (ii) problems of contagion which arise when institutional investors face liquidity constraints in several markets simultaneously: when the price of a particular instrument falls, they are obliged to sell other types of holdings —even instruments that bear no relation to the original— in order to restore their own liquidity; this creates even more pressure when funds are withdrawn from a market that generally operates on the basis of spot transactions, or when these investors are under an obligation to meet certain commitments, including counterpart requirements on derivatives transactions, and, obviously, the larger the stake of high-leverage institutions in the market, the greater the pressure; (iii) the tendency for several agents to employ the same risk assessment systems, which heightens the correlation between the financial behaviour of —sometimes unlike— instruments and exacerbates the effects of contagion; (iv) the tendency to evaluate the performance of institutional investors over short periods of time, which has a similar effect; and (v) the procyclical behaviour of credit-rating agencies.

Figure 2.8 shows the correlation between two risk markets during the episode of turbulence that began with the crisis of 1997: the bond market in emerging economies and high-risk bonds in the United States. In both markets spreads first decreased, then entered a period of violent turbulence, in response first to the Asian and later to the Russian episodes; the Russian crisis had a much stronger impact and the spreads failed to recover a completely normal trend afterwards. Throughout this phase, the fluctuations were much sharper in emerging bond markets. By contrast, in the more recent crisis, which spread out from a United States epicentre, exactly the opposite occurred. In the period as a whole, there is a strong, positive correlation between the two markets.[29] The changing nature of contagion is illustrated in figure 2.8b, which shows the increase in spreads in the main Latin American economies during the five most recent crisis periods. All the countries exhibited a similar upward trend at these times, but the impact was much more powerful during the Asian and especially the Russian crises than during episodes centred in Latin American countries. This suggests that crises in developed countries have a much larger impact, especially when they affect agents with a high degree of leverage, some of which have withdrawn from emerging markets in recent years.

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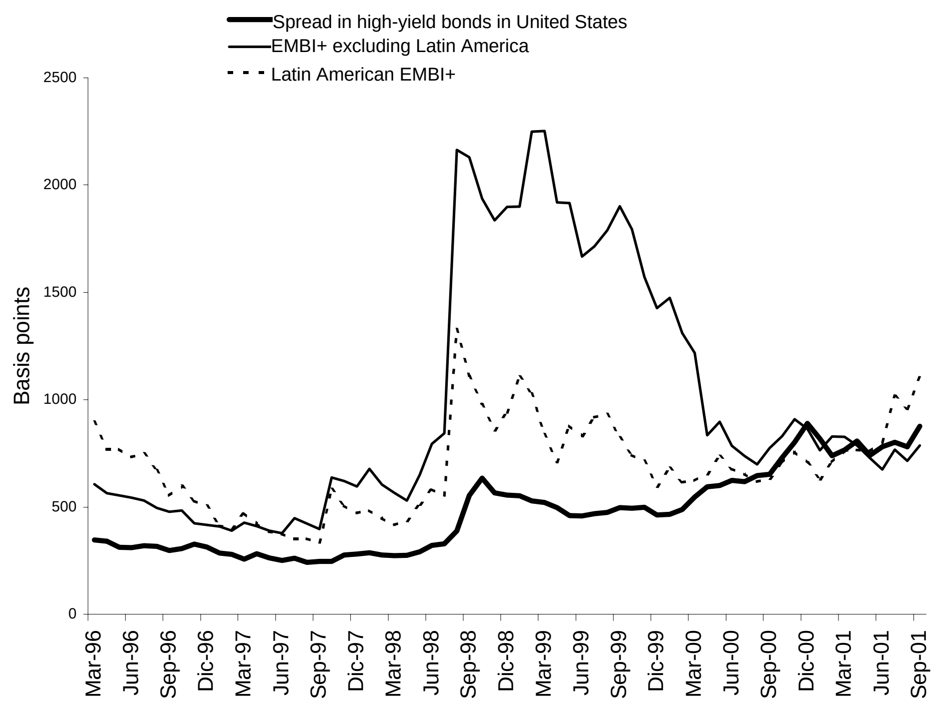
[27] An extensive range of literature has been produced on this subject. Among many other contributions, see Calvo and others (2001), Dodd (2001) and Persaud (2000).

[28] In the case of banking regulation, the rules on capital and loan loss reserves have this effect. In boom periods, increased earnings enable credit expansion, which is further facilitated by the fact that debtors tend to meet their commitments in a timely fashion, which enables reserves to be reduced. During bust periods, however, non-compliance with obligations increases, which means that the reserve position reduces banks' profits and therefore their credit capacity. A number of proposals have been put forward to mitigate this procyclical phenomenon (Ocampo, 1999a and 2002b).

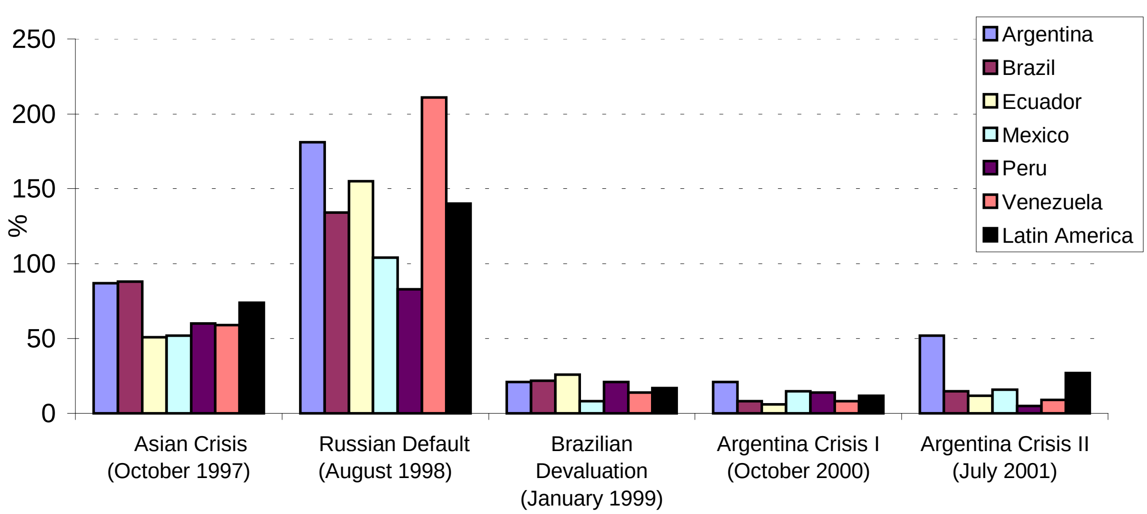
[29] The correlation of monthly spreads of Latin American instruments and high-risk instruments in the United States market was 0.56 in the period from March 1996 to September 2001, but rose to 0.79 between September 1997 and November 1999.

Figure 2.8
SPREADS IN EMERGING MARKETS

A. Merril Lynch High-Yield Master Index and J.P. Morgan EMBI+



B. Increase in bonds spreads (percentages)



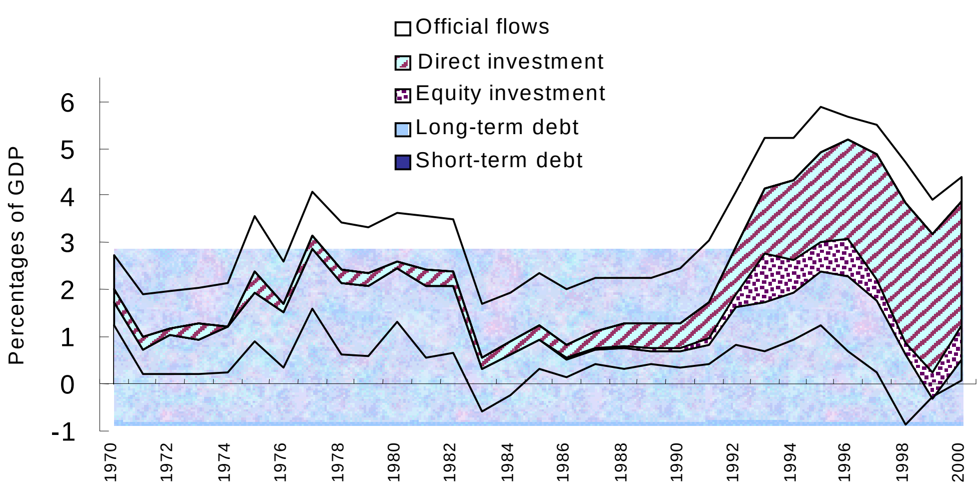
Source: ECLAC, on the basis of data from Merril Lynch and J.P. Morgan Chase.

State interventions to correct these market failures are always flawed and can easily translate into "government failures". Regulation is, a priori, the most important line of action, since it focuses on measures to prevent agents from undertaking undue risk in the first place. The development of regulation tends to lag behind the evolution of markets, however, and can itself generate mechanisms of evasion and avoidance which translate into weaker risk supervision (transactions conducted off the balance sheet, for example) or even suboptimal mechanisms of intermediation. Oversight is also essentially preventive, but is hindered by problems related to the flow of information, and its discretionary nature can lead to abuses. Interventions in response to systemic crises offer incentives to agents who are willing to take on undue risk, which can lead to problems of moral hazard. Lastly, interventions intended to compensate for a market bias towards more risk-oriented investors can create problems similar to moral hazard, including the affording of guarantees to high-risk debtors. Resolution of the problem by means of official financing can generate dependence on the State ("graduation" problems) and can even oblige private creditors to undertake higher risks, owing to the "preferred creditor" status of the official agency. For this reason, it is possible to compensate only partially for volatility and risk discrimination and this can only be achieved by means of an appropriate combination of instruments.

3. Capital flows to developing countries

Over the past three decades, developments in international markets, as described in the preceding section, have been reflected by fundamental changes in capital flows to developing countries.[30] The first notable change is the contrast between the slow growth of official financing flows and the increase in private flows, which are also highly volatile. As shown in figure 2.9, official financing tended to decline as a proportion of developing-country GDP, especially in the 1990s. This is primarily due to the slow growth of its main component: bilateral assistance funds, which declined in real terms over most of the decade. As a proportion of developed-country GDP, bilateral assistance fell from 0.35% in the mid-1990s to an average of 0.22% in the period 1998-2000. The decrease in bilateral assistance has been most pronounced in the case of the largest

Figure 2.9
NET FLOWS TO DEVELOPING COUNTRIES



Source: ECLAC, on the basis of World Bank, *Global Development Finance*, 2001, Washington, D.C., CD-ROM version, 2001.

[30] See UNCTAD (1999a), chapters III and V, and World Bank (1999a), which provide a detailed analysis of these trends.

developed countries, though it has been offset in part by the rising proportion of grants in comparison to concessional credits. Moreover, unlike private flows, official financing has not been pro-cyclical and, indeed, some components of it, particularly balance-of-payments support and multilateral development finance, have displayed countercyclical behaviour.

Private external financing has fluctuated widely owing to the effects of its most volatile components: short-term flows and long-term financing (which, in the figure, includes portfolio flows). During the most critical years, including both the debt crisis of the 1980s and the period after 1997, short-term flows were occasionally negative. Together, these two sources of funding increased from 1.0% of developing-country GDP for the period 1971-1974 to 2.3% for 1977-1982, fell to 0.5% for 1983-1990, peaked at 2.8% for 1993-1997 and dropped again to 0.7% for 1998-2000. A recovery began in 2000, but was interrupted in 2001. Foreign direct investment has remained largely independent of this cycle and has tended instead to follow long-term trends: an increase in the 1980s and a significant upsurge in the 1990s. While it was not affected by the series of crises that began in 1997, it was affected by the 2001 crisis.

This cycle reflects only part of the instability that has characterized private financial markets. Since the time of the Asian crisis, turbulence in these markets has taken various forms over shorter amounts of time: periodic interruptions, of variable duration, in market access, simultaneous increases in risk spreads and shorter maturities (see, in this regard, the preceding section and chapter 5).[31] In any event, it must be borne in mind that these short-term phenomena are compounded by the effects of contagion, which manifest themselves over the medium term and affect access to financing for relatively long periods. In both cases, the essential characteristic of contagion is that it tends to have similar effects on countries with either sound or unsound economic foundations, but which the market classifies in the same risk category. A striking example of this is Colombia's limited access to private banks during the debt crisis, despite its low levels of indebtedness. This is inconsistent with a risk assessment scale in which the variables are access to financing, the terms on which financing is provided or both.

The changes in the composition of financing over the past three decades are detailed in table 2.10. The upsurge in the financing received by Latin America and the Caribbean in the 1970s and its subsequent contraction, which affected only that region, were based primarily on bank financing, both long- and short-term. The type of bank financing that was characteristic of the 1970s (long-term syndicated credits) was not duplicated in the 1990s, when short-term financing took on much greater importance. Undoubtedly, the Basel standards played a major role, since they resulted in a preference for the granting of short-term, low-risk credits. In the 1990s, the Asia-Pacific region was the epicentre of the boom in short-term bank credit and of its subsequent contraction, which was much more severe and widespread in the developing world than the Latin American and Caribbean debt crisis. Reflecting the trend towards banking disintermediation and institutionalization of savings, the upturn in the period 1990-1997 was particularly evident in the bond market and in portfolio equity flows. Their performance during the financing crunch of 1998-1999 varied widely from one region to another, in relation to the averages for 1990-1997: the bond market became negative in Asia-Pacific but rose in Latin America and the Caribbean and in Central Europe, while the opposite occurred in the case of portfolio equity flows. Foreign direct investment has tended to increase in all regions, even during slumps in financial markets.

31 See the International Monetary Fund's periodic reports on emerging markets and ECLAC (2001b, chap. 1), which contain detailed analyses of these trends.

Table 2.10
NET RESOURCE FLOWS: 1973-1999
(*Annual averages; billions of dollars*)

	Developing countries	East Asia and the Pacific	Europe and Central Asia	Latin America and the Caribbean	Middle East and North Africa	South Asia	Sub-Saharan Africa
1973-1981							
Total	**71.3**	**11.1**	**5.3**	**31.8**	**10.4**	**4.1**	**8.6**
Official flows	21.8	3.2	1.3	3.3	5.9	3.5	4.5
Direct investment	5.6	1.1	0.1	3.9	-0.4	0.1	0.8
Equity investment	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt flows	44.0	6.8	4.0	24.6	4.8	0.5	3.3
Bonds	1.2	0.2	0.0	1.0	0.1	0.0	0.0
Commercial banks	21.7	2.9	2.2	14.1	1.0	0.2	1.3
Short-term	16.5	2.8	1.5	8.6	2.3	0.3	1.1
Other	4.5	0.9	0.3	0.8	1.5	0.0	0.9
1982-1989							
Total	**81.0**	**17.6**	**8.8**	**15.0**	**14.1**	**10.1**	**15.3**
Official flows	38.3	5.9	1.4	6.8	6.9	6.1	11.0
Direct investment	13.0	4.5	0.2	5.4	1.4	0.3	1.2
Equity investment	0.8	0.5	0.0	0.1	0.0	0.1	0.0
Debt flows	29.0	6.7	7.1	2.7	5.7	3.7	3.1
Bonds	2.3	1.3	1.1	-0.6	0.2	0.3	0.0
Comercial banks	12.6	2.5	2.3	4.5	1.4	1.9	0.0
Short-term	6.8	1.9	2.5	-2.7	2.4	1.0	1.6
Other	7.3	0.9	1.2	1.5	1.8	0.5	1.5
1990-1997							
Total	**252.0**	**100.5**	**33.3**	**74.4**	**10.7**	**11.5**	**21.5**
Official flows	49.7	9.9	10.5	4.2	4.8	5.8	14.5
Direct investment	84.3	39.1	9.9	27.1	2.8	2.0	3.5
Equity investment	28.4	11.0	2.4	11.0	0.5	2.3	1.2
Debt flows	89.6	40.5	10.5	32.3	2.5	1.4	2.3
Bonds	30.0	12.2	4.0	12.4	0.3	0.6	0.6
Commercial banks	18.2	6.8	1.5	9.6	0.0	0.9	-0.7
Short-term	35.8	18.3	1.9	11.4	2.3	-0.3	2.2
Other	5.5	3.1	3.2	-1.1	-0.1	0.3	0.2
1998-1999							
Total	**264.8**	**49.8**	**60.0**	**118.4**	**7.5**	**2.4**	**19.8**
Official flows	49.8	14.9	8.2	8.8	1.9	5.0	10.9
Direct investment	181.1	59.7	25.8	81.2	4.0	3.3	7.1
Equity investment	25.0	15.1	3.2	2.8	0.8	0.8	2.3
Debt flows	8.9	-39.9	22.7	25.6	0.9	-6.8	-0.6
Bonds	12.7	-18.2	12.1	18.9	1.1	0.0	-1.1
Commercial banks	33.2	1.5	10.6	18.7	0.8	1.5	0.2
Short-term	-34.7	-24.1	1.1	-11.1	-1.0	-0.5	0.9
Other	-2.2	0.9	-1.0	-0.8	-0.1	-7.7	-0.5

Source: World Bank, *Global Development Finance, 2001*, Washington, D.C., CD-ROM version.

The upsurge in private financing in the 1990s occurred in response not only to changes in financial intermediation, but also to interest rate policy in the United States. Low rates exerted a decisive influence by steering institutional investors towards emerging-economy markets (Calvo and others, 1993; D'Arista and Griffith-Jones, 2001), while risk spreads were reduced in response to the larger supply of resources, strengthening the effects of low rates with regard to financing terms. It may be observed that interest rates in the United States and risk spreads in emerging markets developed in a diametrically opposed manner in the period of turbulence that began in 1997, demonstrating that varying perceptions of risk in emerging markets have predominated in the determination of those spreads and of capital flows (see box 2.2). What is more, United States interest rates, in more than a few cases, have responded endogenously to varying perceptions of risk, either because the "flight to quality assets" has raised public debt bond prices, thereby reducing their returns, or because the authorities have responded to market uncertainty by lowering interest rates.

Box 2.2

INTEREST RATES AND EMERGING MARKET BOND SPREADS

One of the key external variables that influence emerging market interest rate spreads are changes in United States interest rates (Calvo and others, 1993; Fernández-Arias, 1996; IMF, 2001a; and Calvo and others, 2001). Conceptually, a rise in United States interest rates is expected to lead, all else equal, to an increase in debt service payments for emerging market borrowers, increasing the likelihood of default and the corresponding risk premium incorporated into bond spreads. Higher United States interest rates could also reduce investors' appetite for risk, reducing their exposure in risky markets and the availability of financial resources in borrowing countries as a result (Kamin and Kleist (1999)). Similarly, a fall in United States interest rates is expected to lead to a decrease in emerging market spreads through its impact on the ability of debtor countries to repay loans. Lower United States interest rates would also be associated with lower emerging market spreads because investors, seeking to enhance the overall return on their portfolios, would switch to emerging market debt whenever yields in mature markets fall.

Evidence for the early 1990s indicates that, prior to the Mexican financial crisis of December 1994, spreads in emerging markets and United States interest rates moved together, confirming these theoretical presumptions. However, in the second half of the 1990s, the behaviour of emerging market bond spreads, new debt issuance and maturity would suggest that other factors were more predominant in the determination of spreads and capital flows than changes in U.S. interest rates.

The empirical evidence of the second half of the 1990s reveals that changes in emerging market bond spreads and United States interest rates moved in opposite directions. From March 1996 to September 2001 there was a significant negative correlation of -0.6 between the 10-year United States Treasury bond yield and the Emerging Markets Bond Index Plus (EMBI+) and the Latin EMBI+ spreads; the correlation between emerging market bond spreads and the United States federal funds target rate over the same period was also negative, albeit less strong (-0.3 for the EMBI+ and -0.4 for its Latin component).

The novel feature of this period is the strength of financial contagion, which led to a widespread increase in emerging market bond spreads during the episodes of market turbulence in the second half of the 1990s, particularly the Asian and Russian crises. Movements in United States corporate high-yield bond spreads were also strongly and positively associated with movements in emerging markets bond spreads.

Moreover, debt flows to Latin America responded more to movements in spreads than to United States interest rates during the period under analysis. Other things being equal, increases in United States interest rates are expected to be associated with capital outflows from emerging markets and declines in United States interest rates, with capital inflows. However, when periods of easing and tightening of United States monetary policy are isolated, the correlation between debt flows to Latin America and United States interest rates does not show the expected negative sign. These flows, including debt securities issued abroad and Brady bonds, showed a positive correlation of 0.6 with the 10-year United States Treasury bond yields. The correlation was particularly strong in the period of the Asian, Russian and Brazilian crises.

In the 1990s, private flows were concentrated in middle-income countries (see table 2.11). Conversely, the share of low-income countries in private financing has been lower than their share in the total population of developing countries, as might be expected, but also lower than their contribution to the developing countries' GDP. This fact is particularly striking in bond financing, commercial banking and portfolio flows, if India is excluded in the latter case. In all these cases, private financing directed to poor countries is minimal. The share of low-income countries in FDI is also smaller than their contribution to the developing countries' GDP. For these reasons, the volatility of capital flows and issues of contagion have become particularly relevant to middle-income developing countries.

Accordingly, low-income countries have continued to depend on dwindling official sources of funds. These countries rely heavily on official development assistance, particularly grants, coming mostly in the form of bilateral aid. This is the only component of net resource flows to developing countries, again with the exception of India, that is distributed in a progressive manner. Multilateral financing has followed the same pattern, except in the case of IMF resources.

The volatility of private financial flows and their considerable concentration in middle-income countries have created large-scale needs for exceptional financing, which have been concentrated in a few emerging economies. As a result, IMF financing has exhibited strong countercyclical behaviour and has been concentrated in a small number of countries; this could have systemic effects. However, it should be stressed that exceptional financing has been lower than it was in the 1980s in relation both to the value of the recipient countries' international reserves and to the value of their exports, and, with respect to the former, also lower than it was in the 1960s (see figure 2.6). This is a clear sign that the level of IMF exceptional financing has tended to lag behind the level of international economic transactions. Obviously, the comparison is still less favourable if the capital account shocks faced by the developing countries are taken as a benchmark, even though, in the view of the Chairman of the United States Federal Reserve Board, "the size of the breakdowns and required official finance to counter them is of a different order of magnitude than in the past" (Greenspan, 1998).

As shown in figure 2.10, the countercyclical behaviour of financing and its concentration in a few countries are closely related. The proportion of IMF financing directed to large borrowers[32] has displayed a strong upward trend over the past two decades. Indeed, IMF financing data underestimate the provision of emergency funds to large borrowers, as they do not include bilateral contributions to the largest bailouts of recent years (Indonesia, the Republic of Korea, Thailand, the Russian Federation, Brazil, Mexico and the "financial armour" provided to Argentina in 2000).[33] These programmes have been severely criticized in developed countries as creating "moral hazard", and this has translated into a less favourable attitude towards exceptional financing. On the other hand, processes aimed specifically at external debt renegotiation have been supported, despite the lack of appropriate international institutions to address this problem.

[32] This group consists of Argentina, Brazil, China, India, Indonesia, Mexico, the Republic of Korea and the Russian Federation.
[33] However, pledged bilateral financing tends to be disbursed in smaller proportions than the multilateral shares in bailout packages.

Table 2.11
NET RESOURCE FLOWS, 1990-1999
(*Annual averages; billions of dollars and percentages*)

	Direct investment		**Equity investment**		**Grants**		**Bilateral financing**		**Multilateral financing (excluding IMF)**		**Bonds**	
	Amount	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**
Developing countries	**103.7**	**100.0**	**27.7**	**100.0**	**29.8**	**100.0**	**4.1**	**100.0**	**15.8**	**100.0**	**30.6**	**100.0**
Excluding China	75.4	72.7	24.8	89.4	29.5	99.0	2.6	62.4	13.9	88.0	29.4	96.0
Low-income countries	*10.2*	9.8	*3.9*	14.0	*15.2*	51.0	*2.5*	59.9	*6.7*	42.4	*1.7*	5.6
India	1.5	1.4	1.7	6.0	0.5	1.8	0.0	0.3	1.1	7.2	0.7	2.2
Other countries	8.7	8.4	2.2	8.0	14.7	49.2	2.5	59.6	5.6	35.2	1.0	3.4
China a/	*28.3*	27.3	*2.9*	10.6	*0.3*	1.0	*1.6*	37.6	*1.9*	12.0	*1.2*	4.0
Middle-income countries	*65.2*	62.8	*20.7*	74.6	*14.3*	48.0	*0.1*	2.5	*7.2*	45.6	*27.7*	90.4
Argentina	6.6	6.4	1.1	4.1	0.0	0.1	-0.2	-5.6	1.1	6.9	4.9	15.9
Brazil	10.9	10.5	2.8	10.1	0.1	0.2	-0.8	-20.4	0.6	4.0	2.6	8.5
Mexico	8.2	7.9	3.8	13.5	0.0	0.1	-0.4	-9.7	0.5	3.3	4.2	13.7
Indonesia	2.1	2.0	1.6	5.9	0.3	0.9	1.3	32.1	0.6	3.8	0.9	2.8
Repúblic of Korea b/	2.6	2.5	3.7	13.5	0.0	0.0	0.4	9.2	0.8	5.1	4.9	15.9
Russian Federation	1.8	1.7	0.8	2.7	0.8	2.7	1.1	27.0	0.7	4.3	1.6	5.4
Other countries	33.1	31.9	6.9	24.8	13.1	44.0	-1.2	-30.1	2.9	18.1	8.6	28.2
	Commercial bank credits		**Other credits**		**Long-term flows**		**Short-term debt flows**		**Total net flows**		**Memo**	
											GDP	**Population**
	Amount	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**
Developing countries	**17.1**	**100.0**	**4.0**	**100.0**	**232.8**	**100.0**	**22.5**	**100.0**	**255.4**	**100.0**	**100.0**	**100.0**
Excluding China	16.6	97.1	1.1	26.6	193.2	83.0	21.7	96.2	214.9	84.2	88.2	74.8
Low-income countries	*0.8*	4.5	*0.4*	9.1	*41.3*	17.7	0.7	2.9	42.0	16.4	*17.0*	*46.7*
India	0.5	2.9	0.1	2.0	6.1	2.6	-0.4	-1.7	5.7	2.2	6.3	19.4
Other countries	0.3	1.6	0.3	7.1	35.2	15.1	15.1	67.1	50.3	19.7	10.8	27.3
China a/	*0.5*	2.9	*2.9*	73.4	*39.6*	17.0	0.9	3.8	40.5	15.8	*11.8*	*25.2*
Middle-income countries	*15.9*	92.5	*0.7*	17.6	*151.7*	65.1	21.0	93.3	172.7	67.6	*71.1*	*28.1*
Argentina	0.6	3.7	-0.1	-1.3	14.1	6.0	3.4	15.1	17.5	6.8	*4.5*	*0.7*
Brazil	5.2	30.2	-0.4	-9.3	20.9	9.0	1.0	4.5	21.9	8.6	*11.0*	*3.3*
Mexico	2.6	15.0	-0.3	-6.5	18.6	8.0	0.3	1.2	18.9	7.4	*6.7*	*1.9*
Indonesia	0.2	1.0	-0.1	-1.3	6.9	3.0	0.9	4.0	7.8	3.0	*2.9*	*4.1*
Repúblic of Korea b/	-0.9	-5.5	-0.1	-3.6	11.3	4.9	5.9	26.4	17.2	6.8	*7.0*	*0.9*
Russian Federation	0.2	1.1	2.0	51.1	9.0	3.9	-0.8	-3.4	8.2	3.2	*7.6*	*3.1*
Other countries	8.1	47.1	-0.5	-11.6	70.9	30.5	10.2	45.4	81.1	31.8	31.4	14.0

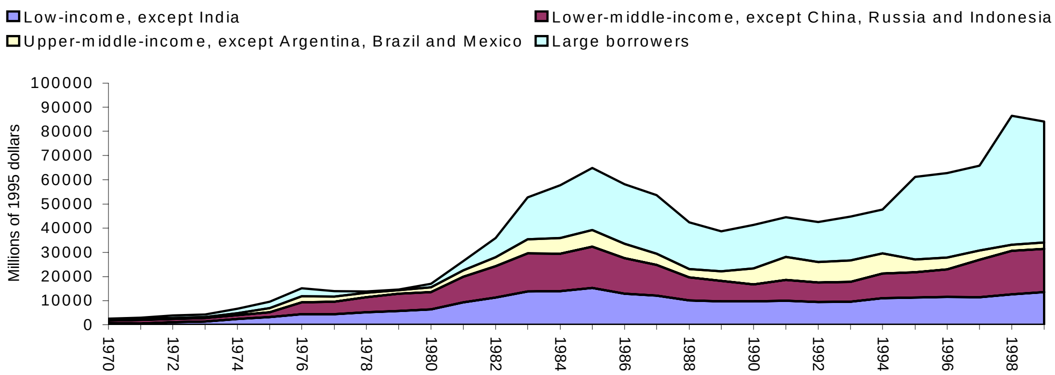
Source: World Bank, *Global Development Finance, 2001*, Washington, D.C., CD-ROM version and *World Development Indicators 2001*, Washington, D.C., CD-ROM version (for GDP and population data).

a/ The World Bank considers China a middle-income country; in this table, it is presented in a separate category.

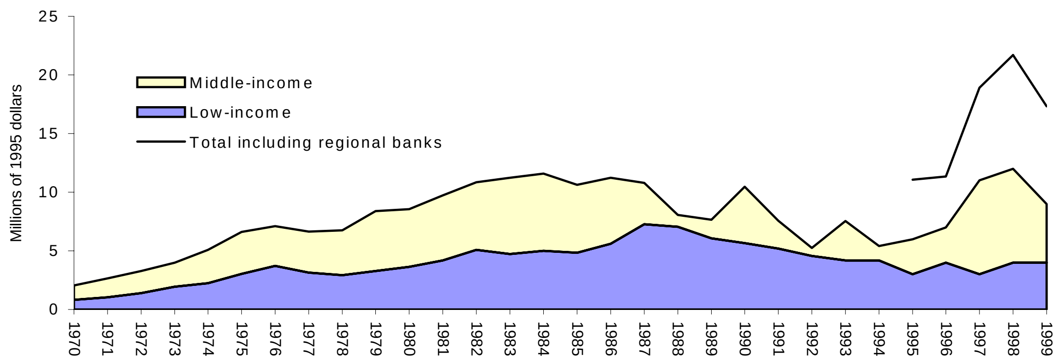
b/ The World Bank considers the Republic of Korea a high-income country; however, Global Development Finance 2001 includes it in the middleincome group.

Figure 2.10
CREDITS OF INTERNATIONAL FINANCIAL INSTITUTIONS

A. International Monetary Fund credits



B. Development bank credits



Source: ECLAC, on the basis of International Monetary Fund (IMF), *International Financial Statistics, 2001,* Washington, D.C., CD-ROM version, December 2001 and World Bank, *Global Development Finance, 2001,* Washington, D.C., CD-ROM version, 2001.

As shown in figure 2.10, World Bank financing and development-bank financing in general for middle-income countries has displayed a similar countercyclical pattern. Such financing complements that of IMF, since it provides governments with long-term resources. In view of the volatility of private financing, these resources are usually the primary, and sometimes the only, source of long-term financing available in times of crisis.

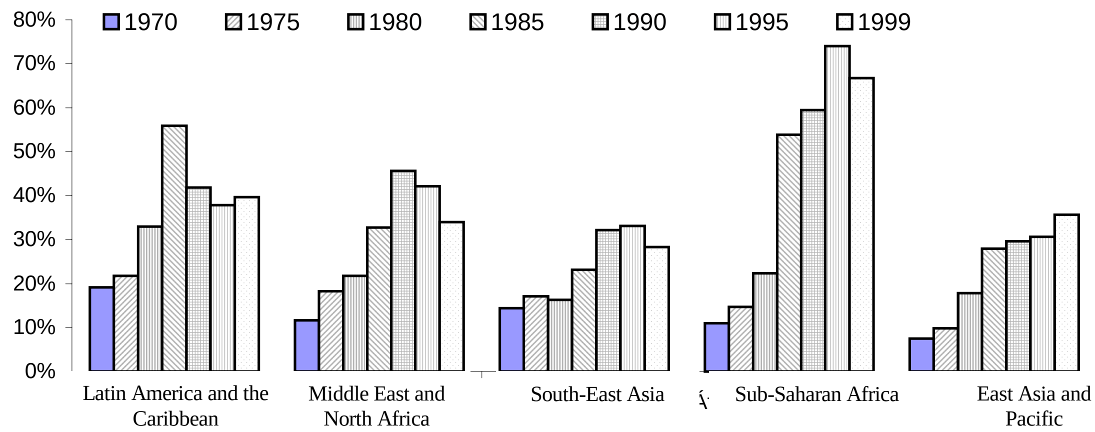
The tendency to direct loans to middle-income countries has not completely crowded out low-income countries. Indeed, the flow of IMF resources to the latter has been fairly stable, and has even increased when they have required additional balance-of-payments support. This occurred in Latin America and the Caribbean in the 1980s and in Asia-Pacific during the Asian crisis. The flow of World Bank resources to low-income countries has followed an upward trend in recent decades.

Overall external indebtedness trends among developing countries have not been positive, although the patterns vary considerably from one region to another. Compared to their levels in 1980, prior to the Latin American debt crisis, the external debt/GDP ratios for all parts of the developing world have risen, but those for certain developing regions (including Latin America and the Caribbean) have fallen in relation to the critical levels reached in the mid- or late 1980s (see figure 2.11.a). In contrast, external debt/exports ratios have developed more favourably (see figure

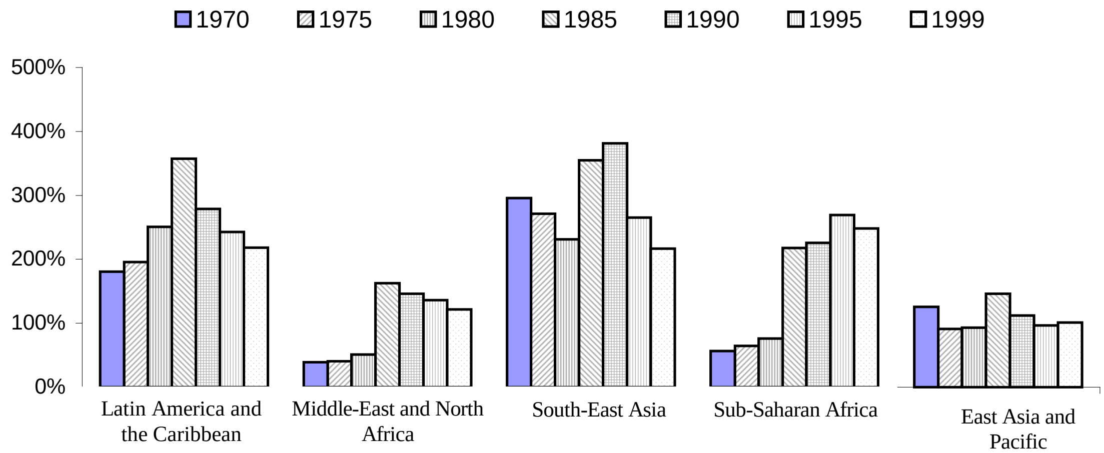
2.11.b). The problem appears more serious when the debt ratios of certain countries are compared to benchmarks indicating what are deemed to be manageable levels. On the basis of World Bank data on 84 developing countries for which information is available for the period 1980-2000, it can be determined that the number of countries with external debt/GDP ratios of less than 40% has fallen from 45 to 23 and that the number with external debt/exports ratios of less than 200% has fallen from 56 to 33.

Figure 2.11
EXTERNAL DEBT

A. Percentage of GDP



B. Percentage of exports



Source: World Bank, *Global Development Finance, 2001*, Washington, D.C., CD-ROM version, 2001.

Nonetheless, the risk of a sudden change in interest rates, such as the one that occurred in the early 1980s, has decreased as a result of the control of inflation in developed countries. In any event, it should be recalled that real interest rates in those countries remained high in the last two decades of the twentieth century (though they declined during the recent crisis) and, particularly, that the margins applicable to developing countries in private capital markets are usually very high. In terms of the traditional criteria of sustainability of debt ratios, calculated by comparing economic growth to real interest rates, the ratio continues to be unfavourable in most countries.

Lastly, the banking system's tendency towards concentration at the international level has spread to developing countries. This process reflects both the expansion of large international banks and the strategy adopted by smaller ones to deal with international competition, as in the case of Spanish banks in Latin America. However, the degree to which banking is concentrated in the hands of foreigners varies widely from one region to another and from one country to another within the same region. Central Europe and Latin America show much higher levels of concentration than the countries of Asia-Pacific (52%, 25% and 6%, respectively, of total bank assets in 1999). The share of foreign banks ranges from a maximum of between 42% and 54% in Argentina, Chile and Venezuela to a minimum of around 18% in Brazil, Mexico and Colombia. This process has been encouraged by the regulatory authorities of developed countries as a means of reducing the banks' exchange rate risks (Hawkins, 2001). The annex on financial services to the WTO General Agreement on Trade in Services constitutes an international institutional framework that provides legal guarantees for this process.

The combination of financial liberalization, penetration by foreign banks and new private-sector external linkage arrangements has given rise to a profound restructuring of the developing countries' financial systems. In many ways, national financial sectors are now more diversified in terms of services, but some of their traditional shortcomings persist. The bias towards short-term operations and high intermediation margins is still the norm, as is credit rationing, especially for small and medium-sized enterprises and low-income families. While local stock markets have expanded in some countries, primary share issues have not increased, as large firms have preferred to issue them in international financial centres. Lastly, despite the major changes introduced in the area of banking regulation and supervision, the stability of local markets has shown no significant improvement, as witnessed by the numerous and recurrent crises they have suffered.

III. International migration

In the first phase of globalization, from the last quarter of the nineteenth century to the early twentieth century, the expansion of trade and high capital mobility were accompanied by an increase in migratory flows, with the result that this period is also known as the "era of mass migration" (Castles and Miller, 1993; Hatton and Williamson, 1998). This wave of migration was directed towards a number of countries in the New World (the United States, Canada, Argentina, Brazil and Australia). Between 1870 and 1920, the United States, which was the chief recipient of these migrants, took in more than 26 million people, primarily from Europe, who came to represent more than 10% of the country's total population (Solimano, 2001).

Some of these migratory flows helped to create an interregional and intraregional economic convergence (European emigration to the New World and to other European countries, respectively), while others accentuated the inequality of the international economic order, as in the case of the Chinese coolies and the Indians transported to tropical plantations. From the outset, two disparate trends prompted by these migratory flows began to emerge: the trend towards the homogenization of wages at high levels in the developed world and the trend towards the convergence of low wages in the developing world.

During that period, the countries of the New World adopted liberal immigration policies, and, in a number of cases, governments used various means to encourage foreigners to take up residence, in response to the need to increase the labour force and to populate their territories at a time of strong economic expansion. Only in the early twentieth century did they begin to apply somewhat more restrictive policies, accompanied, in some countries (Australia, Canada and the United States), by measures that discriminated against Asian immigrants, especially those from China.

The phenomenon of migration gathered new momentum after more than half a century, as part of the third phase of globalization in the last quarter of the twentieth century. In that period, migration to nearly all the countries of the Organization for Economic Cooperation and Development (OECD) increased in comparison to previous decades, although its magnitude was much less than that of late nineteenth-century migration.[34] In some recipient countries, this process reached its peak in the early 1990s (United States, Germany, Japan and Canada), while in others (United Kingdom and Australia) it had reached this point some years earlier. Since that time, largely as a result of the widespread imposition of legal limits on immigration, migratory flows have declined significantly (see table 2.12).

Major changes can also be observed with respect to the regions and countries of origin of immigrants (see table 2.13). Immigration to the United States in the third phase of globalization has consisted primarily of Latin Americans and Caribbeans (46%) and Asians (34%), in sharp contrast to the trend of the nineteenth century, when nearly 90% of the immigrants to the United States came from Europe (Solimano, 2001). In the European Union, internal migration predominates, representing two thirds of the total (66.2%); other major regions of origin are Africa (16.2%) and Asia (10.6%) (Salt, 1999). Almost three fourths of Japan's immigrants come from Asia (53.3%), Latin America and the Caribbean (10.2%) and the United States (8.8%).[35]

Table 2.12

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT: THE 10 MAIN COUNTRIES OF DESTINATION OF IMMIGRANTS

(Thousands of persons)

Recipient country	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Average
United States a/	1 537	1 827	974	904	804	721	916	798	661	647	979
Germany b/	842	921	1 208	987	774	788	708	615	60	674	812
Japan b/	224	258	267	235	238	210	225	275	26	282	265
United Kingdom a/	…	…	204	190	194	206	216	237	258	277	223
Canada a/	214	231	253	256	224	213	226	216	174	190	220
Italy a/	…	…	…	…	…	…	…	…	111	268	190
France a/	102	11	117	99	92	77	76	102	138	104	102
Australia a/	121	122	107	76	70	87	99	86	77	84	93
Switzerland b/	101	110	112	104	92	88	74	73	75	86	92
Netherlands b/	81	84	83	88	68	67	77	77	82	78	79

Source: Organisation for Economic Co-operation and Development (OECD), *Trends in International Migration. 2000 Edition*, Paris, 2000 and Continuous Reporting System on Migration (SOPEMI), *Annual Report, 2001*, Paris, 2001.

a/ Data based on residence permits or other sources.

b/ Data based on population records.

34 In the case of the United States, the chief recipient country, immigration rose to nearly 7.5 million people in the last two decades of the twentieth century, compared to about 2.5 million in the 1950s and one million in the 1940s. However, as a proportion of the country's population, immigrants represented less than 3% in the last third of the twentieth century, which was much lower than the percentages recorded between 1870 and 1920 (over 10%).

35 Salt, 1999, CDMG (99) 29E), 1999 and OECD, 2001a.

Table 2.13
ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT: NATIONS OF ORIGIN OF IMMIGRANTS TO THE MAIN RECIPIENT COUNTRIES, 1999
(Percentages)

Recipient	Primary countries of origin					
	First	Second	Third	Fourth	Fifth	Cumulative
United States	Mexico (19.9)	China (5.6)	India (5.5)	Philippines (5.2)	Dominican Rep. (3.1)	39.3
Germany	Yugoslavia (13.1)	Poland (10.7)	Turkey (7.0)	Italy (5.2)	Russia (4.1)	40.1
Japan	China (21.0)	Philippines (20.3)	Brazil (9.3)	United States (8.8)	Korea (8.2)	67.6
United Kingdom	United States (16.2)	Australia (12.1)	South Africa (8.7)	India (7.1)	New Zealand (5.7)	49.8
Canada	China (20.2)	India (9.2)	Pakistan (4.9)	Philippines (0.8)	Korea (3.8)	42.9
Italy	Albania (13.9)	Morocco (9.3)	Yugoslavia (9.1)	Romania (7.8)	China (4.1)	44.2
France	Morocco (13.5)	Algeria (10.9)	Turkey (5.5)	Tunisia (3.8)	United States (2.6)	36.3
Australia	New Zealand (22.2)	China (11.4)	United Kingdom (10.5)	South Africa (5.9)	India (3.1)	53.1
Switzerland	Yugoslavia (14.7)	Germany (12.8)	France (7.2)	Italy (7.0)	Portugal (5.8)	47.5
Netherlands	United Kingdom (6.4)	Germany (5.7)	Morocco (5.6)	Turkey (5.4)	United States (4.2)	27.3

Source: Organisation for Economic Co-operation and Development (OECD), *Trends in International Migration. 2000 Edition*, Paris, 2000 and Continuous Reporting System on Migration (SOPEMI), *Annual Report, 2001*, Statistical Annex, Paris, 2001.

The composition of these flows reflects the influence of factors such as distance, language, historical relations and cultural affinity on the decision to emigrate. More than half of Japan's immigrants come from China, the Republic of Korea and the Philippines, whereas nearly a quarter of the immigrants to the United States come from Mexico, the Dominican Republic and Canada. The countries of origin of migrants to the United Kingdom and France reflect strong historical and cultural ties.

These ongoing migratory movements have taken place in the context of significant changes in legislation, which, in general, have been much more restrictive than in the past and have been aimed at improving the control of illegal immigration. In the United States, such legislation has been changed several times since the 1960s. The 1965 reform of the Immigration and Naturalization Act established a system of preferences based on family relationships with United States citizens, encouraged the immigration of individuals with the skills and training in greatest demand in the labour market, set quotas by country of origin and introduced measures to eliminate ethnic discrimination. Further legislative changes were introduced in 1986 with the aim of controlling illegal immigration through increased vigilance at the country's borders and programmes to regularize the status of undocumented immigrants. Another reform was introduced in 1996 with a view to strengthening the control of illegal immigration.

Since the early 1990s, the immigration policies of the European countries have been set by the European Union. The main feature of this legislation is the clear distinction laid down in the

Treaty of Rome between immigrants of Community origin and those of non-Community origin. While the former enjoy fully the right to reside and work in any country of the Union, the latter are subject to strict limitations and are required to obtain a working visa before they can become residents. Australia, Canada and Japan have also adopted restrictive immigration policies in recent years, particularly with respect to the granting of permanent residence permits. To counterbalance this situation, special programmes have been implemented to facilitate temporary residence, usually through the issuance of work permits in specific areas, either to lend greater flexibility to the labour market or to address labour shortages in certain sectors (OECD, 2001a).

Thus, even though it has coincided with an increased tendency to reduce obstacles to capital mobility, the free movement of persons is limited to specific regions within the OECD countries and to the most highly skilled workers. However, the individuals most likely to emigrate are relatively low-skilled workers wishing to move from South to North. In addition, since the disappearance of the socialist world, a strong trend towards emigration, primarily to European Union countries, has been observed in the countries of Central and Eastern Europe and in those of the former Soviet Union. Consequently, tighter control over irregular migration and the employment of undocumented workers, along with limitations on the right to asylum on political and humanitarian grounds, have become the major issues to be addressed in the developed countries' immigration policies (OECD, 2001a).

In the 1990s, this relationship between the propensity to migrate and restrictions on the free movement of labour resulted in a considerable increase in irregular migration to OECD countries, which, by its very nature, is impossible to measure with complete accuracy. The persistence of irregular migration has prompted nearly all the OECD countries to tighten controls on the income, residence and employment of foreigners. At the same time, various programmes have been adopted to regularize the status of undocumented residents.

International migration has profound effects on the basic structures of the sending and receiving countries. It is widely acknowledged that inequalities in levels of development are the primary determinant of migration. Accordingly, if globalization results in the accentuation of these inequalities, the propensity to migrate will persist and could even increase. At the same time, the growing interdependence among nations has heightened the transnationalization of communities and has led to the diversification of mobility arrangements. Another factor that encourages migration is the wider dissemination of cultural models, patterns of behaviour and aspirations, since this makes potential migrants more aware of existing global inequalities in levels of development. Moreover, advances in communications and transport have reduced the direct costs of migration.

In contrast to past trends, migration today is not related to the occupation of unpopulated areas. Because it is directed primarily from South to North, the challenge of incorporating immigrants is faced by highly structured societies whose economic, social and demographic conditions differ considerably from those of the immigrants' countries of origin. The integration of immigrants into the recipient societies and the definition of their rights and demands for citizenship have become a major political issue. Institutional responses to this problem have varied, combining both humanitarian and restrictive attitudes, with the latter based on the defence of sovereignty. In the countries of origin, ties with emigrants have become especially important, since they represent not only a source of funds, but also the potential for change and innovation. These ties represent the reverse side of integration and, as shown by the emergence of immigrant communities and their social networks, one of the seeds of transnationalization.

It may be that the growing demand for foreign workers with specific skills, as reflected in the immigration policies of developed countries, is helping to perpetuate and widen the gaps that separate the industrialized countries from the developing world. While the developed countries' importation of human capital has serious consequences for the countries of origin (brain drain), the gradual formation of a global market in highly skilled human resources could mitigate those effects by promoting the circulation and exchange of human resources and the transfer of scientific and technological know-how.

Organizations of immigrants in the main recipient countries, such as those which have emerged in the United States, provide frames of reference for strengthening collective identity, and facilitate the globalization of immigrants' cultural expressions and the spread of their products in the recipient societies. Such organizations help immigrants to maintain close ties with their places of origin; one of the most important of these ties is the sending of remittances. The use and origin of remittances, the channels through which they are mobilized and their real and potential effects on the development of the recipient communities have been only partially assessed, and few policies have thus far been introduced in this area.

Although the debate on migration, its causes and its consequences has awakened greater interest today than ever before, the controversial nature of these issues makes it difficult to adopt global agreements and specific courses of action on the subject. In recent years, it has become clear that international migration must be understood as a phenomenon requiring the adoption of multilateral measures based on cooperation among States. It is also clear that governments and civil-society organizations in countries of origin, destination and transit share a concern for the human rights of migrants, in relation both to the decision to emigrate or stay in the country of origin and to the possibility of exercising citizenship in the countries of origin and destination. These convictions have been strengthened by the need to join forces to combat a crime which has grown to very serious proportions: trafficking in immigrants, which is a source of illicit profit for organizations that operate on an international scale.

Chapter 3

Inequalities and asymmetries in the global order

Globalization has not only engendered growing interdependence; it has also given rise to marked international inequalities. Expressed in terms of a metaphor widely employed in recent debates, the world economy is essentially an "uneven playing field,"[1] whose distinctive characteristics are a concentration of capital and technology generation in developed countries and the strong influence of those countries on trade in goods and services. These asymmetries in the global order are at the root of profound international inequalities in income distribution.

This chapter analyses those inequalities and asymmetries, whose accurate characterization is essential in order to alleviate and, eventually, overcome the problems they cause. The first section provides empirical evidence of the inequalities existing in global income distribution over recent centuries. The second examines the asymmetries that exist between developed and developing countries and the different ways in which they have been approached in the international debate since the Second World War.

1 In contrast to a "level playing field," or one in which all the parties compete under equal conditions.

I. Inequalities in global income distribution

1. Long-term disparities between regions and countries

The widening income gap between different regions and countries has been a feature of the world economy for the past two centuries. Indeed, whereas per capita GDP in the more developed regions of the world was around three times that of the less developed regions in the early nineteenth century, this ratio has grown steadily, and currently stands at just under 20:1 (see table 3.1). The only exception to this trend is found in the period 1950-1973, in which the differential decreased slightly (Madisson, 1995 and 2001).[2]

Table 3.1
PATTERNS OF INTERREGIONAL DISPARITIES

	1820	1870	1913	1950	1973	1990	1998
A. Per capita GDP, by region							
Western Europe	1,232	1,974	3,473	4,594	11,534	15,988	17,921
United States, Australia, New Zealand and Canada	1,201	2,431	5,257	9,288	16,172	22,356	26,146
Japan	669	737	1,387	1,926	11,439	18,789	20,413
Asia (excluding Japan)	575	543	640	635	1,231	2,117	2,936
Latin America and the Caribbean	665	698	1,511	2,554	4,531	5,055	5,795
Eastern Europe and former Soviet Union	667	917	1,501	2,601	5,729	6,445	4,354
Africa	418	444	585	852	1,365	1,385	1,368
World	667	867	1,510	2,114	4,104	5,154	5,709
B. Interregional disparities (percentages)							
Less-developed region/more-developed region	33.9	18.3	11.1	6.8	7.6	6.2	5.2
Latin America/more-developed region	54.0	28.7	28.7	27.5	28.0	22.6	22.2
Latin America/world	99.7	80.5	100.1	120.8	110.4	98.1	101.5
Latin America/less-developed region	159.1	157.2	258.3	402.2	368.1	365.0	423.6
C. Regional share of world production (percentages)							
Western Europe	23.6	33.6	33.5	26.3	25.7	22.3	20.6
Western offshoots	1.9	10.2	21.7	30.6	25.3	24.6	25.1
Japan	3.0	2.3	2.6	3.0	7.7	8.6	7.7
Asia (excluding Japan)	56.2	36.0	21.9	15.5	16.4	23.3	29.5
Latin America	2.0	2.5	4.5	7.9	8.7	8.3	8.7
Eastern Europe and former Soviet Union	8.8	11.7	13.1	13.0	12.9	9.8	5.3
Africa	4.5	3.6	2.7	3.6	3.3	3.2	3.1
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: ECLAC estimates based on data from Maddison (2001).

[2] See also Bairoch (1981). However, this author's estimates of per capita income differentials in the late eighteenth century and early nineteenth century are substantially lower than Maddison's.

Major interregional disparities in per capita GDP were already evident prior to the First World War, but they intensified rapidly between then and the mid-twentieth century,[3] and they havecontinued to increase ever since, though at a slower rate. This, as we will see, is a pattern that has been repeated by other indicators of inequality in global income distribution. The relatively slower increase in inequality after the Second World War coincided with the acceleration of economic growth in the developing world, which was one of the distinguishing characteristics of the second phase of the globalization process.

It should be recalled, however, that this acceleration was initially characterized by highly protectionist policies, which did not give way until much later —the trend began in the 1960s but did not really take hold until the 1980s and 1990s— to greater openness and participation in global trade (see chapter 2).

Latin America and the Caribbean have exhibited a number of distinctive features within this process. First, this was one of the first regions in the developing world to join in the trend towards globalization.[4] Ever since the initial phases of this process, the Latin American and Caribbean region, together with Central and Eastern Europe, has formed part of the group of middle-income countries, which has expanded to include several Asian countries in recent decades. Although no precise data are available on the subject, the gap in per capita output between this group and the most developed region of the world widened between 1820 and 1870, but then stabilized. In fact, the disparity between the per capita GDP of Latin America and the Caribbean and that of the most developed region in the world remained stable, hovering in the 27%-29% range, for a little more than a century and only began to decrease in 1973, dropping to 23% in 1990 and to 22% by the end of the twentieth century (see table 3.1.b). In terms of mean global GDP, the disparity increased from 1870 to 1950 and then began to decrease —slowly until 1973 and more rapidly from 1973 to 1990.

The region's relatively good performance during the early phase of globalization (1870-1913) in comparison with other developing countries was followed by similar successes during the first stages of "inward-looking development", which took place at a time when the globalization process was stalled at the international level. During the second phase of globalization (1945-1973), the Latin American and Caribbean region experienced the highest rates of per capita GDP growth in its history, although the pace of that growth was slightly slower than the global rate.[5] Thus, the most notable characteristic of the period between 1870 and 1973 was the region's inability to make steady progress in approaching developed-country levels. Within this general pattern, some countries experienced periods of rapid growth,[6] followed by periods of much slower growth or even declines. Over this long period, the situation of Latin America and the Caribbean could be described more as one of stabilization in an intermediate position within the world context, with individual cases of "truncated convergence", rather than divergence from the developed countries, although this did occur in some instances.

In reality, the region began to fall behind only during the third phase of globalization (which began in 1973), as it failed to achieve a sufficient degree of integration into the financial globalization process and was then overtaken by the ensuing debt crisis. Moreover, the recovery period following the "lost decade" of the 1980s proved to be a halting one. As ECLAC has shown in various studies, this has been reflected in the fairly disappointing growth rates attained by

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3 Because of Asia's relative weight in the world population, one of the basic reasons for these trends was the economic stagnation of that region (except for Japan and a handful of other countries) until the middle of the twentieth century, which was followed by rapid economic growth in that region after the Second World War.

4 Bulmer-Thomas (1994), Thorp (1998), Cárdenas Ocampo and Thorp (2000a, 2000b) and Hofman (2000) present a more detailed analysis of the region's performance since the mid-twentieth century.

5 If the figures are adjusted for the effects of the demographic transition, both the acceleration of the region's growth rate in 1950-1973 and its later deceleration appear to have been even more pronounced.

6 Among the most noteworthy are the periods of rapid growth registered in three Southern Cone countries in the late nineteenth and early twentieth centuries, in Cuba during the first quarter of the twentieth century and in Venezuela, Brazil and Mexico during several decades of the twentieth century.

theregion in the wake of its major economic reform effort, which began in the 1970s in some countries and spread throughout the region between the mid-1980s and the early 1990s.[7]

Variations in per capita GDP and differences in population dynamics between the different regions of the world have led to significant skewing of the distribution of world production (see table 3.1). In the nineteenth century, the most notable event was the emergence of Western Europe and the "Western offshoots" —as Maddison calls them— in the Americas and Oceania (United States, Canada, Australia and New Zealand), at the expense of Asia. This process led to an overwhelming concentration of the world's production of manufactured goods in the main bastions of capitalism. The trend reversed after the Second World War, but more than half of world output is still concentrated in the developed countries (now including Japan), especially in technology-intensive manufacturing and service sectors. Within this global context, Latin America and the Caribbean steadily increased their share of world production up to 1973, but this trend levelled off thereafter.

Table 3.2 shows the differences in per capita GDP among countries worldwide. As is the case with interregional disparities, the most noteworthy characteristic is the pronounced and sustained increase in inequalities across countries. This process also accelerated until 1950 and then slowed, especially during the second phase of globalization.

Table 3.2
INDICES OF PER CAPITA INCOME INEQUALITY IN THE WORLD

	1870	1913	1950	1973	1990	1998
A. Deviation index a/						
OECD industrialized countries	0.43	0.45	0.50	0.24	0.22	0.22
34 countries		0.72				
48 countries		0.70	0.87			
141 countries			0.96	1.07	1.13	1.22
Developing countries			0.85	0.93	0.94	1.04
Latin America and the Caribbean			0.51	0.56	0.60	0.70
B. Mean logarithmic deviation b/						
OECD industrialized countries	0.08	0.09	0.11	0.03	0.02	0.02
34 countries	0.16	0.23				
48 countries		0.24	0.33			
141 countries			0.54	0.56	0.58	0.65
Developing countries			0.53	0.50	0.42	0.51
Latin America and the Caribbean			0.14	0.14	0.16	0.21

Source: ECLAC estimates based on data from Maddison (2001).

a/ Standard deviation of the logarithm of GDP per capita.
b/ Average of the logarithms of the mean ratio of per capita GDP/per capita GDP of each country.

The only apparent case of convergence in levels of per capita output occurred among developed countries during this second phase, which was their "golden age" (see table 3.2). This phenomenon has been the subject of several detailed studies (see, among others, Maddison, 1991). The process proceeded steadily until 1990, albeit at a slower pace, but then came to a halt in the final decade of the twentieth century. The other historical period in which convergence was clearly occurring was the first phase of globalization or, more precisely, the second half of the nineteenth century. O'Rourke and Williamson (1999) have demonstrated that during this period the United

[7] See, in particular, ECLAC (1996a and 2001), Stallings and Peres (2000) and Escaith and Morley (2001).

States and Europe witnessed a convergence of wage levels, basically as a result of the mass migration of European labour to the New World. Within Western Europe, a process of wage equalization also occurred between several of what were then peripheral countries (especially the Scandinavian countries, Austria and, to a lesser extent, Italy and Ireland) and the most highly developed countries (Germany, France, the Netherlands and the United Kingdom). However, the same authors also note that the process did not encompass other countries of the European periphery (the Mediterranean countries, with the exception of Italy, and those of Central and Eastern Europe) or other regions of the world. Hence, even within the group of countries that today make up the Organisation for Economic Co-operation and Development (OECD), there was a slight divergence in the trend of per capita GDP, and this divergence appears to have been greater when considered in the context of a wider group of countries (see table 3.2).

This subject has been examined thoroughly in the literature on economic growth in the last quarter century.[8] In general, these analyses confirm that there was no worldwide convergence of per capita income levels in the sense that the term is used in this document. In the terminology used in the literature, the expression "unconditional convergence" is employed. However, various studies indicate that there is some statistical evidence of "conditional convergence", in which other factors that influence the growth of countries are taken into account, including the educational level of the population, infrastructure, macroeconomic stability, and political, social and economic institutions. This is basically because these determinants of economic growth are distributed just as unequally as per capita GDP, or even more so. This has led some authors to question the validity of the concept of "conditional convergence".

Table 3.3 illustrates another phenomenon that differs completely from those described above: the marked and growing dispersion of growth rates among the developing countries during the last quarter of the twentieth century —in other words, the increasing number of "winners" and "losers" among developing countries. This dispersion increased just as much in the period 1973-1990 as it did in the 1990s. It is important to note that this trend has been much more widespread than the trend towards greater international disparities in per capita GDP; indeed, it has affected all regions and both low and middle-income countries. Within countries, a similar differentiation has occurred, both across different social sectors and across different geographic regions. Undoubtedly, all these factors contribute to the tremendous uncertainty about the future that exists in contemporary society. This insecurity places further demands on the international system and on the social safety nets of each country, in addition to the more traditional demands for a reversal of the trend towards greater distributive inequality.

Table 3.3
STANDARD DEVIATION OF PER CAPITA GDP GROWTH

	1870-1913	1913-1950	1950-1973	1973-1990	1990-1998
OECD	0.37	0.62	1.53	0.59	1.16
34 countries	0.54	1.04			
48 countries		1.01	2.76		
141 countries			1.73	2.35	2.95
Developing countries			1.69	2.50	3.09
Latin America and the Caribbean			1.50	1.43	2.15

Source: ECLAC estimates based on data from Maddison (2001).

8 See Barro and Xala-i-Martin (1995), Quah (1995), Barro (1997), Pritchett (1997), Ros (2000), Kenny and Williams (2000), and Easterly (2001a, 2001b), among many others.

2. Overall effect of international and national inequality

Several recent studies offer a much more detailed view of trends in international inequality. Figure 3.1 shows the results of Milanovic's study (2001) on disparities in population-weighted per capita GDP. The calculations are highly sensitive to the inclusion of China and India, both of which have extremely large populations and which registered relatively little economic growth during the second phase of globalization (1945-1973), but rank among the most successful countries during the third phase (1973 to the present). When these two countries are excluded, the international disparities between the means lessen substantially from the 1950s to the 1970s, although they widened considerably later, during the last two decades of the twentieth century. However, when China and India are included in the analysis, the results are quite different. Indeed, their excellent performance in recent decades counterbalances the adverse distributive trend in the rest of the world.

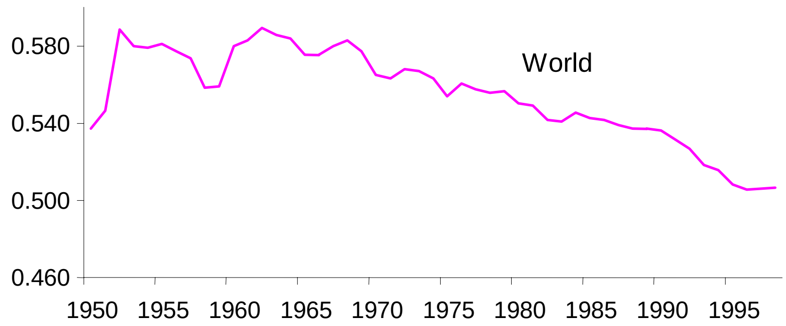
The study by Bourgignon and Morrison (2002) examines the combined effect of trends in disparities across countries and inequalities within them.[9] This analysis utilizes a broader concept of world inequality, according to which the units of analysis are not countries, but their inhabitants. Based on this concept, the authors conclude that international inequalities increased significantly between 1820 and 1910, remained stable from 1910 to 1960, and grew again from 1960 to 1992 (see figure 3.2). Up to 1910, the dominant aspect of this process was the deepening of international disparities, which grew quite markedly until the mid-twentieth century. However, during the period marked by a reversal of the globalization process (1914-1950), that trend coincided with an improvement in income distribution within countries, which curbed the further growth of international inequality. This improvement was linked both to the emergence of the welfare State in Western Europe and the United States and to the socialist revolutions in Central and Eastern Europe. The trend towards an amplification of international inequalities in recent decades can be attributed not only to moderate growth in international disparities, but also to a sharp increase in inequalities within countries.

The combination of these two trends is, in fact, one of the hallmarks of the third phase of globalization (see, *inter alia*, UNCTAD, 1997; UNDP, 1999; and Milanovic, 1999). Indeed, several studies have shown that the relative stability of inequality within countries that marked the world economy in the decades after the Second World War (see, *inter alia*, Deininger and Squire, 1996) was followed by ever greater inequality in the last quarter of the twentieth century. Cornia's figures (1999) are very informative (see table 3.4). According to his analysis, 57% of the population included in a sample of 77 nations lived in countries that exhibited growing inequality in income distribution during the period 1975-1995. Only 16% lived in nations in which inequality decreased. The rest of the study population lived in countries that had stable levels of inequality or in countries for which no trends could be discerned. These general trends are observed, with some variations, across the major regions of the developed, transition and developing worlds.

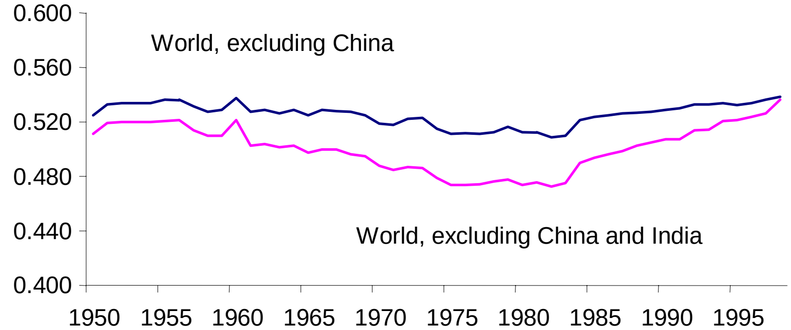
[9] Studies that paved the way for this type of analysis include the works of Berry, Bourguignon and Morrison (1983, 1991).

Figure 3.1
WEIGHTED INTERNATIONAL INEQUALITY, 1950-1998

A. World

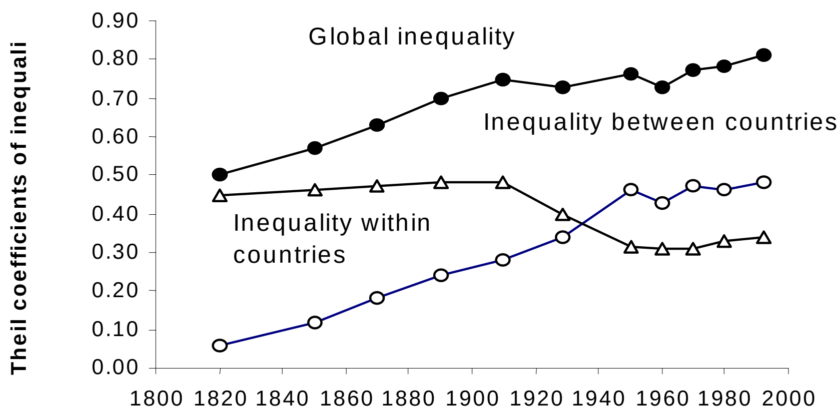


B. Weighted international inequality, excluding China and India



Source: Branko Milanovic, "World Income Inequality in the Second Half of the 20th Century", Washington, D.C., World Bank, 2001, unpublished.

Figure 3.2
GLOBAL INCOME INEQUALITY, 1820-1992



Source: Branko Milanovic, "World Income Inequality in the Second Half of the 20th Century", Washington, D.C., World Bank, 2001, unpublished.

Table 3.4
WORLD TREND IN INCOME INEQUALITY, 1975-1995
(In percentages of population)

Groups of countries	Growing inequality	Stable inequality	Decreasing inequality	No identifiable trend
Industrialized countries	71.8	1.2	27.0	0.0
Eastern Europe	98.1	0.0	0.0	1.9
Former Soviet Union	100.0	0.0	0.0	0.0
Latin America	83.8	0.0	11.4	4.8
South Asia and Middle East	1.4	70.2	14.4	14.0
East Asia	79.4	4.4	16.1	0.1
Africa	31.6	11.9	7.7	48.8
World	56.6	22.1	15.6	5.7

Source: ECLAC, *Crecer con estabilidad: el financiamiento del desarrollo en el nuevo contexto internacional*, Bogotá, D.C., Economic Commission for Latin America and the Caribbean (ECLAC)/Alfaomega, 2001; on the basis of Giovanni Andrea Cornia, "Liberalization, Globalization and Income Distribution", Working Paper, No. 157, Helsinki, United Nations University (UNU)/World Institute for Development Economics Research (WIDER), 1999.

In the case of the developed countries, the trend towards an unequal distribution of income was more marked, since 72% of the population lived in countries in which the gap was widening. It is important to point out that this relatively widespread deterioration in income distribution did not occur in the developed world during the two earlier phases of the globalization process.[10] According to several analyses (Atkinson, 1996 and 1999, and Cornia, 1999), the growth in inequality was due to an expanding wage gap, caused mainly by the erosion of institutions for the protection of labour, coupled with technical progress that favoured the most skilled workers, although trade liberalization may also have been a contributing factor. Some authors (Wood, 1998) attach more importance to this last element. Industrialized countries which continued to have central institutions responsible for wage-setting (Germany and Italy) and those which placed greater emphasis on the role of labour organizations and on upholding the minimum wage (France) were able to blunt these factors' tendency to heighten existing levels of inequality. The greatest increase in the inequality of income distribution took place in Australia, New Zealand, the United Kingdom and the United States, countries in which wage negotiations are carried out in a decentralized manner and labour markets are more flexible.

The developing and transition countries displayed a more heterogeneous pattern. The greatest deterioration in these areas occurred in the countries of Central and Eastern Europe, especially those of the former Soviet Union (see also UNDP, 1999). East Asia also registered greater degrees of inequality, mainly as a result of the widening gap between urban and coastal areas in China, on the one hand, and rural areas, on the other. However, East Asia is also the developing region in which the highest proportion of the population lived in countries where inequality was on the decline. In contrast, most of the population of southern Asia, the Middle East and Africa lived in countries where indices of

[10] The trends characteristic of the second phase of globalization have already been described. In the opinion of O'Rourke and Williamson (1999) and Lindert and Williamson (2001), during the first phase trends varied depended on the type of country concerned and included a deterioration in countries rich in natural resources, improvements in European countries with a broad agrarian base (especially the large countries of continental Europe) and no clearly discernible trend in the most industrialized countries of Europe.

inequality either remained unchanged or where there were no clearly identifiable pattern. In all these regions, the exacerbation of inequalities was linked to growing disparities between rural and urban areas.

The vast majority of Latin Americans live in countries in which the inequality of income distribution increased in the last quarter of the twentieth century. In general, as several ECLAC studies have indicated (1997, 2000b, 2000c and 2001a), inequality that characterized the 1980s —and in some countries, such as Chile, the 1970s— did not abate in the 1990s. On the contrary, countries in which income distribution became even more unequal remained in the majority. One explanation for this trend is the asymmetric nature of trends in poverty and income distribution in the different phases of the economic cycle: the debt crisis had a devastating effect on the poorest sectors, but the subsequent resumption of growth was not accompanied by a commensurate rise in income in these sectors (Cornia, 1999; La Fuente y Sáinz, 2001). The growing gap between wage levels for skilled and unskilled workers, and especially between workers with and without a university education, appears to be one of the main effects of the economic liberalization process (see the aforementioned ECLAC documents, Berry, 1998 and Morley, 2000a).

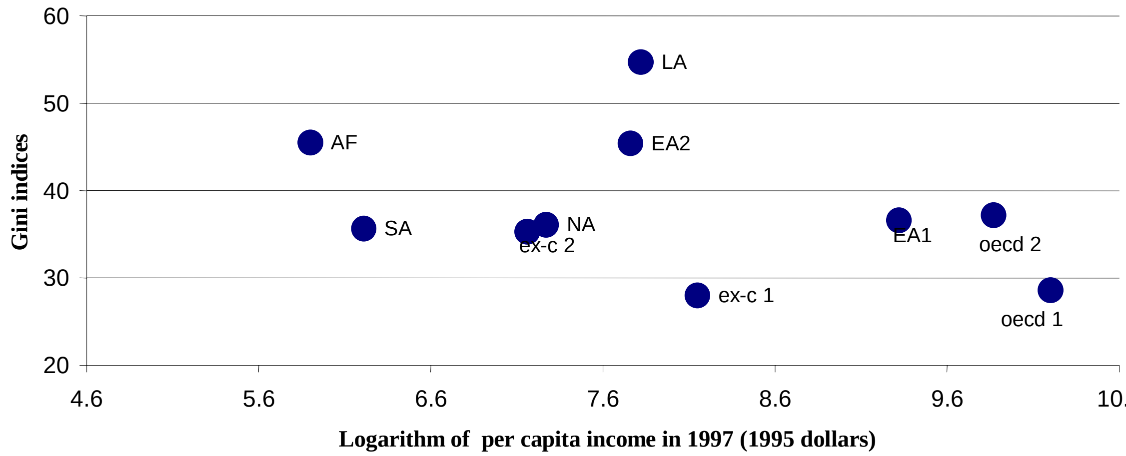
This global state of affairs suggests that new factors —in combination with more traditional ones, such as the distribution of assets and access to education— are strongly influencing income inequality. These new factors, which are associated with the third phase of globalization and with some of the national policy approaches that have accompanied it, are the reduction in earned income as a proportion of total income and the simultaneous increase in business profits and financial returns, growing skill-based wage differentials, and erosion of the State's redistributive capacity. The impact of these factors varies from region to region and even across countries within the same region.

Finally, it should be borne in mind that national income distribution structures reflect very dissimilar regional situations. The Latin American and Caribbean region has the most unequal income distribution in the world (see figure 3.3), followed by the countries of Africa and the second generation of recently industrialized countries of Eastern Asia. The next group consists of the countries of Southern Asia, those of the former Soviet Union, the first generation of recently industrialized countries of Asia and the Anglo-Saxon OECD countries. The last group, which has the best distribution of income**,** comprises the other OECD members and the countries of Central Europe (Palma, 2001).

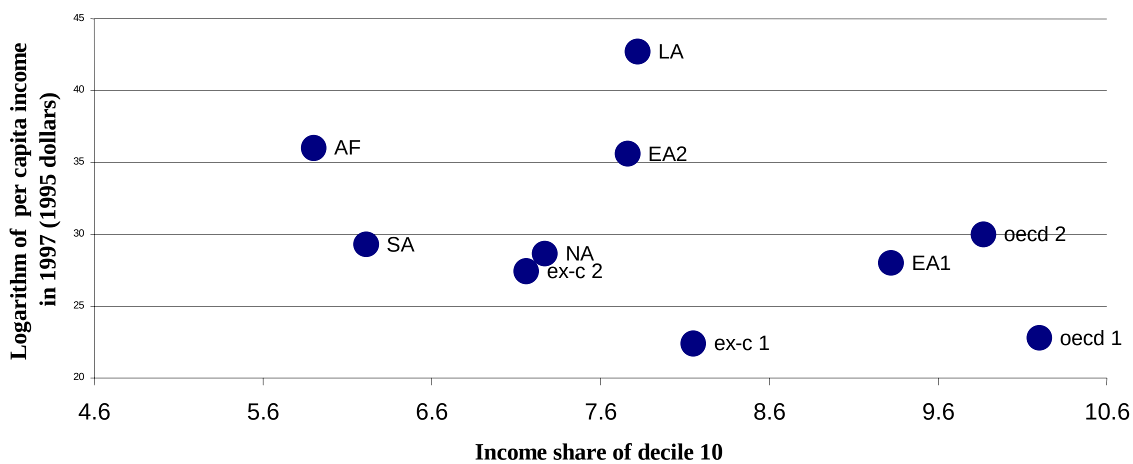
The existence of a highly unequal income distribution is an important consideration, not only because of the ethical and political problems it poses, but also because of its implications for economic growth (Solimano, 2001). Although the reciprocal relationships between growth and equity have long been a subject of controversy, in recent years numerous studies have highlighted the negative effects of inequality on economic growth —the so-called "inequality trap" (see ECLAC, 1992a; Ros, 2000, Chapter 10; Stewart, 2000; and the review of recent literature by Aghion, Caroli and García-Peñalosa, 1999). The tremendous distributive inequalities found in several regions of the developing world, especially Latin America, may thus help account for international differentials in development levels or the blockage of convergence factors. Inequality as an obstacle to growth was a favourite topic of economic debate during the 1960s, and it has awakened new interest in recent years. However, unlike that earlier period (in which the debate focused on whether the concentration of income impeded the development of domestic markets or whether, on the contrary, it facilitated capital accumulation), the implications of inequality in terms of political economy are receiving more attention today. The linkages between inequality and political economy encompass a number of different aspects, including the relationship between social cohesion and investment risk; the difficulties of implementing a predictable fiscal policy in an environment of extreme inequity capable of generating redistributive pressures and populist trends, and the positive impact of a more equal distribution of productive assets on human capital formation and the development of small and medium-sized enterprises. All of these processes are facilitated by a more smoothly operating capital market and by greater access to that market.

Figure 3.3
INEQUALITY AND WEALTH

A. Regional Gini indices and logarithm of per capita income



B. Income share of decil 10 and logarithm of per capita GDP



Source: **LA**: Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela. **AF**: Burkina Faso, Burundi, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea Bissau, Kenya, Lesotho, Madagascar, Mali, Mauritania, Mozambique, Niger, Nigeria, Rwanda, Senegal, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbawe. **EA1**: Republic of Korea, Taiwan Province of China, Singapore. **EA2**: Malaysia, Philippines. **SA**: India, Pakistan, Bangladesh, Sri Lanka, Indonesia, China, Vietnam, Cambodia, Lao PDR. **OECD 1**: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Italy, Japan, Luxemburg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland. **OECD 2**: Australia, Canada, Ireland, New Zealand, United Kingdom, United States. **Ex-c 1**: Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Slovakia, Slovenia. **Ex-c 2**: Belarus, Estonia, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Russian Federation, Turkmenistan, Ukraine, Uzbekistan.

Taken together, the foregoing considerations leave no doubt as to the existence of a definite trend towards distributive inequality worldwide, both across and within countries. At the international level there is no evidence whatsoever that income levels are converging. When convergence has occurred, it has done so only in developed countries and only at specific stages in the evolution of the world economy. A trend towards divergence in development levels, "truncated convergence" and stagnation in mean income levels has been much more common. The deterioration of income distribution within countries, on the other hand, has been widespread in recent decades.

These conclusions suggest the need for caution when examining recent analyses which downplay the second stage of globalization's favourable effects on the developing countries because of their belated and limited integration into the world economy while emphasizing, on the other hand, the advantages gained by the developing countries that did achieve that integration in recent decades (World Bank, 2002a). In fact, the relative isolation of the developing countries in the second globalization phase was accompanied by a general acceleration in the rate of economic growth throughout the developing world —for the first time in history— as well as reductions in some indicators of international inequality (between regions and countries). As was noted in the preceding chapter, however, this positive assessment does not imply any tendency to overlook the problems that marked the development process during that stage. Nonetheless, the most recent phase of globalization has been marked by increasing inequality at the international and national levels, even though, at the world level, this trend has been less pronounced than it was in the nineteenth century and the first half of the twentieth thanks, undoubtedly, to the economic success of China and India.

II. Basic asymmetries in the global order

1. Three asymmetries in the international structure

The persistence and exacerbation of international inequalities in development levels described in the preceding pages has been the subject of considerable debate ever since the Second World War, when the concept of "economic development" gained a prominent place on the international agenda as the world strove to build a new community of nations. From the very inception of the United Nations, economic and social development and peace have been considered essential and interrelated elements for the construction of a new world order. A third such element which serves as their ethical foundation is the defence of human rights (Emmerij, Jolly). This remains the prevailing vision in the United Nations even today (Annan, 2000 and 2001).

Debates about development have revolved around two schools of thought: one that sees development or a lack thereof as essentially being a consequence of national forces, and another that, while recognizing the importance of these factors, points to elements at the international level that tend to engender or perpetuate existing inequalities. This discussion is similar to the controversy about the determinants of social inequalities that has taken place at the national level in the social sciences and in political circles. In this debate, one side views inequality as an effect of differences in individual effort, whereas the other side believes that a lack of true equality of opportunity has a decisive impact.

ECLAC has traditionally aligned itself with the second of these positions in both debates. This stance is rooted in a recognition of the fact that true equality of opportunity does not exist in the real world, either at the national or the international level. Consequently, market mechanisms tend to reproduce, and sometimes exacerbate, existing inequalities. As already mentioned in reference to the international sphere, this should not be construed as an attempt to disregard the importance of national policies. On the contrary, a recognition of the fundamental role of national factors is entirely consistent with the idea that institutional development, social cohesion and the accumulation of human capital and technological capacity are essentially endogenous processes —an idea that is deeply ingrained in the thinking of ECLAC. This position is also consonant with the fundamental importance ECLAC attaches to national efforts aimed at achieving a sound macroeconomy, dynamic productive development, greater equity and environmental sustainability, together with the active involvement of society as a whole in shaping public interests (ECLAC, 2000a).

The essential role played by the international structure also has to do, however, with the way in which it influences what opportunities will be available to countries and what risks they will face, as well as the effectiveness of national efforts to maximize the benefits of integration into the international economy. Just as the State must take redistributive action at the national level to ensure equality of opportunity, national efforts can fully succeed at the global level only if they are complemented by equitable and stable rules of the game together with international cooperation designed to eliminate the basic asymmetries of the global order.

These asymmetries fall into three basic categories. The first is the *extreme concentration of technical progress in the developed countries*, which is the factor that all schools of economic thought identify as the primary source of economic growth in those countries. This concentration means that not only are research and development (R&D) concentrated in the developed countries, but so are the production sectors that are most closely linked to technological change —sectors which are highly dynamic components of world trade flows and of the international production structure and which receive high innovation rents (see chapter 2). The growth impulses generated by technical progress originating in the countries of the "centre" are transmitted to the "periphery" through four main channels: derived demand for raw materials; relocation to developing countries of production sectors considered to be "mature" in developed countries; technology transfer *per se*, including technologies incorporated in production equipment; and the possible participation of developing countries in the most dynamic production domains.

The main problems that arise in this area stem from the fact that, as Prebisch affirms in his classic work (Prebisch, 1951; p. 1) the universal spread of technical progress from the originating countries to the rest of the world has been relatively slow and irregular (Prebisch, 1951; p.1). This is because all of these mechanisms are subject to constraints or costs. In general, demand for raw materials is not income-elastic and, as the entry cost associated with the corresponding activities is low, demand is often affected by downward pressure on prices, especially during periods of diminished global activity (see box 2.1). The "mature" industrial sectors have narrow margins and low entry costs. This may lead to much the same kind of deterioration in profits and prices as is usually seen in the case of raw materials during times of slow growth. The protectionist pressures generated by developed countries are also concentrated in these two sets of sectors.

In addition, economies of scale and external economies, which have been the focus of the classic literature on urban and regional development and of more recent studies on international trade, may give rise to agglomeration economies that tend to lead to the polarization —rather than the convergence— of development levels.[11] This is one of the arguments highlighted by the various proponents of classical theories of economic development.[12]

In addition, technology transfers are subject to the payment of innovation royalties, which are increasingly protected by the universalization of strict regulations concerning intellectual property rights. Due to the "tacit" nature of technology —i.e., the fact that it cannot be fully specified because it is so closely linked to the collective human capital accumulated by

[11] As examples of the copious literature on the subject, see Krugman (1990a); Fujita, Krugman and Venables (1999) and Rodrik (2001a) and UNDP.

[12] See, among others, Rosenstein-Rodan (1943), Nurkse (1953), Myrdal (1957), Hirschman (1958) and, for a more contemporary perspective, Ros (2000).

innovating companies— it may not be easy to transfer, or its transference may only be attractive if it occurs through transnational corporations' networks of subsidiaries. The production of knowledge is the epitome of an activity subject to strong agglomeration economies, as is indicated by its overwhelming concentration at the world level. Developing countries therefore have very limited opportunities to participate in the most dynamic areas of activity, or else their participation is concentrated in low-skill areas (e.g., the assembly of electronic products in export assembly plants). The external economies linked to education and knowledge can, by themselves, hinder any trend towards convergence in productivity levels, as has been pointed out in the literature on endogenous growth.[13] Technological development also requires substantial government subsidies, a situation that rewards greater fiscal capacity as well as, perhaps, the less urgent nature of competing demands for the use of public resources in developed countries.

The combined effect of these factors accounts for the trend towards the stagnation of mean income levels and the "truncated convergence" or outright divergence of income levels, in place of the convergence postulated by conventional theories of economic growth. In fact, the divergence of development levels has persisted despite the impressive industrialization process undertaken in many developing countries during the last half century and, in Latin America, even before that. Although this process has translated into a more diversified production structure in the developing world, except in the most backward regions, at the global level the production structure has continued to exhibit major asymmetries, including the persistence of a heavy concentration of technical progress in the countries of the "centre," their sustained predominance in the most dynamic sectors of international trade and their hegemonic influence in the formation of large transnational corporations (see table 3.5).

The extent of the economic opportunities available to developing countries continues to be determined largely by their position in the international hierarchy, and this situation is the most serious implication of the asymmetries found in the world economy. Certainly, technical progress has spread from the centre through the aforementioned channels, but, in Prebisch's words, this transfer continues to be "relatively slow and irregular" and its fruits have been distributed unequally in the developing countries. Few countries, or sectors and companies within countries, are able to move fast enough to catch up to the world technological frontier, which is a "moving target", while many others succeed only in advancing at the same rate as the frontier, and not a few are left behind altogether (Katz, 2000).

The second type of asymmetry is associated with the *greater macroeconomic vulnerability of the developing countries* to external shocks, which also strain these countries' lesser and very limited means of coping with them. This vulnerability has tended to increase with the greater financial integration that has characterized the third phase of globalization, as have trade vulnerabilities, which have continued or intensified as a result of fluctuations in demand levels and the terms of trade. The increased instability of economic growth in developing countries during the third phase of globalization is a reflection of this fact (see figure 3.4).

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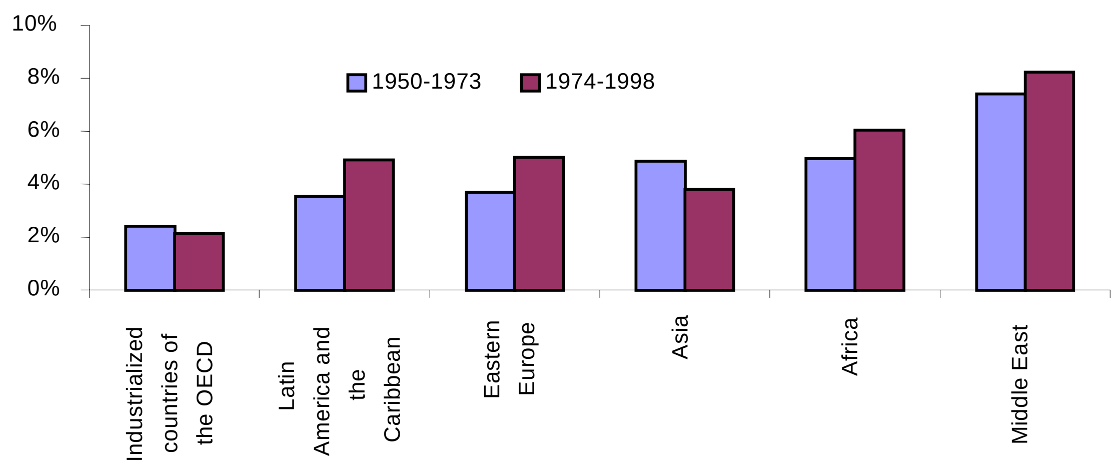
[13] See, for example, the now classic essays of Lucas (1988) and Romer (1990) and the extension of this analysis to international trade by Grossman and Helpman (1991).

Table 3.5
INTERNATIONAL ASYMMETRIES: SHARE OF DEVELOPING COUNTRIES IN THE WORLD ECONOMY
(Percentages of the world total)

	1990	1999
Population	84.0	85.0
Gross domestic product (current dollars)	22.3	23.8
Gross domestic product (purchasing power parity)	43.6	46.9
Gross fixed capital formation (1995 dollars)	23.9	24.0
Industrial value added in 1998 (1995 dollars)		27.5
Rights granted to residents	**1995**	**1999**
Patents	6.1	8.7
Designs	15.3	11.0
Trademarks	33.9	21.9
Utility models	15.3	44.4
Plant varieties	7.0	17.8
500 largest companies		**1999**
Number of companies		5.0
Sales		4.6
Assets		3.6
Market value		5.8
Employees		12.0
Market quotas by categories of technological intensity	**1985**	**2000**
Primary products	62.0	59.6
Resource-based manufactures	31.3	31.8
Low-technology manufactures	33.6	50.3
Medium-technology manufactures	10.8	21.4
High-technology manufactures	16.8	36.6
Other transactions	28.8	41.6

Source: Cálculos de la CEPAL sobre la base de Banco Mundial, *Indicadores del desarrollo mundial*, Washington, D.C., versión en CD-ROM, 2001; bases de datos de la Organización de Cooperación y Desarrollo Económicos (OCDE), Organización Mundial de la Propiedad Intelectual (OMPI), Comunidad Andina y *Fortune*, 2001.

Figure 3.4
INSTABILITY OF ECONOMIC GROWTH
(Regional average standard deviation of growth by country)



Source: Cálculos de la CEPAL sobre la base de Angus Maddison, *The World Economy. A Millennial Perspective*, París, Centro de Estudios de Desarrollo, Organización de Cooperación y Desarrollo Económicos (OCDE), 2001.

The existing financial asymmetries stem from four characteristics of developing countries: (i) the currencies in which their foreign debt is denominated; (ii) the maturity structures offered on financial markets; (iii) the scope of secondary markets; and (iv) the highly disadvantageous relationship between the size of developing-country financial markets and the speculative pressures they face. As a result of the first three of these features, agents that have access to international markets (governments and large firms) must contend with currency mismatches, while those that do not have access to international markets (small and medium-sized firms) are affected by maturity mismatches, and it is generally impossible to have a financial structure that avoids both risks at the same time. This means that developing-country financial markets are much more incomplete than international markets are, and, consequently, some financial intermediation must necessarily take place in the international market. It also means that international financial integration involves dissimilar agents (ECLAC, 2000a, 2001b and Studart, 1996).

The existing macroeconomic asymmetries are attributable to the fact that the international currencies are those of the developed countries and to the procyclical nature of capital flows to developing countries. This pattern is linked to the perception that, with few exceptions, the developing countries are high-risk markets, subject to sharp financial cycles in which phases marked by a greater appetite for risk alternate with droughts triggered by a "flight to quality assets" (see chapter 2).

The effect of all these factors is an acute macroeconomic asymmetry. Whereas the industrialized countries have greater degrees of freedom to adopt countercyclical policies[14] that help stabilize financial markets, the developing economies have virtually no breathing space, since their financial markets tend to intensify cyclical fluctuations while market agents expect the authorities to behave procyclically.

From a historical perspective, the industrialized countries have largely succeeded in freeing themselves of the "rules of the game" associated with the gold standard, but those rules have continued to determine the macroeconomic behaviour of developing countries. The developed countries were able to shake off the restrictions imposed by the rules of the game when they abandoned the gold standard in the 1930s. Since then, they have maintained a high degree of autonomy within the framework of the international macroeconomic agreements associated with the second and third stages of globalization. The developing countries, on the other hand, remained subject to strong external macroeconomic constraints during the second globalization phase, while in the third phase they have become increasingly vulnerable to financial volatility. This has translated into an increase in the centre-periphery macroeconomic asymmetries already evident in the late nineteenth century, during the heyday of the gold standard (Triffin, 1968; Aceña and Reis, 2000).

This fact has been obvious during the frequent crises suffered by the developing countries in recent decades, when markets have pressured them to adopt "depression (macro)economics," as Krugman puts it (1999). More specifically, the developing economies' main response to global financial instability has been a tendency to alternate between phases of "boom macroeconomics" and "depression macroeconomics" (ECLAC, 2000a, vol. III, chap. 1 and 2001b). Since the Second World War, multilateral macroeconomic and financial agreements have clearly offered some temporary relief at critical junctures, but their scope has been relatively limited in comparison with the financial shocks that the developing countries have had to grapple with, and their application is invariably subject to the adoption of austerity measures. Moreover, they have not led to the introduction of preventive measures during economic booms. This issue has been the focus of increasing attention in the international debate sparked by the Asian crisis.

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[14] The degree of freedom is certainly greater in the United States than in the rest of the industrialized economies because its currency carries the greatest weight internationally.

There is also a third type of asymmetry associated with the contrast between the high degree of capital mobility and the limited international mobility of labour, especially among low-skilled workers. This asymmetry is a distinctive feature of the third stage of globalization, since it was not observed in the first stage (when this factor of production was highly mobile) or the second stage (when both factors showed little mobility). As Rodrik has pointed out (1997), the asymmetries in the international mobility of production factors skews the distribution of income, placing the less mobile factors at a disadvantage. In addition, these asymmetries have a disproportionate effect on developing countries owing to the relative abundance of low-skilled labour in those countries. The limited international mobility of this factor also contributes to an oversupply on international markets of goods that are mainly produced by developing countries in production sectors characterized by low entry costs.

"Levelling the playing field" by regulatory means does not eliminate these asymmetries; on the contrary, it may end up by making them worse, both because of the different countries' widely varying levels of institutional capacity for assimilating and enforcing such regulations and because of the differing effects that such regulations have on developed and developing countries. Indeed, the high cost of building up the national institutions needed to implement the Marrakesh Agreement, which established the World Trade Organization (WTO), has been regarded as one of its main flaws.

The distribution of the costs and benefits of levelling the playing field by regulatory means is also clearly unequal, especially because the policies and standards whose application is being extended to the global level are those of the industrialized countries. Protection of intellectual property is the most conspicuous case. Regardless of its virtues in terms of creating incentives for world technological development, the benefits of protecting intellectual property rights accrue mainly to the developed countries, where the bulk of new technology is generated (see table 3.5 and chapter 7). The WTO subsidies code rewards the developed countries for their greater fiscal capacity for channelling resources into authorized mechanisms as opposed to the use of alternative instruments which have no fiscal costs (tariffs, investor and exporter performance requirements, and free trade zones) and which, therefore, have been used extensively by developing countries. The regulations on agriculture facilitate the developed countries' traditional forms of protection (tariffs and quotas), as well as rewarding them for being the only countries with the fiscal capacity to devote a considerable volume of resources to subsidizing agriculture. Prohibiting the application of local content requirements to foreign investors in developing countries runs counter to the general acceptance of rules of origin, which constitute another form of local content requirement, since they force producers to use inputs of a specified origin in order to qualify for a preferential tariff.

This situation has a parallel in the financial arena. As has been made clear in the recent debate surrounding the Basle Accord, the establishment of more rigorous standards or the application of internal bank standards to lender ratings may reduce the supply of funds on markets carrying high risk ratings, which include the developing countries as well as small and medium-sized firms in all countries (Reisen, 2001b; Griffith-Jones and Spraat, 2001). In addition, the establishment of mandatory debt workout mechanisms, unless accompanied by a sufficient supply of official emergency credits, may drive up these countries' borrowing costs.

It should be noted that this regulatory levelling of the playing field is unique to the current phase of globalization, since no attempt was made to carry out this type of process in any of the prior phases. In fact, the developed countries frequently relied on pro-development instruments whose use is not permitted today in the developing countries (see Chang, 2001 and 2002b).

2. The rise and fall of the concept of international development cooperation

The creation of international institutions to regulate the interdependent relations among States was an innovative development in international law in the twentieth century. Indeed, until early in the last century, the purpose of the rules established under international law was to ensure the sovereignty of nations. States defended their full autonomy in the conduct of matters related to their national interests, and they vigorously opposed any limitation of this independence. In reality, these principles of autonomy applied only to the imperial powers and independent nations possessing considerable military power, since in numerous cases bilateral agreements between nations having unequal degrees of power limited the autonomy of the less powerful nation. Agreements in the nineteenth century that opened up China and Japan to international trade and imposed the principles of free trade on the Ottoman Empire were clear examples of this phenomenon, as were, though in a less extreme manner, colonial expansion and military occupation of foreign territories.

In any case, the increase in international trade and financial transactions necessitated the formulation of new rules and the creation of new institutions in order for international markets to operate efficiently and for nations to resolve their disputes without resorting to force. However, as pointed out earlier, these institutions were based on the balance of power among the major States. Only after the Second World War, with the creation of the United Nations and the adoption of the principle of decolonization, did the group of developing countries begin to enjoy respect for their autonomy and their right to express their opinions in international forums. This enabled them to become involved in helping to build international institutions and to gain access to formal mechanisms for voicing their opinions about the asymmetries in the global order. This shift in international power relations and the bipolar confrontation that continued for several decades thereafter formed the global political framework that shaped the evolution of international cooperation for development. The essential elements of this process were the emergence of official development assistance (ODA) and the introduction of the principle of preferential treatment for developing countries in trade agreements.

This change was brought about through the efforts of economists, thinkers and political figures to formulate the concept of economic development, which was then extended to include the sphere of international economic law. Legal experts recognized that, as on the domestic level, the application of the same conditions to vastly different economic and social situations resulted in greater inequalities. For a number of years, international economic law was conceived of as a compensatory mechanism that protected weaker States from stronger ones by granting more rights to the former and imposing greater obligations on the latter. On the basis of this notion of international “affirmative action” for development, the governments of the developing countries endeavoured to introduce and operationalize the development dimension in multilateral forums.

In the years following the Second World War, the reconstruction of Europe took clear priority, and international development cooperation was relegated to a position of secondary importance. This was reflected both in the origins of the World Bank and, especially, in the priority attached to the Marshall Plan. The Latin American countries’ failure to win approval for the implementation of a programme in the region along the lines of the Marshall Plan was also a reflection of the priorities of that time. The region’s interests did not, in fact, meet with a favourable response until the late 1950s, with the creation of the Inter-American Development Bank, and early 1960s, when the Alliance for Progress was launched.

This period in the history of the region paralleled, to a certain extent, what was occurring at the international level. International development cooperation and the debates that surrounded it gathered considerable momentum during the 1950s and reached their zenith in the 1960s and 1970s, when the United Nations Conference on Trade and Development (UNCTAD) was established, the

Generalized System of Preferences was put in place, progress was made in promoting ODA, the United Nations introduced its International Development Strategy and the dialogue on the new international economic order commenced. Nevertheless, the debates and activities that took place during those years did so within a context of international polarization, and the actual progress that was achieved was fairly modest.

The failure of debates on the new international economic order in the early 1980s ushered in a radically different period. These years were marked by waning interest in ODA; the "graduation" of the developing (especially middle-income) countries; the placement of a high priority on regulatory standardization, to the detriment of the principles of preferential treatment; and the promotion of uniform structural reforms within the framework of an excessive amplification of conditionality by the Bretton Woods institutions. Under this new paradigm, the chief objective of reordering the international economy was to guarantee equitable conditions ("a level playing field") that would ensure the efficient operation of free market forces. In this context, the principal gains for the developing countries would be the possible dismantlement of the protectionist measures used by developed countries in "sensitive" sectors and assurances for the progress of an export-led development process within an international trading system based on clear and stable rules. According to this line of thought, the correction of international asymmetries would be based exclusively on the recognition of international responsibility to the less developed countries. This was tantamount to a replication at the international level of the social policy strategy of targeting the poorest sectors as beneficiaries of State action. Here again, the developing countries' gains during this period were modest.

The evolution of trade relations between developed and developing countries clearly illustrates this shift in the principles of international development cooperation. It should be recalled that from 1948 to 1955 —in the early years of the General Agreement on Tariffs and Trade (GATT)— the developing countries participated in the negotiations on an equal footing, with the same rights and obligations as the other parties. However, as discussed in chapter 2, the first six rounds of GATT negotiations favoured intra-industry specialization in the developed economies, while the areas in which internal adjustments would be required in order to respond to possible competition from developing countries (liberalization of trade in agricultural products, textiles and apparel, among others) were taken off the agenda and were not addressed by multilateral trade rules. As Tussie points out (1987/1988, p. 170), thanks to intra-industry specialization, some of the most painful aspects of the adjustment to changing patterns of international trade were overcome. Rather than allowing production to contract and industries to emigrate to other countries, the change could be managed on an intra-firm basis or, at least, within each industry. None of the countries engaging in intra-industry specialization had to cease production or let its control slip from their hands.

In 1958, a decade after the inception of GATT, the Haberler report concluded that the barriers imposed by the developed countries on imports from developing countries were the main cause of their trade problems.[15] This report served as the basis for the creation of Committee III of GATT, which was given responsibility for identifying trade measures that restricted exports from the less developed countries and for devising a programme to reduce those barriers. In 1963, after the committee had been working for five years with no apparent progress, the developing countries succeeded in passing a resolution within GATT calling for an action programme to freeze all new tariff and non-tariff barriers, eliminate all duties on tropical primary products and lead to the adoption of a schedule for phasing out tariffs on semi-processed and processed products.[16] In reality, the developing countries were only seeking application of the principles of the General

[15] The panel of experts that produced this report was composed of Gottfried Haberler, James Meade, Jan Tinbergen and Roberto Campos.

[16] Srinivasan (1996) notes that some elements of this action programme remained on the negotiating agenda of the developing countries 20 years later, at the GATT ministerial meeting in 1982.

Agreement and greater consistency between the policies of the large countries and their discourse in defence of trade liberalization (Dam, 1970). Nevertheless, when the Uruguay Round negotiations began three decades later, the developed countries were still applying most of the barriers identified by Committee III.

The first United Nations Conference on Trade and Development was held in 1964, and in November of that year Part IV of the General Agreement was approved. Part IV provided the legal framework for the work of the Committee on Trade and Development, which, however, remained largely symbolic. Later, in 1968, the developing countries succeeded in establishing the Generalized System of Preferences under the auspices of UNCTAD. During the Tokyo Round negotiations in the 1970s, a coordinated group of developing countries, in which Latin American diplomats played a prominent role, achieved the inclusion of an enabling clause which provided a more solid legal basis for differential and favourable treatment by the developed countries.[17] However, the system was established on a voluntary basis by the developed countries and the preferences did not become binding under GATT (Michalopoulos, 2000). These concessions could therefore be annulled unilaterally, without conferring any right to retaliatory trade measures.

In retrospect, it can be seen that at no time in the history of GATT have the governments of the developed countries balked at the demands for preferential treatment made by developing countries so long as such provisions have not required them to do more than take a tolerant view of the use of more closed trade regimes by developing countries (especially in cases where they are closed only in respect of goods, rather than capital or transnational corporations). However, the developed countries have never acquiesced to demands for more secure and stable access to their markets. This has gradually undermined the real significance of special and differential treatment, since preferential access for developing countries has never translated into contractual obligations.

Together with the international community's growing recognition of the specificities of development, new factors began to take on greater importance and to push the multilateral system in another direction. On the one hand, tariff reductions made the effects of trade and industrial policies more apparent, while the need to deal with non-tariff measures gradually eroded the tolerance for diversity in national policies that figured as the pivotal element in the international consensus to create and maintain the multilateral trading system. On the other hand, as a result of the slowdown in growth and the transformation of the developed countries, they were less inclined to support affirmative actions on behalf of developing countries within the framework of international development cooperation.

The context of the Uruguay Round negotiations proved particularly adverse for the developing countries. The preparations for that round marked a turning point in their negotiating capacity because the GATT ministerial meeting of 1982, in which several developed countries expressed their intention to deepen the liberalization process initiated at the Tokyo Round, preceded the announcement of Mexico's financial insolvency by a few months. The largest debtors, including Brazil and Argentina, recognized the fragility of their bargaining position, which remained quite weak throughout the 1980s.[18] The institutional problems confronting these governments prevented a greater involvement on the part of society in the diplomatic trade debate. Furthermore, because these countries' decision makers lacked sufficient training in technical matters and negotiation skills, they continued to pursue the traditional agenda of market access and maintained a defensive stance in relation to the new issues that were being brought into the debate.

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[17] This enabling clause, also known as the "Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries", became the legal basis for the Generalized System of Preferences (GSP) and the Global System of Trade Preferences (GSTP).

[18] See Abreu (1993), Jara (1993) and Tussie (1993), which discuss the negotiating capacity and positions of the debtor countries.

In response both to internal factors and to pressure from the structural reform programmes being promoted by multilateral financial agencies, many developing countries embarked upon a unilateral liberalization of their economies.[19] By the end of the Uruguay Round, they had consolidated almost all their tariff structures and had, for the most part, given up their demands for greater autonomy in designing and executing policies on investment and productive diversification and even in utilizing trade restrictions to cope with balance-of-payments crises.[20] The provisions on special and differential treatment contained in the Uruguay Round agreements were limited to the extension of deadlines for meeting commitments and implementing technical assistance programmes.[21] To a certain extent, these agreements signified a return to the early days of GATT and to the belief that the increase in trade brought about by liberalization ought to be enough to stimulate the growth and development of all the parties concerned.

More recent international debates and negotiations suggest that a new stage has begun, although its exact nature is not yet entirely clear. Many different factors have contributed to this situation, including the adoption of the Heavily Indebted Poor Countries (HIPC) Initiative, which began to function in the late 1990s; the commitment of some industrialized countries to curb the downward trend in ODA; the debate surrounding the unbalanced results of the Uruguay Round and the difficulties encountered in implementing the WTO agreements; the priority attached to various development issues at the Doha round of WTO negotiations initiated in November 2001; criticism of excessive increases in conditionality under structural adjustment programmes adopted during the debt crisis; the transition being made by the economies of Central and Eastern Europe and the Asian crisis; formal acceptance of the principle of developing-country ownership of economic and social policies within the context of international cooperation policies and lending arrangements made by multilateral organizations; rejection of the “homogenization” of policies and, in part, of the Bretton Woods institutions that promoted it in the past; and, within the policy debate, widespread criticism of the Washington consensus. In fact, many of these positions are shared by the principal international financial cooperation agencies (IMF, 2001b; World Bank, 2002a).

Hence, this is a particularly good time for a constructive debate on development cooperation. Development cooperation should seek to correct the basic asymmetries of the international economic order within the framework of a world economy that is much more open today than it was during the debates on development cooperation of the 1960s and 1970s. It may well be that the United Nations Millennium Declaration (2000a) is the fullest expression of a new vision of the relationship between peace, democracy and development that can serve as the foundation for the construction of a new era of international cooperation for development.

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[19] See Sáez (1999), who presents an analysis of the negotiations, and Krueger and Rajapatirana (1999), who examine World Bank policies on the promotion of trade reforms.

[20] Several countries (including Bolivia, Costa Rica, El Salvador, Mexico and Venezuela) consolidated their tariffs before the end of the Uruguay Round as part of the commitments required for their accession to GATT (Jara, 1993, p. 17). The provisions of the Understanding on Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade of 1994 severely limit the use of quantitative restrictions for reasons related to balance-of-payments problems (GATT, 1994). In 1995 the Committee on Balance of Payments Restrictions rejected Brazil’s arguments for imposing tariff restrictions in order to contend with short-term balance-of-payments problems (see document WT/BOP/R/7, dated 24 November 1995, available on the WTO web site).

[21] According to WTO, the Uruguay Round agreements contain 97 provisions on special and differential treatment for developing countries, which may be classified in the following six categories: (i) provisions aimed at increasing trade opportunities; (ii) provisions that require WTO members to safeguard the interests of developing-country WTO members; (iii) flexibility in meeting obligations; (iv) transition periods; (v) technical assistance; and (vi) provisions relating to measures to assist the less developed countries (see the WTO web site).

Chapter 4

An agenda for the global era

The analyses presented in preceding chapters will serve as a basis for the following examination of some of the elements that will play a fundamental role in the development of a better international economic, social and environmental order. The basic assumption underlying this proposal is that Latin America and the Caribbean must adopt a positive agenda for the construction of a new international order and make a firm commitment to its implementation. This view is founded upon an essential lesson of history: that efforts to simply resist processes whose roots run as deep as those of the current globalization process, as well as the negative agendas that emerge out of such efforts, will eventually fail. Finding ways to build a sounder form of globalization and to achieve the best possible position within that process are, consequently, the best option.

The agenda to be proposed here seeks to overcome the shortcomings of existing institutions. These institutions have, first of all, exhibited a disturbing inability to provide a sufficient supply of global public goods. This failing is compounded by adverse distributional trends at the global level and the absence or weakness of institutional systems for ensuring international solidarity. All of this indicates that the globalization process requires a new institutional framework in which a more efficient management of global interdependence can be combined with the introduction of firm, clearly defined principles of international solidarity. Only then will it be possible, as stated in the United Nations Millennium Declaration, "to ensure that globalization becomes a positive force for all the world's people" (United Nations, 2000a).

There are a number of major obstacles that will have to be surmounted in order to build a new global order. The first is the absence of a set of shared principles that are embraced by all the major players. The second is that, given the asymmetrical power relations found in global society, the various actors differ in their ability to influence this process. The third is the difficulty of forming international coalitions capable of offsetting those inequalities, whether through developing-country partnerships or international alliances of social sectors which feel that their interests are being harmed by the globalization process. In addition to all the above, there is the central paradox of the world of today, as discussed in chapter 1: the gap between global issues and what continue to be essentially national and local political processes.

The challenges involved in building a new institutional order are therefore enormous. The first section of this chapter sets out four basic principles for the creation of a better world order: shared objectives; rules and institutions that respect diversity; complementarity of national, regional and international spheres of activity; and equitable participation coupled with appropriate rules to uphold international governance. The second section draws together the elements of various proposals regarding national strategies for dealing with globalization: macroeconomic stability in a broad sense, the attainment of systemic competitiveness, environmental sustainability and active social policies. The third section looks at the crucial role played by regional actors in a globalized world. The fourth and final section discusses some of the main issues that ECLAC feels should figure on the global agenda: the provision of public goods; the correction of the global order's asymmetries in the areas of finance and macroeconomics, production, technology and factor mobility; and the consolidation of a rights-based international social agenda.

In addition to providing complementary analyses that refer specifically to Latin America and the Caribbean, the chapters contained in the second portion of this book provide a detailed examination of some of the elements of this agenda.

I. Fundamental principles for the construction of a better global order

1. Three key objectives: supply global public goods, correct international asymmetries and firmly establish a rights-based global social agenda

The globalization process has highlighted the need to provide certain "global public goods," such as the defence of democracy (and, hence, of civil and political rights), peace, security (including the war on terrorism), disarmament, international justice, the struggle to do away with internationally organized crime and corruption, environmental sustainability, the effort to combat and eventually eradicate pandemics and to increase cooperation in the field of health and sanitation in general, the worldwide war on drugs, the accumulation of human knowledge, cultural diversity, the defence of public spaces held in common by all, global macroeconomic and financial stability, and, more generally, the development of an appropriate institutional structure for the management of economic interdependence (Kaul, Grunberg and Stern, 1999).[1] There is a huge gap, however, between the recognition of this fact, on the one hand, and, on the other, the weakness of the existing international supply structures for these goods and the amount of resources allocated for this purpose.

[1] The dividing line between "public goods" in the traditional sense of the term (goods whose consumption is non-exclusive) and those with strong externalities is somewhat blurred, and this list therefore includes some goods (e.g., public spaces, many forms of cultural expression and human knowledge) which do not fit the classic definition of public goods.

Support for the international organizations needed to supply or coordinate the provision of global public goods is therefore essential. The emphasis here should be on the coordination of supply rather than on supply functions as such, since in many cases the regional level may be the most appropriate one for the provision of public goods. Another reason for focusing on the regional level is because the concerted efforts of non-governmental organizations and the private sector must be brought to bear on this task. This is why, as a general rule, the provision of global public goods is accomplished through the efficient operation of *networks* of various types of organizations rather than being carried out by individual agencies.

The need to provide sufficient financing for the supply of global public goods has been underscored by a number of recent reports (United Nations, 2000b; Zedillo and others, 2001a). It is important here to differentiate between these kinds of contributions and official development assistance (ODA), since all countries should play a part in financing global public goods based on the principle of "common yet differentiated responsibilities", as formulated in the Rio Declaration on Environment and Development issued at the United Nations Conference on Environment and Development (also known as the Earth Summit) in 1992.

The supply of public goods is not the only item on the international agenda, of course. It must be backed up by the accomplishment of two complementary tasks: overcoming the asymmetries of the global order, and formulating a rights-based international social agenda. These tasks could be included on the public-goods agenda, but doing so would create confusion, because, in the final analysis, they have to do with the equitable distribution of essentially *private* goods. Indeed, the provision of public goods and redistribution are classic, but quite different, duties of the State. Moreover, the elimination of international asymmetries and the formulation of a rights-based social agenda involve different spheres of activity, since the former focuses on rectifying disparities between *countries* whereas the latter focuses directly on individuals.

In order to surmount asymmetries at the global level, it is important to realize that, in the presence of widely differing positions such as those found in a hierarchical international system, attempts to apply equal terms in order to set up a level playing field will only serve to heighten existing inequalities. In the light of the considerations discussed in the preceding chapter, it becomes clear that the global agenda must include action on three different fronts. The first is to enhance the transmission of growth impulses from developed to developing countries via international trade and technology transfer. The second is to work through international lending agencies to give developing countries more breathing space for the adoption of countercyclical macroeconomic policies, help reverse the international concentration of credit and expedite the financial development of these countries. The third is to make sure that the global agenda places just as much emphasis on the international mobility of labour as it does on the international mobility of capital.

If an international social agenda is to be established, every member of the global society must be acknowledged as a citizen of the world and, hence, as possessing certain *rights*. The most cogent expressions of these rights are found in international declarations on civil, political, economic, social, cultural and labour rights, on the rights of women, children and different ethnic groups, and on the right to development.[2] The commitments made by countries at world summits, some of which are accorded special recognition in the United Nations Millennium Declaration, complement those instruments to a great extent. These instruments also reflect a recognition of the fact that the

[2] The right to development was enshrined in United Nations General Assembly resolution 41/128 of 4 December 1986. This resolution defines the right to development as "a comprehensive economic, social, cultural and political process, which aims at the constant improvement of the well-being of the entire population and of all individuals on the basis of their active, free and meaningful participation in development and in the fair distribution of benefits resulting therefrom, …" Sengupta (2001) focuses on the components of justice and equity inherent in this concept and on the importance of making sure that countries' growth rates are not only reasonable but also sustainable and are not achieved at the cost of human rights or a decline in opportunities for personal fulfilment. See, in this regard, Artigas (2001).

responsibility for fulfilling their provisions is primarily borne at the national level. It is to be expected, however, that compliance with international commitments will be a gradual process, since this is the only way that it can contribute to the construction of a true world citizenry. The tensions existing between cultural identity and globalization will inevitably affect this process, and a way therefore has to be found to reconcile the principles of equality on which human rights declarations are based with the “right to be different”.

These three central objectives of the global agenda reflect the fact that, in an interdependent world, the rights of all depend, in the final analysis, on the existence of a “global social covenant”. Embracing this widely accepted principle of nation-building implies an awareness of the fact that economic affairs cannot be separated from the social and political fabric and that, therefore, if nations are to survive and prosper, market forces must function within the framework of an institutional order based on broader, more inclusive social values and aims.

The existing international order suffers from serious shortcomings in terms of its capacity to achieve these three objectives. The United Nations is the appropriate institutional framework for a dialogue about ways of ensuring the global coherence of the system and of filling the voids that exist in relation to international cooperation. Decision-making authority and executive capacity in certain fields are, however, held by a wide range of specialized agencies that work not only at the global level but in the regional and national arenas as well.

2. Global rules and institutions that respect diversity

The essentially national and local nature of policy making has profound implications for the international order. The globalization process notwithstanding, the primary setting for the exercise of democracy will continue to be nations and local communities for a long time to come. The focus for global institutions should therefore be on acknowledging interdependence and managing it proactively. Ultimately, however, these institutions rely on national responsibilities and policies, as sovereignty continues to be a feature of the nation-State.

One of these principles’ implications is that it is futile to promote democracy unless national representative and participatory processes give the people a say in the formulation of economic and social development strategies (Ocampo, 2001). This is why respect for diversity —within the bounds of interdependence and, thus, of the common good of “cosmopolitan society”— is a crucial element of any democratic international order.[3]

This view fits in with the idea that institution-building (institutional capital), social consensus (social capital), the development of human capital and technological capacity (knowledge capital) are essentially endogenous processes. It also reflects the belief that there is not just one “right” path to development and integration into the global economy. There are a range of different options depending on the political and institutional history of each country and the differing challenges and requirements to be met (Albert, 1992; Rodrik, 1999a and 2001b; ECLAC, 2000a).

This principle is embodied in the more recent thinking on cooperation for development, which emphasizes that its effectiveness will depend on there being a sense of national policy ownership. In fact, this principle has won acceptance as a basic guideline for the design of ODA and the policies of international lending agencies (OECD, 1996; World Bank, 1999; and, on conditionality, IMF, 2001). However, quite frequently, it is ignored in practice. Indeed, an effort is often made to “compel” ownership of the policies that international agencies feel are appropriate (Helleiner, 2001). Even so, the importance of ownership is one of the overarching rules governing

[3] The reader will recall Kant’s call for the formation —based on a covenant among States— of a cosmopolitan society. Kant was one of the first philosophers to propose that the social contract be extended to include States, provided that they complied with the “republican clause”, i.e., guarantee individual rights and freedoms, the division of power, the supremacy of the law, and a representative system of government.

the operations of international agencies. Their role is to support national decision-making, not take its place.

3. Complementarity of global, regional and national institution-building

In the absence of suitable institutions, globalization is proving to be a disintegrative force. At the national level, some regions, production sectors and social groups are coming out as "winners" and others as "losers" in the intense Schumpeterian process of creative destruction now being witnessed worldwide (ECLAC, 2000a). This process is not only increasing each country's internal heterogeneity but, at the same time, is also undermining the State's ability to ensure its cohesiveness. The powerful centripetal forces which the global economy has been generating for several centuries now (Prebisch, 1987) impel developing countries to focus on carving out a foothold in industrialized markets and competing among themselves to attract footloose investments. Under these circumstances, integration efforts aimed at forming larger economic units are relegated to a position of secondary importance. A virtuous circle of complementary global, regional and national institution-building is needed in order to cope with these forces.

International debate has gradually given rise to a broad consensus as to the fundamental role of national strategies in determining how successful a country will be in forming linkages with the world economy. Such strategies are also essential in order to handle the disintegrative forces being generated by globalization within each nation. Moreover, as noted earlier, they continue to be the main vehicle for democracy in the global era.

Without a suitable international framework, however, the supply of global public goods will inevitably be insufficient and this, in turn, will hinder national development. What is more, unless a frontal attack is launched against the strong tendency towards inequality at the international level which has been in evidence for the past two centuries, national efforts may prove relatively ineffective. More specifically, within the context of a developing world whose overall growth prospects continue to be a source of dissatisfaction, the heterogeneity existing across countries and between "winning" and "losing" social groups and production sectors may intensify.

Action at the regional and subregional levels plays a critical role as a midway point between the global and national orders. This arena for what ECLAC has termed "open regionalism" (1994) has, however, either been ignored or regarded as a negative element in many of the central proposals being made regarding international economic and social reform. There are, however, at least four arguments that attest to the importance of this intermediate sphere.

The first is the complementarity existing between global and regional institutions in a heterogeneous international community. The advocacy of democracy, peace and disarmament are all examples of instances in which, given the existing degree of international heterogeneity, it is best to base the provision of the corresponding public goods on a combination of world and regional organizations. The protection of strategic ecosystems and many spheres of economic activity —such as macroeconomic policy coordination and others that will be touched upon later— are other cases in point.

The second argument refers to the extremely unequal size of the actors involved in global processes. In political terms, this means that, within the global order, the smaller countries will be able to make their voice heard (or heard much more clearly) only if it takes the form of a regional voice. This has to do not only with the development of rules and standards, but also with the defence of their interests under existing rules and standards. In fact, the paradox of the global system is that global rules are most important for small countries, which are, however, precisely the ones that have the least influence over their formulation and defence. Meanwhile, the most influential actors try to avoid making commitments or to compel other actors to accept their rules. These problems can only be solved if the smaller countries organize themselves.

The third argument, which is closely tied in with the first two, is that regional and subregional institutions enjoy a greater sense of ownership. There are opponents to this view as well, of course, who contend that regional and subregional institutions are less powerful than their individual members. The validity of these arguments will therefore depend on the depth of the corresponding regional agreements, which is what ultimately determines their effectiveness.

As the world becomes increasingly interdependent, the scope of autonomy has shifted to subregional or regional levels in some areas. This is what has been happening in the case of macroeconomic policy. It is also the case with the regulation of competition and of public utilities when transnational corporations enter the market. In all these fields, the regional arena is becoming the crucial one for the exercise of some degree of true autonomy, and it is possible that this will increasingly be the case as time goes on.

The main conclusion to be drawn from this analysis is that global public goods should be provided by a network of world and regional institutions, rather than by one or a few international institutions. A system of this type can be made to function efficiently and may prove to be more balanced in terms of power relations. In fact, this is the most advantageous system for the less powerful countries within the global order.

The construction of a truly new international architecture is founded upon the overall effect of global and regional institutional reforms. Unfortunately, many of the proposals put forward in recent years regarding the financial and, above all, social aspects of the international architecture focus almost entirely on adapting national structures to the global era. In other words, these proposals are looking at the *national* rather than the international architecture, and this is precisely their main weakness.

4. Equitable participation and appropriate governance

The insufficient degree to which developing countries participate in international economic institutions has been a controversial issue in recent years. In some cases —as in the formulation of financial rules and standards— they play little or no role at all. In others, the role they play is not commensurate with the size of their economies, much less that of their populations; this point has been raised, in particular, in connection with their voting power in some institutions. In still other instances, even though decisions are made by consensus, agreements are reached on a different basis; this argument has been made in relation to the world trading system, for example. In addition, a number of experts have pointed out that the cost of active participation in a complex world order may be prohibitive for the poorest and smallest countries.

These circumstances demonstrate the importance of ensuring adequate participation in decision-making at the international level. Achieving this will require positive discrimination in favour of poor and small countries on the part of the international community. As discussed in the preceding section, it will also require an effort on the part of the smaller countries to organize themselves at the regional or subregional level.

Another point to be made here is that preference should be given to institutional schemes having the largest possible number of active participants. Although groups formed by countries that share a particular interest or specific purpose may contribute to consensus-building, such groups should channel their views through established mechanisms rather than taking their place.[4]

The adoption of appropriate rules of governance is another essential element. Principles developed at the national level in relation to democratic and corporate governance can serve as the

[4] See, for example, Culpeper (2000) regarding the proliferation of groups or associations dealing with financial issues.

foundations for building and improving international institutions (Marfán, 2002). There is no single formula for accomplishing this, since constitutions, laws, rules and regulations, and traditions differ in each historical context and evolve over time. It can be said, however, that the most effective and legitimate forms of governance are based on shared principles. These principles do not, moreover, develop spontaneously, and an explicit effort must therefore be made to institutionalize them.

Four principles of good governance can be outlined here. The first is for governmental functions to be carried out by a body with executive powers rather than by an assembly. The second is that the civil rights of the governed take precedence over rules and regulations established by the various levels of government. Consequently, the rights of minorities should be clearly established, while bearing in mind that their identification and recognition as fundamental rights are the end result of a learning process. The third principle is that the authorities should regularly give an accounting of what they have done to safeguard the interests of the community and uphold the rights of all its members. Transparency, timely disclosure and, more generally, accountability are essential components of this community process. The fourth principle is that the authorities should submit to the scrutiny of independent bodies and to outside audits that will provide confidence among minority groups. These groups do not govern, but they do have the right to oversee the actions of those who do hold power. Furthermore, the bodies in charge of enforcing individual rights should have the power to penalize wrongdoing.

A good example of the application of these principles is provided by political governance in a representative democracy, where executive power is exercised by representatives who have been elected by the majority. It is the duty of this branch of government to uphold the fundamental rights of citizens as set down in the Constitution and other laws that apply equally to all citizens and to provide a regular accounting of the ends and means by which the government functions. Oversight of its acts and its enforcement of citizens' rights and of the law are carried out by independent agencies. An important part of this function is the auditing performed by the principal parliamentary minority (the opposition).

Another example can be found in corporate governance. In this case, majority shareholders control the firm's board of directors and management. The dispersion and varying interests of minority stakeholders, on the other hand, make it difficult for them to organize themselves effectively. Good corporate governance seeks to prevent the shareholders that hold a controlling interest from obtaining a disproportionate share of profits or other benefits relative to the size of their stake. To achieve this, executives and members of the board are required to comply with certain rules concerning transparency and timely disclosure and with regulations that set out their responsibilities. In addition, there are independent oversight agencies (including outside auditors) and in-house auditing committees (usually formed by members of the board elected by minority shareholders). These bodies complement the work of regulatory agencies and the judiciary, which have the power to penalize wrongdoing.

The governance of the globalization process could be substantially improved by adherence to these same principles. The large nations are obviously the leaders of the globalization process and hold a dominant position in the major international financial institutions, in which voting power is based on capital contributions. The resemblance ends there, however, since the other principles of governance are not clearly established. For example, it is not certain that the major nations' control over the process is legitimized by their respect for the rights of all countries. Nor is there a universally accepted institutional structure for upholding the rights of less powerful nations. In fact, quite often there is not even a clear idea of what those rights are.

The application of these principles to improve the governance of the globalization process will therefore entail according priority to the fundamental rights of developing countries (especially the smaller ones), institutionalizing accountability and increasing oversight by bodies that will inspire the confidence of all the parties concerned. This approach involves placing certain limits on the power of the most influential countries, since this is the only way to improve the governance of the globalization process. It will also lead to a greater commitment to the global institutional structure on the part of developing countries by increasing their sense of ownership.

II. National strategies for dealing with globalization

1. The role and basic components of national strategies

As has been discussed at length in the literature on institution-building in recent years, in today's global era, any development strategy must be found upon a solid, democratic social covenant to ensure its political stability; non-discretionary local systems and modes of behaviour that provide security as to contract performance; and the formation of an impartial, relatively efficient State bureaucracy. These are also, of course, basic components of a pro-investment environment as well.

These general sorts of institutional elements are not sufficient in themselves, however. They are the backdrop for the development process, but they do not account for the specific forces that drive growth in developing countries or, in many cases, that lead to the depletion of growth impulses.[5] National strategies for today's global era should incorporate at least four core elements: (a) macroeconomic policies designed to reduce vulnerability and facilitate productive investment; (b) strategies for developing systemic competitiveness; (c) a keen awareness of the priorities of the environmental agenda, which, by its very nature, is essentially global in scope; and (d) highly active social policies, especially in the fields of education, employment and social protection (ECLAC, 2000a, 2000b 2001b; ECLAC/UNEP, 2001).

There are no universally valid models in any of these areas. Thus, the institutional learning process and, most importantly, democracy have a broad sphere of action in which to function. One of the most serious mistakes made in the last quarter of the twentieth century was the promotion of a single "solution" in each of these fields based on the principle of full market liberalization. The tendency to equate successful integration into the globalized world with economic liberalization overlooks the fact that many equally successful strategies have *not* been based on all-out market liberalization but instead on various ways of forming "virtuous-circle" linkages between the State and the market. It would be just as mistaken, however, to take the opposite approach and try to resuscitate models which were successful when the world economy was less integrated but which thus correspond to stages in the development of the world economy that are now clearly a thing of the past.

2. Macroeconomic strategy

The experiences of Latin America and the Caribbean during the final quarter of the twentieth century demonstrate that all forms of macroeconomic disequilibrium are economically and socially costly. A number of lessons can be drawn from these experiences. First, macroeconomic discipline is essential, but it should be defined in a much broader sense than it generally has been in economic discourse in recent decades, which has focused attention on fiscal balances and low inflation. This narrower view overlooks many important dimensions of macroeconomic stability, such as balance-of-payments sustainability, the soundness of national financial systems, and the stability of real variables such as economic growth and employment. Macroeconomic management should be directed towards avoiding unsustainable public or private deficits, guarding against financial imbalances in flows or in the way balances are structured, controlling inflation and curbing any instability in real economic variables.

[5] To use the terms employed by Maddison (1991), these factors are associated with the "ultimate causality" rather than with the "proximate causality" of economic growth. See also Ocampo (2002a).

In order to achieve all these objectives, some important policy choices will have to be made and, for these purposes, there is no simple way of defining stability or any universally valid system of macroeconomic management. In a volatile international environment, some degree of flexibility in macroeconomic management has to be combined with suitable regulations. Recent events leave no doubt as to the fact that, in the long run, macroeconomic authorities' credibility can be strengthened more effectively through prudently managed flexibility than through the adoption of overly rigid rules.[6]

Within this framework, one of the authorities' key objectives should be to lengthen the time horizon for macroeconomic management in order to take in the whole of the business cycle and support dynamic long-term growth. Encompassing the entire cycle will provide the necessary scope for the adoption of countercyclical macroeconomic policies that can help forestall unsustainable booms and afford sufficient flexibility in dealing with external crises. The option of employing countercyclical policies is quite limited without the support of international institutions, however, and this has consequently become one of these institutions' basic functions in the current phase of the globalization process. The short- and long-term objectives of macroeconomic policy are, to a great extent, complementary —since more stable economic growth is one of the strongest incentives for fixed capital investment— but they can also confront policy makers with some difficult choices.

Based on these principles, fiscal policy should be designed using a pluriannual horizon. It should also be based on long-term guidelines for ensuring a structural fiscal balance that allow moderate, temporary surpluses or deficits for countercyclical purposes or, alternatively, set an explicit target for the ratio between the public debt and GDP. The active use of stabilization funds (or equivalent instruments) can be the most effective way to build up surpluses during booms that can then be used to contend with crisis situations. The desirable level and structure of public revenues and expenditures will, in the long run, depend on what kind of demands each society's fiscal covenant places on the State (ECLAC, 1998c). In countries with very low tax burdens (as is true of a number of Latin American nations), taxes can be increased to finance the core functions of the State, especially in social sectors. In fact, as recently stated by the World Bank (2002a), the tax burden and levels of public expenditure in the developing world tend to be low in comparison to those of developed countries.

Monetary and exchange-rate management are, of course, closely related. Some degree of flexibility in the exchange regime is essential for countercyclical monetary management (i.e., for the application of restrictive policies during booms and expansionary ones during the downswing in the cycle). The desirable degree of flexibility will be greater in the larger economies that have well developed capital and exchange markets. It may be wise to allow the exchange rate to appreciate in order to soak up excess foreign exchange during booms, while a depreciation may be needed to spur the production of tradables during crises and to provide enough breathing room for reactivation-oriented fiscal and monetary policies.

In financially open economies, the prudential regulation of capital flows, either through the use of reserve requirements or taxes on external borrowing or by means of direct regulation,[7] is an extremely useful supplementary tool for avoiding excessive external borrowing during booms and to prevent liability structures from becoming skewed towards short-term obligations. In more closed economies, caution should be used in opening up the capital account. In fact, if a country does not have a solid financial system, there is really no convincing argument for opening it up at all. Stronger prudential regulation and supervision is one of the pillars of any sound macroeconomic policy, since its core function is to prevent unsustainable financial structures from being spawned during economic booms.

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6 This may, in fact, be the major lesson to be learned from Argentina's experiences over the past decade.

7 Direct regulatory tools include rules on borrowing by public-sector agencies at all levels, direct restrictions on certain types of private flows (short-term borrowing, portfolio flows or external borrowing by non-tradable sectors).

In the long run, economic growth hinges on a combination of sound fiscal systems that provide the necessary resources for the public sector to do its job, a competitive exchange rate, moderate real interest rates and the development of a deep financial market. Macroeconomic policy should be focused on ensuring the first three elements. The last is a complementary process.

The key objective of financial deepening is to provide suitably priced investment finance with sufficiently long maturities. In the absence of a well developed financial market, many investors (particularly the larger ones) will turn to international lenders, thereby substituting exchange risk for maturity risk. Use of this escape valve therefore entails serious hazards, as well being beyond the reach of smaller firms. The liberalization of financial systems in Latin America and the Caribbean has not deepened financial markets or reduced the region's high intermediation costs as much as had been expected. Consequently, the public sector still has an important role to play in promoting the emergence of new intermediaries and financing mechanisms (e.g., pension and investment funds, bond and mortgage markets, and hedging systems) or in arranging for the direct provision of such facilities by well-run development banks.

The existence of this unsatisfied demand for investment finance is compounded by the absence of suitable financial services for micro- and small enterprises and for the poorer households. This situation creates a greater demand for direct or indirect public intervention. Low national savings rates are another constraint on investment financing in Latin America and the Caribbean. Efforts to increase public-sector saving, the creation of corporate savings incentives (especially to encourage firms to retain profits) and special mechanisms to foster household saving (for retirement, in particular) may be useful means of raising national savings rates (ECLAC, 2001b, Chap. 4).

3. Building systemic competitiveness

A dynamic transformation of production structures should not be viewed as a reactive phenomenon that automatically follows from good macroeconomic management, but rather as an active and essential component of any development strategy, even at this juncture in the globalization process (Rodrik, 1999a; ECLAC, 2000a). The core objective of these strategies should be to build systemic competitiveness. This concept, whose first formulations date back to work done by ECLAC over a decade ago (ECLAC, 1990; Fajnzylber, 1990),[8] is based on three main elements. The first is the role of knowledge as the foundation for competitiveness, since it is the only factor that enables countries to produce goods and services capable of "making the grade" on international markets while protecting and increasing their citizens' real incomes. The second is the idea that competitiveness depends less on individual firms than on the performance of each sector as a whole, its interaction with input-supplying sectors and, ultimately, the smooth operation of the entire economic system. The third is that, given the serious imperfections existing in technology markets and strong externalities among economic agents associated with the systemic nature of competitiveness, the development of sound technology markets and production linkages is in large part the outcome of the deliberate efforts of the State, business associations and, particularly, of collaborative initiatives undertaken by the State and private sector to create a virtuous circle that will bolster the system's competitiveness.

The three basic components of this strategy are: (i) the creation of innovation systems to speed up the accumulation of technological capacity; (ii) support for changes in production structures and the formation of production linkages; and (iii) provision of quality infrastructure services. The creation of adequate social safety nets and sustainable environmental management are important complements to this effort. These elements concern different spheres of activity, however, and will be considered later on in this document.

[8] These concepts also contain elements developed concurrently by other authors: see, in particular, Porter (1990).

Given the key role of knowledge, any competitiveness strategy must be based on increased investment in education, vocational and business training, and science and technology. This process, whose aim is the creation of dynamic innovation systems, should be led by the State, but the private sector should also be actively involved. These efforts should focus on increasing the capacity of all actors to absorb knowledge and on developing appropriate mechanisms for the transfer and adaptation of technology and business skills, especially to medium-sized and small firms. Business associations and incentives for various forms of collaboration between these associations and providers of educational and vocational training play a fundamental role in this effort. Innovation systems should be strengthened at all (i.e., local, national and, to a growing extent, regional) levels.

In view of the intrinsic importance and cross-cutting nature of new information and communication technologies, efforts to promote their active use throughout the economic, social and even political (e-government) systems are of vital importance. Access to a quality telecommunications network and to competitively priced information and communications equipment is one of the pillars of this endeavour. Other mainstays include the production of software, incorporation of technology into production and trade, and the formation of business networks that make effective use of new technologies. The incorporation of new technologies into the educational and health-care systems requires special State support and community mechanisms to give low-income sectors access to them, since the threat of a “domestic digital divide” (produced by disparities between different social sectors’ access to new technologies) is a much more serious threat in Latin America and the Caribbean than the international digital divide.

Economic growth necessarily entails an ongoing process of changing production patterns in which some branches of production lead growth while others lag behind. This process is not necessarily automatic or harmonious, since the expansion of new sectors involves the development of a complementary set of activities based on a technological learning process, the establishment of commercial networks and significant coordination costs (Hirschman, 1958; Chang, 1994; Ocampo, 2002a). The diversification of the production structure must therefore be an explicit priority of any competitiveness strategy. This idea has been expressly recognized in the industrialized world, where the process has become virtually synonymous with the development of cutting-edge technologies. It also enjoyed wide acceptance in the past as a component of State-driven industrialization strategies in developing countries, and it is an essential element of the most successful developing economies, especially those in East Asia. Diversification strategies have been discarded in most countries of the region, however.

Within the context of the globalization process, the diversification of production has three priorities. The first is the diversification of the export base and of target markets. This calls for a very active form of commercial diplomacy aimed at securing stable access to external markets, as well as the development of a competitive, high-quality service infrastructure —in the areas of finance, insurance, promotion and certification— to back up exports of goods and services. In this endeavour, one obvious priority is to increase the region’s share of world trade in technology-intensive goods and services.

The second priority is to develop programmes to broaden the linkages of activities oriented towards the international market or dominated by transnational corporations. The weakening of such linkages is one of the most problematic aspects of recent trends in the region. For this reason, “linkage policies” designed to increase the value added in export sectors and/or sectors with a high proportion of FDI should be adopted as a forward-looking priority. Among these linkages, those associated with the provision of technology-intensive services are of special importance. These policies would, in practice, amount to a shift away from a policy aimed at maximizing the quantity of exports and FDI to a policy aimed at improving their quality.

The third priority is to support the formation of production clusters in particular locations. This process is a response to the growing dynamism of local spheres of economic activity in the global era. It is particularly important for steering small and medium-sized enterprises towards production for the international market or linkage with export sectors (ECLAC, 2000a, vol. III, chap. 3).

The other core aspect of competitiveness policy is the provision of *quality infrastructure services*. In a number of countries, various public-private partnerships have succeeded in making significant progress in this regard, particularly in telecommunications, port services and maritime transport, and —to a lesser extent and with wider discrepancies from one country to another— in energy services (electricity and gas) (ECLAC, 2001a, Chap. 5). It must be acknowledged, however, that private participation in these sectors has been accompanied by serious regulatory gaps and, in some cases, has burdened the State with contingent liabilities that do not always have a sound rationale (ECLAC, 1998; 2000a, vol. III, chap. 5). The main problems in terms of infrastructure continue to be found in land transport, including both railways and roads. Shortcomings in both the quantity and the quality of road networks are particularly severe. Accordingly, substantial improvements in road infrastructure, the correction of regulatory gaps and the rationalization of the management of contingent liabilities should be given priority, as should improvement of the efficiency of State enterprises in areas where the State continues to provide services directly.

Progress on all these fronts will require major institutional and organizational efforts to formulate and implement active competitiveness policies, since the pre-existing systems of government intervention in productive development were dismantled or severely curtailed in most of the countries of the region during the economic liberalization phase. Such systems would, in any case, be ill-suited to the new environment. In this area, as in others, it is necessary to “invent” new institutions, whose management will no doubt require an intensive learning process.

The possible models for these institutions are certainly not uniform, since they depend on the specific characteristics of each situation. A public-private partnership is essential to fill the information gaps found in each of these sectors (i.e., the former’s limited microeconomic information and the latter’s insufficient familiarity with global and cross-sectoral processes). In other words, institutional design must take into account both the “forest” and the “trees”. The instruments to be developed for this purpose should be based on checks and balances that establish a clear link between incentives and results (Amsden, 2001) and thereby preclude rent-seeking behaviour on the part of beneficiary firms.

This endeavour should comprise various combinations of horizontal and selective instruments, depending on each country’s institutional context, to be chosen on the basis of shared strategic visions of the directions to be emphasized in joint public-private efforts. This is less an exercise in “picking winners”, as it is commonly called, than an effort to identify opportunities and direct the actions needed to ensure that some of them bear fruit. This type of strategic exercise is one in which all private investors engage on a regular basis. It is hard to understand why some schools of economic thought consider it illegitimate to carry out such an exercise in relation to a particular territory, whether it be a town, a country or even a subregion or region.

4. Environmental sustainability

The agenda for environmental sustainability has gradually made its way into the institutions, public policies and business practices of the countries of the region. While it is not yet, in the fullest sense, an integral part of the development process, the progress achieved thus far constitutes a much better institutional and social foundation than the one available 10 years ago, when the United Nations Conference on Environment and Development was held in Rio de Janeiro. The concept of sustainable development has also been gradually incorporated into educational systems, and the change in society’s perception of environmental issues has strengthened citizens’ awareness and commitment. The primary hurdles that remain in this area have to do with institutional and financial considerations and with the perception by business circles in the region of environmental sustainability as a cost rather than an opportunity.

With respect to institutional mechanisms, steps should be taken to set up clear and consistent regulatory frameworks and to achieve a stable level of public expenditure with a view to generating significant synergies with international financing and private investment. On the basis of existing management methods, the time has come to develop a new generation of more effective and prevention-oriented instruments for the integration of economic and environmental considerations. This process should primarily involve the use of economic instruments to provide adequate incentives to meet sustainability goals and to promote a greater use of clean production technologies by small and medium-sized enterprises. One of the most promising lines of action in this area is the creation of genuine domestic (and regional) markets for environmental services, following the pioneering example of the Kyoto Protocol's clean development mechanism. Such instruments have the dual purpose of generating incentives to minimize environmental costs (the central objective of economic instruments), while at the same time channelling resources to the actors that are best able to provide environmental services most efficiently.

A more active sustainable development strategy will require the allocation of more government resources. One options is to introduce "green taxes," as has been done in some industrialized countries. While great strides have already been made, the further reduction of government subsidies for polluting industries is also important.

Furthermore, current frameworks must be adapted to integrate explicit environmental policies with the implicit ones associated with sectoral economic policies and the patterns of structural change they entail. In view of the regressive trend in energy efficiency taking shape in the region (see chapter 9), such integration and the use of this array of instruments should give priority to the reversal of that trend.

The formation of effective linkages between the economic and environmental agendas also requires a shift from a reactive agenda to one that takes a proactive approach to the relationship between environmental sustainability and economic development. This involves, first of all, identifying the opportunities offered by the global environmental agenda, especially as regards the possibility of becoming net providers of global environmental services, primarily in connection with the climate change and biodiversity agendas. The opportunities afforded by the clean development mechanism at the international level are particularly noteworthy in this regard. This proactive approach also entails taking advantage of opportunities to expedite scientific and technological development through the sustainable use of biotic resources, a better understanding of the region's natural resources and the development of its own technologies for tapping these resources in sustainable ways.

In addition, this approach involves the active use of foreign investment as a channel for the transfer of clean technologies, the exportation of goods and services having a high environmental content —organic agricultural products and ecological or environmentally certified tourism— and the promotion of the international certification mechanisms increasingly demanded by developed-country consumers. In fact, foreign investment and export activities in the region are proving to be the areas that have made the most progress in incorporating clean technologies.

Types of production that rely on an abundant supply of natural resources but are slow in leading to the diffusion of technical progress are being eclipsed by economies that are successfully developing knowledge-based forms of production. It is therefore necessary to redirect the region's model of competitiveness towards new activities and towards an increase in the value added by natural resource-intensive activities. This requires the promotion of industrial activities and complementary services, including those that will increase the sustainability of primary activities.

Because of the territorial specificity of environmental management functions, strong operational links with local authorities need to be forged. Solving high-priority environmental problems in such areas as water resources management, solid waste disposal, ecological land use and urban management requires the decentralization of environmental policies and instruments and a more balanced distribution of public expenditure and private investment at the district and local levels. It is at the local level that the commitment between the State and the citizenry is expressed most clearly. Hence the importance of continuing to promote social consensus-building in relation to the environmental agenda, particularly within the context of provincial and municipal sustainable development councils and the local Agenda 21 framework. Forums of this sort can become powerful tools for organizing public affairs and mobilizing additional resources for the promotion of environmental sustainability at the subnational level.

5. Social strategies in an era of globalization

Globalization has increased the demands of international competitiveness and strengthened the interrelationship between competitiveness and employment. It has also given rise to new social risks. On the social front, national globalization strategies should therefore focus on three areas: education, employment and social protection. Progress in these three areas is a prerequisite for equitable participation in the global era. Moreover, such progress is essential for the implementation of a rights-based international agenda at the national level.

Advances in these three areas are mutually reinforcing. Education is the primary means of halting the intergenerational reproduction of poverty and inequality. At the same time, globalization has increased the need for human resources capable of engaging in new modes of production, competition and coexistence. Employment is at the heart of social integration, as an aspect of social fulfilment and as a source of income, and it therefore determines individuals' ability to gain access to basic consumer goods and thus avail themselves of their basic rights. Such access is crucial in the absence of society-wide safety nets. Among the risks faced by the population are those associated with macroeconomic volatility, the adaptation of new technologies and ways of organizing work, and the elimination of jobs in many sectors as a result of international competition.

In *education*, national efforts should focus on reducing disparities in attendance and achievement between income levels and between rural and urban areas at all levels of education (pre-school, elementary, technical, university). Efforts to achieve greater equity should therefore focus on achieving universal coverage, preferably up to the end of secondary school, while reducing differences in the quality of the education provided to the various socio-economic groups.

In developing their educational systems, the Latin American and Caribbean countries face both traditional challenges and challenges related to new technologies. Meeting them will require a diversified package of policies, which each country must tailor to fit its own characteristics and objectives. Public education expenditure must also be increased, of course, with the general objective being to reach levels similar to those found in OECD countries: 6% of GDP. To improve educational continuity, governments must give priority to increasing the coverage of pre-school education, which is still comparatively limited; expanding secondary-education coverage and graduation rates; increasing the availability and range of technical and professional educational options; and achieving greater consistency between technical/vocational and higher education, on the one hand, and the requirements of the job market and competitiveness, on the other. These efforts should be supplemented by targeted compensatory measures designed to have long-lasting effects in areas in which educational performance is poor; more relevant curricula; large-scale use of new technological resources; and the empowerment of communities to assist in furthering educational goals.

Social inclusiveness requires the development of new approaches to learning. Today, these approaches mainly involve access to knowledge, networking and the use of information and communications technologies. Educators need to make better use of the cultural and educational audiovisual industry by harmonizing cultural programming in the media with schooling, so that the two will reinforce each other. Urgent steps should be taken to ensure that students in poor rural and urban areas can learn to use interactive media that are not available to them at home, since school is the ideal environment for ensuring, distributing and democratizing their use. The modernization of educational tools is not enough, however. It is even more important, in conjunction with these new tools, to develop higher cognitive functions by orienting the learning process towards problem identification and problem-solving, an increased capacity for reflection, creativity, the ability to distinguish between what is relevant and what is not, and planning and research skills, since these functions are vital in an information-saturated world. Progress also has to be made in the design and use of portals (educational content) and in the training of educators (teachers, administrators and families).

In this era of globalization, the primary challenge in the area of *employment* is to prevent the expansion of world trade from resulting in the violation of workers' basic rights or in the downward convergence of wages and working conditions in countries at different levels of development. The Declaration on Fundamental Principles and Rights at Work and its follow-up reaffirms the member countries' commitment to such fundamental rights as freedom of association and the right to collective bargaining, the prohibition of forced or slave labour, progressive abolition of child labour and non-discrimination.

The creation of new jobs is sustainable only when the economic activities concerned are competitive in the long term. This means that productivity must be enhanced. As a means to this end, comprehensive strategies must be devised to increase investment in human resources and ensure that gains in competitiveness are not based primarily on the reduction of labour costs or the concentration of wage increases in the most dynamic or well organized sectors. Productive restructuring and increased labour mobility make it necessary to give workers opportunities to learn how to adapt to new conditions in order to increase their employability. Countries will therefore have to invest in worker retraining based on a new approach and, possibly, a different institutional framework. The development of basic competencies, rather than specific skills, will give workers a knowledge base that will enable them to adapt more easily to the demands of new jobs. Since informal activities, micro-enterprises and small businesses play a major role in generating employment, they should be given access to factors of production (capital and land) and to the tools they need to modernize their operations (managerial and technological know-how), and programmes should be set up to help them gain access to dynamic industrial networks.

To these ends, ministries of labour should espouse a labour policy that places more emphasis on self-regulation by social actors (social dialogue) and encompasses the large groups of workers who remain outside modern sectors (unemployed and informal-sector workers). In addition, they should be repositioned in political and administrative terms so as to give them a place in economic cabinets and to restore, in many cases, their role in setting the direction for labour policy.

The development of *social safety nets* should be guided by the principles of universality, solidarity, efficiency and integrality (ECLAC, 2000a). Progress cannot be made towards universality unless the sharp inequities in access to services and in their quality are corrected. Solidarity should be ensured through a combination of compulsory contributions, public transfers, and cross-subsidies between different income strata and risk groups.

Social safety nets are seriously flawed in terms of both coverage and the new risk structure associated with globalization. The countries of the region, with their chronic shortcomings in the coverage of traditional risks (illness, old age, disability and death, as well as nutrition, housing and education), now face the additional burden of protecting their populations from the effects of such risks as labour and income vulnerability.

Sharp business cycles and the rigidity of real wages —which has been heightened by measures for curbing inflation— have made wage earners more vulnerable to the effects of the business cycle. Since many of the existing social safety nets were designed to serve the needs associated with wage-based employment, it has now become necessary to develop a system of social protection whose coverage extends beyond the formal sector and to create more comprehensive unemployment insurance schemes. Of course, job creation policies will remain crucial in this context. As the experience of some European countries demonstrates, social protection policies should focus on boosting employment as a means of helping to ensure universal social protection. In emergency situations, it is necessary to develop special employment and poverty alleviation programmes for vulnerable sectors, based on permanent institutional arrangements that allow such measures to be implemented quickly and that link them to other objectives such as job training, infrastructure provision and territorial development.

Because of the extent of informal-sector employment and unemployment, the coverage of traditional social safety nets is limited, as is the usefulness of wage-linked contributions as a source of funding. Accordingly, emphasis should be placed on the implementation of systems based on citizenship rather than on employment. Reforms in general, and reforms in the social security system in particular, should introduce combined and complementary insurance mechanisms that reflect the diversity of employment relationships. These types of arrangements will also promote labour mobility and provide protection against external shocks.

The quantity and quality of the social safety nets that can be funded by mandatory contributions, general taxes or a combination of the two depend on each country's current level of economic development and on its fiscal covenant, which embodies political and social agreements about the level of well-being that should be guaranteed to its citizens. The fiscal outlook is not static. Thus, a fiscal covenant for the protection of citizens' rights can include an element of progressivity whereby public contributions for social protection and poverty reduction can be increased at the margin. Moreover, an inclusive system of social protection must place special emphasis on the views of target groups and provide for a constant flow information to the public regarding opportunities for and means of accessing social safety nets and for taking part in decision-making.

III. The key role of action at the regional level

Latin America and the Caribbean has progressed further in terms of regional integration than any other region in the developing world. In recent times this was largely a result of the political impetus that built up around the issue of integration in the late 1980s and early 1990s. Unfortunately, this momentum has waned in the last few years. In addition, the institutional structure remains fragile and the convergence of existing agreements towards the formation of larger areas and the consolidation of customs unions are tasks yet to be accomplished. It is therefore imperative for the countries to renew their political commitment to regional integration. Such a commitment would not be incompatible with broader trade negotiations, such as those directed towards the formation of the Free Trade Area of the Americas or global negotiations. Nonetheless, if regional integration processes are to remain relevant within the context of a hemispheric free trade area or the globalization process, they will need to be deepened in the future.

The momentum displayed by the regional integration process of the late 1980s was a paradoxical phenomenon in the sense that, according to the more orthodox doctrines, integration was (and still is) a force that distorts trade flows. Contrary to those views, however, the evidence suggests that integration tends to create rather than divert trade flows. Moreover, the flows it generates tend to be of a high quality (ECLAC, 1998b). This is borne out by the tendency of regional flows to have greater technological content and to create more production linkages. One of the main advantages of these processes is that countries with similar levels of development can take advantage of specialization economies for intra-industry trade. Another advantage is that lower transaction costs allow smaller firms to participate in intraregional trade, especially between neighbouring countries. This helps to counter the traditional tendency for external trade operations to be monopolized by larger firms within each sector of production or trade.[9]

In consequence, regional markets can provide an excellent training ground for firms —especially smaller enterprises— to learn to deal with the external markets and can therefore help new firms and sectors to venture into export activity. A further benefit of such integration processes is that they provide an opportunity to harmonize a wide range of differing rules and thus reduce the associated transaction costs, thanks not only to geographical proximity but also to the similarity of institutional traditions.

This positive vision of integration is borne out by the increase recorded in intraregional trade, especially within South America, between 1990 and 1997, when the augmented flows consisted primarily of manufactures, and particularly goods with a high technology content. Recently, however, these trade flows have been hurt by macroeconomic instability in the region. In fact, they have proven to be highly elastic in response to abrupt business cycles in a number of the countries, especially in South America (ECLAC, 2001).

Macroeconomic cooperation has thus become essential in order to consolidate trade integration processes. In this respect, progress has been made in all the existing subregional schemes, and these initiatives should continue to move forward from the discussion and exchange of information and the adoption of common macroeconomic rules towards the institutionalization of peer review for preventive purposes and the design of stricter forms of macroeconomic coordination. Such mechanisms may eventually lead, in some cases, to monetary unions. In tandem with these efforts, the prudential regulation and supervision of national financial systems also stands to benefit from progress in the exchange of information, peer reviews and the development of common standards.

ECLAC has also argued (2001b) that efforts must be made to develop regional and subregional financial institutions. Latin America and the Caribbean already have major assets of this type, including a wide network of multilateral development banks made up of the Inter-American Development Bank, the Andean Development Corporation, the Central American Bank for Economic Integration, the Caribbean Development Bank and the Financial Fund for the Development of the River Plate Basin (FONPLATA). The Latin American Reserve Fund has built up a stock of experience which could serve as a basis for using regional resources to provide an increased level of exceptional financing for countries in severe economic difficulties. This could be accomplished either by significantly increasing the Fund's resources and membership or by means of mutual support agreements (swaps) between central banks.

In addition, the expansion of trade generates an increased demand for the harmonization of the different regulatory schemes. These systems comprise technical standards, including phytosanitary requirements, customs codes, and government procurement and servicing regulations. Several of these areas have already seen some progress. It is important to move forward in other areas, however, most notably in relation to rules on competition and on the regulation of public utilities. With respect to rules on competition, the European experience provides grounds for the belief that, as common markets and an active process of intraregional investment are consolidated, agreements on competition issues and, eventually, the adoption of a common policy on competition may have distinct advantages over unfair competition rules applying solely to external trade. A framework of this nature would, among other things, make it possible to deal more effectively with potential unfair practices by transnational corporations.

9 See Berry (1992) for an account of this.

Since high-technology goods account for a large percentage of intraregional trade, it is important to take joint action to promote the development of the corresponding sectors in ways that will avoid the rigidities of the old (and largely unsuccessful) sectoral complementarity agreements. Such measures should seek to generate regional and subregional innovation systems and should include the development of broader schemes for cooperation in education, research and technical development. They could also provide a suitable framework for strategic alliances in the areas of research and development or for the formation of new production clusters made up either of domestic firms in countries that are members of a regional or subregional agreement or of these firms and transnational corporations. A key element in this process would be the establishment of regional funds to facilitate these efforts, following the lead of the Science and Technology Fund created at the initiative of Brazil during the South American Summit held in Brasilia in 2000. Funds of this type should also serve to accelerate the transfer of technology to less developed countries.

In the area of physical infrastructure, in addition to harmonized standards on transport, energy and telecommunications, infrastructural and regulatory networks need to be geared to the demands of regional integration. This kind of approach necessarily entails action at a supranational level. An interesting example in this respect was the creation in 1994 of the Association of Caribbean States to promote greater cooperation in the subregion. The physical integration plans agreed upon at the South American Summit of 2000 and the Puebla-Panama Plan are other indications of progress in this area. A number of border-area development plans are also underway that represent a further example of the major shift in spatial perception brought about by integration. This type of approach is also gradually being introduced in initiatives for the promotion of the sustainable development in the management of shared ecosystems (e.g., the Amazon, the Caribbean Sea, the Andean ecosystem and the Meso-American corridor) and shared river basins.

The uniqueness of the Latin American and Caribbean region stems not only from its natural resource wealth and the global importance of the environmental services it provides, but also from the global hazards inherent in the region’s rapid environmental deterioration. It is extremely important for the countries that have taken the lead in the negotiations regarding the region’s contribution to the two most significant issues on the world sustainable development agenda —climate change and biodiversity— to maintain that position. A clear example of this is the region’s role in the international negotiations on the development of the clean development mechanism provided for in the Kyoto Protocol, which could, in addition, generate income for the region.

Special mention should be made of the potential valuation of the environmental services generated by the region’s ecosystems. Projecting the region’s uniqueness, consolidating the regional effort to protect strategic ecosystems and obtaining worldwide support for this initiative represent the starting point for a regional agenda based on the objective of safeguarding the stability of the most important and valuable ecosystems from a global standpoint.

The existing structure of the region’s environmental institutions needs to be gradually reformed, beginning with the consolidation of the role of the Forum of Environment Ministers and the environmental programmes associated with subregional integration schemes, such as the Central American Environment and Development Committee, the Amazon Cooperation Treaty, the environmental agreement of the Andean Community and the Programme of Action for the Sustainable Development of Small Island Developing States in the Caribbean. Efforts must be made to achieve greater coherence in the economic, social and environmental dimensions of these programmes and to develop an agenda that integrates relevant sectoral policies and brings about a convergence of regional and subregional stances in global debates on sustainable development.

In the social sphere, numerous agreements have been reached by the different subregional integration schemes, as well as a number of broader instruments,[10] but the implementation of these provisions is very limited (di Filippo and Franco, 2000). In this respect it appears preferable to set more limited and concrete objectives whose attainment will have a more thorough-going impact. Two areas are particularly important in this respect. The first is support for labour migration. To facilitate the migration of workers and to ensure adequate protection for them and their families, it will be essential to devise means of transferring social security coverage, particularly in the case of health and retirement benefits, from one country to another.

The second is the area of education. Progress can be achieved in this domain by generating regional exchanges and creating networks of experts, governments and organizations that can operate either by electronic communication or in face-to-face meetings. These contacts would allow experts to discuss and share best practices, successful and imaginative experiences, the strengths and weaknesses of reforms, teaching modalities, school computerization programmes and so forth. It is also important to undertake joint measures to generate educational content, software, portals and textbooks; compare educational achievements; set standards by levels; establish criteria for assessing professional qualifications; and implement in-service teacher training programmes. In addition to contributing to the development of the region’s education systems, these initiatives would facilitate the establishment of regional accreditation systems and contribute to the reciprocal recognition of professional qualifications. It is also important to “educate for regional integration” and thus increase people’s awareness of the fact that they belong to a region that has shares a culture, a history and perhaps a common fate. Basic education is the ideal sphere is which to instil an awareness of regional identity and put an end to xenophobia.

A final point to be made here is that the “democratic clauses” included in integration agreements, the various forums for the region’s Heads of State, and the nascent subregional and Latin American parliaments together provide the cornerstone for a broad agenda of political integration that is as yet in its infancy.

IV. The global agenda

Globalization is a multidimensional process. A detailed examination of some of its dimensions —such as its political or cultural aspects, for example— goes beyond the bounds of this study, however. The analysis of the global agenda presented in this section and in part II is not, therefore, intended to provide a comprehensive treatment of the subject. As a case in point, the discussion on global public goods focuses on just two —the international macroeconomic order and sustainable development— out of a wide range of subjects referred to in the introductory portion of this chapter. The importance that ECLAC places on the correction of international asymmetries, on the other hand, justifies a more detailed consideration of this issue’s three main dimensions: financial and macroeconomic aspects, production and technology, and the international mobility of labour. The chapter concludes with a series of observations regarding the development of a rights-based international social agenda.

[10] There are, in fact, agreements on individual and collective guarantees for migrants, modalities of representation of corporate interests (businesspeople, workers, professionals, consumers), labour mobility and provision of health services in border areas, standardization of educational and professional credentials, and validation of pensions.

1. Provision of global macroeconomic public goods

In recent years there has been a growing awareness of the fact that international financial and macroeconomic stability is a global public good which generates positive externalities for all international market participants and precludes negative externalities associated with contagion, whether from “irrational exuberance” (to use the term coined by Alan Greenspan, Chairman of the Federal Reserve Board), or from financial panics and recessionary impulses in general.

Hence the importance of taking global action on a number of fronts. The first is to build institutions capable of ensuring the global coherence of the major economies’ macroeconomic policies. The lack of mechanisms for fully internalizing the effects that those policies have on the rest of the world is one of the main defects of the existing international order. When policy inconsistencies are manifested in the volatility of exchange rates for the major currencies, they generate additional adverse spillovers for developing countries. IMF should play a central role in efforts to coordinate the major economies’ macroeconomic policies. The scope of such an initiative will extend beyond the bounds of the dialogues being conducted in more restricted arenas, such as the G-7 forum.

The second front is macroeconomic surveillance of all economies with a view to prevention and the formulation of codes of good practice for macroeconomic management (in particular with regard to fiscal and monetary policy, public and external debt management, and management of international reserves). A great deal of headway has been made in recent years, and this is reflected in the greater emphasis that the Fund is placing on prevention in its Article IV consultation process, on monitoring financial markets and on constructing vulnerability indicators or early warning systems.

Work on the formulation of international standards for the prudential regulation and supervision of financial markets and on the provision of market information has also been moving ahead. Although this is clearly a third line of action for ensuring international macroeconomic stability, efforts in this area have come under criticism on a number of counts: (i) the lack of participation by developing countries in the formulation of such standards; (ii) the tendency to standardize such regulations without taking into account differences in the individual countries’ regulatory traditions and absorption capacities; (iii) the attempts made to tie IMF financial assistance to compliance with codes and standards about which no international consensus has been reached; (iv) the limited attention devoted to such topics as the regulation of institutional investors operating in developing countries, direct regulation of highly leveraged activities, and operations in derivatives markets; and (v) the failure to devote sufficient attention to the regulation of rating agencies, whose evaluations have proven to be highly procyclical and have come under severe criticism. Thus, as the process of designing international standards proceeds, steps must be taken to rectify these situations.

An even more complex issue is the lack of initiatives for the design of international standards in respect of capital flows to developing countries. Because of the residual nature of these markets in global terms, they are not a central regulatory concern for the industrialized countries. Their regulation therefore tends to be covered by general standards that could have the effect of drastically reducing flows and/or raising borrowing costs unduly. The idea of giving rating agencies a major role in the industrialized countries’ regulatory systems by extending the application of a rule now used for institutional investors to include commercial banks could create similar difficulties, given the procyclical nature of risk ratings. These issues have been widely debated as part of the discussion of the Basle Committee banking reforms. Care should therefore be taken to ensure that any new regulatory measures that are adopted do not exacerbate the existing system’s discrimination against capital flows to developing countries (Reisen, 2001: Griffith-Jones and Spraat, 2001).

Although, strictly speaking, it does not correspond to the definition of a global public good, international cooperation in relation to issues of taxation is of growing importance, since the tax system is necessarily involved in obtaining a sufficient volume of public resources to finance the provision of an adequate supply of national, regional and global public and *merit goods* (Zedillo et al., 2001; FitzGerald, 2001). Competition for footloose investment has tended to result in the reduction of capital taxes and this, in turn, has either diminished the public sector’s ability to generate resources or driven up the direct or indirect tax burden for less mobile factors of production, especially labour. Given these circumstances, steps should be taken to promote information-exchange agreements among tax authorities, double-taxation accords and other agreements of a broader scope aimed at avoiding tax competition, coordinating measures to combat tax evasion and, eventually, harmonizing tax systems. The treatment of offshore centres warrants particular attention in this respect.

The international institutional structure in this field is virtually non-existent. Consequently, in addition to new agreements, it may be necessary to create a new organization to foster international tax cooperation. Subregional or hemispheric agreements and the expansion of cooperation activities already being pursued by OECD with non-member countries are intermediate options that should also be explored.

2. Sustainable development as a global public good

The 1992 United Nations Conference on Environment and Development was clearly a milestone in the formulation of a global agenda for sustainable development, since it marked the birth of a political consensus of the highest level. This was the beginning of the transition towards a new international environmental regime based on a new generation of environmental conventions and a global programme of action. Agreement was also reached at that time on new principles that would provide a more equitable foundation for international cooperation. Although the international community took up these agreements enthusiastically, this initial momentum began to wane as the decade wore on. Yet 10 years after this conference was held, the principles that were defined there are still very much alive. The World Summit on Sustainable Development to be held in Johannesburg in 2002 should open up new opportunities for making the global agenda more cohesive, strengthening its implementation and forming operational linkages with regional and national agendas.

Some of the most critical items for inclusion on the global agenda which are now being discussed at the international level (United Nations, 2002a; ECLAC/UNEP, 2001) are, first of all, the need to modify unsustainable consumption and production patterns in both developed and developing countries. In this connection, energy efficiency is certainly one of the core issues on the agenda. Clearly, one of the goals here has to be the formation of a world alliance for the use of renewable energy sources and clean, energy-efficient conventional technologies. The Kyoto Protocol is the ideal multilateral instrument for driving this strategy forward. The recent agreements reached at Bonn and Marrakesh, which elaborate upon the Protocol, give reason for cautious optimism regarding the implementation of the clean development mechanism, which, with one prominent exception, has received the support of the entire international community. This mechanism represents the first material expression of a market for global environmental services which should be expanded upon in this and other fields in the future. The negotiation of energy agreements should form part of a broader range of activities designed to promote eco-efficiency and the use of clean technologies at the global level. Progress in this area can be furthered by commitments on the part of transnational corporations to help work towards these goals, the extension of voluntary international standards (ISO 14000), technology transfers to developing countries, and assistance for small and medium-sized enterprises.

Another important sphere of action is the sustainable management of ecosystems and biodiversity. In this case the idea would be to form a global partnership to build a stronger worldwide commitment to the *in situ* conservation of biodiversity and the relevant ecosystems. The efforts of such a partnership, which would be based on quantitative targets and specified means for achieving those aims, would be guided by the core objectives of the Biodiversity Convention. In order to ensure the effective implementation of these initiatives, a multinational clearing house and fund should be set up to finance the conservation and restoration of ecosystems and to identify the global environmental services generated by priority natural ecosystems. This will also entail generating synergies among multinational and regional instruments and conventions dealing with the protection and sustainable use of biodiversity and ecosystems. In relation to the issue of genetic resources, the Cartagena Protocol on Biosafety should be ratified, and approved mechanisms should be employed to assess the possible risk to biodiversity posed by the introduction of genetically engineered living organisms.

Such mechanisms can only be developed if adequate financing for sustainable development can be ensured. To this end, operational strategies are needed for mobilizing global resources to address global problems based on the principle of common yet differentiated responsibilities. The possibility of imposing international levies on environmentally harmful activities that are global in scope should be explored; the revenues obtained from such levies could be paid into special funds that could then be used to find multilateral solutions for those problems. Another possibility would be to apply instruments similar to the clean development mechanism in other fields of activity. This approach could be used to develop genuine global markets for environmental services based on a flexible interpretation of principle 16 of the Rio Declaration on Environment and Development (the "polluter pays" principle) that would permit mitigation actions to be carried out in geographical locations other than the pollution site.

Education, research, development, technology transfer and adaptation, and access to information will play an increasingly vital role in the achievement of sustainability. In Given the existing evidence of the world's increasing ecological fragility owing to cumulative environmental damage on a variety of scales, the precautionary principle is taking on new meaning. Environmental protection efforts are no longer enough; the need for adaptation and mitigation and, above all, for scientific and technological developments to meet new challenges is constantly on the rise. Within this context, mechanisms for protecting intellectual property —including both formal knowledge and informal traditional knowledge— are of particular importance.

The foregoing considerations underscore the need for greater coherence and compatibility between the international trading system (including the protection of intellectual property) and the cause of sustainable development. The declaration issued at the fourth WTO Ministerial Meeting at Doha (November 2001) represents a major stride forward in this respect, since it explicitly acknowledges the need to analyse the interrelationship between WTO rules and multilateral environmental accords. It states in no uncertain terms that countries that wish to adopt measures to protect human, animal or plant health and/or the environment may do so provided that the provisions in question do not constitute discriminatory trade practices or hidden protectionism. In addition, it identifies priority issues for consideration by the WTO Committee on Trade and Environment, including the analysis of environmental measures' impact on market access, particularly in the case of developing countries; provisions referring to the agreement for the protection of intellectual property; and environmental labelling.

3. The correction of financial and macroeconomic asymmetries

Apart from the "systemic" issues relating to global macroeconomic and financial stability which have been discussed in earlier sections, international financial reform efforts should focus on correcting basic financial and macroeconomic asymmetries in the international economic system. This task should be addressed on a comprehensive basis that includes macroeconomic surveillance, the regulation of capital flows, the provision of liquidity during crises, the design of multilateral schemes for dealing with debt overhangs, measures for strengthening multilateral development banks and the achievement of a new consensus regarding the scope of the conditionality applied to official international resources. The aims of this comprehensive effort should be to reduce the segmentation and volatility of developing countries' access to international financial resources and to provide more scope for the adoption by developing countries of countercyclical macroeconomic policies.

A comprehensive approach of the nature suggests that macroeconomic surveillance actions taken by IMF and complementary regional institutions (see section III) should be explicitly oriented towards prevention, i.e., towards preventing the accumulation of imbalances and high-risk debt profiles during economic booms. Programmes undertaken by IMF in conjunction with multilateral banks and with the Bank for International Settlements to support the formation of more solid financial systems in developing countries is a key component of this task. Clear incentives should also be provided for compliance with strict, preventively oriented macroeconomic and financial standards, particularly with regard to automatic access to IMF contingent credit lines during crises. For development banks, this approach will entail the design of credit lines for the express purpose of encouraging developing countries to adopt countercyclical forms of economic management.[11]

From a regulatory standpoint, the main objective should be to reduce the risk associated with operations involving countries whose net borrowings (especially of short-term resources) are disproportionate to the size of their economies and financial sectors. The object here is to discourage high-risk financing at its source. This may require the application of special standards to financial operations with developing countries, rather than the general types of standards that have been designed with a view to industrialized markets. More specifically, rating agencies' risk assessments should not be used for regulatory purposes; these agencies should, however, be regulated themselves and should be required to rate sovereign risk on the basis of objective, publicly known criteria.

Developing countries should, for their part, maintain full autonomy in the management of their capital accounts. International financial agencies should analyse regulatory experiences in this area very carefully and should encourage countries to take steps to constrain external borrowing during booms whenever it becomes apparent that these booms or current account deficits are unsustainable.

Meanwhile, IMF should gradually evolve into a quasi-lender of last resort at the international level. This entails the use of special drawing rights (SDRs) as its main financial instrument. The additional demand for Fund resources during crises should be met with temporary issues of SDRs rather than by means of existing special arrangements to borrow, which are made available at the discretion of a handful of industrialized countries. In the long run, SDRs should be used as a multilateral tool for meeting additional liquidity requirements associated with the growth of the world economy.

In implementing adjustment programmes during crises, the authorities should take account of how they will impact the most vulnerable sectors of the population. The application of this

[11] One of the possible options here would be lines of credit in which national counterpart funds are "saved" in the banks during booms and are then disbursed, together with the banks' contributions, during crises. Another would be the disbursement during crises of lines of credit having accelerated amortization clauses based on specified macroeconomic variables.

principle, which has gained growing international acceptance in recent years, should extend beyond the creation of social safety nets to include the design of macroeconomic adjustment policies themselves. This approach will help ensure a policy mix having the least possible social impact on the poorer sectors of the population (United Nations, 2001a).

Dealing with problems of moral hazard requires preventive macroeconomic surveillance and a sound regulatory scheme. An additional element that is not yet part of the international order would be a suitable mechanism for handling debt overhangs. Although such schemes may be used to manage liquidity problems, there are other more effective tools that have been used in the past for this purpose. One approach is for the regulatory authorities in industrialized countries to bring pressure to bear on banks to keep the relevant countries' lines of short-term credit open. This should, in any case, be the aim of IMF emergency financing. In fact, in the absence of a good emergency financing scheme, problems of illiquidity may turn into problems of insolvency. This is why debt workout mechanisms should be seen as a supplement rather than as a substitute for emergency financing, whose main purpose is the management of solvency problems.

The chief components of this new mechanism should be: (i) collective action clauses to facilitate negotiations with creditors; these clauses should be universally applied to avoid creating a new factor of discrimination against developing countries; (ii) an internationally sanctioned (perhaps by the Fund) standstill mechanism; (iii) voluntary negotiations among the parties regarding public and private external liabilities; these negotiations could be backed up by mediation —and perhaps international arbitration— mechanisms administered either by a new agency or by a panel of experts convened by IMF; (iv) preference in the restructuring process for private financing extended during crisis periods and, in some cases, a requirement that additional resources be provided; and (v) credit from multilateral lending agencies during the renegotiations and the period immediately following their conclusion. In this last case, the focus should be on expediting the countries' re-entry into private capital markets; the most suitable instrument for this purpose may be a system of guarantees backed up by a special fund to be managed by the major development banks.[12]

Maintaining a strong multilateral development banking system is another component of this strategy. These banks have proven to be essential not only in guaranteeing financing to countries lacking access to financial markets, especially the poorer nations, but also in providing long-term financing to middle-income countries when credit on private markets dries up. The countercyclical role played by multilateral lenders —which includes support for programmes to protect the most vulnerable sectors of the population during crises— should not be confused with the provision of liquidity, which is the central objective of IMF actions. A more active use of guarantees to leverage private resources during these periods may be the best course of action. Multilateral banks perform a number of other functions as well: the promotion of innovative activities, especially in relation to social development and private participation in infrastructure projects; support for financial deepening in developing countries and for national development banks' efforts to promote that process; technical assistance in general; and support for the provision of global public goods in coordination with United Nations bodies.

The final element in this integral approach is a new international agreement as to the scope of conditionality. The aim here is to provide a strong foundation in international practices for macroeconomic and development policy ownership. Some progress has been made in this respect, as indicated by the analysis and discussion of this question that occurred within the Fund in 2001. As noted earlier, however, new forms of conditionality sometimes lurk behind words of support for the concept of ownership. Hence the importance of an explicit international agreement on this question. Given the tendency for homogenous views to predominate within international lending agencies, a public debate regarding their visions of development is an essential control mechanism

12 For a more exhaustive discussion of this topic, see UNCTAD (1998 and 2001), Krueger (2001) and Machinea (2001).

and an important exercise in order to make the diverse range of development options a reality (Stiglitz, 1999). Even with such a debate, however, a greater plurality of views within these institutions may well be necessary in order to counter the strong inclination towards institutional homogenization exhibited by these agencies during the past two decades.

4. Overcoming production and technological asymmetries

The transmission of production and technological impulses from the industrialized world to developing countries involves two basic processes: the gradual transference of raw material production, mature industries and demand for more standardized services to developing countries; and technology transfer and developing countries' increasing participation in its generation and in higher-technology branches of production. The international trade agenda should be directed towards the first of these aims, but in the long run, it is the second type of process that will lead to the actual elimination of international asymmetries.

The main items on the trade agenda are well known (UNCTAD, 1999a, Third World Network, 2001; World Bank, 2002b). The first is a broad liberalization of world agricultural trade that includes a phase-out of export subsidies, a substantial reduction in the sizeable production subsidies provided in industrialized countries, the lowering of tariffs on these products and the gradual elimination of the tariff-quota system (which, in practice, amounts to a system of quantitative restrictions). The second is the successful dismantlement of the Multifibre Agreement provided for in the Uruguay Round agreements, together with the reduction of tariff peaks and tariff escalation based on processing levels. The third is the industrialized countries' liberalization of the supply of labour-intensive services (e.g., construction and tourism) in order to permit temporary migration by all categories of labour for the provision of those services. The fourth is the establishment of stricter multilateral antidumping disciplines and guarantees for full observance of the ban on voluntary export restrictions agreed upon in the Uruguay Round.

In addition to these priority objectives, steps need to be taken to ensure broader participation by developing countries in the design of technical standards of all sorts and to facilitate a wider use of WTO dispute settlement mechanisms, whose development was one of the most important improvements made in the multilateral order during the 1990s. Because of the high cost of maintaining negotiating teams and of using the institutional mechanisms that have been established, all of this depends on the proper organization of the smaller and poorer countries' teams, on the existence of legal instruments to backstop dispute settlement procedures involving these countries and on the provision of multilateral resources to finance these procedures.

Above and beyond all these considerations, the international community must realize that strategies for creating systemic competitiveness are a key component of development processes. To this end, the Uruguay Round maintained certain degrees of freedom for import substitution (by means of specified levels of protection and the infant industry principle) and for adjustments in such industries to cope with competition (safeguards), but it significantly reduced the scope of action for middle-income countries' export promotion policies. Disciplines were established for export subsidies and trade-related investment measures were prohibited (performance agreements and local content rules), which reduced the range of discretionality in the active promotion of "infant export industries" and export diversification in general. As in other fields, as a general rule the agreements tend to allow the types of subsidies most commonly used by industrialized countries (subsidies for technology, regional development, environmental protection) while restricting those most frequently employed by developing countries (free trade zones, direct subsidies for export activities, performance agreements). Although the conversion of incentives to bring them into line with the results of the Uruguay Round should continue to be a priority for developing countries, the discussion of policy options available to the countries, especially for diversifying their exportable supply, should be accorded a high priority in the Development Round that began in Doha in late 2001.[13]

Multilateral talks on trade in goods and services are being pursued in Latin America and the Caribbean concurrently with a number of other negotiation processes that are being conducted with industrialized countries by the region as a whole, by subregional blocs and on a bilateral basis. Negotiations with the United States and Canada and the talks being held with the European Union are cases in point. These processes are particularly important because they are directed towards going beyond the bounds of the preferential schemes existing for various subregions (which, by definition, do not constitute permanent commitments) in order to ensure untrammelled access to the major industrialized markets. These negotiations also cover other issues, most notably the protection of investment and intellectual property.

In line with the above considerations, the agreements emerging from these negotiations should guarantee the priority trade objectives discussed here, while also maintaining the developing countries' autonomy to adopt active competition policies focusing, in particular, on the diversification of the export base. Issues relating to the protection of intellectual property will be discussed in a later section.

The Free Trade Area of the Americas is the most ambitious initiative in this area, since its goal is to create the world's largest zone of this type. In addition, it will encompass countries of widely varying levels of development and size. From a strictly commercial standpoint, since the average tariff levels of the United States are already quite low (under 2% as of 2000) and nearly three fourths of the region's exports enter the United States market duty free (ECLAC, 2002), the greatest potential gains for the Latin American and Caribbean countries would be the rollback of tariffs on some heavily protected products (agricultural produce, textiles and wearing apparel, in particular) and, most importantly, the elimination of non-tariff barriers, such as the discretionary use of antidumping provisions.

The inclusion of means of dealing with the widely varying levels of development and sizes of the economies covered by this agreement will be essential, both during the transition period and once it is fully implemented. In the first case, a decisive element will be the provision of technical assistance and funding for the reengineering of production activities so that they can meet the challenges posed by the agreement. In the second, it is important for the countries of the region to maintain the necessary autonomy to adopt active competition policies.

The evidence presented in the preceding chapters indicates that free trade is not in itself enough to guarantee convergence of the countries' levels of development. Past experience suggest that at least two other types of policies are also necessary. Both, it should be said, have played a significant role in the past in bringing about the convergence of income levels in industrialized countries and in the most comprehensive integration process undertaken by the United States with a Latin American economy (i.e., the case of Puerto Rico) (see box 4.1). The first is a policy to promote greater international mobility for labour. This subject will be discussed later on. The second is a policy of transferring resources from the more advanced regions to the less developed ones for the express purpose of bringing about a convergence of development levels. In the case of Puerto Rico, this policy also included generous tax incentives for investment in the island.

[13] Article 10.2 of the Declaration of Doha "Takes note of the proposal to treat measures implemented by developing countries with a view to achieving legitimate development goals, such as regional growth, technology research and development funding, production diversification and development and implementation of environmentally sound methods of production as non-actionable subsidies…". Strictly speaking, the only major restriction in the Uruguay Round agreements is the provision relating to the "diversification of production" and, more specifically, of exportable supply, since subsidies for the other purposes identified therein are broadly authorized in the Marrakesh Accords.

Box 4.1
ECONOMIC LINKS BETWEEN PUERTO RICO AND THE UNITED STATES MAINLAND

The economies of Puerto Rico and of the United States mainland are closely integrated. Puerto Rico shares a common citizenship, defence force, currency and market with the United States, and there is free movement of goods and factors of production between the two. Unlike a sovereign State, Puerto Rico's government does not engage in activities such as coining money or levying duties on imports or exports. It thus forms an economic union with the mainland.

The basic pillars of the development strategy, known as Operation Bootstrap, that Puerto Rico launched in the 1940s were tax incentives, tax credits against federal taxes on income earned by United States corporations in the island (section 936 of the United States Internal Revenue Code, which is now being phased out) and guaranteed free trade with the mainland. Encouraged by these tax incentives, many corporations operating in Puerto Rico chose to retain their profits and deposit them with financial institutions on the island, thereby providing an important source of liquidity for financial intermediaries. A decade ago, 936 funds —as they are called— amounted to about US$ 10 billion and represented around one third of total commercial bank deposits. By the year 2000, 936 funds made up approximately 5.9% of total commercial bank deposits.

Federal transfers have also played a key role in Puerto Rico's economy, although their relative size has been declining over time. In 2000, total federal transfers comprised 20% of GDP. Transfers to persons amounted to US$ 5.5 billion, or 14.3% of personal income (down from 22% of personal income in 1990). About 60% of these transfers were earned benefits, including veteran's pensions, Medicare and social security payments. Grants, which primarily consist of payments made under the food stamp programme, amounted to 39% of federal transfers to persons.

In addition to trade and capital flows, labour also moves freely between Puerto Rico and the mainland, with thousands of Puerto Ricans commuting seasonally. In 1950, Puerto Rico's resident population amounted to 2.21 million, and 226,000 Puerto Ricans who had been born on the island were living on the mainland. By the year 2000, these figures had risen to 3.8 million and 1.2 million, respectively.

Operation Bootstrap spurred robust industrial growth which transformed Puerto Rico's agricultural base into a manufacturing- and services-driven economy. Between 1950 and 1990, the island's GDP grew by 4.4% a year, and the manufacturing sector's share of total output expanded from 22% to 39%. Convergence with the mainland's living standards has, nonetheless, been partial. By 1990, per capita income in Puerto Rico (US$ 6,000) was almost half that of Mississippi's, the state of the Union with the lowest income; this was, nevertheless, an improvement over 1950, when Puerto Rico's per capita income was 39% of that of the lowest-ranking state. As of 2000, however, per capita personal income in Puerto Rico (US$ 10,150) was still close to half that of Mississippi's.

The European Union has clearly been the international arena in which this principle has been upheld most forcefully, thanks to the Union's social cohesion policy. It is symptomatic of the political philosophy underlying these accords that the deepening of economic integration processes seen during the final decade of the twentieth century was accompanied by the increased use of an explicit policy of cohesion (Marín, 1999). What is more, this policy now also embraces the Central European countries that hope to join the Union. The possibility of setting up a cohesion or integration fund to provide the necessary backing for hemispheric agreements was put forward by a number of Heads of State at the Summit of the Americas held in Quebec in April 2001[14] and therefore warrants special attention.

The expansion of the World Trade Organization's negotiating agenda to include new issues has been the subject of a great deal of debate. ECLAC fully acknowledges the need for a firm commitment on the region's part to the international environmental agenda, the enforcement of fundamental labour rights and principles, and the International Covenant on Economic, Social and Cultural Rights. It also, however, shares the view that such commitments pertain to other spheres of international action and should not be linked to commitments relating to international trade.

A multilateral investment agreement could help to simplify the complex network of bilateral and regional accords that have been signed in the past few years, but it would need to meet three basic requirements: its scope would have to be confined to protecting investment; it would have to maintain the developing countries' autonomy in regulating their capital accounts for macroeconomic purposes; and it would have to maintain their autonomy in adopting active policies on FDI, including policies designed to improve the linkages between FDI and national production. It would also be useful to work towards a global competition agreement that would rein in the strong trend towards international concentration in some branches of activity, as well as the anti-competitive practices of some large transnational corporations.[15] In the long run, a mechanism of this type might also serve as a framework for the development of substitutes for more discretionary forms of intervention (such as antidumping provisions). It is not certain, however, that WTO would be the most suitable framework for the conclusion of multilateral investment or competition agreements, and it is even more debatable whether it would be the appropriate agency to implement agreements in these fields. It may well be preferable to create a new international organization which, in addition to agreements in these two areas, could also be responsible for implementing agreements on intellectual property and trade-related investment. WTO could then focus its full attention on the regulation of trade in goods and services.

Another controversial aspect of the Uruguay Round agreements has been the application of multilateral intellectual property disciplines to all WTO members. While this agreement may appear to be essential to ensure the provision of a global public good (the creation of knowledge), the fact remains that this is being accomplished through the concession of a temporary monopoly, i.e., by defining what is potentially a public good as a private good. Since technological development is the activity that is most highly concentrated in industrialized countries, this form of protection —and the redistribution of resources that it entails— reinforces one of the basic asymmetries existing in the international economy.

Given the high cost that this mechanism may have for developing countries, the World Bank (2002b, Chap. 5) has recently stated that its benefits for low-income countries are not clear and that the agreement's implementation should therefore be conducted gradually and should be geared to each country's level of development. Middle-income countries certainly do derive benefits from greater protection of intellectual property for appellations of origin, for intra-industry trade that relies on trademark protection, for cinematography and television, for software and in a number of other cases. This type of protection is also important in providing guarantees for foreign investment and as a means of ensuring that consumers will have secure access to a wide range of products. At the same time, however, the protection of intellectual property raises the cost of technology and

[14] The President of Mexico made particular reference to the possibility of a cohesion fund, and a number of prime ministers from the Caribbean drew attention to the importance of having an integration fund. The Government of Ecuador, which is currently responsible for coordinating the negotiations, later proposed that a fund be established to promote competitiveness.

[15] A *de minimis* clause could be introduced to stipulate that the relevant agreement applies only to firms that have international market shares above a given percentage.

may block technology transfers if the country affording such protection does not produce the good or use the technology in question.

The agreements reached at the fourth WTO Ministerial Meeting represent a major stride forward in the definition of one of the cases —public health— in which the net effects of the protection of intellectual property can be quite harmful. The main problem in this case is that protection can drive up consumer prices so much that large sectors of the population cannot afford the goods or services in question. This case serves to illustrate a broader principle: that the public good represented by knowledge should, under certain circumstances, prevail over the private good whose intellectual property is protected.

This opens the door for a broader discussion of fields in which the public good represented by knowledge should predominate. Some of the most obvious cases are those in which potentially patentable knowledge is scientific knowledge in a strict sense (certain types of knowledge about genetics are one good example) or in which access to certain types of knowledge is the basis for the acquisition of new knowledge (this principle is recognized, for example, in the International Convention for the Protection of New Varieties of Plants, which guarantees access to protected varieties for use as breeding stock for the development of other new varieties). Actually, inasmuch as technological development is the result of a cumulative learning process and relies heavily on acquired experience in the production domain, this last case is part of a larger set of instances which include secondary innovations derived from the adaptation of technology and reverse engineering.

The problem that arises in such cases is all the more serious when a country's priorities in terms of the diversification of its production activities conflict with the protection of intellectual property owned by firms that do not produce the protected good or use the protected technology in that country. In such instances, the protection of intellectual property stands in the way of the country's development objectives. In such cases, as in that of public health, a new consensus has to be reached regarding the limitations that should be placed on the protection of intellectual property or more comprehensive regulations will have to be designed regarding the use of compulsory licenses or the exhaustion of intellectual property rights (see chapter 7).

Another series of problems have to do with aspects of the intellectual property rights agenda that are of interest to developing countries but that have not been properly applied or set down in agreements. One such problem is raised by the need for effective technology transfer mechanisms and means of ensuring greater participation by developing countries in the generation of new knowledge. WTO should accord priority to devising these kinds of mechanisms and instruments, since they are needed to counterbalance the adverse distributional effects at the global level produced by the protection of intellectual property. Another problem refers to the relationship between the protection of intellectual property and the Biodiversity Convention and to the protection of traditional knowledge, including folklore. These considerations also draw attention to the pressing need for the countries of the region to take an inventory of the resources they wish to protect at the international level in order to defend their cultural, intellectual, genetic and geographic heritage.

5. Full inclusion of migration on the international agenda

The full incorporation of the issue of migration on the international agenda is another essential element in the formation of an international system capable of overcoming the asymmetries of the global order. There is no theoretical justification whatsoever for liberalizing goods, services and capital markets while continuing to apply stringent restrictions to the international mobility of labour. Moreover, asymmetric market liberalization clearly has a regressive impact at the global level, since it works to the benefit of the more mobile factors of production (capital and skilled labour) and to the detriment of the less mobile factors (unskilled labour). This constraint also nullifies one of the mechanisms which historical studies identify as having played a fundamental role in the convergence of income levels in today's industrialized countries (see chapter 3). In addition, placing greater restrictions on the mobility of unskilled labour selectively siphons off human capital from developing countries, tends to accentuate skills-based income inequalities, and sets the stage for one of the most harmful industries in the world of today: the smuggling of migrants and other persons. Apart from its significance as an economic factor, migration is a very important source of mutual cultural enrichment and contributes to the formation of a cosmopolitan society.

One of the priority items on the international agenda should therefore be to forge agreements that will increase labour mobility and strengthen the governance of international migration. The main objective here should be the conclusion of a global agreement on migration policy. The scope of existing instruments is, for the most part, quite limited. The broadest instrument of this type (but one that is still awaiting ratification) is the International Convention on the Protection of the Rights of All Migrant Workers and Members of their Families, which was approved by the United Nations General Assembly in 1990. The importance of securing the ratification of this convention lies in its reaffirmation of fundamental guarantees for the human rights of migrant workers and their families, including those who lack proper documentation. It also provides States with a legal instrument that facilitates the development of a uniform system of national legislation.

A closely related element is the reduction of the risks associated with discrimination and xenophobia through ratification of the relevant international instruments and compliance with the plan of action signed at the World Conference against Racism, Racial Discrimination, Xenophobia and Related Intolerance held in Durban, South Africa, in 2001.

Broadening the commitments made in regard to temporary mobility of workers within the framework of the WTO General Agreement on Trade in Services is another important objective. As stated earlier, one of the priorities in this area is to secure greater commitments on the part of industrialized countries with respect to services that are intensive in low-skilled labour, in which developing countries may have comparative advantages.

There is no question about the fact that migration issues should be included on the hemispheric agenda, in multilateral agreements reached between the Latin American and Caribbean region and the European Union, and in regional integration processes. There is also a wide range of bilateral conventions and negotiations that can help to increase the opportunities for international migration. One promising example is the recent commencement of a dialogue between Mexico and the United States on this subject. All of these multilateral and bilateral agreements should seek to increase temporary and permanent labour mobility and to move forward on issues closely related to migration, such as social security and the recognition of individuals' academic and professional or vocational qualifications.

In addition to their efforts to do away with xenophobia and discrimination and to guarantee immigrants' rights, host-country governments should take steps to help migrants become fully integrated into society. This is, in fact, essential in order to ensure the social cohesion of societies in which there are a large number of immigrants. To this end, States should set up mechanisms to facilitate immigrants' access to, among other things, public education and social services in order to ensure their integration and help give them greater economic and social rights. The other side of the coin is for immigrants to respect and integrate themselves into their host culture and to fully comply with the host country's laws.

The home countries of migrants can also benefit from this process in various ways. First of all, they receive remittances, which have become an important source of capital flows for many countries of the region. Reducing remittance transfer costs, promoting programmes that provide emigrants with means of contributing to their home communities and using these resources in productive ways are some of the types of action that could be taken on this front. Links with emigrants can also be used to give their home countries the benefit of their scientific, professional and entrepreneurial skills, as well as to create a market for idiosyncratic products. The countries of the region should also recognize the right of emigrants to take part in their home countries' political processes.

Finally, it is the responsibility of home and host countries to work together to combat the smuggling of migrants. Their efforts in this area should include communication programmes in communities of origin to warn the population of the dangers of such practices.

6. Economic, social and cultural rights: the foundations for global citizenship

One of the main advances associated with the globalization process in recent decades has been the worldwide propagation of values or principles such as respect for human rights, equity, democracy, respect for ethnic and cultural diversity, and environmental protection. Some of the most important principles relating specifically to social development are those set forth in the International Covenant on Economic, Social and Cultural Rights, whose signatories are committed to guaranteeing their citizens a set of goods and services regarded as essential in order for them to lead decent lives. The Covenant identifies the formulation of an international social agenda with the recognition of all members of global society as citizens and, hence, as possessing certain rights. Viewed from another vantage point, the goods and services required to obtain a basic level of well-being are both rights and commodities —"merit goods," to use the terminology of welfare economics. And as such, the societal regulation of these goods is a necessary element in guaranteeing their supply, verifying the progress made in their development and ensuring that claims on such goods are enforceable (ECLAC, 2000a). This process should be regarded as the core element of a holistic anti-poverty programme.

Economic, social and cultural rights, together with civil and political rights, form an indivisible, interdependent whole. It is recognized, however, that the exercise of economic, social and cultural rights is not automatic and that their progressive enforcement will require a determined economic and political effort. This effort is reflected in democratic processes aimed at determining what level of nutrition, health care, education, housing and other rights/merit goods can be supplied on a sustainable basis to all citizens, what (public, private or mixed) mechanisms should be used to supply them, and what level of public resources will be needed to do so.

This necessarily entails a political process leading to the formation of national —but increasingly global— social and fiscal covenants in which access to such goods is seen as the result of a political decision regarding the allocation of resources for guaranteeing citizens' civil rights. These covenants should be shaped by a political debate on the role of the State and the relationship between economic policy and social development —a debate that can ultimately result in a consensus on the relevant priorities and the feasible pace of progress towards the gradual achievement of those rights/merit goods.[16]

Upholding these rights continues to be an essentially national responsibility, however. No clearly defined, stable international policies or mechanisms have yet been devised that would allow countries' aspirations or accomplishments to transcend their national boundaries. Moreover, guaranteeing such rights is the job of the State and does not explicitly involve other important agents, such as business enterprises. Yet another consideration is that there is thus far no clear incentive for the enforcement of these rights, nor methods to ensure their application.

Consequently, the enforceability of economic, social and cultural rights needs to gradually move from regional and national evaluations to a much more clearly defined political enforceability

[16] One of the priority courses of action in this regard is the compilation, dissemination and analysis of information on the status of economic, social, cultural and other rights and the fulfilment of goals agreed upon at world summits with a view to determining priorities, creating a culture of responsibility and bringing about policy changes.

within the context of international forums and, most importantly, representative national forums where international assessments of the countries' fulfilment of their commitments can be discussed. This type of evaluation should be a comprehensive one that includes not only these rights, but also other internationally recognized social rights (the Fundamental Principles and Rights at Work agreed upon within the framework of ILO, the rights of children, women and ethnic groups) and the commitments made at world summits dealing with closely related issues. This political enforceability can gradually lead, under certain conditions, to a legal enforceability within the context of the corresponding national and international courts. The commitments undertaken and their enforceability must at all times be commensurate with each country's level of development and, in particular, its ability to achieve target levels that can be effectively guaranteed for all its citizens, thus avoiding the emergence of voluntarism or populism.

Given the sharp inequalities and asymmetries of the global order, an essential element in the material expression of such rights is the fulfilment of the ODA commitments made within the framework of the United Nations (0.7% of industrialized countries' GDP, with a minimum of 0.15%-0.20% of GDP going to the least developed countries) and adherence to the basic guidelines agreed upon by the international community (i.e., the priority of the effort to combat poverty, and ownership of economic and social development strategies). Within this context, development cooperation should be regarded as a means of supporting rights-based efforts to build democracy, promote civil and political rights, and eliminate poverty. International undertakings such as the "20/20 initiative" are an important step in this direction.[17] Since a global effort of this magnitude will clearly take quite some time to complete, regional or subregional integration programmes can serve as a much-needed intermediate stage in the process.

The responsibility for upholding rights and for their development and application transcends national boundaries and the purview of the State, however. Partnerships will therefore have to be formed with many different actors. The United Nations' awareness of this fact has led it to formulate the Global Compact, which calls upon the entrepreneurial sector in all countries to uphold human rights in business practices and to support suitable public policies on human rights, basic labour rights and environmental protection.[18] This type of initiative, and others undertakings on the part of civil society, can contribute to the consolidation of a genuine rights-based culture, which is the very essence of global citizenship.

[17] For an evaluation of this initiative as it relates to the countries of the region, see Ganuza, León and Sauna (2000).
[18] See www.unglobalcompact.org.

Part II: Regional outlook

Chapter 5

External vulnerability and macroeconomic policy

The volatile capital flows characteristic of the third phase of globalization have brought major instability to economic growth in Latin America and the Caribbean, and the authorities have found it hard to keep the real economy on course in the face of sharp variations in international liquidity. This reflects problems arising from the procyclical macroeconomic management that has become widespread across the region, and also the absence of an international financial architecture capable of correcting the financial-market instability and the glaring asymmetries that exist in financial development and macroeconomic behaviour between developed and developing countries.

This chapter analyses the relation between the new forms of external vulnerability stemming from volatile capital movements, and macroeconomic policy. The first two sections focus on external funding sources available to Latin American and Caribbean countries, and the way fluctuations in such financing have combined with procyclical macroeconomic policies to produce the sharp and pronounced business cycles that were such a feature of the region in the 1990s. Based on these considerations and those discussed in the previous chapter, the two final sections provide a detailed description of a number of items on domestic and international agendas to address this volatility.

I. Composition of external financing and vulnerability

In the 1970s, international credit expansion allowed economies to grow on the back of large balance-of-payments current account deficits and unsustainable structures of expenditure and relative prices; this culminated in the debt crisis (see figure 5.1). In the 1980s, the shift from a net positive resource transfer to a large negative transfer meant a “lost decade” in terms of economic development. Output growth averaging 5.6% per year in the 1970s was followed by severe external, fiscal and financial crises; this led to the adoption of a series of adjustment and stabilization programmes which played a major role in reducing regional GDP growth to 1.2% per year.

In the 1990s, renewed but volatile access to international capital flows gave rise to brief cycles of growth, punctuated by periods of slowdown or outright recession. The net result was unstable and mediocre regional growth averaging 2.9% per year between 1990 and 2001. Although achievements such as fiscal control, lower inflation and enhanced credibility of the macroeconomic authorities are remarkable in themselves, they have failed to generate dynamic and stable economic growth processes in most of the region’s countries.

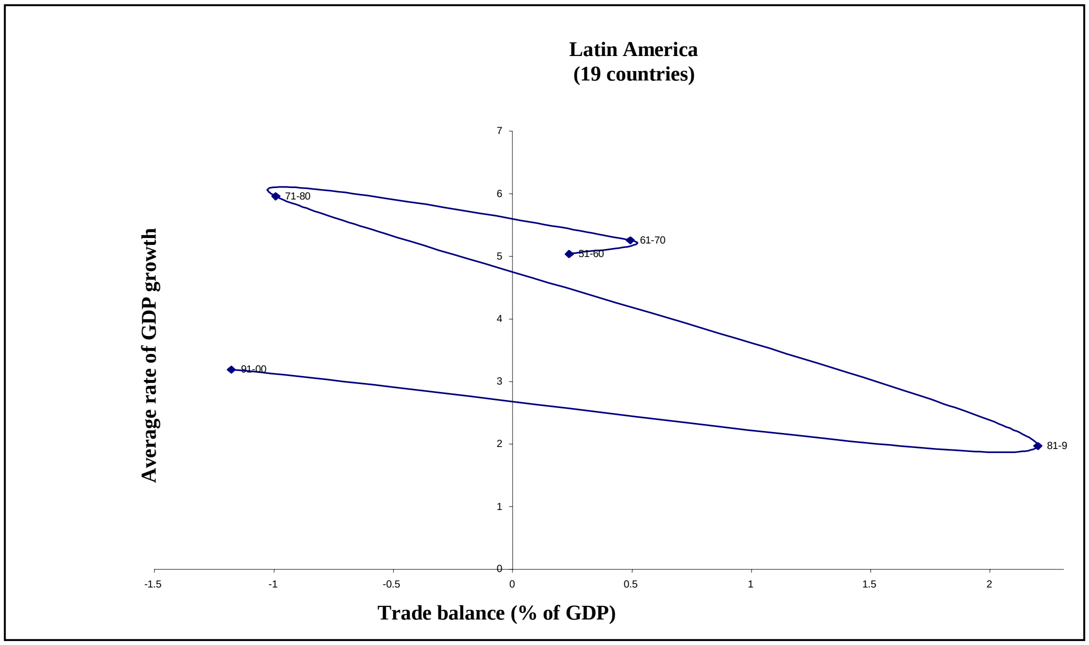
1. Anatomy of capital flows in the 1990s

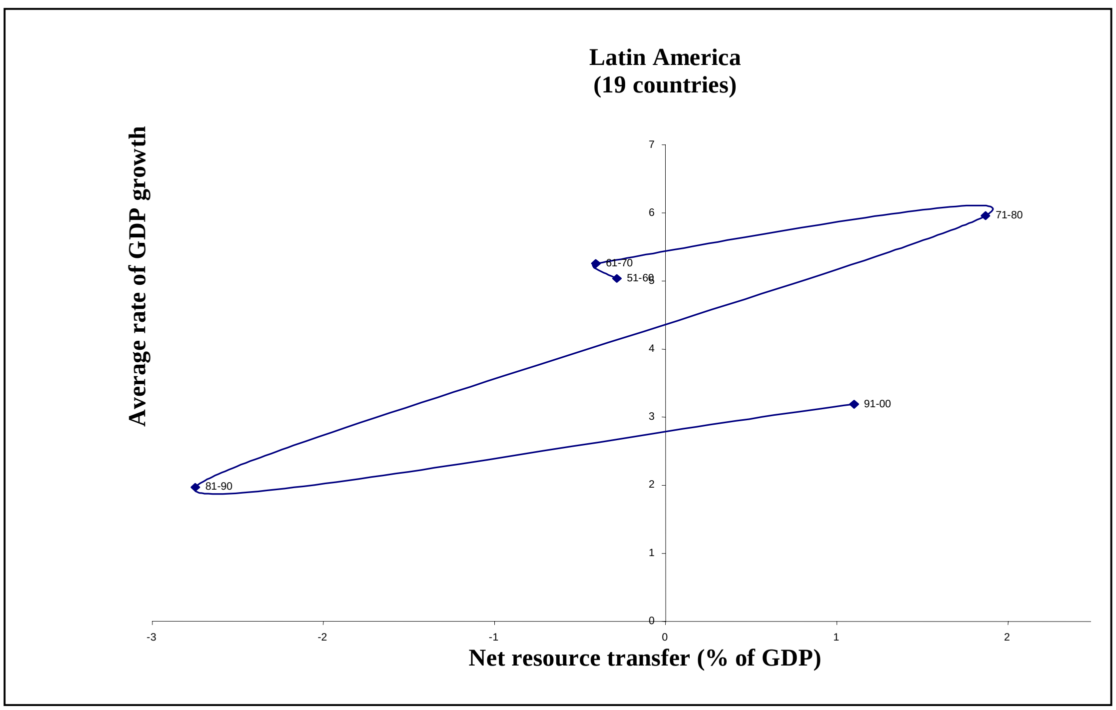
In contrast to the 1970s, when most external financing came in the form of syndicated bank loans, in the 1990s foreign direct investment (FDI) and bond flotations took on this role. FDI trended strongly upwards to account for three quarters of net capital inflows into the region during the decade, interrupted only by the international crisis of 2001-2002 (see table 5.1). Although mergers and acquisitions were important, firstly of privatized firms and later among domestic private-sector enterprises, over half of FDI inflows were used to expand productive capacity.

In clear contrast to FDI, bond issues fluctuated widely, and their financing conditions proved highly sensitive to the vagaries of international markets. The average maturity of new bond flotations varied from three to five years in the first half of the decade, rose to about 15 years in 1997 and then fell sharply to fluctuate between five and eight years in 1998-2001. Financing costs dropped to their lowest level in 1997, but then rose steeply in August 1998 following the Russian moratorium. Since then, they have remained above the levels prevailing until 1997, with a sharp increase in 2001 largely concentrated in Argentina (see figure 5.2).

Like bonds, net inflows from commercial banks were highly volatile and never regained the conditions prevailing before the debt crisis, especially as regards maturities. Equity porfolio flows and American depositary receipt placements (ADRs) have proved to be the most unstable financing sources (see figure 5.2). These two sources of funds and placements jointly fluctuated downwards until 1996-1997, and then fell steadily from 1998 onwards.

Figure 5.1
PATTERNS OF GROWTH, TRADE DEFICIT AND NET RESOURCE TRANSFER





Source: ECLAC, on the basis of official figures.

Table 5.1

LATIN AMERICA AND THE CARIBBEAN: SOURCES OF EXTERNAL FINANCING, 1990-2000

(Net flows in millions of dollars)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000 a/
Total *(A+B+C+D)*	**43,887**	**43,793**	**41,255**	**69,120**	**63,117**	**102,056**	**93,076**	**99,969**	**94,881**	**95,173**	**69,151**
A. Debt											
Official b/	6,823	3,435	1,220	2,674	-1,301	9,307	-8,212	-4,447	9,125	2,275	-2,701
Bonds	101	4,133	4,738	20,922	14,306	11,793	29,764	10,562	18,306	19,067	10,965
Commercial banks c/	2,731	1,275	4,302	201	6,212	15,068	16,200	29,646	-7,994	-16,130	4,339
B. Investment											
Direct	6,758	11,066	12,506	10,363	23,706	24,799	39,387	55,580	61,596	77,313	64,814
Portfolio	896	6,938	8,042	27,185	13,160	7,643	13,893	9,947	1,748	3,893	2,305
C. Grants d/	2,350	4,165	2,622	2,908	2,645	3,333	3,181	2,719	3,215	2,949	3,100
D. Compensatory funding e/	24,228	12,781	7,825	4,868	4,389	30,113	-1,136	-4,038	8,885	5,806	-13,671

Source: ECLAC, on the basis of official figures from the World Bank, the International Monetary Fund and the Bank for International Settlements.

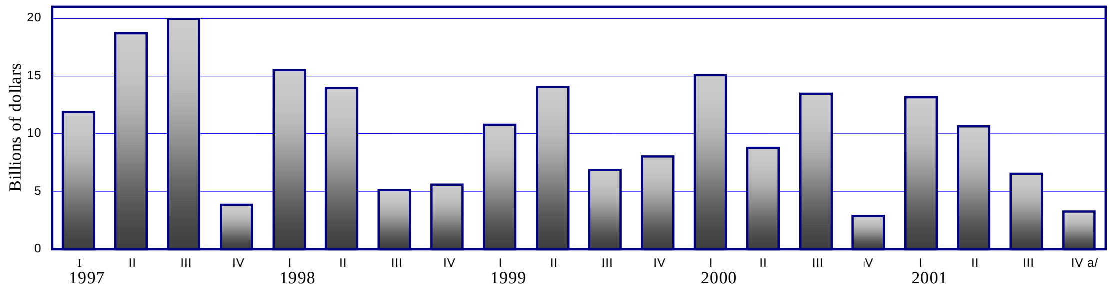
a/ Preliminary estimates.
b/ Includes bilateral and multilateral financing, excluding loans from IMF.
c/ Since 1998 includes short-term flows.
d/ Excludes technical cooperation.
e/ Includes IMF credits and exceptional financing. In the early 1990s, exceptional financing mainly covered interest arrears; in more recent years, however, it has included funds provided by multilateral organizations, apart from IMF and developed-country governments.

In contrast, official and compensatory financing behaved in countercyclical fashion, expanding when private financing dried up in 1995 and again from 1998 onwards. This reflects support provided by the International Monetary Fund (IMF), together with other multilateral financing organizations and a number of developed-country governments in periods that were especially critical for certain countries of the region, particularly Mexico in late 1994, Brazil in 1998-1999 and Argentina in late 2000.

Access to external private financing also tended to be concentrated in the region's relatively larger and more developed economies (see table 5.2). Expressed as a percentage of the respective GDP, total net long-term flows increased in countries with middle and high per capita incomes, but declined in low-income countries. The fall in the latter group was basically the result of a sharp reduction in official financing and grants, only partly compensated by higher FDI (see table 5.3). Despite this unfavourable trend, however, low-income countries received more long-term financing in relation to GDP than middle- and high-income countries: 14% of GDP between 1990 and 1999 in the first case, compared to 5.4% of GDP in middle-income countries and 4.8% in the higher-income countries.

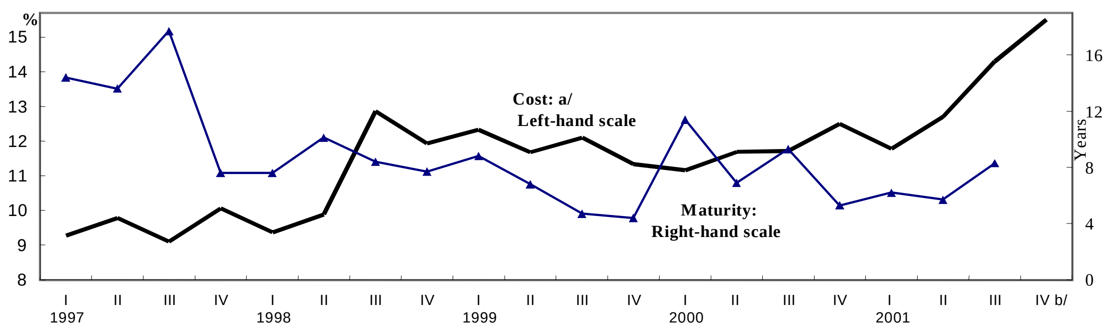
Figure 5.2

a) LATIN AMERICA AND THE CARIBBEAN: INTERNATIONAL BOND ISSUANCE



Source: ECLAC, on the basis of figures provided by the International Monetary Fund, J.P. Morgan and Merrill.
a/ October and November.

b) LATIN AMERICA AND THE CARIBBEAN: CONDITIONS OF INTERNATIONAL BOND ISSUES



Source: ECLAC, on the basis of figures provided by the International Monetary Fund, J.P. Morgan and Merrill.

a/ Sum of average spread on bond placements and the yield on long-term United States treasury bonds.
b/ October and November.

Table 5.2
LATIN AMERICA AND THE CARIBBEAN: NET PRIVATE RESOURCE FLOWS, 1990-1999
(Annual averages, in millions of dollars and percentages)

	Foreign direct investment		**Portfolio capital flow**		**Total private investment**		**Memo (1999): Percentage**	
	Amount	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**GDP** a/	**Population**
Latin America and the Caribbean	**32,937**	**100**	**9,214**	**100**	**42,151**	**100**	**100**	**100**
Low-income countries b/	1,845	5.6	8	0.1	1,853	4.4	5	14.4
Middle-income countries c/	3,844	11.7	902	9.8	4,746	11.3	10	15.4
High-income countries d/	27,248	82.7	8,304	90.1	35,552	84.3	85	70.2
Argentina	5,442	16.5	1,132	12.3	6,575	15.6	16	7.4
Brazil	9,909	30.1	2,785	30.2	12,694	30.1	30	34.2
Chile	1,937	5.9	288	3.1	2,226	5.3	4	3.0
Mexico	8,179	24.8	3,750	40.7	11,929	28.3	27	19.7
Venezuela	1,676	5.1	311	3.4	1,986	4.7	6	4.8
Others	105	0.3	37	0.4	142	0.3	2	1.0
	Bonds		**Loans from commercial and other banks**		**Total private debt**		**Memo (1999): Percentage**	
	Amount	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**	**GDP** a/	**Population**
Latin America and the Caribbean	**13,647**	**100**	**10,691**	**100**	**24,337**	**100**	**100**	**100**
Low-income countries b/	**10**	**0.1**	**97**	**0.9**	**107**	**0.4**	**5.1**	**14.4**
Middle-income countries c/	**914**	**6.7**	**1,100**	**10.3**	**2,014**	**8.3**	**9.8**	**15.4**
High-income countries d/	**12,723**	**93.2**	**9,494**	**88.8**	**22,217**	**91.3**	**85.1**	**70.2**
Argentina	4,871	35.7	578	5.4	5,448	22.4	16.2	7.4
Brazil	2,594	19.0	4,808	45.0	7,403	30.4	30.2	34.2
Chile	528	3.9	1,538	14.4	2,066	8.5	3.9	3.0
Mexico	4,202	30.8	2,317	21.7	6,519	26.8	27.4	19.7
Venezuela	353	2.6	-14	-0.1	340	1.4	5.9	4.8
Others	174	1.3	267	2.5	441	1.8	1.6	1.0

Source: ECLAC, on the basis of official figures provided by the World Bank, *Global Development Finance 2001*, Washington, D.C., 2001, and national sources.

a/ Calculated on the basis of values expressed at current prices.
b/ The low per capita income group of countries consists of Bolivia, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Nicaragua and Paraguay.
c/ The middle per capita income group of countries consists of Colombia, Costa Rica, Jamaica, Panama and Peru.
d/ The high per capita income group of countries consists of Argentina, Barbados, Brazil, Chile, Mexico, Trinidad and Tobago, Uruguay and Venezuela.

Table 5.3
LATIN AMERICA AND THE CARIBBEAN: LONG-TERM EXTERNAL FINANCING BY GROUPS OF COUNTRIES, 1990-1999
(Percentages of GDP)

Groups of countries (simple averages)	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Mean	Std. Dev.
I. Net long-term flows												
Low per capita income countries a/	15.2	22.9	15.6	11.2	12.4	11.3	11.8	14.5	12.6	12.9	14.0	3.5
Middle per capita income countries b/	3.2	4.6	2.3	4.6	5.2	4.2	5.7	9.0	8.4	6.5	5.4	2.1
High per capita income countries c/	1.9	2.3	2.6	3.8	5.0	4.0	7.1	7.3	7.4	6.7	4.8	2.2
II. Official financing d/												
Low per capita income countries	8.6	4.4	3.9	2.5	2.8	2.3	2.2	4.3	1.8	2.5	3.5	2.0
Middle per capita income countries	0.3	1.0	-1.3	-0.4	-1.0	-0.6	-1.2	-0.4	0.0	0.0	-0.4	0.7
High per capita income countries	1.0	0.5	0.4	0.2	0.1	0.2	-0.3	-0.1	0.5	0.0	0.3	0.4
III. Financing in bond markets												
Low per capita income countries	0.0	0.0	0.0	0.4	0.1	0.0	-0.1	-0.1	-0.1	0.1	0.0	0.2
Middle per capita income countries	-0.1	0.0	0.0	0.2	0.5	0.3	0.8	1.7	1.9	1.3	0.6	0.7
High per capita income countries	-0.4	0.1	0.6	1.1	0.8	0.8	1.7	0.4	1.1	1.1	0.7	0.6
IV. Financing through other private sources e/												
Low per capita income countries	-0.4	-0.9	-1.4	-0.3	-0.4	-0.7	0.5	0.5	0.4	0.6	-0.2	0.7
Middle per capita income countries	-0.6	-0.7	-0.1	0.2	0.1	0.3	0.1	1.0	0.1	1.2	0.1	0.6
High per capita income countries	0.0	-0.3	-0.4	-0.7	0.3	0.2	0.3	0.8	1.4	-0.2	0.1	0.6
V. Foreign direct investment f/												
Low per capita income countries	0.8	0.9	6.7	3.3	3.7	3.5	3.3	4.5	5.9	6.3	3.9	2.0
Middle per capita income countries	2.0	1.9	2.4	2.2	4.0	3.0	4.5	6.1	6.0	3.7	3.6	1.6
High per capita income countries	1.1	1.7	1.5	2.0	3.1	2.6	3.2	5.3	4.3	5.7	3.0	1.6
VI. Portfolio investment												
Low per capita income countries	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Middle per capita income countries	0.0	0.0	0.3	0.8	0.8	0.7	1.1	0.3	0.1	0.1	0.4	0.4
High per capita income countries	0.2	0.3	0.4	1.0	0.6	0.3	2.2	0.9	0.1	0.1	0.6	0.6
VII. Grants												
Low per capita income countries	6.2	18.4	6.3	5.2	6.2	6.1	5.9	5.4	4.7	3.4	6.8	4.2
Middle per capita income countries	1.6	2.4	1.1	1.7	0.7	0.5	0.4	0.3	0.4	0.2	0.9	0.7
High per capita income countries	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.0	0.1	0.1

Source: World Bank, *Global Development Finance 2001*, Washington, D.C., 2001.

a/ The low-income group consists of countries which in 1998 had a per capita GDP of less than US$ 2,000, estimated at the market exchange rate, namely Bolivia, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Nicaragua and Paraguay.
b/ The middle-income group of countries consists of Colombia, Costa Rica, Jamaica, Panama and Peru.
c/ The high-income group of countries consists of Barbados, Brazil, Chile, Mexico, Trinidad and Tobago, Uruguay and Venezuela.
d/ Official financing consists of loans from bilateral and multilateral sources.
e/ Includes loans from commercial banks and other private lenders.
f/ Figures refer to FDI inflows, without deducting investment abroad by the reporting economy.

2. External financing and the business cycle

Although the fluctuations the region's economies have experienced over the past decade have varied in type, the most outstanding feature has been the key role that external financing flows have begun to play in determining the business cycle (see box 5.1 and figure 5.3). Although the trade cycle and movements in the international terms of trade continue to play an important role, exposure to volatility and contagion associated with new forms of external financing has become the main source of external vulnerability among the region's economies. The sovereign-bond risk premium, which reflects financial agents' perception of a country's capacity to meet its obligations, has also become one of the most important macroeconomic prices.

Box 5.1
THREE CRISES IN LESS THAN A DECADE

The present crisis in Latin America and the Caribbean is the third time in less than a decade in which regional GDP growth had fallen off steeply and dragged per capita GDP down along with it. The two previous crises occurred in 1995 and in 1998-1999. Because all of these crises have been the result of external shocks, attention is being focused on the channels through which these shocks are transmitted. Their impact is then, of course, reflected on the balance-of-payments trade and capital accounts.

Viewed from this perspective, the three crises have differed from one another in some very significant ways. The differences have to do with these crises' varying degrees of globality, which influences the relative importance of transmission mechanisms in each. This, in turn, has implications for the consequent economic policy responses.

The 1995 crisis was not a global crisis. It originated in a single country (Mexico) and was therefore transmitted through financial rather than trade channels. The devaluation of the Mexican peso in December 1994 triggered capital outflows from various countries and the virtual suspension of voluntary external financing but, ultimately, the only country other than Mexico to be seriously affected was Argentina, which then pulled Uruguay down with it. Trade did, however, provide an adjustment mechanism for this crisis within an international environment marked by significant growth and massive financial assistance for Mexico and Argentina. As a result, the crisis only lasted for three quarters.

The crisis that broke out in Asia in the second half of 1997 falls into the mid-range in terms of its origin and scope. The contagion effect transmitted through trade channels was considerable, but financial channels played the greatest role in allowing it to spread. The trade-based effects chiefly took the form of declining prices for a number of the raw materials of importance to the region, such as petroleum, other minerals and some agricultural products. The financial turbulence that arose in Asia was heightened by the Russian Federation's moratorium and currency devaluation in August 1998. This led to a deepening of the crisis in 1999, which left a trail of financial instability in its wake that is still in evidence today. On the other hand, the United States economy's high growth rate had positive trade effects on Mexico and Central America, and the impacts of the crisis were consequently concentrated in the South American countries.

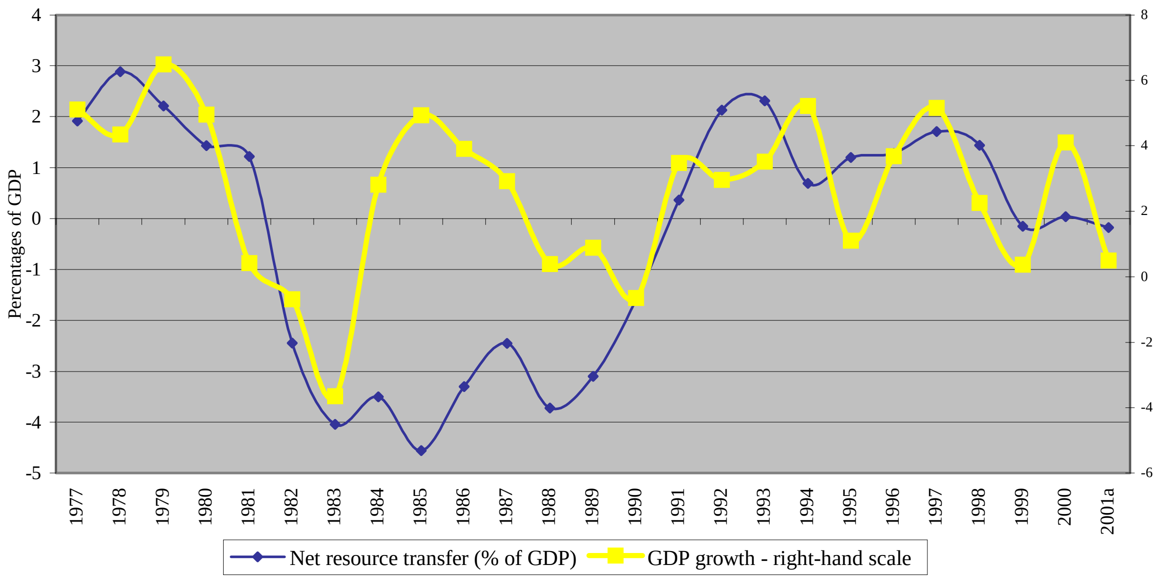
Unlike its predecessors, the current crisis —triggered by a severe slowdown in the world economy that began in a country that has an overarching influence on global and regional economic activity— is truly global in nature. Trade has therefore been the principal channel for the transmission of this crisis, which has been manifested in slower growth or a contraction of export volumes and in a downturn in raw materials prices that has hurt a majority of the countries.

The primarily financial transmission of the first two crises —and the fact that, at the time, the countries were in the midst of stabilization programmes involving the use of exchange-rate anchors— took away much of the economic authorities' manoeuvring room. As external financing tightened, it became necessary to cool down demand by means of what amounted to a procyclical economic policy response. Because of the global nature of the present crisis, measures taken by the countries to boost external competitiveness and galvanize domestic demand, no matter how desirable and necessary they may be, will not be enough to achieve these ends. All these factors point up the need to supplement national policies with international and regional

Fuente: ECLAC, *Preliminary Overview of the Economies of Latin America and the Caribbean 2001* (LC/G.2153-P), Santiago, Chile, 2001. United Nations publication, Sales No. E.01.II.G.182.

Figure 5.3
PROCYCLICAL MOVEMENTS IN ECONOMIC ACTIVITY AND NET RESOURCE TRANSFER

Latin America and the Caribbean: net resource transfer and rate of growth of GDP
(Percentages of GDP and percentage)



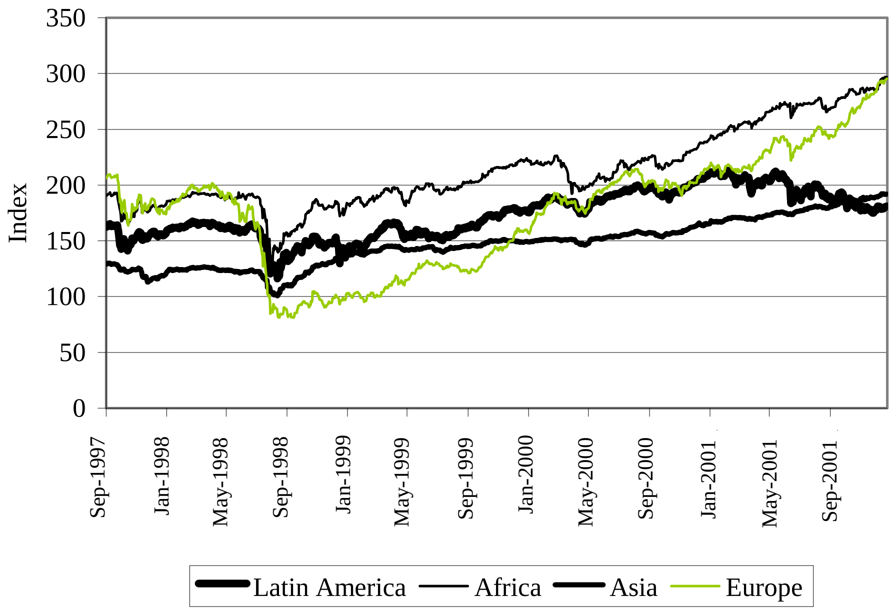
Source: ECLAC, on the basis of official figures.

Parallel sovereign-risk trends among different countries, relatively independent of the soundness of their macroeconomic fundamentals, is a clear illustration of the contagion that has characterized private capital markets, both in times of expansion (contagion of optimism) and in periods of crisis (contagion of pessimism). This phenomenon was especially pronounced during the 1996-1997 upswing and during the Asian and Russian crises (see figure 5.4). Markets have also tended to develop in parallel more recently, but contagion from the Argentine crisis of 2001 was much less marked. In fact it only affected a few South American countries (Brazil and Chile in particular), and even these broke free from Argentine market trends in the final quarter of 2001.

The lessons that emerge from an analysis of the crises endured by a number of countries in the second half of the 1990s (Mexico in 1994-1995; Indonesia, Korea and Thailand in 1997; Russia in 1998; Brazil in 1998-1999; and Argentina in 2001-2002, among others) suggest that the vulnerability of economies to sudden changes on international financial markets is essentially caused by three factors: (i) the size of the deficit on the current account of the balance of payments; (ii) reliance on highly volatile financing flows, especially short-term credit lines and portfolio flows; and (iii) the soundness of domestic financial systems, especially their capacity to withstand interest- rate and exchange-rate fluctuations.

Figure 5.4

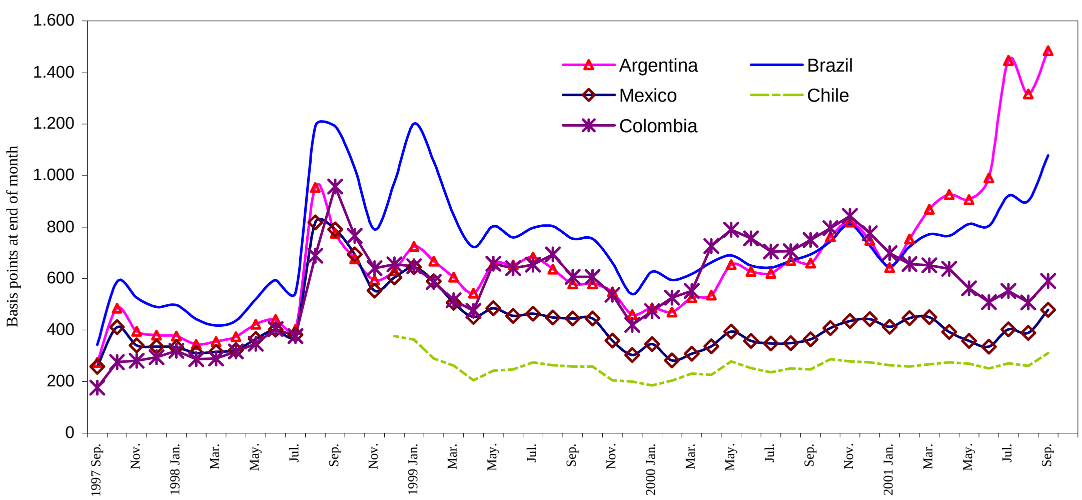
a) TREND OF GLOBAL EMERGING MARKETS BOND INDEX (EMBI)



Source: J.P. Morgan.

b) EUROBOND SPREADS

(With respect to yields on United States Treasury bonds)



Source: J.P. Morgan, *Emerging Markets Bond Index Monitor.*

Against this backdrop, the relation between short-term liquidity requirements (represented by the relative size of short-term debt and other liquid liabilities) and the backing that countries receive to meet such liabilities (represented by available international reserves) have come to be seen as important indicators of external vulnerability (Rodrik and Velasco, 1999). Consequently, lowering the ratio of short-term external debt to international reserves has become an increasingly common macroeconomic policy objective, on which major progress has been made in many of the region's countries since the Asian crisis (see table 5.4). Stronger prudential regulation and oversight of domestic financial systems has also been a major goal, but progress here remains inadequate in several countries, as indicated below.

Table 5.4

LATIN AMERICA AND THE CARIBBEAN: TREND OF BALANCE OF PAYMENTS, 1990-2001

(Annual averages as a percentage of GDP)

	1990-2000	**1990-1994**	**1995-1997**	**1998-2000**	**2001**a/
Current account balance					
Latin America	**-2.6**	**-2.2**	**-2.6**	**-3.4**	**-2.8**
Low-income countries b/	-8.2	-9.4	-7.5	-6.9	-8.2
Middle-income countries c/	-4.2	-2.9	-4.9	-5.6	-3.6
High-income countries d/	-1.4	-1.1	-1.0	-2.1	-1.6
Trade balance					
Latin America	**-0.9**	**-0.4**	**-1.0**	**-1.6**	**-1.2**
Low-income countries	-10.3	-8.7	-10.4	-12.9	-14.4
Middle-income countries	-2.0	-1.2	-3.3	-2.0	-1.3
High-income countries	0.7	1.2	1.0	-0.3	0.3
Balance on capital and financial accounts e/					
Latin America	**2.9**	**2.5**	**3.3**	**3.2**	**1.7**
Low-income countries	4.4	2.2	6.4	6.1	6.5
Middle-income countries	3.7	1.8	5.9	4.5	0.7
High-income countries	2.4	2.4	2.5	2.3	0.2

Source: ECLAC, on the basis of official figures.

a/ Preliminary figures.
b/ The low-income group consists of countries which in 1998 had a per capita GDP of less than US$ 2,000, estimated at the market exchange rate, namely Bolivia, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Nicaragua and Paraguay.
c/ The middle-income group consists of countries which in 1997 had a per capita GDP of between US$ 2,000 and US$ 4,000, namely Colombia, Costa Rica, Jamaica, Panama and Peru.
d/ The high-income group consists of countries which in 1997 had a per capita GDP of more than US$ 4,000, namely Argentina, Barbados, Brazil, Chile, Mexico, Trinidad and Tobago, Uruguay and Venezuela.
e/ Includes errors and omissions.

In the 1990s, the average balance-of-payments current account deficit amounted to 2.6% of GDP, with the trade gap averaging nearly 1%. Unlike the Asian economies, the region's countries have maintained a persistent current account deficit, even in periods of abrupt slowdown in economic growth. This makes them even more reliant on external financing. Nonetheless, the weightings of the individual factors that combine to make up the current account deficit vary widely from one country to another: whereas the trade deficit is a fundamental factor in low-income countries, debt service has been more important in middle- and high-income countries (see table 5.5).

Table 5.5
INDICATORS OF EXTERNAL VULNERABILITY AMONG DEVELOPING COUNTRIES, 1990-2000
(Percentages)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000a/
Developing countries											
Short-term external debt/ Total external debt	16.8	17.2	18.4	18.5	18.3	19.8	20.7	20.1	15.9	15.8	15.9
Short-term external debt/ International reserves	109.0	96.9	102.6	89.2	83.6	79.1	73.7	71.1	57.9	56.5	51.0
External debt service/Exports	18.1	17.2	16.3	16.2	15.9	15.7	16.4	17.1	18.2	21.4	17.0
Total interest/Exports	7.8	7.7	6.7	6.4	6.3	6.6	6.3	6.2	6.9	6.7	6.0
Total external debt/ Gross national product	30.9	32.7	34.3	36.4	38.2	38.3	36.1	36.1	42.9	40.6	37.4
International reserves/Imports (months)	2.9	3.2	3.1	3.6	3.8	3.9	4.2	4.1	4.7	4.7	4.3
Current account balance/ Gross national product	-0.5	-1.6	-1.8	-2.7	-1.8	-2.0	-1.8	-1.6	-1.0	0.0	0.9
East Asia and the Pacific											
Short-term external debt/ Total external debt	17.9	19.2	20.9	22.0	24.7	28.6	31.5	28.1	18.2	16.8	17.0
Short-term external debt/ International reserves	57.0	54.8	72.2	69.7	70.2	78.1	77.3	76.1	41.9	33.6	30.9
External debt service/Exports	15.7	13.4	13.5	14.1	12.1	11.4	12.1	11.2	12.9	15.8	10.8
Total interest/Exports	6.0	5.9	5.0	4.8	4.5	4.7	4.6	4.6	5.1	4.6	4.0
Total external debt/ Gross national product	29.8	30.2	30.6	31.5	32.0	31.0	30.8	33.7	41.6	36.4	32.6
International reserves/ Imports (months)	4.0	4.3	3.5	3.7	4.1	3.9	4.4	4.3	6.4	6.4	5.2
Current account balance/ Gross national product	-0.6	-1.3	-0.9	-2.2	-1.2	-2.3	-2.5	0.4	6.0	4.3	2.9
Latin America and the Caribbean											
Short-term external debt/ Total external debt	16.3	17.6	18.5	20.2	20.1	20.0	18.5	19.1	16.0	14.8	15.6
Short-term external debt/ International reserves	131.8	116.4	97.5	93.7	103.2	93.6	75.7	77.7	76.6	79.0	82.4
External debt service/Exports	24.4	24.1	26.1	27.7	25.3	26.4	31.3	35.6	32.5	41.6	35.7
Total interest/Exports	12.2	12.7	11.3	11.0	11.1	12.2	11.7	11.2	11.9	13.0	11.8
Total external debt/ Gross national product	44.6	43.6	40.9	40.3	37.9	39.9	38.0	36.6	41.1	41.8	38.5
International reserves/Imports (months)	3.6	4.2	4.8	5.2	4.4	4.8	5.2	4.7	4.2	4.0	3.5
Current account balance/ Gross domestic product	-0.2	-1.5	-2.7	-3.3	-3.3	-2.2	-2.1	-3.3	-4.5	-3.2	-2.4

Source: World Bank, *Global Development Finance 2001*, Washington, D.C., 2001.

a/ Preliminary figures.

II. Globalization and real macroeconomic instability

1. Procyclical behaviour linked to the financial accelerator

The close relation between the business cycle and the net resource transfer is determined from abroad by a series of mechanisms operating through domestic financial systems and exchange-rate policy. In periods of abundant capital inflow, economies tend to err on the side of excessive domestic credit and liquidity expansion; in recessions precisely the opposite happens, resulting in an exaggerated liquidity contraction. These powerful financial amplifiers tend to accentuate booms and also intensify the severity of recessions. Moreover, using exchange-rate policy as a nominal anchor, at times of abundant external funding, has resulted in sharply lower inflation rates, but at the cost of increasing appreciation of the real exchange rate. When external capital flows subsequently dry up, this appreciation turns into the Achilles heel of stabilization policy, in many cases giving rise to painful adjustment processes.

When net external capital inflows turned sharply positive in the late 1980s and early 1990s, domestic credit expanded from 22% of GDP in 1988 to 30% in 1993, while stock market indices soared by over three and half times and local currencies appreciated considerably (see figure 5.5). The Mexican crisis of December 1994 brought these phenomena to an halt. A resumption of abundant inflows of international capital in 1996-1997 triggered a new cycle of domestic financial expansion, involving soaring share prices and real appreciation, which was interrupted by the Asian crisis of 1997 and particularly the Russian crisis of 1998. The “wealth effects” generated in upswing periods proved later to be unsustainable. In fact, real appreciations were not reversed during the crises in all countries, particularly those that maintained fixed or semi-fixed exchange-rate regimes.

The instability of private capital flows undermined the capacity of the real economy to react to crisis situations, as trade-protection and export-promotion policies lost importance and the exchange rate became the main determinant of competitiveness. Currency appreciation during expansionary phases, which discourages technological development and the conquest of markets, resulted in losses of productive capacity and marketing networks which, as indicated in studies on “Dutch disease”,[1] have proved persistent in many cases.

Several of the region’s governments have been forced to intervene in their domestic financial systems during crisis periods, assuming the “lender of last resort” function of the central bank. This entails the public sector assuming some of the risks incurred by private agents that overborrowed in the upswing phase, and invariably leads to large fiscal or quasi-fiscal losses (IMF, 1998, chap. IV; ECLAC, 2001a, chap. 1). One of the paradoxes of this situation is that fiscal balance during upswing periods may conceal contingent fiscal liabilities, in the form of “implicit insurance” for private-sector debts, whose magnitude is unknown initially and only becomes evident when crisis breaks.[2]

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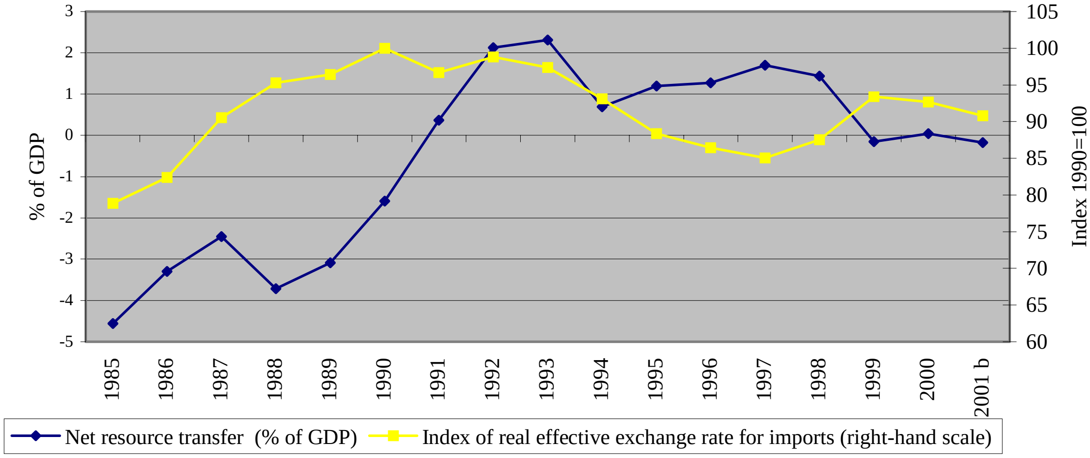
1 This is one of the key conclusions of the literature on “Dutch disease” in its dynamic versions. See, in particular, Krugman (1990b chap. 7) and van Wijnbergen (1984).

2 This situation developed in the 1990s as a result of the risks governments assumed by providing guarantees for private investments in public infrastructure. As such investments are more likely to be made during expansionary periods, but the guarantees take effect during crises (minimum revenue or profitability guarantees, in particular), they acquire a procyclical nature. This is an untransparent practice in the absence of explicit estimates of the fiscal risks involved (ECLAC, 1998d).

Figure 5.5
NET RESOURCE TRANSFER AND APPRECIATION OF CURRENCY AND FINANCIAL ASSETS

a) Latin America and the Caribbean: net resource transfer and index of real efective exchange a/

(Percentage of GDP and indices, 1990=100)



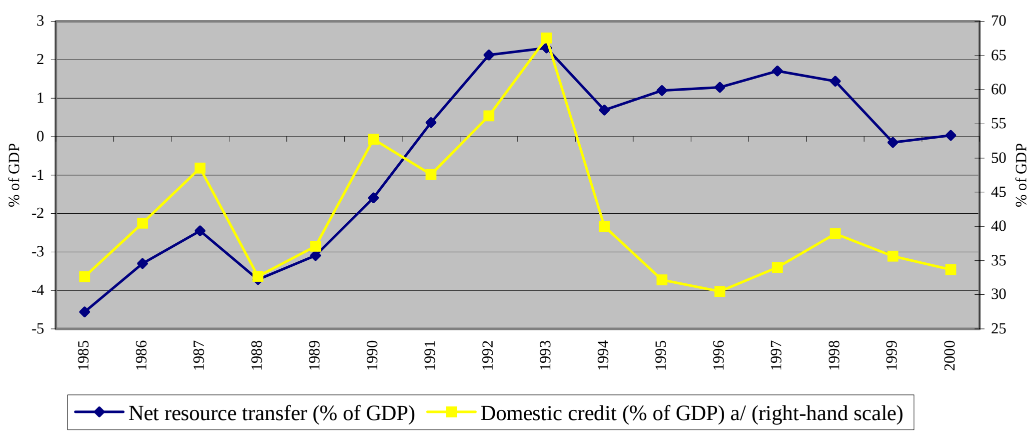
Source: ECLAC, on the basis of figures provided by the International Monetary Fund (IMF) and national bodies and ECLAC, *Postwar Transfer of Resources Abroad by Latin America*, Cuadernos de la CEPAL series, No. 67 (LC/G.1657-P), Santiago, Chile, July 1992. United Nations publication, Sales No. E.91.II.G.9.

a/ The net resource transfer is equivalent to net capital inflows (including non-autonomous flows, and errors and omissions), minus the balance on the income account (profits and net interest payments). For the real effective exchange rate for imports, the median value for Latin America was used; this corresponds to the average of indices of the (official main) real exchange rate of each country's currency against those of its main trading partners, weighted by the relative share of imports to those countries. The weightings correspond to the average for the period 1994-1998.

b/ Preliminary figures.

b) Latin America and the Caribbean: net resource transfer and domestic credit

(Percentage of GDP)



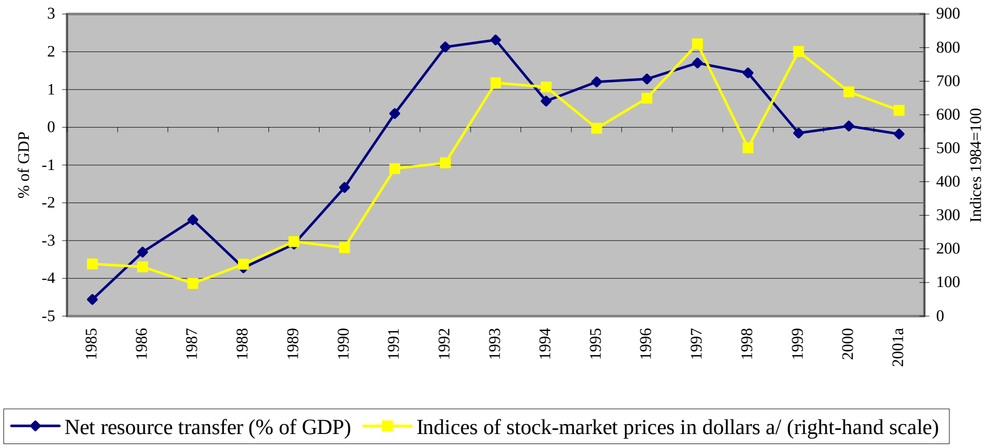
Source: ECLAC, on the basis of figures provided by the International Monetary Fund *(International Financial Statistics)* and national sources.

a/ Figures on domestic credit exclude Brazil for the entire period, and Colombia in 1986 and 1989.

Figure 5.5 (concluded)

c) Latin America and the Caribbean: net resource transfer and strock market price indices in dollars

(Percentage of GDP and indices 1984=100)



Source: ECLAC, on the basis of figures provided by the International Finance Corporation; and ECLAC, *Postwar Transfer of Resources Abroad by Latin America*, Cuadernos de la CEPAL series, No. 67 (LC/G.1657-P), Santiago, Chile, July 1992. United Nations publication, Sales No. E.91.II.G.9.

a/ End-December values of the International Finance Corporation Global Price Index (IFCG) for Latin America. Up to September 2001.

Given the strategic importance of the exchange-rate anchor in price-stabilization programmes, some of the region's countries introduced a variety of forms of asymmetric capital-account control (applying stricter rules on capital inflows than on outflows), in order to avert an excessive appreciation of the exchange rate and calm the volatility of speculative financial capital movements. Besides allowing the central bank to retain a degree of autonomy over monetary policy management, this had a positive effect on the composition of capital flows, as shown by experience in Chile and Colombia (ECLAC, 1998a and 2000a, vol. III, chap. 1).

From the mid-1990s onwards, however, many countries eased capital account regulations, or abandoned them entirely (the last country to do so was Chile, between April and May 2001), moving towards greater exchange-rate flexibility. In fact, the most frequent response to crisis, or the threat of one, was to change the exchange-rate regime. There was a general preference for various types of exchange-rate flexibility albeit with varying degrees of intervention, although clearly there were major regional exceptions to this general rule (see table 5.6). Events in several countries show that adjustments under fixed exchange-rate regimes have been more traumatic in terms of their impact on real economic variables (growth and employment) than when they take place under more flexible regimes.

The trend towards exchange-rate flexibility has gone hand in hand with the spread of monetary policy practices aimed essentially at controlling inflation (inflation targeting). This involves setting annual or multi-year inflation targets, with a view to informing economic agents of the central bank's intentions and making monetary management more transparent. It also allows for more flexible management of monetary instruments in accordance with the trend of inflation and the economic situation in general. Reducing inflation has undoubtedly been the greatest success of stabilization policies over the past decade. Given the high rates of inflation traditionally recorded by several of the region's countries, this is a major achievement. Since the late 1990s, most Latin American and Caribbean countries have managed to keep inflation in single digits.

Table 5.6
LATIN AMERICA AND THE CARIBBEAN: EXCHANGE RATE REGIMES, 2002

Fixed, quasi-fixed or dollarized	**Crawling peg or flotation band**	**Floating** a/
Barbados	Bolivia	Argentina
Belize	Costa Rica	Brazil
Ecuador	Dominican Republic	Chile
El Salvador	Honduras	Colombia
Eastern Caribbean States	Nicaragua	Guatemala
Panama	Uruguay	Guyana
		Haiti
		Jamaica
		Mexico
		Paraguay
		Peru
		Trinidad and Tobago
		Venezuela

Source: ECLAC, *Luces y sombras: América Latina y el Caribe en los noventa*, Santiago, Chile, 2000.

a/ Floating regimes usually involve some degree of central-bank intervention (dirty floating).

2. The procyclical behaviour of public finances

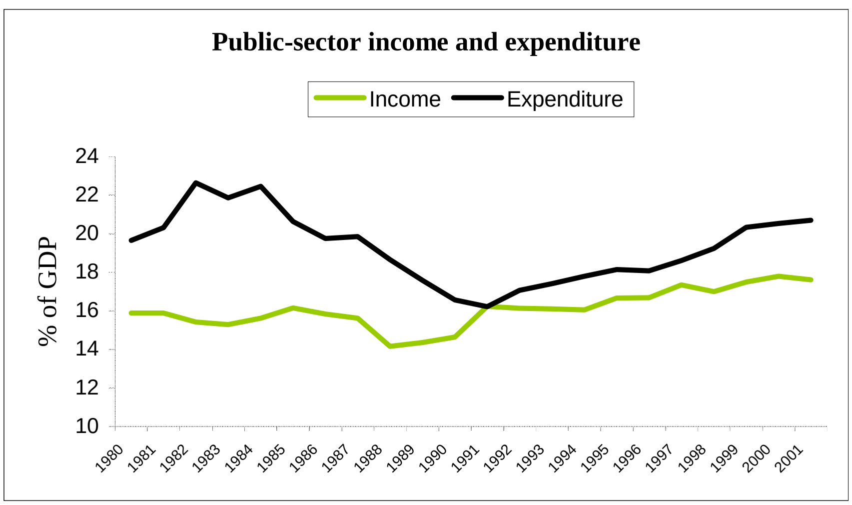
The macroeconomic programmes implemented in the 1990s also gave prime importance to securing gains made during the debt crisis in terms of reducing the fiscal deficit (see figure 5.6). The revival of economic growth and the design of better tax systems enabled fiscal revenues to recover strongly. Between 1990 and 2000, 16 of the region's countries managed to increase central government tax revenue (see figure 5.7). Revenue growth has been particularly notable in VAT, and to a lesser extent among direct taxes. Social security contributions display wide disparities, because several of the region's countries reformed their pension system, which, to a greater or lesser extent, altered the public-private mix of social security financing and coverage.

The recovery of fiscal revenues allowed public expenditure to grow by four percentage points of GDP during the 1990s: from 16.6% of GDP in 1990 to 20.7% in 2001. This also made it possible to restore the level of public-sector social expenditure, which rose from 10.4% of GDP in 1990-1991 to 13.1% in 1998-1999. This latter trend was more pronounced during the first half of the 1990s, after which it began to weaken (ECLAC, 2001c, chap. IV).

In a context of fiscal programming with an annual horizon and public revenues that closely follow the business cycle, targeting the short-term deficit (rather than the structural deficit or level of expenditure) has given rise to procyclical public expenditure policies. An analysis of 31 episodes of variation in the business-cycle-adjusted public-sector deficit[3] shows that fiscal policy behaved procyclically in 25 cases. In 14 of the 16 cases where output growth was above trend, the public-sector deficit was also greater, reflecting expansionary fiscal policy (see figure 5.8). On the other hand, when economies have grown more slowly than the medium-term trend, the public-sector deficit has also been smaller, with a surplus even recorded in 12 of the 16 episodes, reflecting restrictive fiscal policy (Martner, 2000).

3 The cyclically-adjusted deficit is defined as the fiscal deficit corrected for variations attributable to the business cycle. For this purpose, the GDP gap is calculated by estimating trend GDP, using the Hodrick-Prescott filter, and its effects in terms of public revenues and expenditure (Martner, 2000).

Figure 5.6
LATIN AMERICA (19 COUNTRIES): CENTRAL GOVERNMENT ACCOUNTS
(Percentage of GDP)

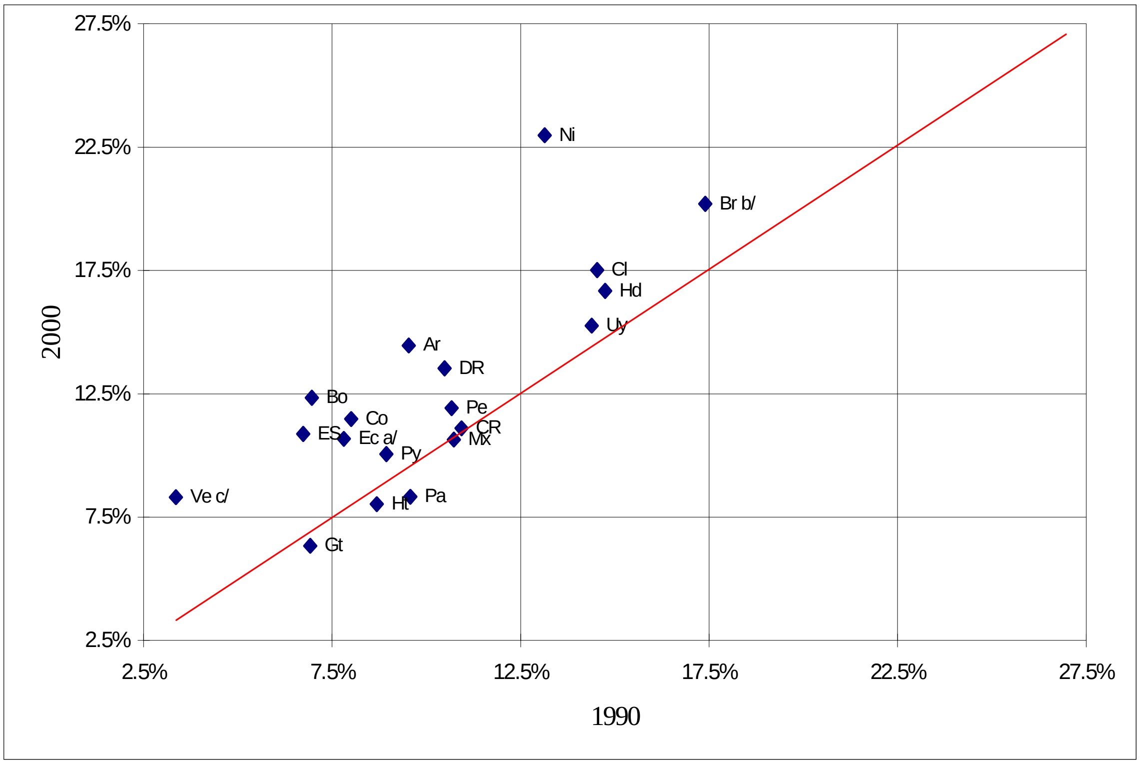


Source: ECLAC, on the basis of official figures.

Figure 5.7

LATIN AMERICA: CENTRAL GOVERNMENT TAX BURDEN, 1990-2000

(Percentage of GDP, net of social security contributions)



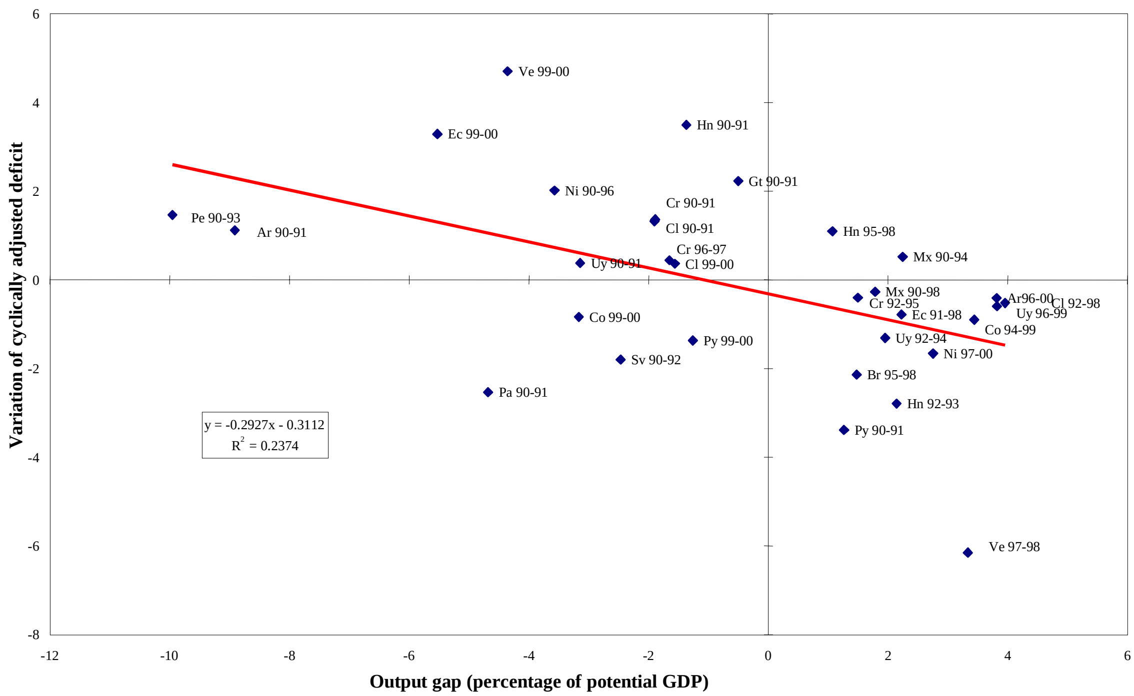
Source: ECLAC, on the basis of official figures.

a/ The 2000 figure for Ecuador actually corresponds to 1999.

b/ The 1990 figure for Brazil actually corresponds to 1991. Includes state-level sales tax on merchandise and services (ICMS), but excludes the contribution to the financing of the social security system (COFINS), the Social Integration Programme - Public Service Assistance Plan (PIS/PASEP), the provisional financial transactions tax (CPMF) and the social contribution on net profits (CSLL), as these have been included under social security contributions.

c/ Figures for Venezuela include net oil revenues.

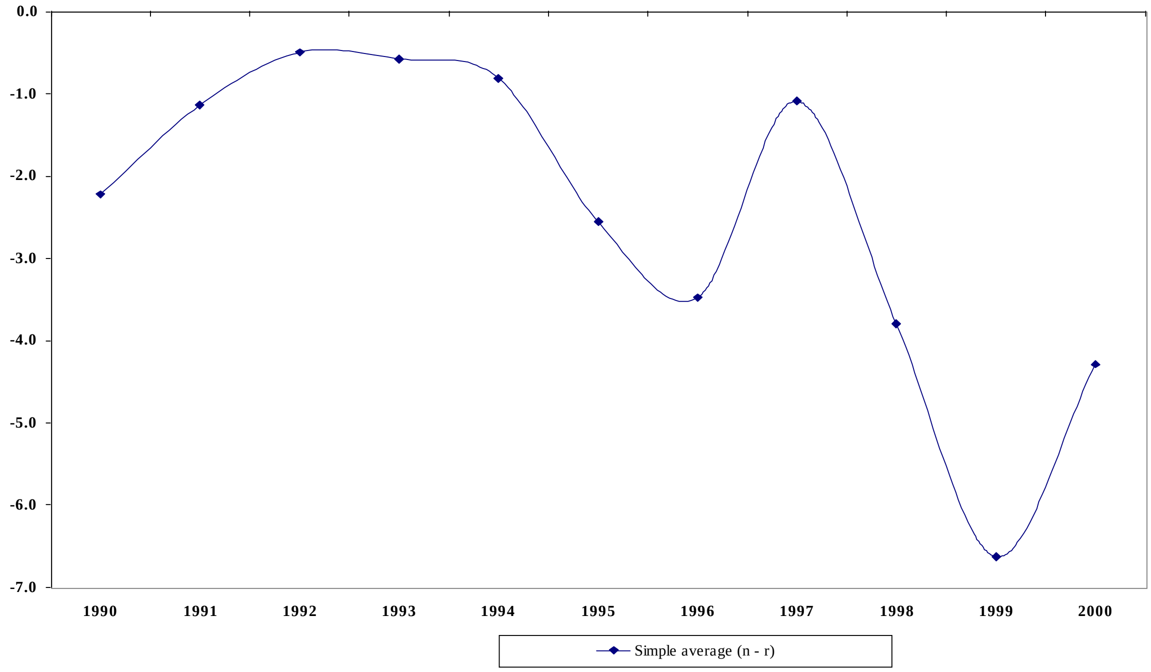
Figure 5.8
LATIN AMERICA: EPISODES OF PROCYCLICAL POLICIES, 1990-2000



Source: Ricardo Martner, *Estrategias de política económica en un mundo incierto: reglas, indicadores, criterios*, Cuadernos del ILPES series, No. 45 (LC/IP/G.123-P), Santiago, Chile, Economic Commission for Latin America and the Caribbean (ECLAC), 2000. United Nations publication, Sales No. S.00.III.F.1. Only includes episodes in which absolute values of the average annual output gap and the average annual variation of the cyclically adjusted deficit are larger than 0.25% for at least two years.

The procyclical behaviour of public finances has tended to become more pronounced as a result of certain features of prevailing monetary policies. Public-sector borrowing at real interest rates above the rate of economic growth causes the debt-output ratio to rise, thereby undermining the sustainability of public finances and resulting in less fiscal slack being available at times of crisis. As shown in figure 5.9, real interest rates on public-sector debt have been much higher than economic growth rates, particularly in recent years, and this has endangered public-sector solvency (see figure 5.9). As a result, a large and often growing proportion of fiscal revenues has been absorbed by interest payments in several countries (Argentina, Brazil, Colombia, Costa Rica, Ecuador).

Figure 5.9
DIFFERENCE BETWEEN RATE OF GROWTH OF GDP AND REAL INTEREST RATE PAID ON PUBLIC DEBT
(Regional average)

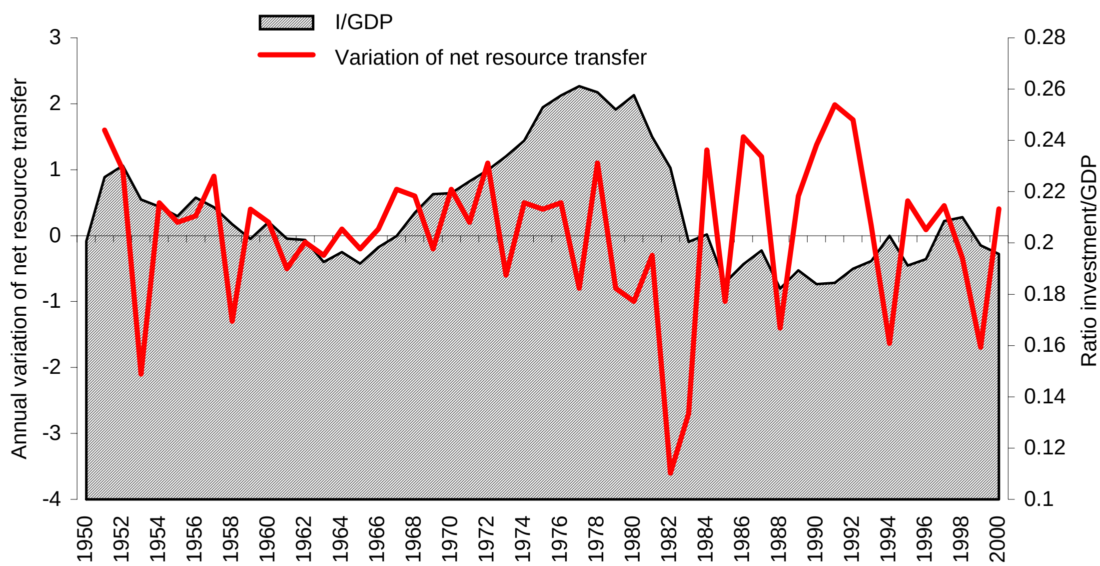


Source: ECLAC, on the basis of official figures.

3. Weak investment process and inadequate financial development

The instability of external financing has had a discouraging effect on investment. This is undoubtedly one of the reasons why the investment rate remains below pre-debt-crisis levels. The decline in the investment coefficient compared to the 1970s has been more pronounced in the larger countries, since these also have greatest exposure to private capital flows. The slight rise in investment seen during the 1990s was achieved thanks to greater external financing, but with no complementary growth in domestic saving and without greater access to long-term domestic or external financing for domestic investors, especially small and medium-sized ones. Figure 5.10 illustrates the weakness of gross capital formation throughout the region and highlights its sensitivity to external financial shocks.

Figure 5.10
LATIN AMERICA AND THE CARIBBEAN: VOLATILITY OF NET RESOURCE TRANSFER AND INVESTMENT/GDP RATIO



Source: ECLAC, on the basis of official figures.

Regression analysis to measure the determinants of investment behaviour in seven of the region's countries shows that a reversal of external capital flows equivalent to 1% of GDP generates a 0.64 percentage point drop in the investment/GDP ratio, as a direct result of the contraction in financing. Furthermore, if this reversal of flows becomes more volatile, provoking greater uncertainty among economic agents, it can induce a further 0.11 percentage point drop in the investment ratio. Other indirect effects of a reversal of flows stem from its effects on expenditure, through the Keynesian accelerator, and on the real exchange rate (Moguillansky, 2002).

Despite the significant changes that have taken place as a result of financial liberalization and the entry of major international financial intermediaries on regional markets, some of the most serious problems of domestic financial systems still persist. It is necessary to continue developing suitable schemes of prudential regulation and supervision in order to ensure adequate levels of solvency and liquidity among financial intermediaries. Shortcomings in this area, compounded by pronounced macroeconomic volatility, have shown through in the financial crises that affected at least 13 countries in the 1990s (ECLAC, 2001a). There has also been insufficient progress in developing long-term domestic saving and financing instruments and in guaranteeing adequate access to financing for business and social sectors that traditionally have been excluded.

The preference among banking systems for short-term financing has persisted. On top of this, intermediation spreads remain significantly wider than those seen in developed countries, which means higher financial costs for the domestic business sector or the need for excessive self-financing. Both of these factors discourage real investment and undermine international competitiveness. They have also strengthened the bias towards seeking finance abroad, but this has served to increase vulnerability associated with currency mismatches and has benefited the larger firms almost exclusively.

In several countries, pension reforms involving various modes of transition from pay-as-you-go to individual capitalization systems have encouraged domestic financial deepening and greater availability of long-term funds. Nonetheless, experience shows that it is hard to channel such resources into real investment, given the preference of these intermediaries, and the rules governing them, for investments of secure return and high liquidity.[4] Precisely for this reason, the development of a major market for long-term private-sector debt bonds and a liquid mortgage market is essential to ensure that adequate resources are channelled from these new intermediaries into productive investment. So far, measures intended to strengthen the equity market have proved frustrating in most countries. In some cases, the creation of financial instruments to stimulate long-term financing is resulting in the development of venture capital, investment and guarantee funds, together with loan insurance, although these remain deficient.

Having played an important role in the financing of economic development during the State-led industrialization phase, many development banks suffered major crises in the 1980s, and a good number of them disappeared. Nonetheless, some intermediaries of this type survived and continue to play a major role in the financial sectors of several countries (including Brazil, Chile, Colombia, Costa Rica and Mexico).

One of the priority activities of development banks during the last decade has been to channel resources towards microenterprises, small and medium-sized businesses, and the lowest-income households. This has given rise to new intermediaries, supported in many countries by multilateral and bilateral cooperation agencies. Despite this, the resources accessible to all these traditionally marginalized sectors remain insufficient.

III. The domestic domain: tackling the globalization of financial volatility through countercyclical macroeconomic policies

Faced with a globalized world and volatile capital flows, the authorities need to tackle financial risks by taking a broader view of macroeconomic stability. Objectives should no longer be confined to those that have monopolized their attention in recent years (control of the fiscal deficit and reduction of inflation), but should also embrace real goals, especially in terms of economic growth and its stability (ECLAC, 2000c, vol. III, chap. 1, and ECLAC, 2001e). Otherwise, it is highly likely that the volatility of external funding will continue to generate pronounced business cycles in developing economies.

In view of this, it is essential for domestic authorities to react prudently to periods of market exuberance, pre-empting situations of vulnerability while also leaving room for policy to cope with barren phases on international financial markets. Both the volatility of financial flows and the accompanying instability in economic growth rates have strongly discouraged productive investment, thereby undermining long-term growth. Instability in the real economy has been as negative for long-term growth as unstable price levels. Greater stability in the real economy in the short run, and stronger economic growth in the long run, are largely complementary goals therefore, but there are non-negligible conflicts between the two which tend to show through at critical moments.

Nonetheless, domestic authorities have limited autonomy in designing countercyclical policies, given the constraints imposed by the volatility of international financing. Accordingly, to expand possibilities for developing countries to adopt countercyclical macroeconomic policies, the domestic efforts mentioned in the previous section need to be complemented by improvements to the international financial architecture. Equally, analysis of the domestic aspects of this strategy,

[4] Moreover, bringing about the transition to these new schemes means running fiscal surpluses to cover the costs of paying pensions to retirees who remain in the old system, and fulfilling minimum pension guarantees (ECLAC, 1998c).

presented below, needs to be complemented by a study of the international factors considered in the final section of this chapter.

1. Prudential management of cyclical upswings: fiscal, monetary and regulatory aspects

Stable economic growth depends on the adoption of sustainable methods for directly influencing the key macroeconomic policy variables. This necessarily means taking a long-term view of policy design, avoiding the accumulation of unsustainable imbalances and taking advantage of the slack produced during expansionary phases to accumulate resources for coping with subsequent lean periods. The measures adopted to achieve this objective should concentrate on the fiscal, monetary and exchange-rate domains, along with prudential regulations, capital flows and the regulation and supervision of domestic financial markets.[5]

Coping adequately with the recurrent business-cycle vulnerability of public accounts requires public administration to be capable of responding to three fundamental challenges. The first of these is adherence to a long-term fiscal rule throughout the cycle, to avoid the economic and political costs of abrupt adjustments. This requires the development of tools to shift the budgetary process towards a framework of discipline and flexibility, clearly identifying transitory factors and ensuring fiscal management consistent with a financial position corrected for fluctuations in the level of activity and raw material prices. Secondly, it requires structural deficits to be identified well in advance to prevent excessive public borrowing from imposing a burden on future generations. This, in turn, requires multi-year fiscal programming, based on projections of the potential growth of the economy, with moderate assumptions being adopted that avoid “optimism bias” (in which positive episodes are viewed as permanent, while negative ones are assumed to be transitory), to ensure fiscal management that is more consistent in the long term. Thirdly, it is necessary to overcome the bias against capital expenditure, which stems from the fact that it is generally more sensitive to fiscal adjustments than current expenditure.[6]

Fiscal policy should be designed on a multi-year basis, with a long-term horizon defined on the basis of structural balance (or a small surplus or deficit), or else establishment of a target for the ratio between public debt and GDP. Despite progress made on budgetary programming, current fiscal-policy rules in many countries still tend to prioritize short-term targets that look no further than the annual cycle and lack clauses for coping with the unforeseen situations that are always occurring. In this regard, the passing of fiscal responsibility laws and the adoption of fiscal rules in some countries of the region in recent years are major steps in the right direction.[7] The achievement of countercyclical macroeconomic policy goals is also facilitated by the use of public-income stabilization funds, both for taxes and for revenues dependent on the price of raw material exports, when these are relevant. There are several outstanding examples of these in certain countries, which can be used as a basis for designing public-income stabilization funds of a general nature.[8]

Monetary and exchange-rate measures should aim to prevent periods of abundant external financing from causing excessive expansions of external and domestic credit and unsustainable

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[5] The literature on the domestic macroeconomic management of financial volatility is extensive. Recent contributions include World Bank (1998, chap. 3), ECLAC (1998c, 2000c, 2001c), Ffrench-Davis and Reisen (1998), Furman and Stiglitz (1998), Helleiner (1997), Heymann (2000) and Ocampo (1999a, chap. 5 and 2002b).

[6] Many countries are making major efforts to adapt their budgetary processes to the goal of stimulating and protecting public investment. For this purpose, it is helpful to plan and manage current and capital expenditures separately.

[7] Starting in 1999, several of the region’s countries (Argentina, Brazil, Ecuador and Peru) have passed fiscal responsibility laws that include multi-year targets and rules aimed at avoiding procyclical fiscal-policy behaviour. Similarly, Chile adopted a structural surplus rule making it possible to insulate public expenditures from transitory reductions in revenue.

[8] Several of the region’s countries have a tradition of using stabilization funds for revenues earned from raw materials (coffee and oil funds in Colombia; copper and oil in Chile; and oil in Venezuela). These have been added to general tax-revenue stabilization funds in the context of new fiscal responsibility laws. For a discussion of the usefulness of these general tax stabilization mechanisms, see ECLAC (1998b).

appreciations of the real exchange rate. This assumes a certain degree of discretion on the part of central banks to intervene on the foreign-exchange market whenever they detect strong pressures for currency appreciation; they also need to be able to intervene simultaneously in the money market to keep monetary expansion within the ranges needed to meet the inflation target, which usually acts as a monetary policy anchor. Such interventions may have two counterproductive effects, however. Firstly, they may result in high interest rates which attract capital inflows, thereby inducing a further appreciation of the local currency. Furthermore, if signs of crisis are already in the air, high rates may speed up financial deterioration and result in additional fiscal pressures (the cost of bailing out financial sectors and more costly domestic public borrowing, when this is on a large scale). In this type of situation, experience in the region has shown such policies to be more effective when they are accompanied by regulations on capital inflows, active prudential regulation and oversight of financial systems, and an explicit liability policy aimed at improving the time profile of public- and private-sector debts, whether domestic or external.

Given current levels of development in the region's capital markets, compounded by highly volatile capital flows and a deficient international financial architecture, full capital-account convertibility is not a first-best policy. On the contrary, tools for the prudential management of capital flows are desirable, whether direct (special deposits or taxes on external financing, direct regulation of portfolio flows) or indirect (tax rules).[9] The capital-account regulation schemes adopted by Chile and Colombia in the 1990s represent some of the best practices in this field.[10] As complementary tools of macroeconomic policy, the prudential regulation of capital flows gives the authorities extra room to adopt restrictive monetary policies during cyclical upswings and avoid unsustainable appreciation of the exchange rate; in the form of liability policy, they discourage short-term flows in particular, and make it possible to improve the structure of external financing.[11] Their advantages include the fact that they are applied to financial and non-financial agents alike, through a non-discriminatory price instrument.

Permanent schemes of prudential regulation, whose strictness increases or decreases over the cycle, are preferable to alternating between free capital entry and quantitative controls on outflows at times of crisis. In fact, the latter may prove totally ineffective if applied in improvised fashion during crises, since, instead of producing the desired effects, it can lead to massive avoidance or evasion of controls and a loss of policy credibility.

Strict control over mismatches between foreign-currency assets and liabilities in the financial system is an essential element of any prudential regulation arrangement. Nonetheless, direct access to external credit by non-financial firms, especially the larger ones, undermines the effectiveness of such rules in preventing mismatches between foreign-currency assets and liabilities throughout the economy as a whole. Mismatches accumulated by non-financial agents during times of expansion also affect the soundness of the financial system, because it is difficult to cover the local-currency liabilities that non-financial agents with debts abroad will subsequently face.

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9 This point of view reflects a long tradition at ECLAC. Some of the most rigorous analyses of unstable capital flows and policies for managing them before the "tequila crisis" were done by ECLAC in 1994. See the second edition of the report prepared at that time by ECLAC (1998b, part III). In addition, UNCTAD (1998), United Nations (1999), Akyüz and Cornford (1999), Eichengreen (1999), Griffith-Jones (1998), Griffith-Jones and Ocampo (1999) and ECLAC (1999e) all provide expositions on the advisability of imposing restrictions on capital flows, in a world characterized by an imperfect financial safety net.

10 Chile and Colombia have successful experience in managing capital flows through the imposition of unremunerated reserve requirements on financial flows. Up to May 2000, Chile also required portfolio and direct investment inflows to remain in the country for at least one year. Colombia regulates such investments directly.

11 Studies on the topic conclude that this instrument has had positive effects on the term structure of external debt by raising the cost of short-term borrowing without significantly affecting longer-term flows (Agosin and Ffrench-Davis (2001); Agosin (1998); Le Fort and Lehmann (2000); Ocampo and Tovar (1999); and Villar and Rincón (2000)). Some studies also suggest that the use of special deposits has made it possible to effectively reduce capital inflows, or equivalently, give a wider margin for sustainably raising domestic interest rates or changing expectations of devaluation, or both of these objectives simultaneously. Such effects have been the subject of major controversy, however. Valdés-Prieto and Soto (1998) and de Gregorio, Edwards and Valdés (2000) present a contrary view.

The alternative of combining instruments for prudential regulation of financial intermediaries with explicit tax mechanisms to discourage foreign borrowing by non-financial agents, among other taxes on firms' net foreign-currency borrowing (Fischer, 1998), may be an effective substitute. This type of measure does not cover borrowing by private individuals, however, nor does it apply to stock-market investments. Moreover, the design of flexible taxes on non-financial firms' foreign borrowing is much more complex than the regulation of capital flows at the border.

2. The exchange-rate regime

The most important lesson to be drawn from events in the region and in the world at large over the past few decades is that there is no exchange-rate regime that is optimal for all countries at all times.[12] Each country has to decide the degree of nominal exchange-rate flexibility it requires, according to its objectives and real possibilities for managing the other macroeconomic policy variables.

Contrary to this opinion, in the 1990s a belief developed that the only stable exchange-rate regimes in the current phase of globalization are those at the two ends of the spectrum —either a fully flexible regime, or a "hard anchor" for the exchange rate (currency board or dollarization). This view is based on the susceptibility of soft anchors and managed flexibility to speculative attacks stemming from a perceived inconsistency between exchange-rate policy and policy in the rest of the economy. Such reasoning points up a real problem, namely the difficulty of maintaining fixed exchange rates (soft anchors and, in some cases, hard anchors too) in the face of major expectations of devaluation. The main problem currently faced by exchange-rate regimes in developing countries, however, is their capacity to manage trade shocks and fluctuations in the capital account, which are largely *exogenous*, and at the same time prevent them from resulting in more pronounced economic cycles, or in incorrect or unstable relative prices that discourage development of the economy's tradable sectors. The contradictory demands of flexibility and stability required to fulfil these complex objectives can only be responded to under extreme regimes, forgoing some of their elements.

A nominal anchor, accompanied by prudent fiscal and monetary policies, contributes to price stability and, consequently, to real exchange rates that provide stable incentives to the economy's tradable sectors. Nonetheless, the volatility of capital flows tends to inject major instability into the domestic activity of countries adopting this type of exchange-rate regime. In addition, the absence of mechanisms to facilitate relative price adjustment in the face of negative external shocks (falling export prices, devaluation of the currency of a major trading partner, or revaluation of a currency to which the country's own exchange rate is linked) may entail high adjustment costs, including long periods of recession or slow growth caused by a structurally overvalued exchange rate. Given the weak control of the money supply that this type of regime entails, the central bank cannot exercise the functions of "lender of last resort", and this creates major problems if crises affect the domestic financial system.

In contrast, flexible exchange rates allow the economy to absorb international trade and financing shocks. They also make it easier to adopt a monetary policy aimed at stabilizing the business cycle, and partially discourage short-term credits and certain types of portfolio flow. They do not help mitigate medium-term financing cycles, however. On the contrary, expected fluctuations in the real exchange rate can actually accentuate such cycles (Ffrench-Davis and Ocampo, 2001). Fluctuations in the real exchange rate usually send contradictory signals about tradable goods- and service-producing sectors, which discourages investment in them. When major monetary mismatches occur, fluctuations in the exchange rate have wealth effects (gains from

[12] Frankel (1999), Hausmann (2000), Velasco (2000) and Williamson (2000) provide more detailed analyses of the issues discussed in this section.

appreciation during the upswing and losses from devaluation during crises) that accentuate the business cycle.

The great virtue of intermediate regimes, of “managed flexibility”, is their potential to reconcile flexibility with stability. Examples of such regimes include crawling-peg mechanisms, currency bands, the establishment of indicative targets or bands that the authorities are willing to partially defend, and dirty floating. All these regimes involve some degree of flexibility, making it possible to absorb external shocks and adopt counter-cyclical policies, while also aiming to provide more stable incentives for international specialization. In this context, the desired level of flexibility will basically depend on the size of the economies concerned (greater flexibility is desirable in the larger economies), the depth of domestic financial and foreign exchange markets (greater flexibility in countries with greater domestic financial depth), and the degree of capital-account openness (greater flexibility when capital accounts are more open).

As this latter condition suggests, effective management of intermediate regimes may require active regulation of capital flows to manage the pressures arising from international financing. Such schemes can also come under speculative pressure when macroeconomic policy as a whole fails to inspire the necessary credibility. For this reason, more flexible intermediate regimes have an advantage, particularly in larger economies with open capital markets.

3. “Self-insurance” mechanisms

Another way of promoting stability is to keep an adequate level of liquid funds (current or contingent) available to absorb transitory negative external shocks and prevent speculative attacks on the local currency. All countercyclical policy requires resources to be accumulated during boom periods (both external and fiscal, and slack in the financial system), to be used later in times of scarcity. Nonetheless, the accumulation of international reserves may prove very costly, because, as recent crises have shown, net capital outflows can amount to several percentage points of GDP. The costs of such reserves need to be weighed against the expected benefits of their role as a self-insurance mechanism.

Some countries have tried to achieve this same objective by negotiating contingent credit lines with international private-sector banks; but the market for these is still incipient and the amounts available may be inadequate at times of acute crisis, especially those involving contagion phenomena. This suggests that the most appropriate mechanisms are collective insurance schemes based on the provision of international liquidity through multilateral mechanisms and regional arrangements, as discussed below

4. Prudential regulation and supervision of financial systems

In recent years, unstable domestic financial systems have triggered or propagated external crises and fluctuations throughout the rest of the economy. Globalization has also shown that systemic risk is correlated across countries, and this has led the international financial community to encourage adoption of suitable prudential regulation systems, governed by internationally accepted recommendations, particularly those drawn up by the Basel Committee on Banking Supervision.

Strengthening the stability of domestic financial systems requires progress to be made on five fronts: (i) improving regulation and oversight of credit, currency and market risks in the commercial banking sector; (ii) strengthening the regulation of financial conglomerates; (iii) restricting concentration in the banking system, since oversized banks can suffer from moral hazard in the sense of being considered “too large to go under”; (iv) improving criteria on the presence of foreign financial institutions that are not subject to reliable supervision and consolidated regulation of conglomerates in their home country; and (v) tightening regulations on the first-tier State banking system to require adherence to market standards when evaluating portfolio quality, similar to those applicable to private commercial banks.[13]

Apart from strengthening the solvency of financial systems, banking regulation and supervision aims to provide space for countercyclical policy. Spain has adopted regulatory standards for this purpose, aimed at evaluating credit risk over a horizon encompassing the whole business cycle. Their purpose is to eliminate or partly offset the procyclical effect of traditional rules for assessing and prudentially providing against risk. These lead to underestimation of risk and hence excessive credit expansion in the upswing phase, but also the need to maintain substantial reserves against doubtful loans at times of crisis, thereby intensifying the credit drought characteristic of such periods. This type of regime should be generalized and complemented with exceptional prudential provisions and stricter rules for risk-rating during expansionary phases, especially in the case of financial institutions whose portfolios grow very rapidly. It would also be a good idea to place a limit on the value of equity and real estate that can be used as loan collateral. On the other hand, during recessions it is important to prevent regulatory standards from accentuating credit constraints and the lack of liquidity among economic agents, by establishing mechanisms that make it possible to apply stricter prudential standards gradually over time.

5. Domestic financial development

Stable and deep development of domestic financial systems has positive effects for saving and the financing of investment, and reduces the vulnerability of economies to external financing cycles. The development of active markets for equities, financial derivatives and both public and private debt, together with securitization, secondary mortgage markets and the establishment of other regimes aimed at risk diversification, as well as increasing participation by institutional investors such as pension funds, insurance companies, mutual funds, and investment and venture-capital funds are some of the many examples of this process.

Any policy adopted for this purpose should also make it possible to overcome market failures, and even the lack of markets, or certain segments or components thereof. This gives a key role to institutional development policies aimed at creating regulatory conditions that encourage the emergence of new market segments and financial intermediaries, and also much more direct participation by the State in this process, preferably as a catalyst for increasing participation by the private sector.

The financial development process assumes conditions of macroeconomic stability that are consistent with the goal of lengthening maturities on financial saving and creating instruments through which this can occur. It also requires adequate protection of financial contracts against inflation risks. One of the main ways of achieving this is by index-linking long-term financial instruments and contracts.

The liquidity of an instrument is directly related to the breadth of its market; in other words, the presence of multiple agents capable of absorbing fluctuations in the supply and demand for securities without excessive variations in their prices, thereby stabilizing markets. This underscores the need to support the development of secondary debt markets and “market makers” (investment banks or other intermediaries authorized to act as such) to play this stabilizing role. Given their characteristics in terms of quantity, uniformity and lower risk, domestic public-debt securities tend to act as market leaders and benchmarks for other instruments. A lengthening of the maturities applicable to such securities could therefore help extend the time horizon of the market as a whole.

As they contain real guarantees and allow greater homogeneity in the securities traded, securitized mortgage loan packages can also promote market development, especially for longer-

[13] Held (1994), ECLAC (1998b, chap. XII) and Livacic and Sáez (2000) develop these arguments further.

term securities —in this case provided there are institutions that effectively perform the securitization and market-making function. Two publicly owned agencies, known as Ginnie Mae and Fannie Mae,[14] played a key role in the United States in setting up a market such as the one described.[15] The strong development of the mortgage lending system in Chile is associated with the creation of an indexed unit of account, which makes it possible to protect long-term financial saving from the effects of inflation.[16] The development of new institutional saving agents in the wake of pension system reform in 1981, and the recovery of bank solvency after the banking reform that followed the financial crisis of 1982-1986, gave rise to an active market for financing long-term operations based on securitized mortgage instruments. In both cases, public policy proved crucial in setting up the institutional structure needed to deal with important aspects of the financing of activities that require longer horizons.

When economic agents act as financial investors —in other words, when they are not directly involved in real investment activities— the need for risk management is crucial. In some cases this is performed by specialized institutions. The function of risk rating and control tends to be carried out by a "first-tier" institution, which applies standardized procedures for assessing the risks of direct investors and reduces portfolio risk through diversification. This is backed up by investors' payment capacity and, in the case of housing, is guaranteed by mortgages. The first-tier institution consolidates a number of individual loans and offers them to the market as a single financial asset. When these are acquired by institutional investors, commercial credit risk (the probability of the original debtor defaulting) is confined to the first-tier institution, since the rating gives it comparative advantages. Meanwhile, financial risk (the likelihood that future interest rates will differ from current ones, causing the prices of the assets in the portfolio to fluctuate) is shifted to the financial investor. In both cases, regulations are needed, along with other capital requirements and provisions guaranteeing the solvency of the investing intermediary.

Mechanisms for hedging the risk of losses, which facilitate the development of long-term lending, also have an important place in the institutional structure. Examples are guarantee funds and loan insurance, aimed mainly at hedging commercial risks. Financial risks can also be covered in a deep secondary market through the development of an active market for financial derivatives. In this case, accounting rules should clearly and transparently reflect the assets and liabilities underlying the respective operations, in order to determine the corresponding capital requirements.

Since not all intermediation involves banking activity, there is a need for oversight of the distribution of tangible and intangible assets between the banking sector and the associated financial activities. This requires consolidated supervision schemes for financial conglomerates or, at least, for the subset of activities of a banking consortium. Transparency, the provision of timely and reliable information, and governance of the management of third-party funds and resources to safeguard the property rights and trust of non-controlling owners are fundamental.[17] Transparency is another relevant factor for proper management of firms' corporate ownership. Primacy of the property rights of investors in institutional funds compared to those of their managers, and equality of property rights —although not management rights— between minority and controlling shareholders, are two aspects that should be given priority in the construction of a regulatory framework aimed at developing deeper domestic capital markets in the region.

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14 The official formal names of these institutions are Government National Mortgage Association and Federal National Mortgage Association, but they are usually referred to by the nicknames mentioned in the text.

15 In 1970 Ginnie Mae introduced the world's first securitized asset for housing finance, thereby creating a new market. At the same time, the government withdrew from Fannie Mae, thus giving a major boost to private participation in a market that previously had been promoted by the public sector.

16 Argentina, Colombia and Uruguay have also often used index-linked financial assets for housing finance.

17 The following are essential for this purpose: accounting records; periodic audits that are independent and reliable; the establishment of oversight committees; independent risk rating; separate accounting of fund managers' own assets from those of the third-party fund; and capital requirements for fund managers, the level of which should be sufficient to inspire trust in their solvency to protect investors' funds in the event of management contingencies and failures.

Establishing an appropriate regulatory framework may be insufficient to ensure access to credit for small firms and those investing in innovative areas. In the first case, a lack of collateral usually limits SMEs' access to credit, while in the second case excessive caution with respect to risk holds back real investment. Public support takes a variety of forms, but its aim is always to limit exposure to the risk of losses. The establishment of guarantee funds with both public and private participation, and subsidies for loan insurance premiums, are possible mechanisms for covering and absorbing the credit risks of smaller firms. In addition, institutions such as venture capital companies, also with public-private participation, may prove useful for funding investments by small firms.

A strong public development-bank sector could become an important component of a financial development policy such as the one described. In a modern version, public agents such as these should engage primarily in creating and completing markets, in accordance with the guidelines indicated. As regards their more traditional functions, they may also participate directly in lending activities. This is very important in order to guarantee adequate access to credit for smaller firms, in conjunction with other private, cooperative and solidarity-based intermediaries. Frequently, banks of this type offer new and small-scale clients their first chance to create a financial track record, after which they can graduate to the banking sector in the private market. In this way, they enable informal activities, small-scale farm owners, technological innovators, and small and medium-sized firms in general to gain access to banking services in the normal way.

The market can make a major contribution to permanent and continuous scrutiny of portfolio risk, when the development-bank sector is an autonomous extrabudgetary institution taking in third-party funds, without State guarantee, and when it is periodically subject to portfolio risk rating by the Superintendent of Banks and other agencies. To strengthen payment collection policies, they can be organized as first-tier commercial banks subject to private banking regulation and oversight procedures. For this they would need to make their commercial operations more transparent, improve their collection policies and rapidly detect the financial effects of short-term political pressures. They could also be organized as second-tier banks and deal with the problems of targeting, improving financial resource bidding rules and applying a combination of rate subsidies for partial loan insurance premiums, or, alternatively, operating partial guarantee funds and providing subsidies for credit risk rating by first-tier intermediaries and training in project management and design for potential beneficiaries. Subsidies and transfers should be subject to appropriate social and economic evaluation, and be well designed and operationally transparent; in addition, the fiscal cost they involve should be explicit and financed with properly budgeted public funds.

IV. The international domain: strengthening the governance of financial globalization

In the previous chapter it was argued that achieving greater international financial and macroeconomic stability should be seen as a global public good, offering positive externalities to all countries participating in world markets. This argument highlighted the crucial role played by strong international financial institutions in correcting the glaring disparities that exist in financial market development and asymmetries in the macroeconomic behaviour of industrialized and developing countries.[18] These asymmetries stem from a structural feature shared by all developing

[18] The literature on the issues dealt with in this section is abundant. On the concept of "global public goods" applied to the international financial system, see Helleiner (2000a), Kaul, Grunberg and Stern (1999) and Wyplosz (1999). On international financial reform, see, among others, IMF (1998, 1999a and 2000a), ECLAC (1999e), United Nations (2000b), UNCTAD (1998), Akyüz and Cornford (1999), Eatwell and Taylor (2000), Eichengreen (1999), Fischer (1999), Griffith-Jones and Ocampo (1999), Ocampo (1999a and 1999b) and White (2000).

economies, namely the fact that their currencies are not used as an exchange and reserve assets in international transactions. This asymmetry puts them in an unfavourable position to cope with the volatility that characterizes financial globalization, because it induces unstable access to international markets and a procyclical bias in macroeconomic policies. Overcoming these problems requires sound domestic policy-making, backed by an international institutional framework that supports efforts in that direction.

The components of the reforms needed to achieve this objective were summarized in the previous chapter. This one describes some of them in more detail, in particular the following: (i) development of an international and domestic financial institutional framework to prevent the build-up of excessive financial risk and provide adequate information to markets; (ii) building capacity to respond in timely fashion to the crises that threaten international financial stability; (iii) solution of overborrowing problems and equitable distribution of the costs of crises between lenders and borrowers; (iv) the role of the multilateral development bank sector; and (v) enhancement of the role of regional and subregional institutions in all these fields.

1. Creation of an institutional framework promoting financial stability

International financial stability requires minimum standards on two key issues: prudential regulation and oversight of financial systems, and the supply of information needed to enable authorities and financial markets to function properly. Although these issues are being analysed in the Financial Stability Forum set up by the Group of Seven, developing countries are inadequately represented in this mechanism. The relevant standards need to take into account different countries' absorption capacities and regulatory conditions. Given the global nature of markets, there is a need to move forward simultaneously in the direction of better coordination and greater communication between the supervisory bodies of the various countries.

Prudential regulation and supervision should aim to pre-empt systemic problems by preventing financial agents from assuming excessive risk and ensuring that their assets are proportional to the risks assumed. The strictness of the rules should be consistent with the risks that agents assume jointly as well as individually. This implies the need to expand the boundaries of supervision in two directions: firstly, to non-financial agents that have asset-ownership relationships with financial agents, which will require a move towards consolidated supervision of conglomerates; and secondly, to nonbank financial agents such as mutual funds. In the case of industrialized countries, stronger emphasis should be placed on regulation and supervision of institutions and operations displaying the highest levels of leverage and greatest international presence. In addition, to discourage high-risk financing in developing countries at source, particular importance should be given to risk rating in operations carried out with countries that increase their net borrowing, especially short-term, and to a disproportionate extent in relation to the size of their economies, financial sector and reserves available to service their external liabilities. Moreover, all countries need to take effective steps to prevent and penalize money laundering and other financial crimes, following United Nations recommendations on these issues.[19]

Major challenges still remain on the issue of financial system regulation and oversight. The Basel Committee proposal to provide against risks of expected losses and establish minimum capital requirements using internal ratings-based models, instead of the current practice of using standardized criteria, could raise the cost of international bank lending to developing countries and accentuate their procyclical behaviour (Reisen, 2001b; Griffith-Jones and Spraat, 2001). In addition, establishment of a regulatory system such as the one proposed could change the conditions of banking competition internationally. The greater development and sophistication of banks in

[19] See Blum and others (1998) and United Nations (1998).

developed countries would put them at an advantage, since their portfolio costs and the capital requirements applicable to them would be lower. Any reform of international regulatory standards should strive to avoid such effects.

Efforts to standardize the quality, quantity and transparency of the financial and accounting information received by economic agents are intended to improve market efficiency and the stability of capital flows (Ahluwalia, 2000). One of these, in which nearly 50 countries are participating, involves development by the International Monetary Fund (IMF) of standards for the quality and timeliness of economic and financial information provided to markets. The International Standards of Accounting and Reporting (ISAR) being studied by the United Nations Conference on Trade and Development (UNCTAD) represent another praiseworthy initiative that may lead to more uniform accounting between countries. The International Accounting Standards Committee has also developed a set of basic criteria for adoption by the International Organization of Securities Commissions (IOSCO) to help develop deep and transparent international capital markets.

The provision of transparent information undoubtedly helps markets to function better. The key problem is not a matter of imperfections in the factual information on which economic agents base their operations, but the volatility of their opinions and expectations (Ocampo, 1999a; Eatwell and Taylor, 2000). Often, basic information on the macroeconomic conditions of developing countries has been available, but has been interpreted differently at different times, depending on economic agents' expectations. This has even been true of the agents that are supposedly best informed, namely investment banks, risk-rating agencies, intergovernmental organizations and governments themselves.

Risk-rating agencies require special mention in this context. As private-sector institutions responsible for providing information to investors, their performance has been far from satisfactory. Their characteristically procyclical pattern of risk assessment[20] was one of the factors underlying the volatility of opinions and expectations held by economic agents operating in emerging markets during the pronounced cycles of financial expansion and collapse in the 1990s. Instead of smoothing out financial cycles, which should be one of the aims of a good information system, they have actually tended to intensify them.

Consequently, rules are needed to force such institutions to classify sovereign risk according to publicly known, strict and objective parameters. Such principles could serve as a basis for the establishment of frameworks for regulating and supervising their activities and for the development of mechanisms for exchanging information between them and the regulatory bodies. One alternative worth considering is the possibility of complementing the sovereign risk-rating that these agencies currently perform with a rating system applied by supervisory bodies in the countries of issuance, according to objective and internationally agreed parameters.

2. Emergency financing

Unlike the systems that have developed over more than a century in individual countries, the international financial system does not have suitable instruments for coping with crises. These include the central-bank function of "lender of last resort", preventive mechanisms for intervening in ailing financial institutions, deposit insurance and rules for the refinancing or liquidation of institutions in financial difficulties. The purpose of such mechanisms is to preserve the integrity of the payments system and prevent economic and social losses arising from haphazard and unfair management of financial crises. Although such instruments were designed to respond to crisis situations, they also act preventively by helping to prevent destabilizing expectations from arising and leading to systemic crises.

[20] The recent cases of Enron and Kmart show that this problem is common to corporate risk-rating activities.

With respect to the growth of the international financial market, IMF has been left behind, for while it can create money to generate liquidity by issuing special drawing rights (SDRs),[21] the exceptional funds needed to handle the most serious crises of recent decades have depended on arrangements to borrow. These allow IMF to obtain loans from the main industrialized countries, along with bilateral contributions from these countries to complement the corresponding bailout programmes. The uncertainty caused by this procedure undermines the Fund's capacity to send signals that bolster confidence (Eichengreen, 1999; Ocampo, 1999a; Rodrik, 1999a). The first of the main innovations made during the 1990s involved the creation of an emergency funding mechanism enabling IMF to respond rapidly in serious crisis situations. The other two correspond to new services: the Supplemental Reserves Facility, designed to respond to exceptionally large financing needs, and the Contingent Credit Line, designed to help countries suffering from financial contagion phenomena. The first of these facilities has functioned relatively well, but the second has not produced the expected results. To gain access to this credit line, countries have to sign a contingent agreement, but, given the potentially negative signal that this sends to markets, and the small amount of resources available, it is hardly surprising that no country has yet applied to make use of the facility. One possible modification could be to provide automatic access to this credit line to countries that receive a positive rating in the consultations held under article IV of the IMF Articles of Agreement.

The potential benefits of IMF support for countries that have satisfactory macroeconomic fundamentals, but face capital flight that threatens to destabilize their economies, are so important that they justify continued efforts by the international community to find better ways to perfect and develop the mechanisms analysed (see proposals by Williamson, 1996; Ezekiel, 1998; and Ahluwalia, 1999, among others). A facility containing sufficient funds for these purposes, with rapid and automatic disbursement, would make it possible to change the international regime and the behaviour of economic agents by sending out a powerful signal discouraging speculative behaviour. This is the right way to turn the Fund into the "international quasi-lender of last resort" that the current phase of financial market globalization requires.

To achieve this aim and respond flexibly to financing needs during periods of crisis, IMF resources require considerable expansion. Possibly the most appropriate of the available alternatives would be to make temporary issues of special drawing rights in crisis periods, which would be available to all member countries. These temporary issues would be eliminated later, unless it was desired to create permanent liquidity.[22] Of course, greater use of SDRs in the international financial system is an objective in itself, long advocated by developing countries; it should not be conditional on the adoption of specific credit lines.

Macroeconomic programmes adopted in the IMF framework should be governed by a consideration of their effects on the most vulnerable sectors of the population, not only through adequate social safety nets, but also through macroeconomic adjustment measures that take their social impact into account. As always when conditionality is applied, a principle to be observed is that adjustment policies should be effectively supported by the domestic authorities, in accordance with the principle of ownership. Apart from anything else, this principle is essential to guarantee appropriate institutional development and the sustainability of adjustment measures.

3. The solution to problems of overborrowing

In the absence of an emergency financing facility that partly acts as an international lender of last resort, crisis-hit countries must drastically adjust their economies or unilaterally suspend both

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[21] All SDR issues must be explicitly approved by the IMF Executive Board, with a majority of 85% of the votes. The last issue was made in January 1981.

[22] See United Nations (1999), Ocampo (1999a), Council on Foreign Relations (1999), Meltzer and others (2000), and Camdessus (2000). With respect to the two last-mentioned, see Ezekiel (1998) and Ahluwalia (1999).

debt service and capital outflows. Both of these alternatives can have a high cost in terms of growth, employment and poverty. To avoid the costs of these unilateral measures, organized multilateral rules need to be designed to deal with this type of problem.

For countries that have solid macroeconomic fundamentals but suffer from liquidity problems, the first line of defence should be emergency financing. This gives them the breathing space needed to adapt the time profile of their external obligations. External support is crucial in such cases, to prevent a temporary illiquidity situation from degenerating into insolvency in the wake of irrational panic among the investor community. A temporary suspension of external payments should only be necessary in extreme cases. Alternative mechanisms that have been used during some recent crises (by the Republic of Korea and Brazil, among others) include pressure from the regulatory authorities of industrialized countries to persuade commercial banks to renew their credit lines to affected countries.

On the other hand, in cases of insolvency, renegotiation and possibly a reduction in liabilities is an imperative need, where delay will harm debtors and creditors alike, and can also result in an inequitable distribution of crisis costs among the latter (i.e., between those who withdraw their capital early and those who keep it in the country during crisis periods). Even in such cases, as indicated below, the renegotiation of external obligations should be a complement rather than a substitute for emergency financing.

Any institution that considers itself international in this field should uphold voluntary negotiation between the parties as a basic principle. At the same time, however, multilateral rules are needed to give legal force to the suspension of payments and debt renegotiation, and allow the country to tackle the two basic problems of coordination that arise in negotiations of this type. These are: (i) the possibility that some lenders, and even borrowers, may refuse to participate in the solutions proposed (the free-rider problem); (ii) the potential slowness of the process or the successive negotiations, which impose high costs on debtors and creditors alike (a negative-sum game).

To solve the first of these problems, loan contracts need to contain collective action clauses, whether in the case of sovereign bonds, bonds issued by private institutions or loans extended by the private banking sector. Such clauses should include rules to ensure that certain agreements apply to all obligations.[23] The clauses should be of a universal nature, also applicable to debt contracts entered into by industrialized countries, to prevent markets from punishing the countries using them through higher interest rates or more restricted access to funds.

Suspensions of payments should be decreed by the debtor country and be complemented with restrictions on portfolio capital outflows. They should also be sanctioned by a multilateral institution, in order to give them legitimacy and legal force. This is also important to avoid moral hazard problems among debtors; that is, unjustified declarations of moratorium. The International Monetary Fund could participate in such operations, recommending that countries should use this mechanism and possibly acting itself to legitimize suspension of payments. Some analysts consider that IMF already has powers to take measures of this type under article VI. In addition, the Fund should continue its practice of granting loans to countries that have fallen behind in their payments but are making efforts in the right direction (lending into arrears), as this encourages creditors to cooperate in solving crises.

To avoid prolonged and repeated negotiations, it would also be helpful to design mediation mechanisms and, where necessary, a multilateral arbitration procedure which the parties could voluntarily apply to settle disputes in debt refinancing or renegotiation processes. As a creditor, IMF is not the appropriate institution to fulfil these functions, which should therefore be assigned to

[23] There are important precedents for the mandatory introduction of this type of clause in debt contracts, especially in bond issues in the British market (Griffith-Jones, 1998).

another institution within the multilateral system. Negotiations and agreements should be wide-ranging and cover liabilities in both the private and public sectors. It would also be useful to encourage the adoption of flexible agreements, contemplating relatively foreseeable contingencies, in order to avoid renegotiations and explicitly encourage creditors to continue extending funds to countries in difficulties during critical periods. Such lending could be linked to restructuring programmes in some cases. Financing extended to countries during crisis periods should be given priority in any restructuring.

In the period following the successful conclusion of debt restructuring, countries will not have access to private capital markets. Agreements need to take this situation into account by providing grace periods for servicing the restructured debt. Multilateral banks have a crucial role to play during this period, by providing additional funding. As the key objective of restructuring programmes is to help countries get back into private capital markets, one scheme that would be worth studying involves setting up multilateral bank guarantee funds for this very purpose.

4. The role of multilateral development banks

Multilateral development banks, such as the World Bank, together with its regional counterpart the Inter-American Development Bank (IDB) and subregional ones such as the Andean Development Corporation (ADC), the Central American Bank for Economic Integration (CABEI), the Caribbean Development Bank (CDB) and the Financial Fund for the Development of the River Plate Basin (FONPLATA), have played a decisive role in lending to countries, especially the relatively less developed ones, that have no access to private capital markets. In the case of countries that do have access to such markets, especially middle-income countries, multilateral development banks also play an important role in providing countercyclical financing to cushion the effects of external shocks.

This type of support has been a complement rather than a substitute for the balance-of-payments financing provided by IMF and a number of bilateral sources, particularly as development banks are the only long-term financing sources available at times of crisis. For that reason, they make it possible to moderate the necessary fiscal adjustment, set up social safety nets for the most vulnerable sectors and avoid cutbacks in critical social programmes. Support from such institutions has played a major catalyzing role in maintaining and restoring confidence in countries during crisis periods, and hence in renewing private capital flows, which is no less important. Such characteristics have made development banks a highly valued asset for shareholder governments in developing countries, as is reflected in the commitments assumed during their capitalization processes.

Multilateral financing also has undeniable advantages in terms of its conditions, since the corresponding loans are granted for longer periods and at lower interest rates than those offered by private sources. These characteristics are particularly pronounced in the case of the new commitments aimed at relatively less developed countries, a fact which, together with the greater importance of such resources for these countries, highlights the preferential treatment these institutions provide. Such treatment also extends to the region’s relatively higher-income countries.

The low risk classification characteristic of multilateral banks stems from a mix of developing countries’ commitment to meet their obligations to them, backing from developed countries in the case of the World Bank and IDB, and conservative management of their asset-capital and portfolio concentration ratios. Even those that do not receive contributions from industrialized countries have a lower risk rating than the countries of the region, which enables them to gain access to external funds at a lower cost than the countries themselves can. The case of the Andean Development Corporation (ADC) is highly significant in this respect, since its shareholders consist exclusively of developing countries in the region. This fact, together with the strong portfolio quality generally displayed by multilateral banks, suggests that private agents tend to overestimate the main risk, though not only during crisis periods. Overestimation of risk represents a market failure that, in itself, justifies the action of multilateral development banks.

The loan portfolios of regional and subregional institutions have a diversified profile that varies from one institution to another. These institutions have tended to prioritize social development projects, and have played a pioneering role in funding sustainable development programmes and channelling resources towards traditionally excluded productive sectors, particularly small and medium-sized business. At the institutional level, it is also worth mentioning their support for State modernization programmes. In addition, they are involved in the development of physical infrastructure, certain productive sectors and, in some cases, foreign trade operations, especially those related to integration processes.

These institutions use three mechanisms in their role as catalysts of private financing: (i) guaranteeing timely payment on public debt, or the timely payment of liabilities (in the form of guarantees or subsidies) assumed by the State in support of private projects; (ii) direct financing or co-financing of innovative private projects, contributed directly by the bank or by the relevant financial corporation; and (iii) venture capital provided by the financial corporation to innovative firms. These mechanisms have served as catalysts for private-sector investments in infrastructure. There have also been a number of pioneering operations to guarantee public debt service on bond flotations made during periods of great uncertainty on capital markets. In all these cases, private-sector investors value not only the soundness of multilateral institutions, but also their privileged relationships with governments. Such operations should be expanded further, on clear additionality criteria; in other words, the creation of support mechanisms that do not exist in the private market at a given moment. There is also the possibility of providing guarantees for bond issues by countries that have not previously made use of such financing mechanisms.

In view of the crucial role of domestic financial development, multilateral banks can also play a major role in the creation of financial markets in developing countries by supporting the restructuring of institutions guaranteeing adequate financial governance and modernization of domestic financial markets. Support should concentrate on creating national development banks and on their operations to provide funding for micro-enterprise and small and medium-sized businesses. Multilateral banks can also help create markets by issuing their own debt paper on developing-country markets, which serves basically to foster the development of long-term financial saving instruments.

Technical assistance, whether provided directly or linked to project funding, has been another characteristic of these institutions, in addition to their role in providing a meeting place for member countries for information exchange and analysis of successful and, equally importantly, failed development experiences. In close collaboration with United Nations agencies, they can also help ensure an adequate supply of certain global public goods in areas such as public health and the environment.

5. The role of regional institutions

As can be inferred from the preceding pages, Latin America and the Caribbean has a very comprehensive regional network of multilateral banks, probably the most complete in the developing world, consisting of the Inter-American Development Bank (IDB) and several subregional institutions. It can also claim several of the most advanced trade integration processes and one of the few regional mechanisms for balance-of-payments support in developing countries. Progress achieved on all these fronts needs to be consolidated, and new areas of cooperation added.

One of the most important of these is macroeconomic cooperation. Given the extreme sensitivity shown by intraregional trade, especially in South America, to business cycles and fluctuations in the exchange rates of national currencies (ECLAC, 2001d), closer coordination of macroeconomic policies has become a key element in consolidating integration processes. The loss of autonomy that has occurred in these domains is another good reason to seek subregional and regional spaces in which such autonomy can be regained at least partially.

Progress has been made in this field in all subregional integration agreements.[24] These cover a wide range of increasingly deep processes: (i) dissemination of greater information on macroeconomic policies and personal knowledge of Ministry of Finance and Central Bank staff in the different countries; (ii) institutionalization of mechanisms for peer review of such policies, as a contribution to the preventive goals of global macroeconomic supervision and gradual internalization of the effects of local policies on neighbouring countries; (iii) definition of common macroeconomic targets and rules for fiscal and monetary policy, and for public and foreign borrowing; and (iv) possible establishment of solid macroeconomic coordination mechanisms, leading in the long run to the creation of monetary unions. Obviously, one should not be blind to the problems posed by the more advanced phases of this process, as revealed by the experience gained over three decades by the European countries. For this reason, objectives clearly need to be modest in the short term, focusing on the first three areas mentioned.

An initiative highly complementary to the above would be to establish mechanisms to coordinate policies for prudential regulation and supervision of financial systems. What is desirable in this area is the development of mechanisms for peer review of such policies, and possibly the design of more specific minimum standards than those of the Basel Committee. The fact that some of the main international banks operate in several countries of the region further underscores the importance of coordination in this field.

Several authors have also referred to the importance of having regional institutions capable of providing balance-of-payments financing, stressing their advantages over an international architecture consisting exclusively of a global fund (see Agosin, 2000; Mistry, 1999; ECLAC, 1999e). Institutions of this type can help modify financial agents' expectations and behaviour with respect to the region as a whole, thereby preventing contagion. Such a system would be able to channel resources to participating countries more rapidly, on better terms and in potentially larger volumes, thereby providing them with much stronger defences at times of crisis.

The Latin American Reserve Fund is one of the few institutions of this type in the developing world. In over 20 years' service, it has lent major sums to the five member countries of the Andean Community (Bolivia, Colombia, Ecuador, Peru and Venezuela). For the smaller countries (Bolivia and Ecuador), it has been just as important as the International Monetary Fund.

At the international level, the most ambitious proposal of this type has been to create an Asian Monetary Fund —an idea that was studied at the initiative of Japan in the IMF meeting held in Hong Kong in 1997 (Hamada, 2000). This idea crystallized recently, albeit on a smaller scale, in the agreement signed by 13 Asian countries —the members of the Association of South-East Asian Nations (ASEAN), China, the Republic of Korea and Japan— in May 2000, to establish swap agreements between their respective central banks (Park and Wang, 2000).

A scheme of this type, either in the framework of the Latin American Reserve Fund or independently of the number of members and functions, could serve to considerably expand mechanisms for supporting countries in the region that face balance-of-payments crises. By way of

[24] The region's four integration schemes (CARICOM, the Central American Common Market, the Andean Community and MERCOSUR) have all made progress in agreements to define common macroeconomic targets on inflation, fiscal deficit, domestic and external public borrowing, the current account deficit and international reserves, among other issues. In each case the aim is to achieve greater macroeconomic stability, to strengthen capacity to cope with external crises and avoid damage to intraregional trade stemming either from sharp exchange-rate fluctuations or from deep recessions among the members of a subregional bloc. The earliest and most ambitious of these integration schemes is CARICOM, which has reached agreement to move towards tax harmonization, free circulation of persons, capital and services, and even monetary union. For a detailed analysis of the nature of these processes and the difficulties they face, see ECLAC (2002) with respect to CARICOM, see chapter 11 of this volume.

example, estimates by Agosin (2000) suggest that a regional fund consisting of just 15% of the international reserves of the South American countries could have financed all the external assistance channelled through these countries' emergency programmes in the last decade, except those corresponding to Argentina and Brazil.

Regional funds could be recognized by IMF as an integral part of a world system to support countries facing balance-of-payments crises. For this purpose, they could also be authorized to receive IMF loans quite automatically. Such funds could also be authorized to acquire special drawing rights denominated in their members' currencies, which they would then lend to countries in crisis.

Chapter 6

The integration of Latin America and the Caribbean in global trade and production circuits

The rapid internationalization of markets and production characteristic of the current phase of globalization has been accompanied in Latin America and the Caribbean by far-reaching structural reforms. These reforms have generated drastic changes in production and trade incentives and in transnational corporations' strategies and positions in the economies of the region. Clearly, patterns of integration in the global economy have reflected the structural diversity of the region's economies in terms of factor endowment, size of the domestic market, geographic location, business and institutional development, and accumulated technological capacity.

More than a decade after the emergence of these new patterns of integration with the global economy, Latin America and the Caribbean have clearly succeeded in boosting their export sectors and becoming a magnet for FDI. Despite these overall advances and unquestionable progress in some countries and production sectors, however, these changes have not been sufficient to improve the region's structure of comparative advantages in ways that would enable it to move forward in changing its production patterns based on the generation and absorption of technical progress throughout the production system or to achieve greater social equity (ECLAC, 1990 and 2000a). Consequently, the region has not been able to reduce the productivity gap between it and the developed world. At the same time, the structural heterogeneity of business enterprises, regions and social groups has been intensifying.

This chapter considers the main aspects of Latin American and Caribbean integration in global trade and production. The first section examines the different patterns of production specialization and composition of trade in goods and services. The second focuses on investment flows and the different corporate strategies being used in the region. The third considers the role played by regional and subregional arrangements as a stepping stone to global integration. The fourth and final section presents a public policy agenda for enhancing integration in the world economy and identifies measures for adoption at the national, regional and international levels.

I. Trade specialization in Latin America and the Caribbean

1. General trends

In the 1990s, Latin America and the Caribbean had one of the world's highest growth rates for merchandise trade in terms of both volume and value. Between 1990 and 2001, the average annual increase in merchandise exports amounted to 8.4% in terms of volume and 8.9% in value. These rates were surpassed only by China and the more buoyant Asian economies. However, imports into the region grew at even higher rates (11.7% in volume and 11.6% in value). These figures were far higher than those posted elsewhere, except for China, where the rate was nearly as high as it was for the Latin American and Caribbean region. As shown in figure 6.1, both exports and imports grew much faster than GDP, which showed only a modest increase. Between 1990 and 2001, GDP grew at an average annual rate of 2.7%, which was just one third as much as exports and one quarter as much as imports.

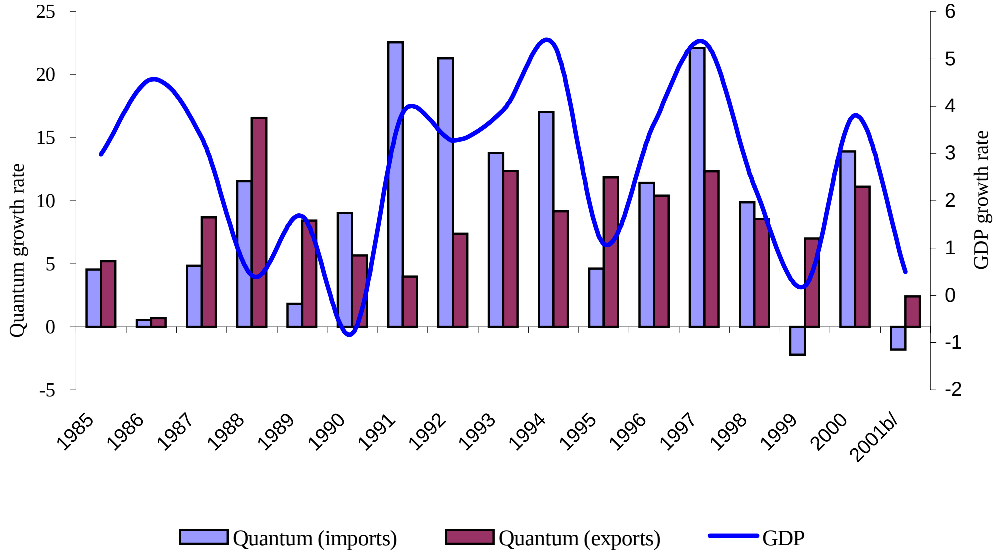
Owing to these uneven trends, the average increase in the exports/GDP ratio was 20.4% for 1999-2000. The import coefficient increased even faster, to stand at 21.4% for 1999-2001; this marks a sharp contrast with the figures for the 1980s, when imports into the economies of the region averaged around 10% of GDP.[1] The imbalance between the performance of exports and imports has generated larger trade deficits, and this, together with debt service payments and profit remittances, has led to a deterioration in the balance-of-payments current-account position. The region's deficit gradually deepened between the late 1980s and the mid-1990s and has remained high since then, even in years when economic growth was sluggish. On average, between 1994 and 2001, the current account deficit was equivalent to 3.0% of regional GDP.

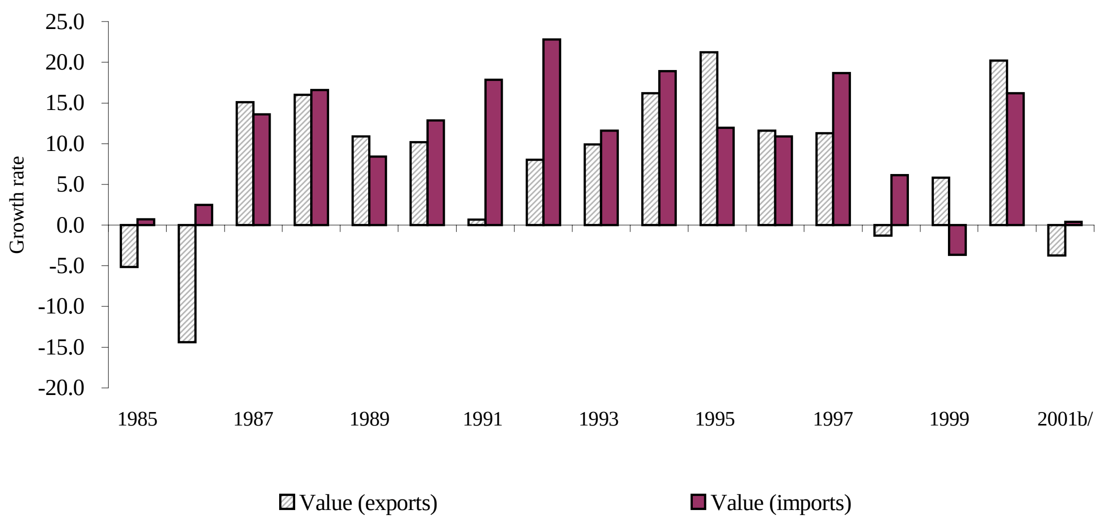
It is important to note, within this pattern, the increasing share of the overall deficit in trade in goods and services that is accounted for by the imbalance in the commercial services account.[2] In fact, between 1992 and 2001, the deficit on the services account was equivalent to two thirds of the total trade deficit (see table 6.1). Even in years such as 1995, 1996 and 2000, when the region recorded a surplus on the merchandise trade balance, this was far outweighed by the deficit on the services account.

[1] Although in the last 15 years consumer goods have come to represent a much larger share of merchandise imports than before (increasing from one tenth to one fourth of the total), capital and intermediate goods still account for the lion's share of the region's imports.

[2] The World Trade Organization (WTO) defines commercial services as the sum of transport, travel and other commercial services. Therefore, it does not include government services, investment income or compensation of employees.

Figure 6.1
LATIN AMERICA AND THE CARIBBEAN:a/ **TRADE AND GROSS DOMESTIC PRODUCT, 1985-2001**





Source: ECLAC, on the basis of official figures.

a/ Includes 19 countries of the region: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Dominican Republic, Uruguay and Venezuela.

b/ Preliminary estimates (Preliminary Overview).

Table 6.1
GROWTH IN TRADE IN GOODS AND SERVICES IN LATIN AMERICA, 1990-2001
(Millions of current dollars)

	1990	1991	1992	1993	1994	1995
Trade in goods						
Exports	136,283	137,150	146,420	160,811	188,120	227,938
Imports	105,159	123,798	151,345	168,959	200,620	224,875
Trade balance: goods	31,124	13,352	-4,925	-8,148	-12,500	3,063
Trade in services						
Exports	25,114	26,794	29,460	31,349	35,139	36,838
Imports	33,273	36,085	40,240	44,504	47,780	48,625
Trade balance: services	-8,159	-9,291	-10,780	-13,155	-12,641	-11,787
Trade balance: good and services	22,965	4,061	-15,705	-21,303	-25,141	-8,724

	1996	1997	1998	1999	2000	2001
Trade in goods						
Exports	254,948	283,740	279,523	297,849	356,938	344,716
Imports	249,169	304,898	317,470	304,001	352,778	346,934
Trade balance: goods	5,779	-21,158	-37,947	-6,152	4,160	-2,218
Trade in services						
Exports	40,769	40,902	44,903	43,139	48,748	46,722
Imports	54,504	57,326	62,200	58,726	66,274	66,756
Trade balance: services	-13,735	-16,424	-17,297	-15,587	-17,526	-20,034
Trade balance: goods and services	-7,956	-37,582	-55,244	-21,739	-13,366	-22,252

Source: ECLAC, Division of International Trade and Integration, on the basis of official data from 19 countries in the region: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Dominican Republic, Uruguay and Venezuela.

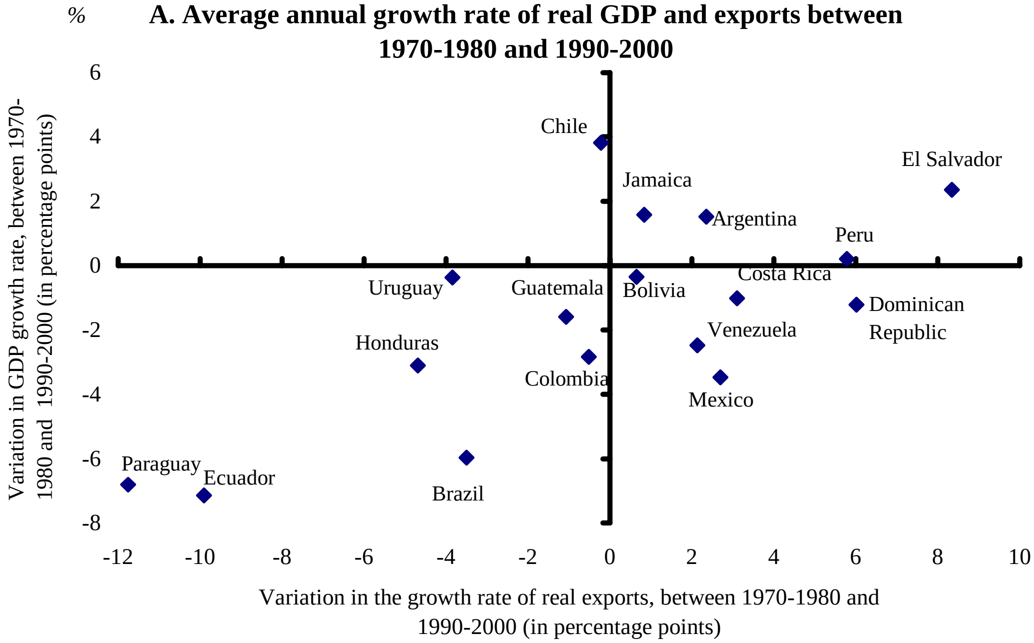
The sharp, generalized downturn in the region's terms of trade in the 1980s was followed by a slight upward trend in the 1990s (see box 2.1 in chapter 2), although the results varied from country to country. In any event, this trend was not strong enough to make up for the ground lost in the 1980s. In 2000, for example, the terms of trade for non-oil-exporting South American countries were still one third below their1985 level.

One of the notable features of the region's situation during the last decade was undoubtedly the contrast between its strong export performance and success in attracting FDI (see section II), on the one hand, and the weakness of overall production, on the other. In fact, despite the economic upturn seen in the region during the 1990s, economic growth rates remained well below those observed before the debt crisis.

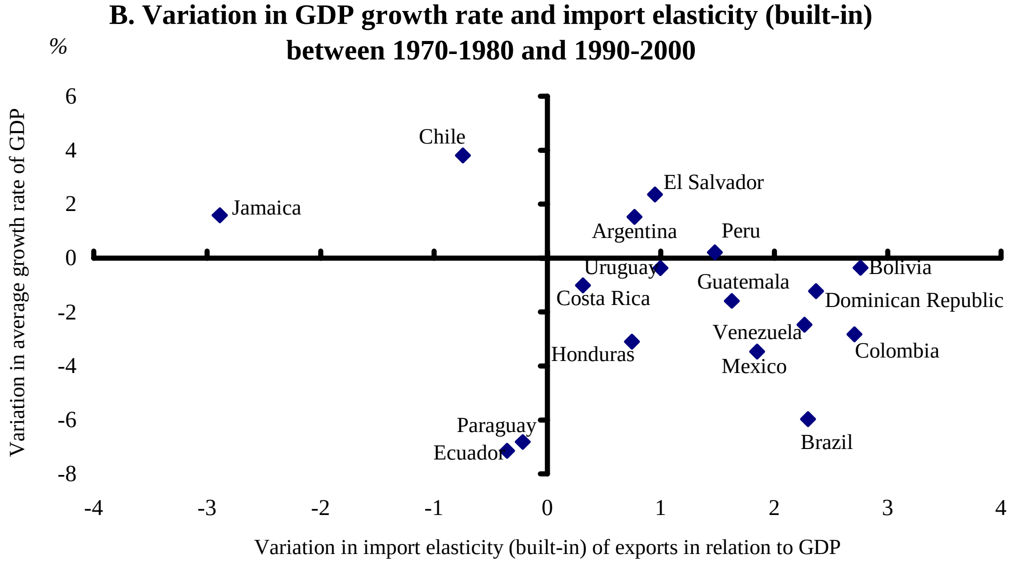
Overall, this result can be seen as the net effect of the opposing impacts on aggregate demand of export growth and a sharp increase in the import coefficient (Moreno Brid, 2002). If the periods 1990-2000 and 1970-1980 are compared, a positive link can clearly be discerned between the region's export performance and the rate of economic growth (see figure 6.2.a). Nevertheless, the group of countries with a faster growth rate was smaller than the group in which production growth was slower than in the 1970s. Moreover, this occurred even in some countries which managed to step up the development of their export sectors significantly, such as Mexico, the Dominican Republic and Costa Rica.

Figure 6.2

A. Average annual growth rate of real GDP and exports between 1970-1980 and 1990-2000



B. Variation in GDP growth rate and import elasticity (built-in) between 1970-1980 and 1990-2000



Source: Juan Carlos Moreno Brid, "¿Por qué fue tan bajo el crecimiento económico de América Latina en los noventa? (una interpretación estructuralista)", 2002, unpublished.

This result is largely attributable to the sharp rise in the implicit elasticity of imports to GDP (figure 6.2). This increase has been associated with a reduction in levels of protection, the tendency towards a revaluation of the exchange rate that accompanied this reduction in many countries and the high import content of inputs in many of the most robust export industries, especially in the manufacturing sector. Although the unprecedented level of import penetration did contribute to the modernization of the production apparatus and to an expansion of new export sectors based on the increased incorporation of imported inputs, it also weakened the linkages between growth sectors —associated with export activity and foreign investment, among other factors— and production activity as a whole. In net terms, this effect has tended to prevail over the effect of export growth.

The strength of export performance has varied in the different countries of Latin America and the Caribbean. While the region as a whole saw its world market share rise from 4.5% to 5.6% between the beginning and the end of the 1990s, this increase was limited to a small number of countries (primarily Mexico, the Central American countries, Argentina, Chile and Colombia) (table 6.2). Mexican exports made particularly strong gains. As a result, by 2000 Mexican exports accounted for almost half of the regional total in terms of value, whereas at the end of the 1980s they had amounted to only about one quarter (the figures for both years include the exports of assembly industries). In contrast, the region's leading exporter in the late 1980s —Brazil— saw its share of total Latin American and Caribbean exports shrink from one quarter to one sixth.

Export specialization in the region followed three basic patterns during the last decade. The first, which was exhibited mainly by Mexico but also by some countries of Central America and the Caribbean, was characterized by integration into vertical flows of trade in manufactures centred chiefly in the United States market. In the second, which mainly corresponded to South America, the countries belong to horizontal production and marketing networks, especially of natural-resource-based commodities. This group is also characterized by highly diversified intraregional trading activity and by a lower concentration of destination markets. The third pattern is based on the export of services, mainly for tourism, but also financial and transport services, and is the predominant pattern in some countries of the Caribbean and Panama. As will be discussed below, the strategies of transnational corporations have a strong impact on these patterns of integration into world trade flows.

Overall, as was seen in chapter 2, the increase in the region's share of international trade was more a reflection of competitiveness gains in slow-growth items than of its integration into the more dynamic global trade flows. Thus, the quality of the region's export specialization, measured in terms of the relative weight of high-demand products in the export basket, continues to be poor. What is more, no signs of improvement were seen during the 1990s except in the cases of Mexico and some countries of Central America and the Caribbean Basin, all of which exhibited the first of the regional specialization patterns described above (see table 6.2 and ECLAC, 2002).

The two markets accounting for the largest relative increases in exports from Latin America and the Caribbean in the 1990s were the region itself and the United States. These upswings are associated with the strong influence exerted by Brazil, in the first case, and by Mexico, in the second (see figure 6.3). Even if these two countries are excluded from the calculations, however, these two destination markets maintain their higher ranking, with the regional market in the lead. The more developed markets (United States, European Union and Japan) absorbed more than half of the exports from all the countries and groups in 2000, with the sole exception of Mercosur (excluding Brazil). Overall, the regional market, as the destination for more than a quarter of total exports in all cases except Mexico, is extremely important. As will be discussed in section III, the regional market is even more important when the composition of trade is considered in qualitative terms.

Table 6.2

LATIN AMERICA AND THE CARIBBEAN: CHANGES IN MARKET SHARES AND RELATIVE SPECIALIZATION INDEX FOR HIGH-DEMAND PRODUCTS

	Market share (%)				**Relative specialization index for high-growth products** a/		
	1990	**1993**	**1996**	**1999**	**1990-1993**	**1993-1996**	**1996-1999**
Mexico	1.292	1.446	1.911	2.441	0.515	0.844	0.679
Mercosur b/	1.552	1.528	1.545	1.499	0.645	0.828	0.655
Argentina	0.365	0.373	0.475	0.472	0.461	0.709	0.497
Brazil	1.093	1.070	0.987	0.949	0.793	0.950	0.860
Paraguay	0.034	0.024	0.028	0.022	1.514	1.206	0.525
Uruguay	0.059	0.062	0.056	0.056	0.454	0.537	0.736
Andean Community	0.888	0.822	0.913	0.822	0.298	0.622	0.369
Bolivia	0.024	0.019	0.020	0.017	0.125	0.680	0.748
Colombia	0.209	0.208	0.231	0.238	0.696	1.113	0.700
Ecuador	0.098	0.107	0.111	0.101	0.139	0.309	0.172
Peru	0.114	0.101	0.115	0.105	0.322	0.546	0.649
Venezuela	0.444	0.387	0.436	0.361	0.250	0.561	0.219
CACM c/	0.190	0.230	0.274	0.350	1.550	0.975	1.323
Costa Rica	0.070	0.084	0.086	0.127	1.458	1.162	1.568
El Salvador	0.022	0.029	0.043	0.050	2.848	1.030	1.443
Guatemala	0.053	0.063	0.073	0.083	1.471	1.082	1.220
Honduras	0.035	0.044	0.058	0.073	1.156	0.628	1.501
Nicaragua	0.011	0.009	0.014	0.016	0.484	0.354	0.670
CARICOM d/	0.182	0.163	0.145	0.131	0.787	0.711	0.348
Antigua and Barbuda	0.001	0.001	0.002	0.001	5.695	0.101	1.875
Bahamas	0.034	0.026	0.014	0.013	0.332	0.959	0.140
Barbados	0.005	0.004	0.005	0.004	5.368	0.804	2.609
Dominica	0.005	0.006	0.005	0.006	1.022	0.921	1.351
Granada	0.004	0.003	0.002	0.002	8.260	3.216	6.391
Jamaica	0.001	0.001	0.001	0.001	2.179	0.093	0.643
Montserrat	0.009	0.012	0.012	0.011	0.440	0.461	0.882
Saint Kitts and Nevis	0.044	0.041	0.038	0.033	1.121	0.734	0.737
Saint Lucia	0.000	0.000	0.000	0.000	38.380	0.606	1.750
Saint Vincent and the Grenadines	0.001	0.001	0.001	0.001	8.666	1.848	1.408
Trinidad and Tobago	0.004	0.003	0.003	0.003	0.626	0.242	0.357
Belize	0.005	0.004	0.003	0.002	1.884	1.223	1.219
Guyana	0.017	0.011	0.011	0.011	0.023	0.042	0.042
Suriname	0.052	0.048	0.048	0.044	0.716	0.877	0.222
Others							
Aruba	0.003	0.015	0.017	0.016	0.301	0.947	0.007
Chile	0.286	0.293	0.331	0.301	0.320	0.669	0.725
Cuba	0.037	0.025	0.024	0.017	1.015	1.377	0.895
Haiti	0.014	0.004	0.004	0.007	0.548	0.168	0.537
Cayman Islands	0.003	0.004	0.004	0.005	0.077	1.024	1.130
Netherlands Antilles	0.035	0.034	0.030	0.020	0.474	0.629	0.079
Panama	0.080	0.079	0.063	0.048	1.630	0.679	0.843
Dominican Republic	0.072	0.087	0.092	0.099	0.257	1.522	1.030

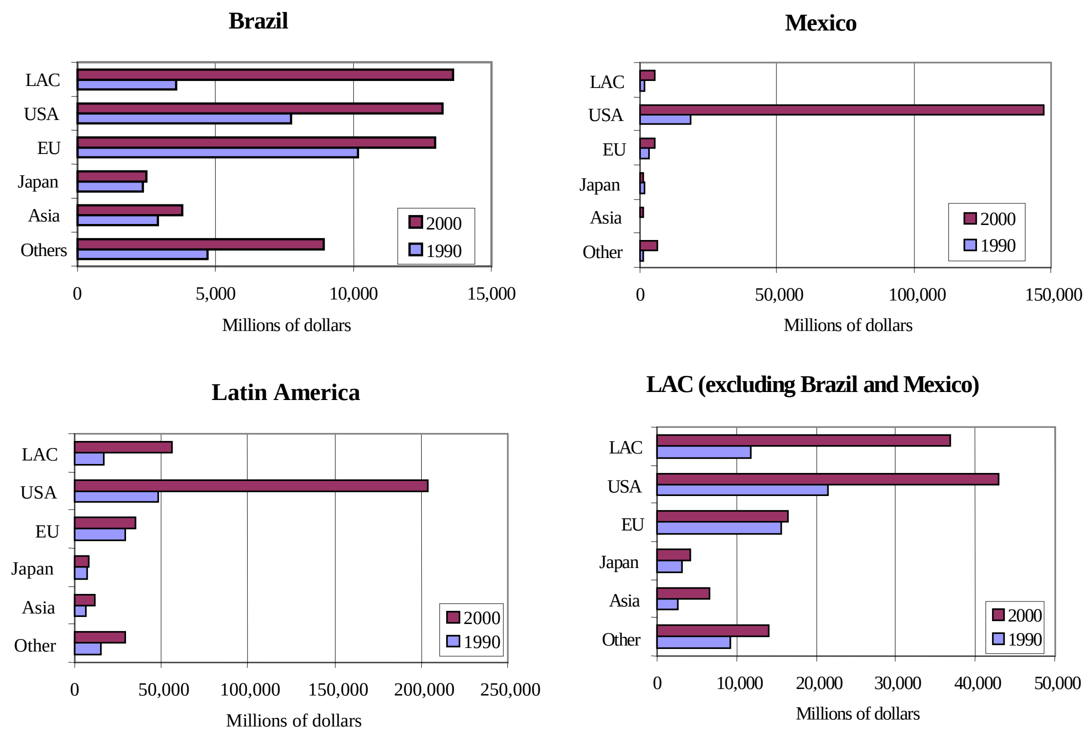
Source: ECLAC, on the basis of data obtained from the Competitive Analysis of Nations Program (2002 version).

a/ Ratio of exports of high-growth products to exports of low-growth.
b/ Southern Common Market.
c/ Central American Common Market.
d/ CARICOM Community.

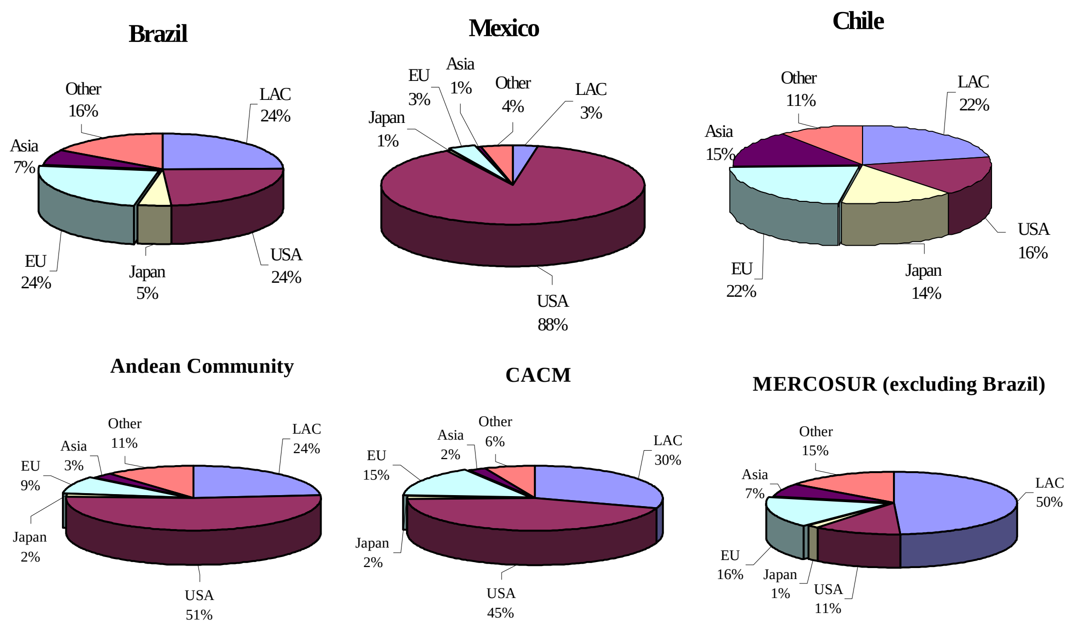
Figure 6.3

LATIN AMERICA AND THE CARIBBEAN: DESTINATION OF EXPORTS, 1990 AND 2000

A. In millions of current dollars



B. In percentages of total exports in current dollars, 2000



Source: ECLAC, on the basis of United Nations COMTRADE data.

2. The composition of trade in goods

Statistics for the last 15 years confirm the fact that a profound change has taken place in the composition of regional exports in terms of their technological intensity (see table 6.3). The most conspicuous pattern is a sharp reduction in the relative weight of exports of primary goods and natural-resource-based manufactures —from 73.5% of the region's total sales abroad in 1985 to 44.3% in 2000— and the relative increase in exports of other manufactures (low-, intermediate- and high-technology products), which more than doubled their percentage share of the export basket, rising from 24.3% in 1985 to 52.3% in 2000. For the reasons described above, these changes were much more intense in Mexico, in some Central American countries (Costa Rica, Honduras and El Salvador) and in some Caribbean countries, mainly the Dominican Republic. The trend in the two major South American blocs —Mercosur plus Chile, and the Andean Community— was similar, albeit considerably less pronounced.

This relative decline notwithstanding, the first category of goods (primary products plus resource-based manufactures) has still accounted for a large percentage of South American exports in recent years, especially in the cases of Mercosur (59%) the Andean Community (84%) and Chile (89%). This category also remains significant for CARICOM (72%). On the other hand, these goods represented a much smaller percentage of exports from the Dominican Republic (13%), Mexico (17%), the members of the Central American Common Market (37%) and Panama (39%).

As mentioned in chapter 2, most of these goods belong to the category of "falling stars" or even "retreat products". In other words, demand for them is at a low ebb on international markets. In the case of primary goods, the region's share of world trade has climbed from 7.1% in 1985 to 9.8% in 2000, but the opposite is true for resource-based manufactures, which contracted from 5.0% to 4.6%. The main export products are crude oil and oil products, animal feed, coffee and coffee substitutes, copper, fresh and dried fruits, iron products, oilseeds, other materials and their concentrates and wood pulp. Most of these products are subject to wide price swings, some face long-standing restrictions on market access (i.e., agricultural produce) in developed countries and others are subject to new restrictions (steel and rolled steel). Most of the manufactures are commodities produced by technologically mature, machinery- and equipment-intensive industries.

In the last decade Mexico has become the most dynamic and diversified exporter of non-resource-based manufactures. It has opted for a closer trade relationship with the United States under the North American Free Trade Agreement (NAFTA), since this guarantees it more stable access to that country's market, which absorbs almost 90% of its exports. This has led to significant changes in its export mix. These changes are illustrated by the following three sectors, which represent different technological levels: garments (low technology), the automotive industry (intermediate technology) and electronic equipment (high technology).

Mexico increased its share of the United States market for imported garments from 3.4% in 1992 to more than 15% by the end of the decade (ECLAC, 2000d). This market penetration was initially accomplished through what are known as "shared-production facilities,"[3] and it was achieved at the expense of some Asian countries. Since the entry into force of NAFTA, Mexico has increased its share by crowding out other Central American and Caribbean countries on the basis of the rules of origin contained in that treaty. It is interesting to note that, as a result, the Central American countries have been obliged to sign free trade agreements with Mexico and the Caribbean

[3] The shared-production mechanism was designed to help United States corporations to compete with Asian corporations on the United States market. Basically, what this mechanism does is to permit products made with United States inputs to enter that country's market with low tariffs and to exempt them from quota limits. Taxes have to be paid only on the value added incorporated into these products abroad, which primarily consists of low-paid labour.

Table 6.3
SELECTED COUNTRIES: EXPORT STRUCTURE BY CATEGORY OF TECHNOLOGICAL INTENSITY 1985 AND 2000
(Percentage of exports)

Countries/Regions	Primary products		Natural resource-based manufactures		Low technology manufactures		Intermediate technology manufactures		High technology manufactures		Unclassified products	
	1985	2000	1985	2000	1985	2000	1985	2000	1985	2000	1985	2000
Latin America and the Caribbean	**50.0**	**27.3**	**23.5**	**17.0**	**7.9**	**14.0**	**12.1**	**24.6**	**4.3**	**14.0**	**2.2**	**3.1**
Mexico	53.4	11.7	10.3	5.8	5.8	14.7	18.0	38.5	9.9	25.3	2.6	3.9
Mercosur	**42.6**	**34.7**	**23.9**	**24.1**	**12.8**	**11.0**	**15.8**	**21.2**	**2.7**	**6.6**	**2.1**	**2.4**
Argentina	56.3	49.8	24.8	21.9	8.9	8.5	6.6	16.2	2.6	2.4	0.8	1.2
Brazil	38.6	27.1	24.6	25.5	13.5	11.6	19.4	24.3	2.9	8.9	1.0	2.5
Paraguay	77.0	57.4	17.6	14.5	4.4	8.7	0.5	0.8	0.2	0.7	0.4	17.9
Uruguay	31.8	36.7	9.7	20.5	22.2	22.0	5.1	13.6	0.6	2.8	30.5	4.4
Andean Community	**59.8**	**59.5**	**32.8**	**24.5**	**2.8**	**6.3**	**2.9**	**6.4**	**0.3**	**0.9**	**1.4**	**2.4**
Bolivia	71.4	56.0	17.7	24.7	1.9	13.4	0.4	1.1	0.3	1.0	8.3	3.8
Colombia	73.8	59.4	13.7	13.2	4.5	10.4	5.4	10.4	0.6	2.0	2.1	4.5
Ecuador	88.0	76.1	9.3	15.4	0.4	3.4	1.4	2.9	0.4	0.9	0.4	1.3
Peru	44.6	41.8	41.9	35.6	7.1	14.5	3.9	2.4	0.4	0.5	2.0	5.1
Venezuela	50.8	59.9	44.2	30.1	1.8	2.6	2.3	6.2	0.1	0.4	0.9	0.7
Central American Common Market	**71.6**	**27.7**	**10.9**	**9.2**	**8.5**	**39.7**	**4.4**	**6.6**	**3.7**	**14.5**	**0.9**	**2.2**
Costa Rica	67.2	29.1	7.9	8.5	14.5	17.1	6.5	8.3	3.2	34.3	0.7	2.8
El Salvador	67.9	13.4	8.4	9.8	9.0	62.7	4.2	5.9	9.8	6.4	0.7	1.8
Guatemala	69.9	36.1	14.4	12.4	6.6	39.9	5.1	7.4	3.2	2.5	0.8	1.7
Honduras	77.7	21.4	14.3	6.4	5.1	65.2	1.7	4.1	0.6	1.3	0.6	1.6
Nicaragua	87.2	46.9	6.9	8.8	1.1	36.7	1.3	2.5	0.4	0.3	3.0	4.7
CARICOM	**41.7**	**37.4**	**39.3**	**34.9**	**5.4**	**10.2**	**5.7**	**11.6**	**6.0**	**1.4**	**1.9**	**4.6**
Antigua and Barbuda	23.8	41.1	6.4	7.3	43.9	2.6	21.5	46.1	2.7	1.6	1.7	1.3
Bahamas	6.8	20.6	73.9	46.4	1.3	1.9	5.1	21.0	11.1	3.7	1.8	6.4
Barbados	2.0	14.3	17.5	41.5	15.5	14.1	12.5	17.0	49.7	8.9	2.9	4.2
Dominica	61.7	28.1	11.1	12.5	4.1	7.2	22.1	40.2	0.6	5.9	0.5	6.3
Granada	88.9	42.8	3.8	8.8	3.9	6.1	1.3	32.8	1.2	1.4	0.8	8.1
Jamaica	58.8	46.3	21.8	22.6	11.7	25.6	5.3	2.9	0.7	0.4	1.6	2.2
Montserrat	16.0	26.0	33.7	10.4	13.8	12.8	11.5	14.3	4.9	34.1	20.1	2.4
Saint Kitts and Nevis	17.2	0.9	27.5	19.8	30.2	8.2	8.3	41.7	10.3	24.8	6.6	4.6
Saint Lucia	86.8	55.1	4.0	9.3	8.0	15.3	0.9	7.3	0.2	7.4	0.2	5.0
Saint Vicent and the Grenadines	83.2	42.7	7.0	5.0	6.0	5.2	2.7	42.1	0.4	1.0	0.8	4.0
Trinidad and Tobago	52.5	29.2	36.8	47.6	2.9	7.9	5.9	13.4	0.6	0.3	1.4	1.5
Belize	17.6	60.4	54.5	25.8	17.6	6.4	7.2	3.8	0.8	2.0	2.3	1.6
Guyana	50.2	33.1	37.7	37.6	1.7	3.3	6.1	2.1	0.8	0.5	3.5	23.5
Suriname	83.7	81.3	12.9	5.6	0.9	0.9	0.9	2.2	0.2	0.5	1.4	9.5
Others												
Chile	41.0	40.3	50.9	48.6	1.3	3.0	3.6	5.7	0.4	0.7	2.9	1.7
Cuba	35.7	22.2	55.0	69.2	4.5	1.7	3.1	3.5	1.1	1.7	0.6	1.6
Haiti	18.4	8.9	4.5	2.9	52.8	85.2	14.3	1.0	7.5	0.3	2.5	1.6
Caiman Islands	53.9	2.3	2.1	7.0	2.7	1.0	36.3	85.3	1.1	2.6	3.9	1.9
Panama	32.5	24.9	15.3	14.3	7.7	18.1	34.7	26.7	5.6	12.0	4.2	3.9
Dominican Republic	23.7	4.9	24.3	8.6	28.2	62.7	9.9	17.5	1.1	3.5	12.8	2.9
Memo:												
Republic of Korea	4.8	1.7	9.3	12.0	48.7	16.9	21.7	29.2	14.4	38.4	1.1	1.8
China	35.0	4.7	13.6	6.9	39.7	47.6	7.7	17.3	2.6	22.4	1.4	1.1
Taiwain Province of China	5.0	1.3	9.1	4.8	48.2	21.8	20.7	25.0	15.9	45.5	1.2	1.5

Source: ECLAC, on the basis of information obtained from the CAN (Competitive Analysis of Nations) computer software (2002 version).

countries have had to negotiate amendments to the Caribbean Basin Initiative in order to maintain their competitiveness vis-à-vis Mexico on the United States market (Pérez and others, 2001).

The defensive restructuring of the United States automotive industry in response to Japanese competition resulted in advantages for Mexico (and Canada) since, under the NAFTA rules of origin, at least 60% of the total value of vehicles must originate in NAFTA member countries (Mortimore, 1998). By the late 1990s, more than 13% of United States imports under this heading came from Mexico, and three of Mexico's leading exports were passenger vehicles (10% of the total), vehicles for the transport of goods (4%) and motor vehicle parts and accessories (4%). Thus, Mexico already has an export platform that is fully incorporated into the internationally integrated production systems (IPS) of the major motor vehicle manufacturers.

Similarly, in the electronics industry Mexico is already a part of the internationally integrated production systems of firms based in the United States (IBM, Hewlett Packard and Compaq, to name a few), Asia and Europe (e.g., Sony, Sanyo, Phillips and Siemens) and of contract manufacturers such as SCI Systems and Flextronics. A number of these firms were already operating in Mexico under the shared-production mechanism provided for in Mexican legislation on export assembly (*maquila*) activities. The application of NAFTA rules of origin and the imminent disappearance of the *maquila* industry as a legal category have obliged European and Asian firms to transfer part of their production activities to Mexico in order to increase local content. Thus, by the end of the 1990s, most imports into the United States under this heading originated in Mexico; the major products in this category were television sets (4.3% of total Mexican exports), telecommunications equipment (4.1%) and computers (3.9%).

These examples clearly demonstrate that Mexico has been one of the winners —and perhaps *the* major winner— in the region in terms of international competitiveness. There is, however, need for caution in evaluating these developments, particularly with respect to the relationship between export growth and economic growth. Contrary to the experiences of some Asian countries, Mexico's successful export sector has not been able to carry the rest of the economy along with it, since GDP growth has remained relatively lacklustre during the last decade and the domestic economy has become increasingly heterogeneous.

Some Central American and Caribbean countries have points of similarity but also major differences with respect to Mexico. Apart from the changes observed in Costa Rica following the arrival of Intel Corporation, integration into international trade flows is, for most of the countries in the subregion, based largely on the manufacture of garments for export to the United States under preferential arrangements. In the early 1980s, the establishment of the shared-production mechanism provided access to the United States market at reduced tariffs as well as higher quotas for garments made with United States inputs. For their part, the countries in the subregion promoted these assembly activities by setting up export processing zones where inputs could be imported duty free and tax breaks were provided. Under the Caribbean Basin Initiative, United States firms importing such goods enjoyed tax exemptions or had to pay tax only on the value added abroad, which was mainly wages.

The sale of these products to the United States market triggered a significant change in the pattern of exports. However, apart from the considerable increase in low-technology manufactures (see table 6.3), the benefits generated by the shared-production mechanism were fairly limited. On the one hand, the mechanism penalized the incorporation of local inputs and, on the other, it unleashed a veritable "incentives war" among countries eager to attract investment (Mortimore and Peres, 2001). The changes brought about in Costa Rica when the Intel production activities in that country were incorporated into the corporation's internationally integrated production system, in combination with the supplementary actions undertaken by the Government of Costa Rica, may generate more thorough-going changes, however. In that respect, Costa Rica's experience may be closer to that of Mexico in its high-technology manufacturing sector, as would seem to be indicated by the fact that Costa Rica's exports of manufactures jumped from 3.2% of total exports in 1985 to 34.3% in 2000.

Among the South American countries, Brazil warrants special attention. This is a continental-scale economy in which the domestic market strongly influences strategic corporate decisions. The country's foreign-exchange policy was partly responsible for its relatively sluggish export performance during much of the 1990s, but this situation changed dramatically following the macroeconomic adjustments implemented in 1999, which gave rise to a new and more buoyant phase in its export performance. In addition, Brazil is undoubtedly the country with the most active technology policy in the region. As a result, it is the only country to have increased its share of high-technology trade flows by developing its own technology in a sector as complex as the aerospace industry. This has been accomplished with the help of a locally owned aeronautics firm (EMBRAER) and the consolidation of a very strong technological corridor (Campinas-São José do Campos). However, these categories still account for no more than a small share of Brazil's total exports, which continue to be composed primarily of natural-resource-based products and of manufactures exhibiting a low degree of product differentiation and intermediate technological intensity (Miranda, 2001 and table 6.3).

Significant trends in South America include the headway being made in relative terms by Bolivia, Colombia and Peru in low-technology manufactures and by Argentina, Uruguay, Colombia and Venezuela in intermediate-technology goods. The latter include consumer durables and, in particular, automotive products, which are covered by special sectoral agreements within the framework of the two South American integration schemes: Mercosur and the Andean Community.

The technology-based classification of exports of manufactures being used here calls for a note of caution. First, trade statistics based on customs records classify products that cross national boundaries, but do not record how much value was added by local manufacturing processes; this valued added has tended to be low in some relatively successful export activities in recent years. Second, the fact that several countries may be involved in the internationally integrated production systems of transnational corporations that produce high-technology goods does not necessarily mean that each of them participates in high-technology production processes. As pointed out in chapter 2, both design and engineering activities and research and development tend to be much more concentrated in the parent companies than in the rest of the integrated system (see chapter 7).

3. Trade in services

In the last two decades, international trade in services has grown faster than trade in goods. In 2000, it exceeded US$ 1.4 billion, or around 20% of total trade in goods and services. It was also more concentrated than merchandise trade, since in 2000, the five largest exporters together accounted for 42% of total trade in services, compared with 38% in the case of goods. The increasing weight of services in the global economy and world trade, owing both to their intrinsic value and to their impact on economic activity as a whole, led to their inclusion in the Uruguay Round and, subsequently, to the General Agreement on Trade in Services (GATS).[4]

In 2000, exports of services from Latin America and the Caribbean stood at US$ 56.2 billion, or 3.9% of the world total (see table 6.4). The region runs a trade deficit on the services account,

[4] This agreement defines four forms of trade in services: (i) *cross-border supply*, that is, services provided by one country to another, such as international calls; (ii) *consumption abroad*, that is, services, such as tourism, used by consumers of one country in another country; (iii) *commercial presence*, which is when a company from one country sets up subsidiaries or branches in another country to provide services; and (iv) *movement of natural persons*, travel by a provider in one country to another for the purpose of providing services.

which, as already mentioned, has had a significant impact on its balance of payments. The region's imports of services amounted to US$ 66.4 billion in 2000, or 4.6% of world imports.

Table 6.4
VOLUME AND COMPOSITION OF EXPORTS OF SERVICES, 2000
(Billions of dollars and percentages)

	Value	Composition		
		Transport	Travel	Other
World	**1 438.1**	**22.9**	**32.5**	**46.6**
Five leading exporters				
United States	274.6	18.6	36.6	44.8
United Kingdom	99.9	18.2	21.7	60.1
France	81.1	23.9	38.1	38.0
Germany	80.0	24.3	22.0	53.8
Japan	68.3	37.5	5.0	57.5
Latin America and the Caribbean	**56.2**	**15.4**	**53.6**	**31.1**
Mexico	13.7	10.0	60.5	29.5
CACM countries	3.9	18.2	56.0	25.8
Panama	1.8	54.0	25.7	20.3
Caribbean	15.2	9.1	70.2	20.7
Cuba and Dominican Republic	6.0	3.5	87.1	9.4
CARICOM a/	9.2	13.5	57.9	28.6
Countries of the Andean Community	5.9	26.3	51.3	22.4
Countries of Mercosur and Chile	15.7	16.9	34.8	48.3
Brazil	9.4	13.8	19.3	66.9

Source: ECLAC, Division of International Trade and Integration, on the basis of official data from the countries.

a/ For some CARICOM countries the statistics included are for 1998 and 1999.

As is well known, international service transactions tend to be underestimated owing to serious shortcomings in the coverage, classification and measurement of these flows. The data shown in table 6.4 correspond to the classification used for balance-of-payments statistics, which basically distinguish between three groups: transport services, travel services and other commercial services.[5] In the main industrialized countries, with the exception of France, this last category accounts for the greater part of service exports. In the case of Latin America and the Caribbean, on the other hand, more than half of total service exports come under the heading of travel, which highlights the importance of the region as a tourist destination. The percentage is particularly high in Mexico (60.5%) and the countries of the Caribbean (70.2%), especially Cuba and the Dominican Republic (87.1%) and some of the small island States of the subregion. The most notable cases in which other categories account for a large proportion of service exports are Panama, which provides transport services through the Canal (54% of its tertiary-sector exports) and Brazil, whose exports of technological services have been expanding since 1985 and exceeded US$ 1.2 billion in 1999 (Ministério da Ciência e Tecnologia, Brazil, 2001).

Many of the smaller Latin American and Caribbean economies' linkages with the global economy are primarily based on services —especially tourism— rather than on their exports of goods. The Central American countries' income from tourism accounted for 4% of GDP in 2000 and represented over 12% of their total exports of goods and services. In some countries of the Caribbean, the impact of tourism on the economy is even greater. In 2000, tourism revenues,

[5] The *IMF Balance of Payments Manual* defines these groups as follows: "transport" includes all services used for conveying passengers, goods and other objects; "travel" includes all goods and services acquired in the host economy by visitors on stays of less than one year; and "other commercial services" includes communications, construction, finance, insurance, information and information technology, royalties and licences, other business, personal, cultural and recreational services, and government services not included elsewhere (IMF, 1993).

measured as a percentage of GDP, totalled approximately 6% in Cuba; 15% in the Dominican Republic; 16% in Jamaica; over 20% in Saint Vincent and the Grenadines, Saint Kitts and Nevis, Barbados and the Bahamas; and 40% in Antigua and Barbuda and Saint Lucia.

II. Foreign direct investment flows to Latin America and the Caribbean

The significant increase in international capital mobility and the intensification of productive and corporate restructuring processes, in addition to the accelerated pace of the economic reforms implemented in Latin America and the Caribbean in the 1990s, led to an unprecedented increase in FDI flows to the region. As shown in table 6.5, these flows increased more than fivefold, if the average for 1990-1994 is compared to the maximum level recorded in 1999, but fell in both 2000 and 2001. Nevertheless, inflows in those two years were still three times as high as those recorded in the first half of the 1990s (see table 6.5). In fact, in that decade, FDI became the main source of external financing, displaying a pattern which, except during the recent crisis, has tended to be countercyclical (see chapter 5). However, the counterpart to these investment flows to the region are outflows in the form of repatriation of profits, which have been increasing in recent years.

Table 6.5
LATIN AMERICA AND THE CARIBBEAN: FOREIGN DIRECT INVESTMENT INFLOWS, 1990-2001
(Millions of dollars and percentages)

Countries	1990-1994 a/	1995	1996	1997	1998	1999	2000	2001 b/
1. Latin American Integration Association (LAIA)	14,371	28,084	41,741	61,458	66,661	82,769	70,404	45,490
Argentina	2,971	5,610	6,949	9,161	7,292	23,984	11,665	5,383
Bolivia	85	393	474	731	957	1,016	733	551
Brazil	1,703	4,859	11,200	19,650	31,913	28,576	32,779	17,292
Chile	1,219	2,957	4,634	5,219	4,638	9,221	3,675	4,455
Colombia	818	968	3,112	5,562	2,829	1,468	2,376	2,310
Ecuador	293	470	491	625	814	690	720	600
Mexico	5,430	9,526	9,186	12,831	11,312	11,915	13,286	12,775
Paraguay	98	103	149	236	342	87	82	80
Peru	785	2,056	3,226	1,781	1,905	2,390	680	723
Uruguay	…	157	137	126	164	235	298	250
Venezuela	836	985	2,183	5,536	4,495	3,187	4,110	1,071
2. Central America and the Caribbean	1,410	1,926	2,068	4,140	5,542	5,261	3,657	3,000
3. Caribbean financial centres	2,506	1,270	8,627	7,827	12,130	17,113	13,941	11,000
Total (1+2+3)	**18,287**	**30,934**	**52,413**	**73,084**	**84,295**	**103,930**	**87,266**	**59,490**

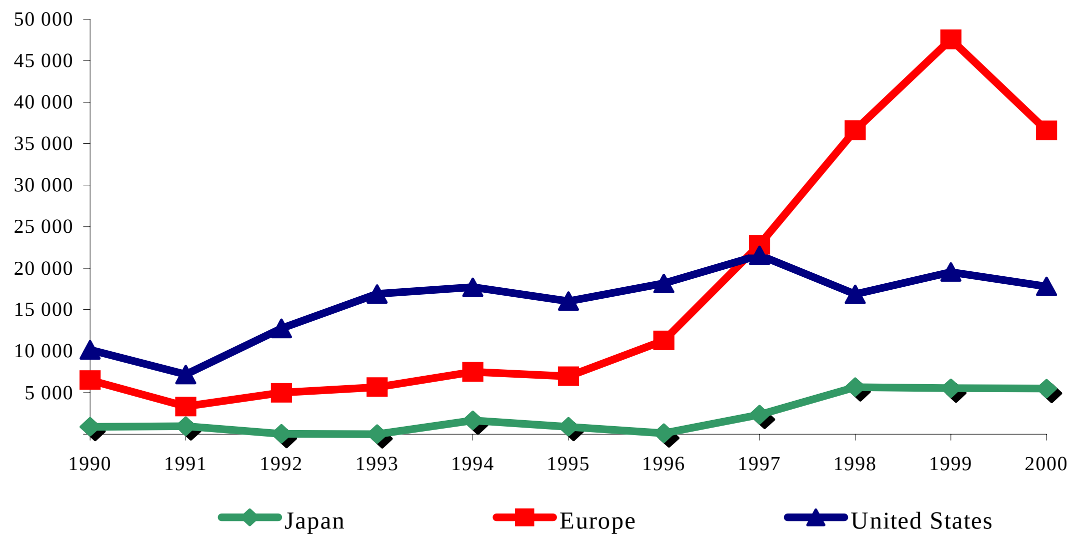
Source: ECLAC, Unit on Investment and Corporate Strategies, Division of Production, Productivity and Management.

a/ Annual average.
b/ Preliminary estimates.

Although the region's three largest economies have been the main focus of attraction of FDI (more than half of the inflows in the first half of the decade and two thirds in the second), the medium-sized and small countries have received flows that are significant in relation to the size of their economies. The international financial centres located in the region have lost relative importance: they received 14% of inflows in 1990-1994, but only 5% in 1995-2000.

There have been significant changes in terms of the origin of flows, especially in the second half of the decade, when investments from Europe increased sharply (see figure 6.4). Spain, in particular, became the second largest investor in the region, after the United States, and the leading European country in this regard. Flows from the United Kingdom, the Netherlands, France, Germany, Italy and Portugal also showed significant increases, while FDI flows from Asia, especially Japan, were less brisk.

Figure 6.4
FDI FLOWS TO LATIN AMERICA AND THE CARIBBEAN, BY COUNTRY OF ORIGIN, 1990-2000
(In millions of dollars)



Source: ECLAC, Unit on Investment and Corporate Strategies, Division of Production, Productivity and Management, based on IDB/IRELA, *Foreign Direct Investment in Latin America: Perspectives of the Mayor Investors,* Madrid and the Inter-American Development Bank (IDB), and on data from the central banks and statistical offices of the investing countries.

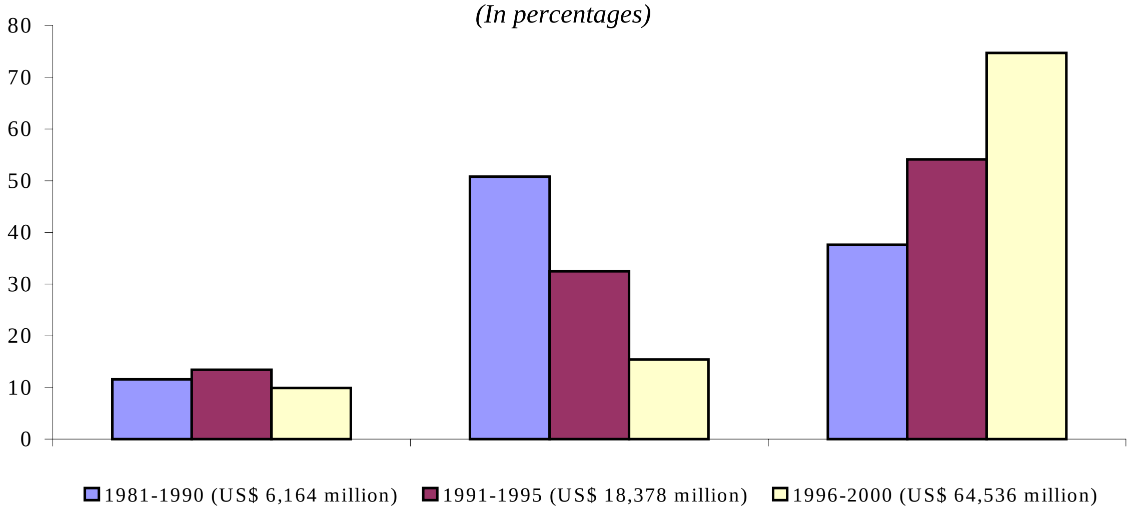
In terms of composition by sector of activity, the most decisive element in recent foreign investment trends has been the rapid growth of investment in the services sector (see figure 6.5). European FDI, in particular, has been channelled primarily to that sector, especially to telecommunications and energy, the banking sector and retail commercial chains (Calderón, 1999). Investments from the United States, once heavily concentrated in the manufacturing industry, started to diversify into services in the second half of the decade, initially with emphasis on energy and telecommunications and, more recently, on financial services.

This marks a dramatic shift in foreign investment patterns in the region, which contrast with those that prevailed in the first post-war decades and up to the late 1980s, when FDI was channelled mainly into manufacturing for the supply of protected domestic markets. Investment in these activities also changed significantly in the last decade. Owing to both changes in international market competition and the economic reforms being undertaken in the region, new transnational manufacturers entered the market and some of the older ones had to redefine their strategies. Some withdrew, opting, in some cases, to supply the domestic market through imports. Others, intent on defending or expanding their market share, rationalized their operations (basically through defensive strategies with respect to competition from imports)[6] or

[6] For example, a survey conducted in Brazil revealed that increased competition on the local market forced subsidiaries of transnational corporations to seek efficiency by reducing their product lines, resorting more to outsourcing arrangements and raising their import coefficient and intra-group trade (Miranda, 2001).

restructured their activities through new investments more in keeping with the new context (ECLAC,2000d).

Figure 6.5
LAIA COUNTRIES: SECTORAL DISTRIBUTION OF FOREIGN DIRECT INVESTMENT, 1981-2000
(In percentages)



Source: ECLAC, on the basis of figures from national sources in the recipient countries.

The nature of the new FDI structures can be determined more precisely using the classification proposed by Behrman (1972) and disseminated by Dunning (1993b, 1994). These authors have identified four types of basic strategies which foreign corporations use, depending on whether they seek (i) natural resources; (ii) markets; (iii) economic efficiency or (iv) strategic capacities (see table 6.6). In addition to these general aims, which may include multiple objectives, their actions may be either defensive or proactive.

Transnational corporations engaged in manufacturing in the region basically follow the second and third strategies. Generally speaking, a distinction can be made between those operating in South American countries and those operating in Mexico and the Caribbean Basin. In the first group, the basic objective remains market capture, but in the context of the more open economies and larger markets that have developed as a result of subregional integration processes. Major investments have been made in the automotive industry, food and beverages, machinery and equipment and chemicals. In the case of the automotive industry in MERCOSUR, some companies with a strong earlier presence, such as Ford Motors, General Motors, Volkswagen and Fiat, have made huge investments to defend their market share, especially in the compact car segment. Other transnational corporations, including DaimlerChrysler AG, Renault-Nissan, BMW, Toyota and Honda, have also entered the market seeking to secure and retain market niches.

The most obvious examples of the strategy aimed at achieving greater productive efficiency by incorporating local plants and processes into integrated production systems that operate internationally, under the leadership of different transnational corporations, are found in Mexico and, to a lesser extent, in some Caribbean Basin countries. As has already been pointed out in earlier analyses, these are, for the most part, transnational corporations seeking to take advantage of positive factors —low wages, geographic proximity and preferential access to the United States market— to enhance their capacity to compete in that market. This is very clear in the case of their involvement in the production of vehicles, computer equipment and electronics, in the garment industry under NAFTA and in the garment assembly industry in the Caribbean Basin countries.

Table 6.6
LATIN AMERICA AND THE CARIBBEAN: STRATEGIES OF TRANSNATIONAL CORPORATIONS IN THE 1990s

Corporate strategy / Sector	Efficiency	Raw materials	National or regional market access	Strategic capacities
Primary		**Oil/gas**: Argentina, Bolivia Brazil, Colombia, Venezuela **Minerals**: Argentina, Chile, Peru		
Manufactures	**Automotive**: Mexico **Electronics**: Caribbean Basin, Mexico **Clothing**: Caribbean Basin, Mexico		**Automotive**: Mercosur **Agribusiness**: Argentina, Brazil and Mexico **Chemicals**: Brazil **Cement**: Colombia, Dominican Republic, Venezuela	
Services			**Finance**: Argentina, Brazil, Chile, Colombia, Mexico, Perú, Venezuela **Telecomumnications**: Argentina, Brazil, Chile Peru **Electric power**: Argentina, Brazil, Central America, Chile, Colombia **Natural gas distribution**: Argentina, Brazil, Chile, Colombia **Retail trade**: Argentina, Brazil, Chile, Mexico	

Source: ECLAC, Unit on Investment and Corporate Strategies in the Division of Production, Productivity and Management.

In primary activities and related manufactures, most firms follow strategies that pursue a combination of the first and third of the above-mentioned objectives; that is, access to natural resources coupled with efforts to achieve productive efficiency within the framework of competition on world commodity markets. The sphere of these operations has been expanded as a result of the opening of sectors and activities previously closed to private investors and, in particular, foreign corporations. In mining and quarrying, inroads by transnational corporations were part of a new pattern for organizing production and applying new technologies. A study by Kulfas, Porta and Ramos (2002) shows that firms that have invested in agro-industry and mining in Argentina have a high export ratio. The same applies to the mining sector in Chile (Moguillansky, 1999).

With respect to services, the size of the local market, regulations and technological changes were the decisive factors for transnational investors seeking market access (the second of the strategies mentioned). This trend stems from a combination of regional and international factors. First, the privatization of State assets, public utility concessions and the large-scale liberalization of the telecommunications, energy and financial sectors prompted the main transnational corporations to make massive inroads into regional markets. Second, the increase in global competition, changes in international regulatory frameworks and rapid and constant technological changes have promoted the globalization of these industries. In these circumstances, a group of emerging transnational corporations is starting to consolidate its position in the services sector. Its regional impact is measured in terms of the population’s access to new products and services, dissemination of international best practices and contributions to the systemic competitiveness of economies.

In short, by means of these basic strategies, transnational corporations have enhanced the Latin American and Caribbean countries’ linkages with the international economy. Thus, some firms in different countries of the region are beginning to join the vertical networks of some international integrated production systems, while others are joining horizontal networks with a strong presence in international markets. Such strategies are also helping to modernize certain sectors of infrastructure which are essential for building systemic competitiveness. There are still no indications, however, that any transnational corporations in the region are pursuing strategies geared to the fourth objective, namely the pursuit of strategic capacities (such as research and development), as may be observed in the OECD countries and in some Asian economies.

As in the case of the world economy as a whole, the purchase of existing assets has played an important role in foreign investors' strategies in the region. This activity was associated first with the privatization processes undertaken in Argentina, Colombia, Peru and Venezuela, among other countries, in the early and mid-1990s, and particularly in Brazil in the second half of that period. Towards the end of the decade, in contrast, the purchase of local private firms took on growing importance as part of an intense process of mergers and acquisitions in the areas of public services, banks and financial services, trade and energy firms. On the whole, however, the purchase of existing assets has represented two fifths of direct investment flows and was thus exceeded by investment in new assets (ECLAC, 2000d).

In the final years of the 1990s, the sudden increase in the share represented by mergers and acquisitions was due to the large amounts involved in a few operations. In 1997 and 1998, Brazil privatized its telephone (TELEBRAS) and electric power distribution services. In 1999, Argentina’s Yacimientos Petrolíferos Fiscales (YPF) was sold to Repsol and Chile’s ENERSIS was sold to Endesa-Spain. In 2000 the so-called "Operation Veronica" took place, in which Telefónica of Spain increased its ownership of its subsidiaries in Argentina, Brazil and Peru to almost 100%. Similarly, in the banking sector, the Spanish banks Banco Santander Central Hispano (BSCH) and Banco Bilbao Vizcaya Argentaria (BBVA) purchased local banks in Brazil and Mexico; in the latter country, a United States bank (Citicorp) also made a major purchase. As these examples show, one of the outstanding features of foreign investment trends was the acquisition by foreign investors, at the end of the decade, of firms which had previously been purchased by local firms under privatization processes.[7] Two of the largest operations were the above-mentioned commercial banking purchases in Mexico and some public utility purchases in certain South American countries (Garrido, 2001; Kulfas, 2001).

The importance of the services sector in attracting FDI in recent years can be measured by its pre-eminence in the process of mergers and acquisitions. Out of a total of 494 operations in the region in 1999-2000, 347 were for services, and accounted for US$ 67 billion (73.5%) out of a total of almost US$ 94 billion. Almost half of the operations concerned basic services (electricity, gas, water, mail and telecommunications), while some business services (financial intermediation, computer services and related activities and other business services) accounted for another 13%.

7 In contrast, the locally owned Carso Group maintained control of Teléfonos de México (TELMEX).

These developments produced significant changes in the ownership structure of the region's largest firms in the 1990s. Among the 1,000 largest Latin American firms in terms of consolidated sales, the number of foreign-owned firms rose from 312 to 395 between 1990-1992 and 1998-2000, and their share of total sales grew from 29.9% to 41.6%.[8] The number of State firms fell from 114 to 63 and their share, from 32.5% to 17.1%, while local private firms increased their share of total sales from 37.7% to 41.3% (see table 6.7).

Table 6.7

LATIN AMERICA (10 COUNTRIES): SHARE OF TOTAL SALES IN EACH SECTOR OF THE 1,000 LARGEST FIRMS, BY TYPE OF OWNERSHIP (1990-1992; 1994-1996; 1998-2000)

(In percentages of total)

Sectors/ownership	1990-1992 a/			1994-1996			1998-2000		
	FE	**LP**	**PE**	**FE**	**LP**	**PE**	**FE**	**LP**	**PE**
Primary sector	**19.3**	**6.3**	**74.5**	**19.3**	**14.5**	**66.2**	**19.7**	**17.9**	**62.5**
Mining and oil	19.3	6.3	74.5	19.3	14.5	66.2	19.7	17.9	62.5
Manufactures	**48.6**	**45.4**	**6.0**	**53.5**	**44.9**	**1.6**	**55.0**	**44.8**	**0.3**
Agroindustry	31.3	66.6	2.1	36.6	62.9	0.6	44.2	55.8	...
Automotive and auto parts	87.0	12.3	0.7	90.5	9.5	...	83.4	16.6	...
Electrical equipment and electronics	68.6	30.1	1.3	89.6	9.5	0.9	84.4	15.0	0.6
Engineering	9.8	57.7	32.5	15.9	73.4	10.7	30.0	70.0	...
Chemicals and pharmaceuticals	77.5	21.4	1.1	79.1	20.9	...	71.3	28.7	...
Petrochemicals	37.4	47.7	14.9	22.5	75.8	1.7	21.8	78.2	...
Cement industry	16.4	83.7	...	31.2	68.8	...	24.6	75.4	...
Cellulose and paper	11.2	79.4	9.3	18.0	82.0	...	19.4	80.6	...
Other manufactures b/	33.0	67.0	...	28.4	71.6	...	27.2	69.9	3.0
Services	**10.2**	**53.0**	**36.8**	**19.3**	**54.0**	**26.7**	**36.9**	**49.7**	**13.4**
Trade	13.3	84.4	2.3	22.9	75.5	1.6	37.1	60.9	2.0
Telecommunications	22.5	38.1	39.5	38.1	17.9	44.0	59.4	36.1	4.5
Electricity	0.2	6.3	93.5	11.7	20.3	68.0	34.7	18.4	46.9
Transport services	7.1	63.5	29.3	4.8	76.7	18.4	16.8	79.5	3.6
Construction	10.3	89.7	...	...	100.0	...	6.8	93.2	...
Public services	...	...	100.0	...	27.2	72.8	10.4	8.2	81.4
Other services c/	16.9	83.1	...	11.0	86.4	2.6	18.6	79.2	2.2
All sectors	**29.9**	**37.7**	**32.5**	**35.5**	**42.7**	**21.9**	**41.6**	**41.3**	**17.1**

Source: ECLAC, on the basis of figures provided by the Departamento de Estudios de América Economía, and figures from other financial sources: Exame (Brazil); Mercado (Argentina); Expansión (Mexico); Semana (Colombia); Estrategia (Chile); and figures from the public reports and balance sheets of the companies.

Note: FE = foreign enterprises, LP = local private firms, PE = public enterprises.

a/ The sample for this period includes only 800 companies.
b/ Includes leather and footware, machinery and equipment, rubber and plastics, photography, publishing, glass, and the textile industry.
c/ Includes tourism.

[8] For the years 1990-1992 the sample covers a total of 800 enterprises.

In terms of the economic sectors in which these 1,000 firms operate, the most significant changes took place in primary and service activities. In the primary sector, consisting mainly of oil and mineral extraction, State firms still predominate, although the share of local firms has grown. In the service sector, however, sales by foreign firms rose from 10.2% to 36.9%. In the manufacturing sector, foreign firms also increased their share of sales, from 48.6% to 55.0%.

As these changes in ownership took place, transnational corporations also expanded their involvement in exports. In the group of the 200 largest exporting firms, which account for almost one half (47%) of exports from the region, transnational corporations increased their share of exports from 29% in 1990-1992 to 43% in 1998-1999. It is no surprise that today, more than half of the region's 20 largest exporting firms are transnational corporations (see table 6.8).

Table 6.8
THE TWENTY LARGEST EXPORT COMPANIES IN LATIN AMERICA, 2000
(Millions of dollars)

N°	Empresa	Country	Activity	Ownership	Exports
1	PDVSA	Venezuela	Oil	State	41,462
2	PEMEX	Mexico	Oil	State	16,300
3	Delphi	Mexico	Metallurgy	Foreign	7,651
4	DaimlerChrysler	Mexico	Automotive	Foreign	6,941
5	General Motors Mexico	Mexico	Automotive	Foreign	6,768
6	Volkswagen Mexico	Mexico	Automotive	Foreign	5,174
7	Grupo Carso	Mexico	Tobacco	Local private	4,779
8	Sanborn's	Mexico	Trade	Local private	4,132
9	Ford Mexico	Mexico	Automotive	Foreign	3,514
10	Codelco	Chile	Mining	State	2,994
11	Cemex	Mexico	Cement	Local private	2,962
12	Nissan	Mexico	Automotive	Foreign	2,720
13	Ecopetrol	Colombia	Oil	State	2,565
14	Embraer	Brazil	Aviation	Local private	2,302
15	Hewlett-Packard	Mexico	Computing	Foreign	2,176
16	Grupo Minero Mexicano	Mexico	Mining	Local private	2,068
17	Repsol YPF	Argentina	Oil	Foreign	1,975
18	Lear	Mexico	Food	Foreign	1,877
19	Visteon	Mexico	Auto parts	Foreign	1,676
20	Panamerican Beverages	México	Soft drinks/beer	Foreign	1,625

Source: ECLAC, on the basis of figures provided by the Departamento de Estudios de América Economía, and figures from other financial sources: Exame (Brazil); Mercado (Argentina); Expansión (Mexico); Semana (Colombia); Estrategia (Chile); and figures from the public reports and balance sheets of the companies.

III. Integration processes in the region

1. Subregional integration schemes and intraregional free trade agreements

In the first half of the 1990s, the various subregional integration processes advanced at a rapid rate. The accords signed in 1986 between Argentina and Brazil with a view to establishing a preferential trade zone preceded the unilateral liberalization efforts of the two economies and marked the start of a revival of integration processes. In 1991, following the accession of Paraguay and Uruguay, the bilateral agreement was converted into the Treaty of Asunción, by which MERCOSUR was created. Similarly, at the end of 1989, a meeting of the Andean Presidents in the Galapagos reactivated the Andean Pact, which years later became the Andean Community. The Central American Common Market (CACM) and the Caribbean Community (CARICOM) went through similar processes.

Accordingly, at the end of 1994 MERCOSUR became a free trade area, with few exceptions, and its member States agreed to establish a common external tariff, which came fully into force for Argentina and Brazil in 2001, while Paraguay and Uruguay are to complete the process by 2006. The Andean countries, in turn, managed to liberalize most of their mutual trade in the first half of the 1990s. Colombia and Venezuela fully adopted the common external tariff in 1992, while Ecuador adopted it partially the following year. Bolivia and Peru have not yet joined the agreement and continue to apply their respective national tariffs, which are basically flat-rate.

In contrast, the negotiations that have been held since the mid-1990s to achieve a convergence of these two processes to form a free trade area and, possibly, a common market in South America have made little progress. Thus far, these efforts have resulted in two preferential trade agreements —one with Argentina and one with Brazil— concluded by the Andean Community. The Meeting of the Presidents of South America (Brasilia, 2000) gave new political impetus to this process of rapprochement, and the countries concerned are determined to complete it in the shortest possible time.

There has been free trade in CACM since the mid-1990s, although each member country maintains a significant number of safeguards and restrictions on reciprocal trade. The CARICOM countries had also liberalized most of their intraregional trade by that time. In the second half of the 1990s, the two subregional processes agreed on separate agendas for reducing and rationalizing their respective common external tariffs, but to date these agreements have not been fully implemented in relation to the most sensitive products, and there is still a degree of tariff dispersion within each grouping. This process of reduction and convergence of national tariffs is also affected by the difficulties faced by various countries, particularly the smallest ones, owing to the negative impact of tariff reductions on fiscal revenue.

At the same time, a significant number of partial agreements have been reached, almost all bilateral in nature, which have been termed "new generation". This description refers to the fact that they have demanding goals with regard to the liberalization of trade in goods and the incorporation of commitments in complementary areas such as services and investment promotion. In part, these agreements have been promoted by the new commitments and issues contained in NAFTA and have taken shape, in particular, in the bilateral and multilateral treaties in which Mexico is the primary stakeholder. In the context of LAIA, about 10 such agreements have been signed, in addition to those signed by Mexico with Costa Rica and Nicaragua, as well as a large number between member States of LAIA, on the one hand, and countries of Central America and the Caribbean, on the other, which generally provide preferential treatment to the latter.

In the context of these processes, intraregional trade recovered from the severe slump it experienced in the 1980s, expanding at a very quick pace between 1990 and 1997. Growth was particularly rapid within the two South American integration agreements. Between 1990 and 1997, trade within MERCOSUR increased fivefold, and trade within the Andean Community increased somewhat more than fourfold. Central American trade also grew quickly over this period, although not as fast as trade in the two South American blocs. A similar but less marked trend was observed in CARICOM (ECLAC, 2001b).

One result of rapid trade growth in the two South American blocs was a reversal of the historical relationship in which the level of intraregional trade was higher for smaller economies. In 1997 the largest intraregional trade flows were concentrated in MERCOSUR. In the Andean Community, if oil exports are excluded, the share of trade within the bloc was also very high. In any case, however, trade within these groupings is still far from the levels reached in the European Union, where intraregional trade has accounted for about 60% of total trade for the last few decades (Ocampo, 2001b).

Towards the end of the last decade, subregional integration processes were hard hit by the effects of the Asian crisis, which gave rise to a sharp downturn in activity throughout the region and severe crises in a number of countries. At the institutional level, compliance with existing obligations was delayed and countries were reluctant to take on new commitments. Various countries resorted to trade contingency measures (antidumping, safeguards and countervailing duties) to control imports of any origin. In contrast to the situation during the crisis of the 1980s, however, there was no generalized breakdown of compliance with the agreements. Most affected were the two South American blocs: between 1997 and 1999, MERCOSUR and the Andean Community experienced overall declines of 26% and 30%, respectively. Both blocs experienced a partial recovery in 2000-2001. Trade in CACM did not suffer such a decline; in fact, it even continued to grow. Consequently, the increase in trade within CACM for the decade as a whole was similar to that within MERCOSUR. This is explained primarily by the Central American subregion’s lower level of sensitivity to the international financial crisis and its strong linkages with the United States economy, which had high growth rates in the second half of the past decade.

Commercial flows within the different integration systems not only grew very rapidly, but were also increasingly concentrated in industrial goods, especially the more technology-intensive ones. This pattern is particularly clear when Mexico is excluded, as that country's sales of manufactures to the United States have shown spectacular growth since the entry into force of NAFTA, as indicated earlier. As shown in table 6.9, the proportions of intraregional exports of non-natural resource-based manufactures (low-, mid-level and high-technology) from the MERCOSUR countries and Chile (an associate member) are higher, in all cases, than the respective proportions of exports to industrialized countries. The same is true of the Andean Community countries, although in this case it also applies to the corresponding shares of natural resource-based manufactures. In CACM and CARICOM as well, the share of all manufactures exported within the region is larger than the share exported to industrialized countries. Mexico is the only country which exports similar percentages of its manufactures to other countries of the region and to industrialized countries, mainly the United States.

The growth of trade flows and the development of new regulatory frameworks for foreign investment have brought about an unprecedented boom in intraregional direct investment. Although still modest in terms of volume compared to the very dynamic flows of FDI to the region (about 5% of the total), these flows are significant owing to certain characteristics that make them particularly important for effective integration of the region’s production and trading systems. Such investments have taken place both in the manufacturing industry and in the trade and service sectors. They are also part of a broader set of responses adopted by firms in view of the new situation, which range from strategic alliances between firms located in different countries to processes of industrial concentration in which some firms in the region, particularly those in the largest countries, have played a significant role.

Table 6.9

LATIN AMERICA AND THE CARIBBEAN: EXPORTS BY DESTINATION AND LEVEL OF TECHNOLOGY, 2000

(In percentages)

Countries/Regions	Primary products		Resource-based manufactures		Low-technology manufactures		Intermediate-technology manufactures		High-technology manufactures		Unclassified products	
	Intra-regional	Indus-trialized	Intra-regional	Indus-trialized	Intra-regional	Indus-trialized	Intra-regional	Indus-trialized	Intra-regional	Indus-trialized	Intra-regional	Indus-trialized
Latin America and the Caribbean	**24.6**	**27.0**	**26.0**	**14.3**	**13.1**	**14.7**	**26.5**	**25.0**	**8.1**	**15.6**	**1.6**	**3.5**
Mexico	7.3	11.9	16.2	5.4	14.5	14.9	35.5	38.8	24.9	25.0	1.6	4.1
Mercosur	**26.1**	**37.2**	**19.5**	**25.8**	**12.1**	**11.0**	**33.7**	**15.8**	**7.2**	**7.2**	**1.5**	**3.0**
Argentina	41.8	58.4	20.2	20.9	7.4	10.1	26.2	7.2	3.4	1.6	1.1	1.7
Brazil	8.5	30.9	18.3	27.6	16.3	10.9	44.8	18.5	11.7	9.0	0.4	3.1
Paraguay	56.0	64.2	11.7	20.6	7.1	12.6	0.8	0.6	0.7	0.7	23.6	1.4
Uruguay	29.0	46.9	28.1	12.5	17.4	22.6	19.6	7.8	4.3	1.1	1.6	9.1
Andean Community	**36.7**	**66.0**	**32.0**	**22.5**	**11.9**	**4.7**	**14.8**	**3.8**	**3.3**	**0.2**	**1.4**	**2.8**
Bolivia	71.7	35.0	20.4	29.4	5.8	24.2	1.2	0.9	0.7	1.5	0.1	9.0
Colombia	21.4	72.2	21.4	10.4	20.0	7.2	26.2	5.0	7.4	0.3	3.6	4.9
Ecuador	58.7	81.4	23.9	13.3	7.6	1.9	7.4	1.0	2.3	0.4	0.1	2.0
Peru	25.3	36.5	45.3	38.6	16.3	16.8	9.2	0.8	2.0	0.1	1.9	7.1
Venezuela	38.7	66.3	39.1	27.3	7.8	1.1	12.4	4.3	1.5	0.1	0.4	0.8
Central American Common Market	**11.8**	**31.0**	**29.3**	**4.5**	**22.5**	**44.4**	**22.1**	**3.3**	**10.3**	**15.0**	**4.0**	**1.8**
Costa Rica	5.8	33.4	29.9	4.9	21.1	16.9	21.4	6.1	12.9	36.8	9.0	1.9
El Salvador	8.7	14.8	29.8	2.3	30.0	75.3	21.2	0.6	9.4	5.4	0.9	1.6
Guatemala	12.5	43.9	27.3	5.6	22.8	47.9	25.0	1.3	9.2	0.1	3.2	1.2
Honduras	11.8	21.8	35.0	3.7	16.9	70.4	23.6	2.1	12.4	0.2	0.3	1.7
Nicaragua	58.6	44.6	24.6	5.4	7.7	43.3	7.2	0.8	1.2	0.1	0.7	5.7
CARICOM	**20.8**	**41.0**	**51.7**	**31.3**	**12.4**	**9.9**	**12.5**	**11.2**	**1.8**	**1.1**	**0.8**	**5.5**
Antigua and Barbuda	4.4	16.6	19.8	9.6	26.2	1.6	46.0	68.9	2.4	1.3	1.2	2.0
Bahamas	26.9	20.0	47.0	46.8	4.1	1.7	5.1	22.8	16.7	1.7	0.1	7.0
Barbados	29.8	2.1	35.5	47.0	14.4	13.6	14.0	19.0	3.2	13.2	3.1	5.2
Dominica	7.6	39.7	7.4	14.9	5.6	7.1	77.9	21.9	1.5	7.1	0.1	9.3
Granada	24.3	47.2	38.5	2.1	28.8	1.0	7.8	38.2	0.4	1.6	0.2	9.9
Jamaica	13.3	47.8	60.6	20.4	12.7	26.8	11.9	2.5	0.7	0.3	0.9	2.3
Montserrat	24.5	18.9	51.2	6.5	11.7	15.4	11.8	18.8	0.8	36.9	0.0	3.5
Saint Kitts and Nevis	19.9	0.3	71.5	18.1	5.9	8.3	1.4	43.1	0.6	25.6	0.6	4.7
Santa Lucia	8.4	62.0	64.1	1.3	21.8	14.4	4.5	7.7	0.4	8.4	0.8	6.3
Saint Vincent and the Grenadines	49.0	42.3	32.8	0.7	13.6	3.9	4.0	47.4	0.3	1.1	0.3	4.6
Trinidad and Tobago	12.6	36.3	58.4	42.7	14.3	5.5	13.6	13.5	0.4	0.2	0.7	1.8
Belize	19.1	64.1	55.0	25.5	4.5	6.9	7.6	1.4	13.4	0.3	0.5	1.8
Guyana	46.4	31.1	44.0	36.4	5.5	3.1	2.5	2.1	1.5	0.3	0.2	27.0
Suriname	88.9	80.4	10.3	4.7	0.3	0.9	0.4	2.4	0.0	0.6	0.0	11.0
Other												
Chile	24.2	47.7	45.7	45.5	9.5	1.5	15.6	3.2	2.6	0.2	2.4	1.9
Cuba	10.0	25.2	53.5	69.1	4.0	1.6	19.7	1.7	12.5	0.3	0.4	2.0
Haiti	20.5	8.7	13.6	2.8	20.2	85.8	38.5	0.7	2.7	0.3	4.6	1.6
Cayman Islands	13.1	1.8	61.0	4.3	3.0	0.4	11.8	89.7	0.8	2.3	10.4	1.5
Panama	3.7	52.5	18.7	10.6	32.6	4.6	22.1	21.8	22.3	2.0	0.6	8.5
Dominican Republic	19.4	4.7	19.7	8.5	27.1	63.6	26.0	16.8	6.4	3.5	1.3	3.0

Source: ECLAC, on the basis of figures obtained from the CAN computer program (2002 version).

In contrast, existing subregional integration arrangements have not prompted movements of labour. In fact, labour migration essentially reflects differences in levels of relative development rather than integration processes (see chapter 8). Some of the migration flows are long-established (Argentina's attraction of labour, for example), while others have appeared or accelerated in recent years (migration to Chile, migration from Nicaragua to Costa Rica and migration from Haiti to the Dominican Republic). At the same time, some migration flows have declined or have generated return flows (from Colombia to Venezuela and, currently, from Argentina to Bolivia, Chile, Paraguay and Peru).

2. Other integration arrangements

In addition to the renewed effectiveness of the four existing imperfect customs unions, which have the ultimate aim of establishing common markets, there have been three other important developments: Mexico’s integration under the North American Free Trade Agreement (NAFTA); the proliferation of free trade agreements with countries outside the region; and the negotiations on the establishment of the Free Trade Area of the Americas (FTAA).

The North American Free Trade Agreement entered into force on 1 January 1994, and is the first reciprocal understanding between a developing country and developed countries. This agreement emerged from the United States government’s multitrack trade policy, Mexico’s process of economic and political reform and Canada’s policy of economic integration. Both the Canadian and the Mexican economies were already closely associated with that of the United States through agreements that allowed advantage to be taken of differential costs for labour factors, mainly by means of outsourcing between firms.

NAFTA provides not only for the elimination of the usual barriers to trade in goods, such as tariffs and quotas, but also for the liberalization of trade in services and the protection of intellectual property and investments. It also addresses less traditional concerns such as the environment, labour standards and human rights issues. The Agreement’s most noteworthy elements include a sophisticated dispute settlement mechanism, mainly to handle complaints from member States concerning antidumping practices.

There have also been other important initiatives geared to strengthening the region’s trade and investment links with other integration arrangements and countries of the world. Governments in the region have given priority to the conclusion of free trade agreements with the European Union. Mexico concluded such an agreement recently, and both Chile and MERCOSUR have made progress in this direction. Asia is another area of growing interest to Latin American governments. The preferred arrangement has been the inclusion of Latin American countries in the Asia-Pacific Economic Cooperation Council (APEC). Mexico was accepted in 1993, whereas Chile and Peru have been full members since 1997 and 1998 respectively. Lastly, some Asian countries have recently shown an interest in strengthening their bilateral ties with Latin American countries, as evidenced by the free trade agreement between the Republic of Korea and Chile.

The participants in the Third Summit of the Americas, held in Quebec in 2001, agreed that the Free Trade Area of the Americas should enter into force in 2005. FTAA is the most ambitious integration project in the world, as it will include 34 countries with a joint population of 800 million and an economy of about US$ 10 trillion. At the same time, the signing of this agreement will require the countries involved to overcome enormous challenges: on the one hand, ensuring that all members benefit despite the huge disparities in the size of their economies and in their relative levels of development; and on the other, enabling all the countries to take full advantage of the benefits deriving from trade liberalization on the continent.

IV. The Latin American and Caribbean agenda for trade and investment

As was emphasized in chapter 2, global experience indicates that there is no single development model for market economies, nor is there any single form of participation in international networks for investment, production and marketing of goods and services. The modalities for participation depend on a combination of factors, some of which are inherent to individual firms (assets and capacities), while others are specific to the industrial branches (organization of markets) or associated with the characteristics of individual countries. The latter include the availability of natural resources, the quality of human resources, the existence or absence of innovation systems, the efficiency of infrastructure services and the quality of the institutional framework and the traditions it follows.

Diversification of production and sustained increases in productivity are the result of long-term developments involving a constant technological, commercial and institutional learning process. They therefore depend on past experience; that is, they have a high historical content. The quality of the diversification of the production system depends on the breadth and depth of the series of networks linking firms within and between sectors and on the quality of their productive resources and institutions. Competitiveness is determined by the capacity of these networks to establish links with investment, production and marketing chains that operate worldwide. Both processes are therefore essentially systemic. Accordingly, measures to ensure more rapid and lasting increases in global productivity must address all these components. This means implementing not only neutral or horizontal policies (that is, policies that are independent of the sector in question), but also targeted policies that have a lasting impact on systemic competitiveness and production chains.

In recent years, multilateral regulations have reduced the amount of leeway available to countries in the design and implementation of incentive systems to achieve these ends. However, the practices of the industrialized countries themselves show that there is still room for active economic and social policies, despite the commitments undertaken within WTO. In this regard, the regional sphere offers an opportunity to enhance productive complementarity, learning processes and integration of physical infrastructure, as well as the bargaining power of individual countries in relation to global-level organizations and the large corporations operating in the region (see chapter 4). It is thus important that national and regional efforts should be supported by the fine-tuning of multilateral rules to create a macroeconomic and financial framework that helps to reduce the external vulnerability of the region's economies. Steps should be taken to consolidate legal stability in order to guarantee market access for the goods and services produced in the region and, at the same time, to open up opportunities for diversifying the production structure and, especially, exports.

1. The national agenda: export promotion policies

As shown in chapter 4, the creation of systemic competitiveness is the focus of actions at the national level. This involves the development of innovation systems, as will be analysed in chapter 7; the provision of high-quality infrastructure services, as discussed in previous publications (ECLAC, 2000a and 2001a); and the implementation of policies to diversify the production structure, which will be the focus of this chapter.

In the current phase of globalization, the process of diversifying the production structure requires, first of all, an explicit effort to broaden the export base and increase the number of target markets. As noted earlier, while undeniable progress has been made, in the 1990s the external sector was still a fundamental constraint on the growth of the Latin American and Caribbean economies. Many of the countries based their international participation on a limited number of products in sectors showing slow growth at the global level. Those countries that did manage to enter dynamic sectors, such as Mexico and some Caribbean countries, also show the highest degrees of concentration in the target markets for their exports, which are directed primarily to the United States.

The key to any export promotion policy is a competitive exchange rate. This is especially true when countries are making the transition to more open economies, as is still the case in the region. Therefore, reaching and maintaining a competitive exchange rate should be an essential and explicit objective of macroeconomic policy and one of its main contributions to growth in open economies.

Active commercial diplomacy is another basic element. The aim of this strategy is to guarantee market access, identify new opportunities and combat the various practices that restrict free trade. It is therefore necessary to train high-level negotiating teams and to develop appropriate mechanisms for communication between these teams and the private sector and for keeping prospective exporters apprised of opportunities offered by different preferential agreements or arrangements. It is also important to create expert groups that can make efficient use of the dispute settlement mechanisms established under trade agreements, particularly those of WTO. This means that joint teams of experts should be formed with the smaller countries and that effective tools should be developed to provide multilateral support to their governments.

Lastly, a competitive exchange rate and commercial diplomacy should be complemented by a comprehensive export promotion policy geared to diversifying the export base, especially in favour of more technology-intensive areas, and to reducing the concentration of exports on just one or a few target markets. Export promotion instruments should be adapted continually to make them more efficient and, at the same time, more consistent with the commitments made under WTO and other trade agreements. This should not, however, preclude efforts in future WTO negotiations to expand developing countries' range of action, which was severely limited as a result of the Uruguay Round. In this regard, special efforts should be made to secure greater freedom to promote incipient export sectors, in some cases reinstating rules that allow improved internal linkage of export activities. At least in the relatively smaller countries, some of the special benefits of free zones should be maintained, even though current regulations call for them to be dismantled in the coming years.

The first instrument of this comprehensive policy to promote external trade is the provision, to export firms, of ready access to imported inputs at international prices, either by refunding indirect taxes or by waiving tariffs. The latter is the most effective tool for regular exporters and in fact has been the key to export growth in South-East Asia and Mexico. In addition to improving these instruments, governments should develop other mechanisms to allow indirect exporters —that is, firms that sell inputs to direct exporters— to recover the duties and other indirect taxes they pay. This is necessary to strengthen the backward linkages of exports and enhance the stimulating effect of export growth on the rest of the national economy, as discussed below.

Access to financing and to export insurance is another essential component of export promotion policies that has become increasingly important worldwide, particularly for small and medium-sized enterprises that do not have access to foreign credit. With a few noteworthy exceptions (including Brazil, Colombia and Mexico), the application of this measure is still quite deficient, especially with regard to export insurance.

A third instrument is the establishment of public or mixed export promotion agencies and the use of these agencies' foreign branch-office networks or of diplomatic delegations to boost exports. These agencies can make a decisive contribution to facilitating access to the information needed to export products, and can provide data to prospective buyers on the supply of exports. They can also play an important role in encouraging exporters to organize in different ways, by product or by target market, to take advantage of economies of scale and the externalities arising out of their combined presence in international markets. Making more active use of these institutions to forge close ties of cooperation with trade associations of exporters or producers and with private businesses that offer complementary information services for export firms, as well as certification of quality and environmental standards, can be a key factor in making the export sector more dynamic.[9]

One type of activity that has not received enough impetus is the establishment of an investment banking industry or other private entities specializing in channelling venture capital towards new activities or firms involved in diversifying the export base. For decades, public development banks in several countries played a prominent role in promoting new investment, first for import substitution but later, increasingly, for exports. Some of these institutions are still engaged in the latter activity. The decline in their relative importance has not, however, been offset by private initiatives. Despite a few isolated efforts, the Export Promotion Office of Chile (PROCHILE) is still unique in this regard. Such efforts should be integrated with those aimed at promoting high-technology enterprises.

Although the new WTO rules restrict most export subsidies, there is still room for designing incentive programmes which some countries can use to support innovations in the export sector.[10] In establishing incentive programmes, it is important to observe the following criteria: they must be designed to promote exports of new products or to new markets; the support must be moderate and must target firms that are really willing to share the cost of the programme; the assistance must be temporary; in order to avoid permanent subsidies, the results of the programmes must be subject to periodic external evaluations so that they can be modified or suspended it they do not contribute to an increase and diversification of exports; and the programmes must be jointly designed and administered by entities of both the public and private sectors.

The development of free zones merits some special consideration. Today there are about 200 such areas throughout Latin America and the Caribbean, involving both trade and production. On the whole they have been an important vehicle for job creation[11] and new exports. For this reason, some smaller countries in Central America and the Caribbean now see them as one of the fundamental elements in their development strategy. The incentives they offer are subject to scrutiny by WTO, given that they entail export subsidies. In this regard, under current agreements, the income tax exemptions offered by many free zones should be phased out by 2005. Another appreciable benefit offered by these areas is exemption from tariffs on inputs and capital goods, which have also declined in importance due to the overall reduction in tariffs and the proliferation of free trade agreements, as well as the creation of general tariff refund or waiver systems. The rules of origin typically included in trade agreements also limit their benefits.

For this reason, the survival of subsidies will depend less on the tax benefits they offer than on the efficacy of their distribution and production support services and the agglomeration economies they manage to create. Moreover, it should be noted that, according to a recent ECLAC study (Buitelaar, Padilla and Urrutia, 1999), *maquila* industries, which tend to develop in free zones, can —under certain conditions— promote various forms of learning and technical progress. In this process, the ability to develop quality control engineering, which improves the chances of gaining a foothold in more specialized product niches with greater value added, is of particular importance.

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[9] In this sphere, the Export Promotion Office (PROEXPORT) of Colombia, the Export Promotion Office of Chile (PROCHILE) and the Banco Nacional de Comercio Exterior (BANCOMEXT) of Mexico are some of the best examples of promotion agencies in the region.

[10] In particular, WTO allows the use of horizontal subsidies (not specific to export activities per se). Subsidies are authorized for technological development projects to cover up to 75% of their costs. There is also leeway for some direct subsidies under the *de minimis* clause (GATT, 1994; Tussie, 1997).

[11] Clothing assembly, for example, provides approximately one million direct jobs in the countries of the Caribbean basin, including Mexico.

2. The national agenda: policies on linkages and clusters

A country's success in positioning itself within the international economy is not measured only in terms of the percentage of GDP represented by its exports, the growth rate and diversification of its export products and by a reduction in the concentration of destination markets. Consideration should also be given to how well the export sector is integrated into the national production system and how much it contributes to the progressive leveling of productivity rates throughout the national economy as a whole. The combination of high export growth rates with low overall economic growth in the countries of the region is a sign that the weakness of the linkages existing between dynamic sectors -associated with export activity and foreign investment, among other factors- and production activity as a whole is having adverse macroeconomic effects. In addition, various ECLAC studies indicate that total factor productivity is not increasing fast enough to reduce the productivity gap between the region and the developed world (ECLAC, 2000a and 2001a, Katz, 2000). Furthermore, the fact that some sectors and firms are undergoing a rapid modernization process at the same time that informal labour is expanding is an unmistakable sign of growing structural heterogeneity, which denotes situations in which firms, social sectors and regions have sharply differing levels of productivity (ECLAC, 2000a).

These trends indicate that efforts to enhance export development should be accompanied by policies that will expand the national and regional linkages of activities geared to the world market. The economic literature reflects a consensus that market mechanisms alone do not generate spillovers from export activities and foreign investment to the less dynamic sectors (Baldwin, 1956). As a result, policies and institutions are needed to implement and/or accelerate, as appropriate, the growth impulses which the firms that are more fully integrated into the world economy can transmit to the economy as a whole. Policies designed to create more and better production linkages should be based on four complementary lines of action: the development of business support enterprises (backward linkages), progression along the value chain (forward linkages), the promotion of various forms of association among business enterprises; and the provision of logistical services that can be outsourced by such firms.

The first of these lines of action will involve negotiating with large firms, particularly transnational corporations, in order to induce them to promote the operations of business support firms that can increase the local content of inputs, parts and components in final export goods and thus create backward linkages. This potential exists in various sorts of internationally integrated production systems (e.g., the automotive, electronic and aeronautics industries). A number of recent cases illustrate the power of such initiatives. For example, the main aircraft manufacturers (Boeing Corporation, General Dynamics Corporation, Honeywell Aerospace and General Electric Aircraft Engines) have announced their decision to make Mexico the base for the manufacture and assembly of parts for their various models and, to this end, have arranged for their suppliers to visit a number of industrial parks in that country. In Brazil, the production facilities of General Motors, in Gravataí, and of Volkswagen and Renault, in Paraná, were set up at the same time as those of their suppliers because their production processes are organized in such a way that their vehicle parts and components have to be supplied as integrated systems. In Peru, domestic purchasing by the mining industry is concentrated in energy and in engineering, construction and environmental services, but there is considerable potential for increasing local supply as Peruvian firms raise the quality of their products and lower their costs in order to meet the standards of the large-scale mining industry (UNCTAD, 2001). The tourism industry —a particularly important activity for the countries of the Caribbean basin, but one that has growing potential for other countries as well— also offers significant opportunities for expanding the local supply of inputs, which in many cases is surprisingly limited. The success of all these initiatives will, of course, depend on what supplier development programmes that relevant governments and the private sector manage to implement and on the levels of quality, speed and reliability that they attain.

The above actions focus on strengthening the backward linkages of exported goods, but it is also possible to promote the development of forward linkages, in line with the now classic distinction drawn by Hirschmann (1958). These types of initiatives are critical in order to progress along the value chain which begins —mainly, but not exclusively— with the use of natural resources. Such efforts may be particularly important for the South American countries, since, as noted earlier, they are exporters of natural resources and manufactures based on those resources. In the majority of cases, however, the countries will have to move a long way up these value chains before they reach the point where they are exporting goods with a higher level of processing and technological content in the food, lumber and paper, petroleum and petroleum products, and mining-based industries. This line of action is also applicable to assembly activities, where opportunities exist to move towards more complex products, as appears to be happening in Mexico. The tourism industry also offers the possibility of moving on from the operations of hotels to the organization of tourism packages, recreational activities, cultural events and time-share systems.

The most productive linkages, of both types, can be promoted through a variety of business partnership schemes, of which there are three main types: joint ventures between large corporations, licensing and franchising arrangements between a large corporation and several small firms, and enterprises involving a number of SMEs. Joint ventures basically combine the assets of two or more firms. One example would be a venture in which the process or product technology of a transnational corporation is combined with the market access and local-market knowledge of local firms. Another is when firms that are located in different countries and have complementary assets establish partnership agreements within the framework of subregional integration processes in order to gain markets in other countries. The aim of the second type of partnership is to establish a set of shared technical standards, quality control regulations, and trade and management practices. Examples of this type of scheme include supplier development programmes and licensing or franchise operations. The negotiations between Costa Rica and the transnational Intel Corporation are an interesting example of such a scheme because a key stipulation of the agreement refers to the modernization of local suppliers and their integration into the corporation's network. One of the reasons why this was possible was that the Government of Costa Rica and the local Chamber of Industry, together with other institutions, were already conducting a series of programmes to provide SMEs with the technological, commercial and management training they needed to join the production chains of large local and foreign corporations. Lastly, partnerships among SMEs allow them to pool information, resources, markets or support services in order to coordinate their capacities or knowledge more effectively. These schemes are generally based on a local industrial structure, such as an industrial district.

The final linkage-building mechanism is the development of logistical, quality-control, marketing and technical consultancy services, which all come under the general heading of business services. Evidence can be found in the region of the potential offered by these linkages within the framework of outsourcing arrangements. For example, a breakdown of the gross product of Buenos Aires shows considerable growth in information sciences and related activities, engineering design and development, and other business services, which together generated around 13% of the city's employment and 11% of its value added in 2000 (ECLAC, 2000e). In Brazil, the State of São Paulo is the main centre for technology and services. A recent survey conducted by the Brazilian Geographical and Statistical Institute (IBGE) found that non-financial enterprises that provide specialized services to other firms generate sales of over US$ 13 billion per year and employ almost one million people (IBGE, 2002). In Chile, a survey of engineering consultancy firms found that the main source of demand for their services is generated by resource-intensive sectors of production. In the wine industry, for example, these firms provide coding and quality control, project design and implementation, sanitary controls, water purification and treatment, and plant construction, among other services (Acosta, 2002).

The development of production linkages has its spatial expression in the formation of production clusters. A cluster is generally defined as a geographical and/or sectoral concentration of firms engaged in the same or closely linked activities which allow them to accumulate substantial external economies of agglomeration and specialization and to act jointly in order to achieve greater collective efficiency. There are a number of mature production clusters in the world,[12] and some incipient ones in Latin America and the Caribbean. These include a cluster in the footwear industry in New Hamburg, Brazil, an oilseed complex in Argentina and the clusters that have developed around the copper industry in Chile, the iron and steel sector in Brazil and the forestry industry in both Chile and Brazil.[13]

Well-designed public policies to encourage interaction between firms, make markets function better and strengthen learning, research and technological innovation capacities are essential at all stages in the development of clusters. The main lines of action for such policies are: (i) to conduct, in conjunction with the private sector, strategic planning exercises to analyse the development potential of input- and equipment-supplying activities and of increasingly complex processing industries and related services, in particular engineering and consultancy; (ii) to target those activities within existing clusters that are most in need of foreign investment —because of the advanced status of their technology, their need for access to international markets, or the amounts involved— and make them the focus of efforts to attract the most suitable transnational corporations; (iii) to identify key matrix technologies for cluster development, to help them to maintain a dominant cutting-edge position at the local level through selective R&D policies, and to facilitate technological updating and adaptation through missions abroad, the promotion of licensing arrangements and joint ventures; and (iv) to determine the infrastructure needs of the cluster in the short, medium and long terms, especially in the areas which are of greatest public interest and responsibility, such as physical, scientific and technological infrastructure and human resource endowments (especially of skilled and highly skilled technicians and professionals) (Ramos, 1998).

3. The regional agenda

Existing regional agreements have displayed a disturbingly high degree of vulnerability to the crises that have hit the South American economies in recent years. This suggests that, in addition to questions relating specifically to the integration of production and trade, the integration agenda should address the issues that have long been debated in connection with what has become known as the international financial architecture. Yet thus far only one of these issues —the coordination of macroeconomic policies— has begun to figure on integration agendas (ECLAC, 2002). The experience of the European countries over the last quarter of a century offers a clear demonstration of the difficulties involved in this process. Although a number of optimistic analyses have been put forward on the subject, some of which even refer to common subregional currencies, it is clear that the objectives must necessarily be modest in the short term. The harmonization of fiscal rules and the establishment of mechanisms for pursuing a dialogue (and perhaps, in time, mutual oversight) regarding monetary policies should be the immediate objectives.

Intraregional trade has demonstrated that regional agreements can be an important tool for encouraging export diversification with a view to creating more interconnected markets that enable firms located in the region to benefit from economies of scale. It is widely acknowledged that

[12] The most successful include the industrial districts of Emilia Romagna in Italy and Baden Wurttenmberg in Germany, Silicon Valley and Route 128 in the United States, the newly developed computer industry in Ireland and electronics industry in Scotland, electronics and software clusters in Bangalore, India, the cluster that has formed around the production of simple surgical instruments in Sialkot, Pakistan, and a microelectronics cluster in the Hsinchu Science Park in Taiwan, Province of China.

[13] Since 1997, ECLAC has been conducting a research and technical cooperation programme that focuses on the production clusters that develop around natural resources (see Buitelaar, 2001 and Dirven, 2001).

regional markets play a key role in expanding non-traditional exports, creating product and brand differentiation, and producing more knowledge-intensive goods and services with greater value added. The learning curve that starts with experience in regional markets may thus serve as a trampoline to new international markets. Current technologies and modalities for the organization of production enable firms to engage in joint actions without running up against the problems inherent in the old schemes of sectoral complementarity. Joint action of this nature should form part of broader agreements on the integration of technological R&D efforts that can, in turn, lead to the formation of true regional innovation systems (see chapter 7) and serve as a means to transfer technology to less developed countries.

In the agricultural sector, technological complementarity agreements and the development of phytosanitary rules could form the basis of a common policy. The difficulties associated with the asymmetry of existing production schemes —owing to the use of price bands in a number of countries— demonstrate the importance of implementing joint schemes (based, perhaps, on regional stabilization funds) to mitigate the internal transmission of the sharp price cycles characteristic of some agricultural goods.

The regional arena also offers considerable growth opportunities for SME exports. These firms, in particular, stand to gain a great deal from using regional markets as a platform for learning about export activity. Practical experience can be gained in the regional arena regarding such facets of the export process as delivery times, quality control, technical assistance, marketing and participation in trade fairs. In addition, the regional market is large enough to offer SMEs the different market scales they may need to increase their efficiency. Contact with neighbouring markets also helps SMEs to improve their technological and management practices as they exchange experiences and learn to become more adaptable.

From a regulatory and institutional perspective, countries tend to be more willing to accept new objectives and issues and to undertake greater commitments within the framework of regional schemes than they are in multilateral agreements. In a number of areas, moreover, the regional process can proceed more quickly and produce more concrete trade and investment results than the multilateral process. Regional agreements can thus facilitate liberalization and coordination in areas that are too complex to be negotiated or very difficult to address in multilateral forums. For example, in sensitive areas such as government procurement, antidumping measures and services agreements, policies for liberalization and the regulation of competition may be more viable in a regional context than in the global forums. Regional integration agreements are also more conducive to debates on subjects such as the establishment of rules and technical standards. Indeed, great strides have already been taken in many of these fields in Latin America and the Caribbean.

With respect to physical infrastructure (transport, telecommunications and energy), it is important to develop networks that will serve the purpose of regional integration rather than simply in order to meet domestic requirements. The South American Summit of 2000 and the Puebla-Panama Plan, which was signed in 2001 by the Presidents of Mexico and the Central American countries, represented an important step towards visualizing infrastructure as an essential dimension of regional integration. The development of regional oil and gas pipelines and electricity distribution networks would clearly help to boost trade in energy, whose potential is already apparent in number of binational schemes. Recent experience shows that projects in this area, as well as in transport and communications, are capable of attracting substantial public and private resources. The Inter-American Development Bank, together with subregional and national development banks, has already begun to assign priority to financing projects of this type.

Harmonized transport regulations and more appropriate customs rules are also crucial elements in facilitating intraregional trade. In addition, telecommunications infrastructure and regulations must be made compatible across countries in order to develop a more dynamic regional market for industries associated with information and communications technology.

This view of infrastructure as a dimension of integration implies the need to develop a similar perspective with regard to national territories. Progress has been made towards creating a vision of this sort in relation to the sustainable development of shared ecosystems (the Amazon, the Andean ecosystem and the Central American corridor) and hydrographic basins. Border-area development plans offer another example of this integration-generated shift in the conceptualization of national territories. These processes are incipient, however, and their strategic importance is only just beginning to be recognized.

Great potential gains are offered by the regional harmonization of rules in a large number of areas, but regulations on competition and public utilities, in particular, merit closer attention. With respect to rules on competition, the European experience suggests that as markets become more integrated and consolidated, a common competition policy has clear advantages over the unfair competition rules that are usually attached to trade and integration agreements. One of various advantages afforded by a framework of this sort is that it permits more effective management of the operations of transnational corporations in the different countries.

The idea that market regulation can serve as an arena for regional policy is equally applicable to utilities (particularly energy and telecommunications). The harmonization of regulatory standards could play an important role, given the heavy involvement of transnational corporations in these sectors in a number of countries and the difficulties encountered by national authorities in ensuring effective competition. In particular, harmonization would preclude arbitrage between different regulatory frameworks and would foster competition, not only within countries, but also at the subregional or regional levels.

WTO provides a set of rules and disciplines that offer protection and guarantees for legitimate national interests in trade relations. In this respect, subregional and regional forums are essential for exchanging information, consolidating positions on trade negotiations at the hemispheric and global levels, and defending member countries from infringements of the established rules. Regional and subregional agencies provide a natural channel for the convergence (coordination, harmonization and unification) of criteria for the definition of rules that, without violating global rules, take regional and subregional interests into account. This would make it possible to agree upon common rules and disciplines for the regulation of services, for intellectual property legislation (for example, in the controversial area of pharmaceutical patents) and for trade-related investment measures.

In order to move forward in these areas, the region needs a much stronger institutional structure, especially for subregional integration agreements and, at some future point, perhaps for broader initiatives. This is the only way that the region can make progress in the areas of macroeconomic coordination, common competition and regulatory policies, physical infrastructure for integration, and the advocacy of common interests within hemispheric and global processes. These institutions also play a key role in protecting the interests of smaller countries with respect to their larger partners within the agreements and, hence, in fostering confidence in these integration processes.

4. The international agenda

The globalization process has taken international trade negotiations far beyond conventional agreements on the cross-border purchase and sale of goods (tariff or quantitative restrictions) to touch upon issues that previously fell exclusively within the domain of national policy (services, international movements of the factors of production, regulatory regimes, environmental and labour standards, etc.). In consequence, today the issue of market access must be addressed in a much more integrated and consistent manner than in the past, encompassing a range of actions from trade policy to investment and competition policy. This systemic approach makes it necessary to define and implement suitable and coherent policies on a variety of fronts and to back them up with technically solid and operationally versatile institutions.

In chapter 4 it was mentioned that multilateral rules are now being oriented towards the establishment of a uniform regulatory framework premised upon the need for a "level playing field". This shift, however, has failed to take account of the asymmetries existing among the various players in the world economy. This approach is not only inappropriate, but also overlooks features that were essential to the economic convergence of today's developed countries. The European integration experience is an ample demonstration of this. The incorporation of Spain, Greece and Portugal and the subsequent unification of Germany show that the convergence of regulatory and institutional models among countries and regions carries a high cost which can only be met though redistributive action on a basis of solidarity.

The main apprehensions among the countries of the region with respect to the current process of multilateral negotiations are the following: (i) serious limitations on access to sectors that are essential to the development of the countries of the region; (ii) restrictions imposed by the Uruguay Round on the developing countries' manoeuvring room in defining their own policies; (iii) the complex institutional adjustments called for in a number of the agreements and the shortness of the transition periods provided for making those adjustments; (iv) scant consideration of the difficulties they have to overcome in order to meet the higher requirements established for their exports; (v) the few concrete, effective results obtained from the Uruguay Round provisions on special and differential treatment for developing countries; and (vi) the fear that recognition of legitimate demands for the right to work and for environmental protection may be transformed into trade barriers and obstacles to a more balanced integration of the developing countries into world markets.

If these problems are to be overcome, the international community must recognize the legitimacy of the developing countries' use of an array of policy tools to improve their position in the global economy. This means that these countries need to maintain their prerogative to design and pursue investment and diversification policies in order to take greater advantage of the opportunities offered by international markets. The negotiating interests of the Latin American and Caribbean countries are therefore grouped around two different, but related, sets of issues: first, issues relating to market access, which are essentially static, since they refer to the markets existing within the current production and export structure; and second, issues of "policy space," which involve the use of policy tools directed at diversifying countries' trade patterns in order to gain a stake in the dynamic segments of the globalized economy.[14]

It is therefore essential that the development dimension of trade negotiations should be expressed as a genuine commitment on the part of the international community not only to open up crucial markets for developing countries, but also to create an environment conducive to the development of more dynamic production structures that will enable them to improve their international position. In the preparatory activities for the Fourth WTO Ministerial Conference, held in Doha, Qatar, in November 2001, the developing countries succeeded in arriving at a united position regarding their demand that multilateral rules should offer a real opportunity for them to

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[14] A proposal made by the Government of Venezuela in 1998 suggests that several issues addressed in the agreements, such as those concerning Trade-Related Investment Measures (TRIMs) and aspects of intellectual property rights associated with trade (TRIPs), should be consolidated within a multilateral framework for investment. This framework would be broader than a multilateral agreement on the protection of foreign investment ("Espacio de las Políticas de Desarrollo en las Negociaciones del Milenio", Geneva, 22 December 1998).

diversify their production structures and reduce their economies' external vulnerability.[15] This position was acknowledged as legitimate in the negotiating mandate which was agreed upon at the meeting and should form the basis for giving real and effective meaning to the term "special and differential treatment".

This requires that the negotiations produce explicit and enforceable commitments in favour of developing countries on both old and new issues. These issues include: the liberalization of trade in agricultural products, to include reductions in current levels of protection, the gradual elimination of the "tariff-quota" system applied to agricultural products (which in practice operates more as a quantitative restriction than as a tariff), the discontinuation of export subsidies and substantial reductions in agricultural subsidies in developed countries; a more rapid reduction of the industrialized countries' trade barriers affecting manufactures, in particular labour-intensive goods such as textiles and clothing, and those on which tariff escalation hampers the development of forward linkages with resource-intensive activities; the strengthening of WTO rules and disciplines in order to prevent abuses, in particular with respect to antidumping measures; measures to ensure that technical rules, including sanitary and phytosanitary regulations, do not become barriers to trade; and liberalization of trade in services that are of particular interest in terms of developing-country exports, which means that the negotiations must address the question of labour migration and the formulation of rules to govern short-term employment in another country.

In the sphere of global economic negotiations on trade and on financial issues, the developing countries must emphasize their need for special and differential treatment that will enable them to increase their rate of development. It is particularly important to consolidate progress that has already been made in the different international agreements on this subject and to prevent any ground from being lost in this regard. In practice, special and differential treatment as applied to trade issues consists of two basic elements: non-reciprocal improvements in the access of developing countries' exports to the markets of industrialized countries; and flexibility and discretionality in developing countries' policies with respect to their own markets.

This means that the negotiations should ensure, first of all, that the industrialized countries will provide meaningful access to the sectors and modalities of supply that are of interest to developing-country exporters. It also means that the industrialized countries should make a commitment to concentrate their demand in those sectors and types of transactions that the developing countries are prepared to liberalize. Furthermore, the industrialized countries should undertake not to insist on the removal of the conditions that each developing country attaches to its commitments. Lastly, in order to secure developing countries' right to pursue policies to strengthen their services sectors and accomplish national policy objectives, the measures they adopt and the associated regulations must continue to be governed exclusively by national legislation (article VI of the General Agreement on Trade in Services). In this respect, in keeping with the sentiments of many developing countries, the negotiating guidelines for trade in services appear to represent an improvement in their negotiating position. The guidelines provide that the Council on Trade in

[15] The proposals on specific issues raised by the developing countries reflect interests such as the following: increasing their role in the trading system and in the institutions that govern it, having greater flexibility in meeting commitments, securing access to goods and services markets –sectors and modes– of interest to them, and maintaining or broadening the conditions for implementing development policies. They have also shown an interest in upgrading the multilateral structure of institutions to promote participation, transparency and dispute settlement and in strengthening a number of disciplines which they consider to have been especially costly for them to implement, such as antidumping measures. Lastly, the developing countries have been reluctant to become involved in negotiations on new issues –such as investment and competition– before the existing difficulties with respect to the implementation of the Uruguay Round agreements have been resolved (ECLAC 2002).

Services is to suggest ways and means to accomplish the goal of wider participation by developing countries in services trade.[16]

Lastly, special and differential treatment should include the right of developing countries to regulate their economic activities in such a way as to pursue development objectives, to maintain some barriers to trade and to furnish adequate support for local firms. In accordance with the analysis conducted in the two previous sections, the most critical elements of flexibility are those needed to facilitate the adoption of comprehensive export-promotion policies designed to guarantee the diversification of the export base and of destination markets and of policies to improve national and regional production linkages in the activities that are most closely associated with international markets.

Trade-related aspects of intellectual property rights must not be allowed to become an obstacle to the transfer of new technology to developing countries or to attach too high a cost to the process. They must also be made to work as an effective instrument to protect areas of interest for developing countries, such as traditional knowledge and biological wealth (see chapter 7). The countries of the region must conduct an objective analysis of the costs and benefits inherent in negotiations on new issues —particularly investment and competition— while difficulties with the implementation of the Uruguay Round agreements remain. In this respect, even taking into account the positive aspects of negotiations on these issues, it has not been clearly established that WTO would be the most appropriate forum for efforts to advance in these spheres of international cooperation (see chapter 4).

The Latin American and Caribbean region's participation in multilateral negotiations on trade in goods and services is taking place alongside a number of other ongoing negotiation processes with industrialized countries. The Free Trade Area of the Americas (FTAA) initiative merits particular attention within this context both because it is intrinsically important and because the pace of the negotiations has recently been stepped up. The FTAA negotiating agenda is broad and varied, ranging from traditional issues such as access to goods markets to trade in services and the protection of intellectual property. The negotiations seek to be consistent with WTO rules and disciplines and —where possible and appropriate— to improve upon them. A number of issues, however, such as investment and competition policies, transcend the WTO framework.

The FTAA disciplines would require the creation, and in some cases the reformulation, of national rules and institutions governing the protection of intellectual property, the development and administration of standards, and the design and implementation of competition policy, among others. The countries stand to benefit from the adoption of common disciplines that strengthen national reform policies. These disciplines can also require some difficult policy choices, however, especially for the less developed countries. For example, restrictions on requirements regarding local or technological content can prevent countries from using these policy tools to foster the diversification of the economy and export base. By the same token, the liberalization of financial services may hinder the appropriate management of capital account volatility and may thus make many countries more vulnerable to financial cycles, with the resulting effects on the sustainability of trade flows.

For many Latin American and Caribbean countries, the benefits to be obtained from increased market access and from trade liberalization will depend on their being able to pursue

[16] Paragraph 2 of the section on the objectives and principles of the negotiating guidelines is of particular interest in this respect, as it indicates that, "The negotiations shall aim to increase the participation of developing countries in trade in services". Paragraph 3 of the same section goes on to specify that, "The process of liberalization shall take place with due respect for national policy objectives, the level of development and the size of economies of individual Members, both overall and in individual sectors. Due consideration should be given to the needs of small and medium-sized service suppliers, particularly those of developing countries." See (WTO, 2001).

active polices to increase systemic competitiveness and thus expand their exports. In addition, the diversification of exports to include products with greater value added and greater technological content and the expansion of their linkages with the rest of production activity are vital in order to translate increased export capacity into economic growth. Mechanisms are also required for restructuring firms and, eventually, non-competitive sectors, on the one hand, and for enabling SMEs to participate in hemispheric trade flows, on the other. In fact, it is of crucial importance for the new rules and institutions to be based on a recognition of the asymmetries existing between countries. This is the only way that the fragile production structures of many Latin American and Caribbean countries can be strengthened while at the same time promoting new sustainable and dynamic comparative advantages.

It must be emphasized that free trade alone cannot guarantee convergence in levels of development within the framework of a process as complex as FTAA. This is why, as discussed in chapter 4, two additional elements are absolutely vital: increased international mobility of labour and the transfer of resources from more to less advanced regions for the explicit purpose of ensuring the convergence of levels of development. These elements have, moreover, played a key role in the consolidation of the most successful integration process the world has seen thus far, the European Union.

Chapter 7

Strengthening innovation systems and technological development

Macroeconomic stabilization and liberalization have been perceived by most policy makers as a sufficient condition for the local acquisition and absorption of the benefits to be derived from liberalizing trade, investment and technology flows. Despite the success of a number of countries in some facets of macroeconomic stabilization, however, the shift in the incentive system that has occurred in the past two decades has not led to entirely satisfactory behaviours in terms of creating technological capabilities at the national level and reducing the productivity gap vis-à-vis the more highly developed countries. Moreover, the region has also been slow in developing its capacity to adopt and disseminate new technological paradigms such as information technology, biotechnology and genetic engineering. These outcomes can be understood by looking at the changes that have occurred in the innovation systems of Latin America and the Caribbean.

This chapter discusses these changes and considers the strategic challenges facing the countries of the region as they seek to achieve a sustained technological development process on which to base their systemic competitiveness and bring their production apparatuses into the digital era. The first section briefly outlines the conceptual framework of the analysis of technological development. The second summarizes the evolution and current configuration of national innovation systems in the region, with emphasis on the main changes produced by external openness and globalization, and looks at the countries' levels of expenditure on science and technology. The third section gives a panoramic view of the regional situation in terms of information and telecommunications technologies and the capabilities needed to computerize production activities and participate in global networks. The fourth section considers the regulatory framework for property rights at the regional and global levels and the options it offers for the development of local technological capabilities. The fifth section contains guidelines for active policies to strengthen innovation systems (at national but also local and regional levels) in the context of competitiveness and technological development strategies, to promote the incorporation of information technologies and to protect intellectual property rights in keeping with those strategies.

I. Innovation systems and technological development

Firms respond to signals from their environment when they acquire and adapt technology and improve it over time in order to enhance their technological capabilities and competitive advantages. Such decisions are influenced by the structure of incentives, factor and resource markets (skills, capital, technology, suppliers) and institutions (in the fields of education and training, technology, finance and so on) with which the firm interacts. Innovation is therefore an *interactive process*, which links agents that respond to market incentives, such as firms, to other institutions that operate on the basis of strategies and rules that are independent of market mechanisms. The combination of agents, institutions and rules on which the absorption of technology is based has been called an *innovation system* —generally a *national* innovation system— which determines the rate of generation, adaptation, acquisition and dissemination of technological know-how in all production activities (Nelson, 1988; ECLAC, 1996b).

According to this approach, the main components of a national innovation system operate and are linked at three different levels, each of which offers a different framework for formulating and promoting economic policies (Freeman, 1987; Nelson, 1993; Cimoli and Dosi, 1995). First, the firms and their production systems are crucial (although not exclusive) recipients of know-how, which in large part is absorbed into operational routines and modified over time on the basis of rules of conduct and higher-level strategies (research activities, decisions on vertical integration and horizontal diversification, etc.). Secondly, the firms themselves become linked through networks with other firms and with non-profit institutions, government agencies, universities and organizations devoted to promoting production activities. These networks and policies, whose purpose is to improve the environment for carrying out scientific and technological activities, play a fundamental role in firms by strengthening or restricting opportunities for enhancing their technological capabilities. Lastly, at the broader national level, modes of behaviour at the microeconomic level form networks where a combination of macroeconomic effects, social relations, rules and political constraints is produced.

The generation and absorption of technology —and the consequent achievement and improvement of international competitiveness— are thus *systemic processes*, since the performance of the innovation system depends on a set of synergies and externalities of various kinds whose scope goes beyond business enterprises' profit-maximization responses to changes in incentives. In this view, technological opportunities and obstacles, together with the experiences and skills acquired by the various agents of the innovation system, which flow through the system from one economic activity to another, establish a specific context for each country or region. This means that any given set of economic incentives generates different stimuli for, and constraints on, innovation. In cases where there is a significant divergence between economic incentives and the stimulus to innovation represented by externalities, a firm's price-based allocation of resources to innovation will be suboptimal.

Ultimately, firms respond appropriately to the challenges of competitiveness if they operate in efficient markets and have well-established linkages to dynamic networks with strong institutions. In developing countries, in addition to the imperfect information and externalities that impede an appropriate response to these challenges, many business-related markets and institutions are deficient or non-existent. Both suppliers and basic service firms may be influenced by factors that lead to a shortage of technological capabilities and a lack of competitiveness.

In the field of scientific and technological knowledge, problems of uncertainty and imperfections in the price system prevent market mechanisms from operating well enough to assure a socially optimal allocation of resources for the generation and dissemination of this scarce good. This is precisely why the developed countries have adopted a proactive attitude in this area that has led them to facilitate the private patentability of government-sponsored university research, subsidize basic and applied research programmes in fields such as information and communications technologies (ICT) or the human genome, channel government procurement towards technologically dynamic firms, etc.

The history of today's developed world shows that in many fields of productive activity it has been the public sector that initially took the lead by promoting the development of a basic and applied research activity and building up a long list of institutions whose mandate is to stimulate the technological behaviour of the private sector. This has clearly worked in the cases of agriculture, atomic energy and telecommunications (leading to the development of the Internet), the broad spectrum of health disciplines (including the recent development of the human genome), the defence industries and many others. This is happening, moreover, in areas that are highly sensitive to international competitiveness, in which the governments of developed countries are especially eager to build an institutional base and national technological capabilities on which the private sector can then consolidate its internationally competitive position.

In Latin America and the Caribbean, the transition towards more open, deregulated and privatized economies has entailed a profound transformation of the innovation systems established in the State-led growth phase. Many recent studies reveal that the shortage of public resources and institutions capable of promoting the creation of dynamic, knowledge-based comparative advantages is one of the factors that explains why the region's innovation systems have not facilitated the accumulation and diffusion of technological capabilities. This transition process has inhibited interaction between the three above-mentioned components and, hence, national technological capabilities. Activities to promote the development of national networks have not had enough support in terms of linkages between the different agents of the innovation system. In other words, the production system has modernized a small part of the economy, owing to the effects of greater openness, but this has not been accompanied by a sufficient effort to stimulate the creation of national networks, such as a system of linkages with knowledge-producing and knowledge-diffusing institutions operating outside the market, i.e., an entrepreneurial culture and institutions that would help businesses interact with one another.

II. The evolution of innovation systems

1. Innovation systems in the State-led industrialization phase

During the State-led industrialization phase, a vast universe of public goods- and services-producing research and development (R&D) enterprises and institutes arose and spread throughout the region. In the great majority of countries, the public sector undertook to provide telecommunications, energy and transport services, among others, while it developed and expanded public education and health systems. This process created an enormous range of R&D institutes and laboratories, which were provided with equipment, skilled personnel and budgets to support the tasks directly related to the production of goods and services. Public development banks also helped in the work of expanding the production and technology infrastructure. In general, it can be said that during this period a widespread and sustained institutional "supply" model prevailed (Katz, 1987).

Many studies document the important technological role played by the public sector during these years in various countries, as it helped create technological infrastructure, train human resources, perform technological outreach work in the agricultural sector. All these efforts contributed to the development of a highly idiosyncratic technological and innovative culture. Far from portraying a failure, many studies show that these projects often led to successful production and technology programmes and to significant modernization of the national production apparatus (Katz, 1987; Stumpo, 1998). Industrial exports increased —often reflecting improvements in locally invented products and processes— as did technology transfer among the countries of the region.

Within this environment, the production system developed its technological capabilities and forms of behaviour depending on the type of firm and the origin of the capital involved. One type of technological behaviour can be seen in the core group of national enterprises, which fall into one of two very distinct subgroups: locally financed small and medium-sized enterprises; and large national conglomerates. The technological behaviour of foreign enterprises, for their part, continued to be dictated by the strategies and capabilities of their parent companies. We shall consider each case separately.

As far back as the 1930s (and in some countries earlier), with the help of tariff protection and the support of development banks, a large number of small and medium-sized local enterprises —many owned and run by families— that produced food, textiles and clothing, shoes, furniture, printed matter, tools and agro-food industrial machinery, among others, arose and flourished in Latin America. Even though they entered the industrial world with manufacturing plants that were little more than improvised craft shops and that were frequently equipped with second-hand or home-made machinery, and despite their low level of technical and production know-how, in time many of these enterprises became leaders in successful growth experiences. They set up their own technical teams, developed innovative product designs and production proccesses, trained their workers and advanced along a highly idiosyncratic, long-term learning curve. In this case, the creation of product and process technologies was undertaken without prior outside support, other than the ability to copy technology and the technical training that many immigrant entrepreneurs brought with them from their countries of origin.

The large public firms and locally-owned private conglomerates, which normally devoted themselves to the manufacture of consumer and intermediate goods or to the provision of services (energy, telecommunications) displayed a different model of technological behaviour. These firms developed their production and technological capabilities in those sectors that were considered strategic for the industrialization policy at the time. The development of technological capabilities was more prominent and included everything from advances in the building and operation of new factories to the establishment of engineering departments and project offices that could design and optimize the use of production facilities. In many cases, these advances were promoted by public institutes, which took charge of many of the necessary tasks. Thus, for example, in the energy and telecommunications sector, State enterprises and research institutes were set up and provided with abundant financial resources.

On the other hand, from the very beginning foreign capital in Latin America functioned as the engine for growth in knowledge-intensive branches such as automobiles, pharmaceutical raw materials, petrochemicals, production equipment and machinery. Rather than considering the possibility of following a development strategy based on local capital and technology, the first steps towards industrialization in these fields focused on finding foreign enterprises to develop these production sectors and to provide the necessary capital and technology. This meant that, from the beginning, producers took foreign product designs, process technologies and production organization routines and adapted them to local conditions rather than designing local models. The presence of these enterprises produced significant externalities. Indeed, capital goods and the flow of engineering, managerial and marketing knowledge from foreign enterprises deeply affected the industrial culture of the era, introducing working habits, labour rules and practices, quality control standards and forms of subcontracting that were often unknown in the local environment (Katz and Ablin, 1978).

In spite of the above and of the many cases where the public sector's technological effor successful sectoral development programmes, from a broader perspective the national innovation systems in those years did not, as a whole, become real engines of growth due to their fragmentary nature and lack of depth. Indeed, although these engineering efforts certainly made it possible to open up and develop a great many new industrial sectors and new factories that could not only replace imports but also produce exports, and while it is also true that many enterprises were able to advance along their learning curve, it must be pointed out that only occasionally were innovative products and processes created on a worlwide scale.

2. Changes in innovation systems brought about by external openness and globalization

Over the course of the past two decades, deep-seated changes in the region's innovation systems have been consolidated (Cimoli and Katz, 2001). These changes are attributable not only to inertial phenomena left over from the State-led development stage but also to more recent causal factors: on the one hand, the pro-competitive structural reforms of recent decades and, on the other, the growing globalization of production processes in which the world economy is involved.

According to recent ECLAC studies, structural reforms led to the restructuring of the region's production apparatus in a way that oriented it, on the one hand, towards non-tradable goods and services and, on the other, towards static comparative advantages (the production of raw materials and industrial processing of natural resources in the Southern Cone countries, and unskilled, labour-intensive *maquila* industries in Mexico and a number of smaller Central American and Caribbean countries). This process failed to create dynamic, knowledge-based comparative advantages that would increase the value added of exports and improve the position of the region's enterprises in world markets (ECLAC, 2001a; Reinhardt and Peres, 2000; Mortimore and Peres, 2001).

Globalization has also helped to transform innovation systems. On the one hand, globalization has led to profound changes in consumption patterns. While it has levelled out differences in taste and reduced selectivity by homogenizing consumers on the basis of internationally recognized brand names, it has also enhanced the value of ethnic, small-scale and handicraft products. On the supply side, the innovation systems of the countries of the region have shifted, tending to become more internationalized owing to greater integration into internationally integrated production systems (IPS), which are managed at the global level by transnational corporations. Organizing production and consumption on a global scale means making the most of economies of scale, capturing the advantages of specialization and making use of opportunities for rationalizing costs. Moreover, it means thinking of consumers as a homogeneous group of people who, regardless of their culture or specific circumstances, exhibit similar preference functions.

The development of these organizational models for production entails a necessary reduction in the degree of independence and vertical integration of each member of the IPS, given the fact that all must operate on the basis of a homogeneous product and production routine, adhere to uniform specifications and use parts, intermediate components and inputs acquired anywhere in the world. Otherwise, there would no longer be any possibility of trading intermediate inputs in real time with the other members of the network, and economies of specialization would decrease. Accordingly, there has been an increase in the acquisition of international licences and better access to foreign product designs and process technologies, encouraged by the rise in the number of firms operating on-line with their head offices or licensing firms abroad. All this has consolidated new organizational models for production, while at the same time radically modifying the paradigm for technological accumulation processes and relations between actors within innovation systems (Cimoli and Katz, 2001; Katz and Stumpo, 2001).

Since planning and organizing production and consumption on a global scale entails operating in a number of different locations, it is clear that the institutional framework —patent rights, tax or customs legislation, environmental regulations, etc.— must not differ too much from one country to another; this helps a global entrepreneur to feel more comfortable in choosing a location for the various segments of the production system. In other words, the model entails endogenous pressure towards institutional homogenization, although this does not necessarily have to be compatible with the national interest of each country belonging to a given IPS. Examples abound, and the growing pressure being exerted on developing countries by developed countries to "level the playing field" —i.e., eliminate national idiosyncrasies in order to pave the way for a more uniform, transnationalized production structure— is clear evidence that globalization leaves national governments with fewer degrees of freedom. This does not mean, however, that these degrees of freedom have disappeared altogether; indeed, the new rules of the game appear to consist in knowing how to identify and take advantage of them.

As part of this process, national legislation has been converging towards intellectual property laws similar to those of the developed countries, which protect intellectual rights over software and regulate the national use of trademarks, domain names, geographical indications, etc. This involves a gradual process of institutional standardization, which has been accelerating in recent years as a result of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) of the Uruguay Round of trade negotiations.

The performance of innovation systems is directly related to the production structure and the firms and public institutions that constitute it. Four patterns of behaviour are associated with the transformation and new pattern of acquisition of technological and innovative capabilities that today characterizes the production system and its enterprises (Cimoli and Katz, 2001).

The first pattern involves a *simultaneous process of modernization and inhibition of national capacities*. Owing to the globalization of production and greater integration with an international IPS, many local subsidiaries of transnational corporations (TNCs) have narrowed their product mix, specializing in one (or a few) products out of the range produced by the corporation at the global level and, at the same time, importing the remaining items from that product range. On the other hand, the incorporation of computer-based equipment and machinery and the transition to digital forms of labour organization have accelerated integration into global IPSs. This ultimately influences the nature of production processes, which today have less down time, shorter lead times between design and manufacture, and lower defect and rework rates. In other words, productivity has risen not only because of the increase in the capital/labour ratio but also because of the gradual introduction of a more highly sophisticated generation of machinery and equipment that necessarily involves more efficient styles of labour organization.

The decline in the prices of imported capital goods brought about by trade liberalization encourages the replacement of local machinery, equipment and skilled labour. On the one hand, this tends to increase the capital-intensiveness of the various production sectors. On the other, as imported equipment becomes less expensive than locally-produced equipment, the latter is replaced, and the local capital goods industry's market share shrinks. Finally, since the new machinery incorporates operational capabilities previously provided by skilled workers and engineers, the demand for this type of worker declines.

The great advantage of the IPS is therefore that it captures the benefits of economies of scale, but its cost for the countries of the region derives from the abandonment of the local adaptation of products and processes in favour of the "commoditizing" of goods and services. There is thus a significant reduction in the development of national technological capabilities derived from the reduction of these adaptive efforts. Recalling that these efforts were an important part of the technological behaviour model during the State-led growth stage, it is clear that the transition to the IPS world entails a major change in the structure and behaviour of Latin American innovation systems. Linkage with other countries deepens and becomes a determining factor of a firm's behaviour, but this could well be happening at the expense of the inhibition of national technological capabilities or even a decline in the density of network of domestic linkages.

The second pattern is the *marginalization and destruction of national production chains.* While advances in the internationalization of processes are taking place, another part of the production apparatus is being increasingly marginalized from the new industrial organization model now being consolidated. Thus, major pre-existing production chains are being disrupted, and national producers —in many cases small and medium-sized enterprises— have lost access to markets as their products are replaced by imported substitutes. A similar process has occurred in the area of technical services for production (typically technological know-how for improving and adapting products and processes), which can be obtained more frequently on-line and in real time from abroad. This marginalization has been compounded by old and new problems of access to factor markets (cost of long-term capital and asymmetries in access to technological knowledge or land), which has had a significantly greater impact on small and medium-sized family-owned and run firms than on large local or foreign firms.

The third behavioural pattern that has been emerging is *uneven specialization in the production of knowledge*. Although there are sharp differences across countries in terms of the new specialization pattern and the way in which, in each case, firms and industries have been absorbing new sectoral technological and competitive regimes, a common feature in the region is that enterprises have tended to specialize in relatively less technology-intensive production activities and processes. The region is rich in natural resources and in unskilled and semi-skilled labour, but it is rather poor in its capacity to create, adapt, disseminate and use new technologies. Many firms participate in the manufacture of industrial commodities, i.e., highly standardized products in which only limited domestic technology efforts are carried out. Moreover, unlike the major producers of industrial commodities, such as paper and pulp in the case of Sweden or Finland, or minerals in the case of Canada or Australia, the major Latin American conglomerates that produce these goods have made little effort to move towards patterns of specialization involving a greater technological content. Nor have they managed to achieve a greater degree of vertical integration involving the manufacture of relatively high-technology intermediate machinery and equipment or inputs. Instead, these entrepreneurial groups have opted to remain at the low end of the natural resource-processing value chain without attempting any greater technological deepening. One consequence of this is that they have made little or no use of biotechnologies in fields such as forestry or food production. Nor have they involved themselves in new disciplines in such fields as mineralogy, aquaculture or others associated with the sustainable exploitation of their natural resource base. In other words, they have chosen to tap the available natural resources, without subsequently moving towards the acquisition of knowledge rents or committing significant amounts of resources to technological deepening.

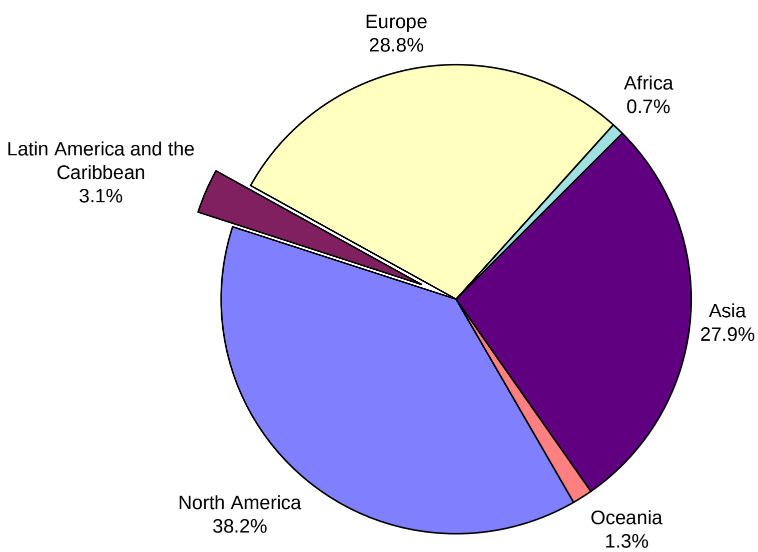
The fourth behavioural pattern is *the transfer of some pre-existing R&D activities out of the region.* Many foreign-based enterprises that have recently established operations in the region, through the purchase of a pre-existing local plant, have chosen to cut back or simply discontinue, national R&D efforts and the project offices that local firms had set up to support their production and investment activities in previous decades.

The transition to an international IPS has led to the outward transfer of engineering and R&D activities previously carried out by local firms. These firms had tended to specialize in the simplest segment of the global production process, which generally involved assembly work (*maquila* activities) or the first stages of natural resource processing, while leaving both product design and the search for new production processes in the hands of the parent company. At the same time, the privatization of State utilities has led to the closing of technical departments and the reduction of expenditure on local engineering activities in fields such as energy, telecommunications or transport. The new foreign operators involved in these sectors are bringing new product, process and labour organization technologies into the region from their respective parent companies and their international suppliers of intermediate inputs and production services. Although the service structure is being rapidly modernized in these cases, this process is, paradoxically, making much less use of local engineering services and local R&D activities.

3. Science and technology expenditure

In general, expenditure on science and technology (S&T) in Latin America is very low. The countries of the region spend only 3.1% of the world total on this item (see figure 7.1).

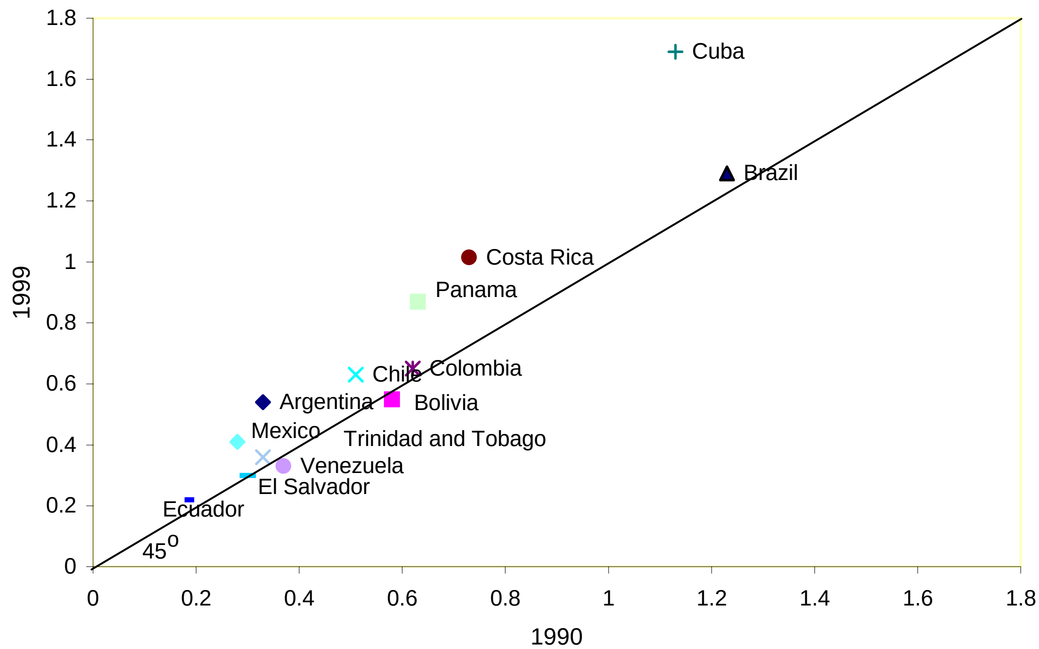
Figure 7.1
WORLD INVESTMENT IN RESEARCH AND DEVELOPMENT, 1996-1997
(*Percentages*)



Source: UNESCO Institute for Statistics (UIS), *The State of Science and Technology in the World 1996-1997*, Montreal, Quebec, 2001.

During the long period when the State-led industrialization strategy prevailed, S&T expenditure —even in the large countries of the region— in no case exceeded half a percentage point of GDP, with the bulk of this being spent by State enterprises and public sector-institutes. In the 1990s, S&T expenditure by most countries of the region remained at approximately the same levels (see figure 7.2). The highest relative expenditure levels continue to be posted by Brazil, Costa Rica and Cuba. This stability of spending as a percentage of GDP clearly indicates that the allocation of resources for the creation of new technology is still not a high priority in the region.

Figure 7.2
LATIN AMERICA AND THE CARIBBEAN: EXPENDITURE ON SCIENCE AND TECHNOLOGY AS A PERCENTAGE OF GDP



Source: United Nations Educational, Scientific and Cultural Organization (UNESCO), Ibero-American Network of Science and Technology Indicators (RICYT) and ECLAC.

In Latin America and the Caribbean R&Dexpenditure is largely government-funded; the private sector finances only a third of total R&D activities (see table 7.1). This situation stands in contrast to that of the United States, where private enterprise finances 69% of R&D.

Table 7.1
LATIN AMERICA: EXPENDITURE ON RESEARCH AND DEVELOPMENT, BY FUNDING SECTOR, 1999 a/
(*Percentages*)

	Government	**Business**	**Other** b/
Argentina c/	40.40	26.00	33.60
Bolivia	24.00	20.00	56.00
Brazil	57.20	40.00	2.80
Chile	64.30	21.50	14.20
Colombia	70.00	13.00	17.00
Costa Rica	53.46	20.16	26.38
Cuba	58.80	41.20	
Ecuador	39.80	32.50	27.70
El Salvador	51.90	1.20	47.00
Mexico	71.10	16.90	12.00
Panama	44.60	0.70	54.70
Uruguay	9.40	35.60	55.00
Venezuela c/	31.50	44.80	23.70

Source: United Nations Educational, Scientific and Cultural Organization (UNESCO), Ibero-American Network of Science and Technology Indicators (RICYT) and ECLAC.

a/ Latest available year.
b/ Includes funding from higher education, private non-profit organizations and foreign sources.
c/ Data corresponding to funding for science and technology activities.

Latin American and Caribbean researchers represent between 3% and 7% of the world total, according to the standard sources and estimation method used for this purpose. Still, although the gap vis-à-vis the more industrialized countries remains large, the region has a considerable endowment of human resources. Among the Latin American and Caribbean countries, Argentina, Uruguay, Chile and Costa Rica have the highest ratios (more than one per 1000) of researchers to the economically active population (see table 7.2).

Table 7.2

LATIN AMERICA AND THE CARIBBEAN: NUMBER OF RESEARCHERS PER 1,000 MEMBERS OF ECONOMICALLY ACTIVE POPULATION

Country	**1999** a/
Argentina	2.57
Bolivia	0.38
Chile	1.35
Colombia	0.47
Cuba	1.2
Ecuador	0.31
El Salvador	0.2
Mexico	0.74
Nicaragua	0.29
Panama	0.78
Trinidad and Tobago	0.66
Uruguay	1.8
Venezuela	0.45

Source: United Nations Educational, Scientific and Cultural Organization (UNESCO), Ibero-American Network of Science and Technology Indicators (RICYT) and ECLAC.

a/ Most recent year available.

During the implementation of liberalization policies and strategies in the region, a steady increase over time in S&T spending as a proportion of GDP would have been advisable in order to bolster international competitiveness. In general, public policies kept a low profile during the reform period, however. This, combined with the region's low starting point in this respect, further weakened Latin American and Caribbean innovation systems in terms of knowledge production and diffusion. In addition to the fact that the production system had been encouraged to specialize and become part of the global production system in non-knowledge-intensive sectors, public policy perpetuated the structural weakness of most science and technology activities.

III. Information and communications technologies (ICTs)

1. The nature of changes generated by ICTs

The Latin American and Caribbean countries are gradually moving into the digital era. Digital production raises four different sets of issues. The first is that of infrastructure, which includes computers, telephone lines, fibre-optics networks, wireless telecommunication networks and any other physical components the industry needs to operate. The second is the software applications industry. Products and services traded in these markets are based on the informatics infrastructure and permit production and commercial activities to be carried out on-line. The third level is that of intermediaries, which enable agents to interact with one another and hold virtual meetings in the horizontal and vertical portals market. Finally, the fourth level is that of on-line transactions in the broad sense of the term, which includes e-commerce, e-health, e-government, etc. This is where effective use is made of digital interaction to conduct commercial, educational, health-care and other transactions.

The first level is a very dynamic global industry that embraces both the digital infrastructure needed for network integration and the production of computer and telecommunications equipment to operate within these networks. The installation of such infrastructure and the achievement of connectivity are essential steps for any country wishing to enter the digital era. On the other hand, local production of equipment is not a necessary condition and, in fact, international experience shows that it does not lead directly or automatically to the computerization of the national production apparatus, nor to a more intensive use of ICTs. Thus, there are countries such as the Republic of Korea that produce a significant amount of ICT equipment but are behind the times in terms of e-commerce, while others that have virtually no ICT production sector, such as Australia, are e-commerce pioneers (OECD, 2001b). Accordingly, even though —unlike a number of developing economies in East Asia— only a few Latin American and Caribbean countries have developed the capacity to produce parts and equipment, this does not hinder them from computerizing production activities or hooking up to global networks.

In general, the Latin American and Caribbean countries have increased their use of human resources and software to gain access to local and international networks. This process has accelerated in recent years for export-oriented firms that have joined a global IPS. Moreover, the restructuring of the region's production apparatus is paving the way for the emergence of a new set of local technological capabilities for the provision of production services —transport, marketing, packaging, etc.— and computer software and applications, in which many new small and medium-sized local enterprises are showing signs of development. In contrast, most of the more traditional small and medium-sized enterprises that produce for the domestic market are having tremendous difficulties in absorbing information technologies into their activities.

This process of modernizing production and adopting software began years back with the spread of CAD/CAM (computer-aided design/ computer-aided manufacture), which reduced both lead times and inventories in the manufacturing process. This was only the beginning of a long road towards the computerization of operational routines, which later included the dissemination of Enterprise Resource Planning (ERP), Supply Chain Management (SCM) and Customer Relationship Management (CRM). The incorporation of these systems, as a whole, involves the operation in real time of the entire value chain in which a firm operates, including not only its own internal processes but also those of its suppliers and customers. This has facilitated the spread of much more highly sophisticated production organization routines. These routines operate on the basis of a complex series of high-cost software, which limits their availability to small and medium-sized enterprises.[1]

This software is often produced within the firm itself by vertically integrated industrial organization departments. Lately, however, a dynamic application service providers (ASP) industry has arisen. This industry has been taking over the preparation and finalization of specific services of this type, which are subject to significant economies of scale.[2] The use of these new production technologies is inducing a profound change in the way work is organized and in firms' management and administrative principles, as well as giving rise to a local infant industry in this field.

[1] The available information indicates that the operational software needed for the integrated application of ERP, SCM and CRM costs nearly US$ 1 million and requires at least a year to set up and learn to use.

[2] Years ago, the choice facing firms was "develop or buy". Today, the choice of developing software seems justified only in the case of large enterprises or in those with very specific functional requirements which cannot find adequate solutions in the market (see Novis, 2001).

2. The progress of connectivity in the region

All the major Latin American and Caribbean countries began the year 1998 with less than 1% of their population connected to the Internet. Since then, Internet use has increased tremendously, turning the region into the fastest-growing Internet community in the world. Although connectivity is still low in some countries of the region, it is expanding rapidly. In the region as a whole, 84% of the existing telecommunications infrastructure is digital and almost all of it is automated. The fastest-growing network is mobile telephony, with 70 million cellular phone subscribers as of the first four months of 2001. Together with the development of infrastructure, the use of the Internet has been expanding rapidly, although it is still at an early stage. For example, less than one fifth of the agents in the region with Internet connections engage in e-commerce. Moreover, although some countries of the region, such as Chile and Brazil, have started using the Internet as a means of interacting with the public and providing services (telephone service, banking or government offices), and this practice is expanding to other countries, there is still a great deal of scope for progress in this and other areas (Hilbert, 2001).

Table 7.3 shows the speed at which this dimension of technological progress is evolving in the world. In 67 countries for which comparable data are available, the median number of Internet hosts rose from 0.3 per 10,000 inhabitants in 1995 to 7.2 in 2000, and the average went from 3.6 per 10,000 inhabitants to 30.4. There was also less dispersion across countries, which means that the countries that were further behind made a great effort to close the gap during that period. As a whole, Latin America and the Caribbean took a giant step forward. Indeed, in 1995, only three countries (Chile, Costa Rica and Panama) showed a greater degree of connectivity than expected, based on their per capita GDP. Five years later, nine countries (Argentina, Belize, Brazil, Chile, Costa Rica, Colombia, Mexico, Trinidad and Tobago, and Uruguay) did so (see figures 7.3a and 7.3b).

Table 7.3 also illustrates trends in connectivity gaps between different groups of countries. Taking the most technologically advanced countries as the basis for comparison, 17 Latin American and Caribbean countries narrowed this gap; this can be seen more clearly in the mean ratios (from 1.6 to 4.4) than in the index based on the median number of Internet hosts per 10,000 inhabitants. It is noteworthy, however, that, far from widening, the digital divide between the region and the leading countries narrowed for middle- and high-connectivity countries and remained virtually stable for the seven Latin American countries with a lower level of connectivity.

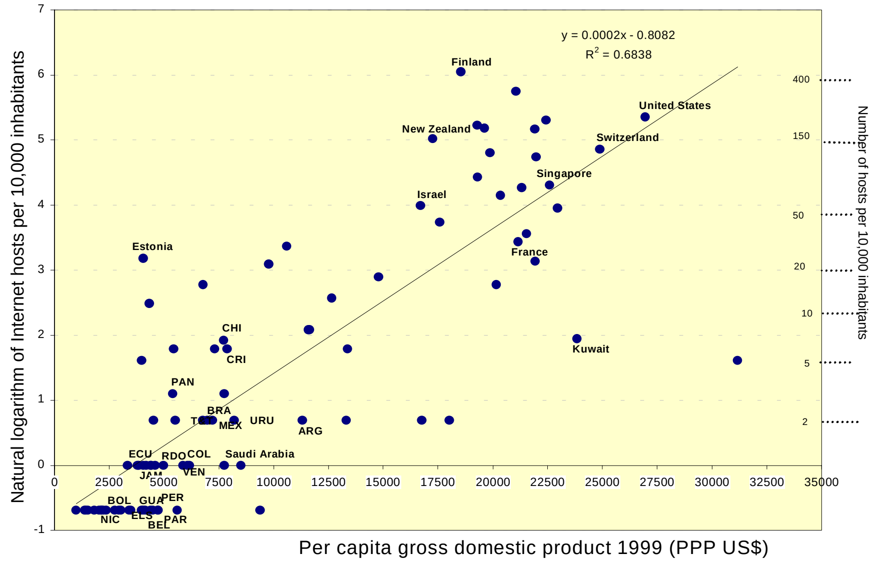
Table 7.3
CONNECTIVITY LEVELS AND GAPS, a/ **1995-2000**
(*Means, medians and variation coefficients for the number of Internet hosts per 10,000 inhabitants, and mean and median ratios*)

	Mean & VC. b/		**Mean ratio**		**Median**		**Median ratio**	
	1995	**2000**	**1995**	**2000**	**1995**	**2000**	**1995**	**2000**
Total (67 countries)	3.56	30.37	30.1	31.9	0.30	7.20	3.8	9.2
	2.04	*1.65*						
Total excluding LAC (50 countries)	4.71	39.27	39.8	41.3	8.09	55.30	102.4	70.7
	1.72	*1.41*						
Leaders (18 countries)	11.83	95.07	100.0	100.0	7.90	78.25	100.0	100.0
	0.86	*0.62*						
Potential leaders (19 countries, 4 LAC)	1.15	14.12	9.7	14.8	0.60	11.40	7.6	14.6
	1.08	0.67						
Dynamic followers (24 countries, 12 LAC)	0.14	2.26	1.2	2.4	0.05	0.40	0.6	0.5
	1.72	1.97						
Dynamic followers excluding LAC (12 countries)	0.15	0.98	1.3	1.0	0.05	0.15	0.6	0.2
	2.21	*2.43*						
Dynamic followers, LAC only (12 countries)	0.13	3.54	1.1	3.7	0.10	1.20	1.3	1.5
	0.65	1.61						
Marginalized (6 countries, 1 LAC)	0.05	0.18	0.4	0.2	0.05	0.15	0.6	0.2
	0.00	*0.72*						
Latin America and the Caribbean (17 countries)	0.19	4.18	1.6	4.4	0.10	1.90	1.3	2.4
	0.99	*1.23*						
Latin America and the Caribbean (medium and high group, 10 countries) c/	0.28	6.82	2.4	7.2	0.20	6.70	2.5	8.6
	0.73	*0.78*						
Latin America and the Caribbean (low group, 7 countries) d/	0.06	0.41	0.5	0.4	0.05	0.40	0.6	0.5
	0.38	*0.35*						

Source: United Nations Development Programme (UNDP), *Human Development Report, 2001. Making New Technologies Work for Human Development,* New York, 2001, table A.2.4, p. 62; *Human Development Report, 1998. Consumption for Human Development,* New York, 1998, table 1, p. 130.

a/ Gaps are calculated on the basis of the values of the leading group adjusted to 100.
b/ The variation coefficient is italicized.
c/ Argentina, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Mexico, Panama, Trinidad and Tobago and Uruguay.
d/ Bolivia, Ecuador, El Salvador, Jamaica, Nicaragua, Paraguay and Peru.

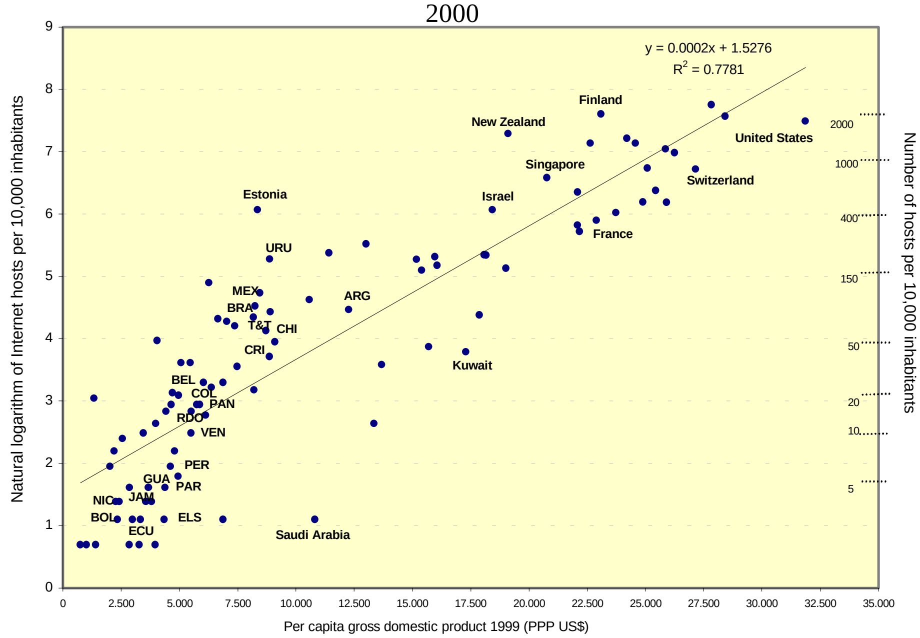
Figure 7.3a
CONNECTIVITY a/ **AND GDP IN THE WORLD** b/
1995



Source: United Nations Development Programme **(**UNDP), *Human Development Report, 2001. Making New Technologies Work for Human Development*, New York, 2001, table A.2.4, p. 62; *Human Development Report, 1998. Consumption for Human Development,* New York, 1998, table 1, p. 130.

a/ Number of Internet hosts per 10,000 inhabitants.
b/ For 89 countries. Excludes those with 0-1 hosts per 10,000 inhabitants in the year 2000 and countries for which no data was available.

Figure 7.3b
CONNECTIVITY a/ **AND GDP IN THE WORLD** b/
2000



Source: United Nations Development Programme **(**UNDP), *Human Development Report, 2001. Making New Technologies Work for Human Development,* New York, 2001, table A.2.4, p. 62 and table 1, p. 146.
a/ Number of Internet hosts per 10,000 inhabitants.
b/ For 96 countries. Excludes those with 0-1 hosts per 10,000 inhabitants in the year 2000 and countries for which no data were available.

Table 7.4 summarizes the changes in connectivity in Latin America and the Caribbean in the second half of the 1990s. It shows the increases in the number of Internet hosts per 10,000 inhabitants in Argentina, Belize, Brazil, Colombia, Mexico, Trinidad and Tobago and Uruguay. These countries, which in 1995 were below or near the internationally expected average in terms of their per capita income, rose above it in 2000, together with Chile and Costa Rica. On the other hand, Bolivia, Ecuador, El Salvador, Guatemala, Jamaica, Nicaragua, Paraguay and Peru remained at lower levels of connectivity than those expected in relation to the prevailing world averages in 2000.

Table 7.4

LATIN AMERICA AND THE CARIBBEAN: LEVEL OF CONNECTIVITY a/ **IN 2000 AND TREND BETWEEN 1995 AND 2000, COMPARED TO WORLD PATTERN** b/

Connectivity in year		**2000**		
		High	**Medium**	**Low**
1995	High	Chile (s > s: **6.2**) Costa Rica (s > s: **4.1**)	Panama (s > l: **1.9**)	
	Medium	Uruguay (b > s: **19.6**) Mexico (l > s: **9.2**) Argentina (b > s: **8.7**) Brazil (l > s: **7.2**) Trinidad and Tobago (l > s: **7.7**)		
	Low		Belize (b > s: **2.2**) Colombia (b > s: **1.9**) Dominican Rep. (l > l: **1.7**) Venezuela (b > l: **1.2**)	Peru (b > b: **0.7**) Guatemala (b > b: **0.5**) Paraguay (b > b: **0.5**) Jamaica (l > b: **0.4**) Nicaragua (b > b: **0.4**) Bolivia (b > b: **0.3**) Ecuador (l > b: **0.3**) El Salvador (l > b: **0.3**)

Source: United Nations Development Programme (UNDP), *Human Development Report, 2001. Making New Technologies Work for Human Development,* New York, 2001, table A.2.4, p. 62 and table 1, p. 146; *Human Development Report, 1998. Consumption for Human Development,* New York, 1998, table 1, p. 130.

a/ Internet hosts per 10,000 inhabitants. Figures in bold correspond to the rate for 2000.

b/ See figure 7.3. The trend in of the number of hosts per 10,000 inhabitants in 1995-2000 is shown for each country in comparison to the world pattern in terms of annual per capita GDP: *s* indicates that the number of Internet hosts in the country is above the world average; *b* indicates that it is below the world average; and *l*, that it is approximately the same as the world average in terms of the country's per capita GDP. For example, b>s means that the country rose above the average after being below it; b>1 means that it went from being below the average to being near to the expected value in terms of its per capita income, etc.

Although Latin America and the Caribbean as a whole did not lag behind in terms of connectivity, it is a matter of concern that the countries of the region with lower per capita incomes lost ground in this respect, making it even more difficult for them to become part of the information economy.

Moreover, the fact that a large group of countries in the region show higher degrees of connectivity than would be expected judging from their per capita incomes and have narrowed the gap separating them from the leading ICT countries does not guarantee them a place in the digital era within the next few years or in technological innovation processes, nor does it ensure a sufficient diffusion of technological innovation. In order to mainstream the production apparatus in global IPSs and networks, the alignment of the countries' development levels with international standards will not suffice; what is required is a form of connectivity that converges with that of the technologically developed countries. Moreover, in order to keep the digital divide between the region and these countries from widening if growth in the region proves to be slow and unstable, additional efforts will have to be made to prevent the business cycle from determining how much is invested in technological infrastructure and capabilities, since this could well result in obsolescence or backwardness in this field of rapid global change.

Another source of concern is the enormous "domestic digital divide" that exists in both social and productive terms, which in many ways represents a greater threat to the region than the international gap. Indeed, although service costs have tended to fall, they continue to shut out a large part of the Latin American and Caribbean population. The still relatively low rate of telephone connectivity in the lower-income segments of the region and the cost structure of telephone service are factors that hinder active Internet use on the part of poorer households and small enterprises. Computer equipment also is still too expensive for lower-income households and smaller enterprises and micro-enterprises. Although some governments in the region have taken the initiative in providing Internet access in schools for lower-income groups, no equivalent steps have been taken to facilitate access or the development of special networks for small and medium-sized enterprises. Although fixed telephone lines are currently the simplest and most affordable way to communicate or connect with the Internet, the rapid spread of mobile telephones could begin to make access available to lower-income segments. This would require substantial reductions in the cost of such services, however.

IV. Intellectual property rights

1. Standardization of intellectual property regulations

Over the past two decades, an international debate over intellectual property has been generated by, for the most part, circumstances emerging from the internal functioning of the United States economy. Owing to the relative loss of that economy's competitiveness in the 1970s, a considerable number of pharmaceutical, electronics and entertainment companies lobbied the Department of Commerce to accord a higher priority in its multilateral agenda and in bilateral negotiations to legislation on patents and other forms of intellectual property with a view to strengthening protection for agents holding such rights. What lay behind this position was the idea that research findings were diffused much too rapidly to competing firms of other nationalities and that the patent system did not provide enough protection to United States firms, which were spending money on creating new technologies. It was in this context that two important legislative changes were made in the United States: the Patent and Trademark Amendments Act of 1980, better known as the Bayh-Dole Act, and the Federal Courts Improvement Act of 1982 (Coriat and Orsi, 2001; Abarza and Katz, 2002; Slaughter and Rhoades, 1996). These changes authorized public R&D institutions (especially universities) to patent their research findings and exploit them through joint ventures with private firms, or through the creation of start-ups by academic groups or university researchers. At the same time, important breakthroughs were being made in the field of human genetics, informatics and computer sciences in academic centres, and these institutions made highly significant advances in those years with the support of public research and development funds (Mowery and others, 1999).

The authorization of private patents on these discoveries and the founding of scientific firms to market them help to explain why the annual register of patents in the United States economy has grown so rapidly since the 1980s and why the competitive position of that country was revitalized in many high-technology markets during the 1990s. A change in United States requirements for the patenting of an invention was another factor in this connection. This change took the form of a 1982 regulation that relaxed the novelty requirements for the issue of a patent. Thereafter, proof of commercial success gradually came to win greater acceptance as grounds for patenting an invention.

As a result, patent applications and the issuance of patents to residents and foreigners by the United States Patent and Trademark Office increased significantly (see table 7.5). At the same time, the Office has become increasingly important as a global centre of patenting activity, since it is where most countries, enterprises and institutions prefer to have their inventions and discoveries recognized. As for the most dynamic sectors, as represented by the number of patents issued by this Office, there has undoubtedly been an enormous increase in patenting in the sectors of molecular microbiology, drugs, pharmaceutical raw materials, transistors and other electronic elements (see figure 7.4)

Table 7.5

UNITED STATES: PATENTS OBTAINED, BY COUNTRY

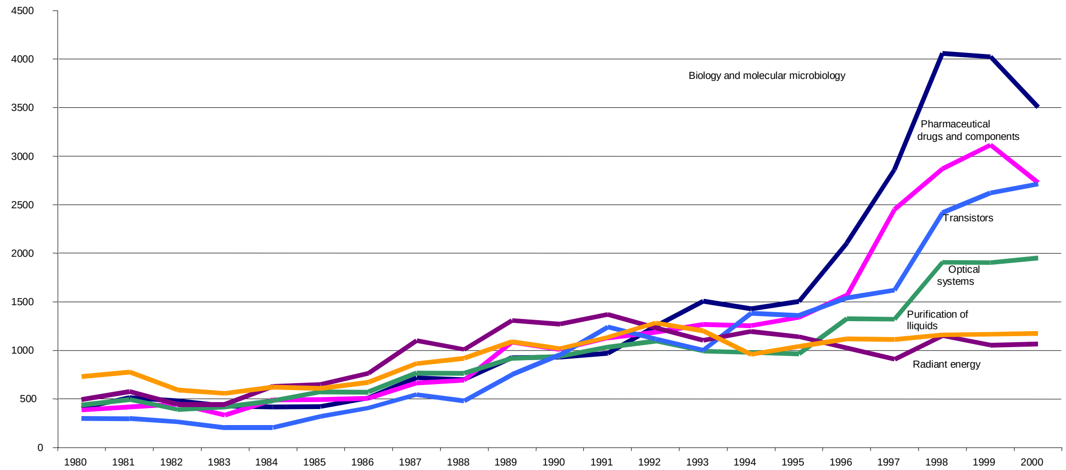
	Ranking 2000	**Pre 1987**	**1987**	**1990**	**1995**	**2000**	**Total**
Total		1,559,118	82,952	90,364	101,419	154,497	3,081,418
United States origin		1,047,922	43,520	47,390	55,739	85,072	1,870,059
Foreign origin		511,196	39,432	42,974	45,680	72,425	1,211,359
Japan	1	131,465	16,557	19,525	21,764	31,296	452,737
Germany	2	122,423	7,884	7,614	6,600	10,324	231,330
United Kingdom	3	62,376	2,775	2,789	2,478	3,667	101,680
France	4	46,050	2,874	2,886	2,821	3,819	89,218
Canada	5	26,102	1,594	1,859	2,104	3,419	57,290
Switzerland	6	27,404	1,374	1,284	1,056	1,322	44,635
Italy	7	16,044	1,183	1,259	1,078	1,714	34,146
Taiwan, province of China	10	950	343	732	1,620	4,667	24,646
Republic of Korea	11	259	84	225	1,161	3,314	18,169
Israel	15	2,069	245	299	384	783	8,161
Mexico	24	1,253	49	32	40	76	1,907
Brazil	28	453	34	41	63	98	1,263
Argentina	32	504	18	17	31	54	904
Venezuela	36	197	24	20	29	27	557

Source: United States Patent and Trademark Office.

In this context, the less developed countries experienced strong international pressure to change their patent legislation. The final result of this process was the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) concluded at the Uruguay Round of trade negotiations, which established minimum standards for the regulation of intellectual property in the countries members of the World Trade Organization (WTO) in 1993. The normative content of the agreements and the widespread acceptance of trade liberalization strategies profoundly changed the existing incentive system.

Besides establishing minimum standards, the TRIPs Agreement expanded the number of products or sectors subject to patents (including, for example, pharmaceutical products, whereas previously only pharmaceutical processes were patentable) and permitted the importation of the patented product to be accepted as sufficient utilization of a patent, features that had not previously gained general acceptance in national codes.

Figure 7.4
UNITED STATES: NUMBER OF PATENTS OBTAINED, BY MAIN SECTORS OF ACTIVITY



Source: César Morales, "Situación y Perspectives de los DPI sobre la biotecnología y transgénicos", document presented at the seminar "Genetically modified organisms: their impact on Latin American agriculture" (Termas de Cauquenes, 20-22 November), 2001, on the basis of the United States Patent and Trademark Office (USPTO).

The many studies that have been made through the years on the advantages and disadvantages of the patent system in the developed countries have not managed to demonstrate clearly whether patenting has positive or negative long-term effects.[3] For the developing countries, the net balance is even less clear. Thus, the TRIPs Agreement represented a cost, in raising the price of patented products and technologies, as the World Bank (2002c, chapter 5), among other analysts, recently pointed out. Moreover, this protection can slow down national learning processes and the narrowing of the technological gap between the developing and the industrialized countries by blocking processes —of imitation and reverse engineering— that were common in the developing countries and still are today in the late-industrializing economies. This practice therefore raises costs when the registration of intellectual property rights is not accompanied by an effective use of the technology in the country granting the protection, and in such cases the patent serves little purpose other than to reduce competition. The management of intellectual property is, moreover, a complex and costly business. It requires legal, technical and administrative skills which are generally scarce in the developing countries. This also limits its potential benefits.

Such disadvantages should be offset by the potential benefits which the protection of intellectual property offers to the developing countries, especially the middle-income countries that make up most of the region. Apart from protecting the findings of their R&D activities, which systemic competitiveness strategies should help to increase, it is an essential factor in the development of some markets, in which trademark protection and (in some cases) indications of origin are important, or of service markets such as television products, films or computer software. In many of these cases, protection is particularly valuable in intraregional trade. Other benefits, especially those associating protection of intellectual property with the attraction of foreign direct investment (FDI), are only useful when the investor makes effective use of the technology in the recipient country.

[3] Thus, one of the first and most exhaustive of these studies, done in 1950 by Fritz Machlup, concluded that, "[I]f one does not know whether a system "as a whole" (in contrast to certain features of it) is good or bad, the safest "policy conclusion" is to "muddle through" .... If we did not have a patent system, it would be irresponsible... to recommend instituting one. But since we have had a patent system for a long time, it would be irresponsible, on the basis of our present knowledge, to recommend abolishing it. "This last statement refers to a country such as the U.S. —not to a small country and not a predominantly nonindustrial country, where a different weight of argument might well suggest another conclusion".

2. Latin American patent activity

According to information from the World Intellectual Property Organization (WIPO), patenting trends and patterns in Latin America and the Caribbean differ considerably from those in the developed economies and in the newly industrialized countries in South-East Asia (see table 7.5). In these countries, the flow of patents granted to residents has tended to grow at an equal or greater rate than those issued to non-residents. In contrast, in Latin America and the Caribbean the number of patents applied for by non-residents is growing much faster than those requested by residents. This trend is associated with the use of patents by foreign corporations to market and import their products, which in many cases tends to hinder the development of local production and technological capabilities (Aboites and Cimoli, 2001).

In contrast to patent activity in the United States Patent and Trademark Office, where the flow of patents is now the highest in the world, the countries of Latin America and the Caribbean as a whole granted only one fifth the number of patents applied for by the Republic of Korea alone. A difference can also be seen in the structure of patent applications. Latin American applications are concentrated in mechanical and chemical engineering, while the industrialized and newly industrialized economies generate considerably more patent applications in technologies associated with telecommunications, electronics and biotechnology.

Latin America is in quite a different position with regard to the patenting of plant varieties, however. Advances in genetic research and genetic engineering have resulted in a significant increase in applications for these patents, which may be granted to processes and products such as new varieties of hybrid plants, transgenic plants or processes for endowing them with certain desirable features. Plant patents requested from WIPO show a growing Latin American presence (Morales, 2001), which in recent years has come to represent more than 10% of the world total (see table 7.6). Moreover, there has also been an increase in the number of countries of the region that are applying for and obtaining plant patents. In 1994 only Argentina and Chile did so, while in 1999 the list included Brazil, Colombia, Bolivia, Ecuador, Mexico, Paraguay and Peru.

It should be pointed out, however, that despite the existing agreements, significant differences of opinion remain among the WTO countries, and even among the developed countries themselves, with respect to the most appropriate type of protection for intellectual property consisting of plants, animals and processes used to produce them. Thus, for example, the European countries that have signed the International Convention for the Protection of New Varieties of Plants do not recognize patents on plant varieties. To remedy this situation, the TRIPs Agreement recognizes the right of countries to exclude plants and animals other than microorganisms and biological processes for the production of plants or animals from the patent regime. Be this as it may, the countries should take the necessary steps to protect plant species, whether through patents, new varieties of plants or a combination of the two.

V. Policies to facilitate changes in production and technological patterns

As noted in chapter 4, an essential component of national strategies in an era of globalization is an active strategy designed to create, expand and maintain systemic competitiveness. To that end, the strategy must link together the development of technological capabilities, support for changing production patterns, development of production chains and the building of quality infrastructure.

Table 7.6
WIPO: PLANT PATENT APPLICATIONS AND AWARDS

WIPO: Plant patents

	Applications			Patent awards			Countries/groups
Year	**Residents**	**Non-Residents**	**Total**	**Residents**	**Non-Residents**	**Total**	
1994	120	260	380	104	108	212	Latin America (Argentina and Chile)
	507	247	754	484	223	707	United States
	678	279	957	336	83	419	Japan
	3,003	2,532	5,535	2,348	2,341	4,804	European Union
1995	154	110	264	62	99	161	Latin America (Argentina, Chile, Uruguay)
	232	220	452	201	186	387	United States
	766	213	979	507	91	598	Japan
	2,258	1,163	3,241	2,081	1,855	3,936	European Union
1996	105	664	749	72	50	122	Latin America (Argentina, Chile, Colombia, Ecuador, Uruguay)
	677	374	1,051	362	192	554	United States
	736	203	939	426	51	477	Japan
	2,089	816	2,905	1,859	1,366	3,448	European Union
1997	183	307	490	108	253	361	Latin America (Argentina, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru)
	609	412	1,021	397	184	581	United States
	818	236	1,054	559	159	718	Japan
	2,062	638	2,700	1,793	639	2,432	European Union
1998	139	491	630	87	371	458	Latin America (Argentina, Chile, Colombia, Ecuador, Mexico, Paraguay, Uruguay)
	7	4	11	9	14	23	United States
	793	241	1,034	869	148	1,017	Japan
	2,001	606	2,607	1,611	565	2,176	European Union
1999	219	338	557	140	235	375	Latin America (Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru)
	829	472	1,293	399	228	627	United States
	649	118	767	456	148	604	Japan
	1,899	622	2,521	1,263	511	1,774	European Union

Source: César Morales, “Situación y Perspectives de los DPI sobre la biotecnología y transgénicos”, document presented at the seminar “Genetically modified organisms: their impact on Latin American agriculture” (Termas de Cauquenes, 20-22 November), 2001, on the basis of the United States Patent and Trademark Office (USPTO).

This section examines some criteria that could be used to guide the first component of this strategy. In view of the importance of ICTs for the integration of firms and individuals into global production networks, special consideration is given to policies designed to encourage the adoption, use and development of such technologies. At the same time, in view of the growing importance of the protection of intellectual property rights in global institutionality, possible ways to reconcile these rules with local technological development are analysed.

1. Reinforcing innovation systems: active strategies and policies

When national innovation systems are the core environment in which enterprises acquire and develop their technological capabilities, their strength, density and dynamism are necessary conditions for technology development and dissemination, continued increases in productivity and the maintenance of international competitiveness. Consequently, the reinforcement of national innovation systems has become one of the main objectives of systemic competitiveness policies.

Both the public sector and private enterprise must play key roles in strengthening national innovation systems. Producers of goods and services must necessarily deepen their commitment to the development of new technologies by financing and carrying out R&D activities downstream from basic and applied research phases. It is the job of the public sector, however, to ensure adequate levels of basic research. The public sector's efforts should be seen as complementary to research carried out meanwhile by the private sector and as providing an environment for the generation of externalities in this regard. The State must promote, guide and coordinate innovative activities and the formation of linkages among the scientific and technological apparatus of universities, development banks, public and private R&D laboratories, and the production sector. To that end it must operate as a central agent that selects and prepares technological projects that will be of interest to the private sector only once the initial uncertainty and problems of inappropriability of benefits have been resolved through government intervention.

Market imperfections in the innovation system, appear to be stronger and more pervasive than those of technologically advanced countries. Public policy should include measures and programmes, formulated in partnership with the private sector, to resolve market failures in the long-term financing of innovative projects, accumulation of technological capabilities, access to technological knowledge and business management and the training of skilled human resources. At the same time, public policy should contrive the means to encourage the development of institutions, synergies and strategic complementarities within the production system.

On the other hand, given their importance, efforts to strengthen the externalities, complementarities and synergies of innovation systems should be an integral part of the competitiveness and technological development strategy rather than being confined to isolated programmes. Linking horizontal, sectoral and regional innovation policies with competitiveness policies, based on this strategic vision, should be the job of a specialized agency recognized as such within the institutional order.

A reasonable mix of horizontality and selectivity should be part of public policy in this area. This mix could be achieved through generic incentives to spending on innovation activities by private firms, such as tax deductions or preferential funding of R&D, and specific incentives, such as co-financing or subsidies for technological projects, risk-sharing programmes for designing new technologies, systems of open competition for R&D tax incentives or bids for developing sectoral technological programmes. Existing synergies and complementarities in each society and in each national scientific and technological apparatus can be taken advantage for these purposes, but a focused effort should also be made to create dynamic comparative advantages in sectors that are complementary to the current pattern of production specialization. The contemporary trend towards marketing complex products that include everything from the good or service itself to post-sales consumer relations opens up a wide range of possibilities for enriching the mix of export products, increasing national value added and incorporating local engineering effects.

Just as important as having world-class technologies in export sectors and moving towards more abundant and sophisticated regional and national production chains in fields of national excellence, or encouraging the development of dynamic comparative advantages by creating new products and production processes, is the objective of boosting the average productivity of the economy, which in Latin America and the Caribbean lags far behind developed countries' levels. The digitalization of production processes and a rapid and appropriate transition to the era of computerized production processes now appears to be an urgent task in order for the region to take advantage of the new window of opportunity offered by the world of ICTs. This is also true of biotechnologies, which can contribute to a rational and environmentally sustainable exploitation of the natural resources that underlie a substantial portion of the comparative advantages enjoyed by many of the countries in the region today.

This strategy should explicitly include the role to be played by transnational corporations (TNCs). In Latin America and the Caribbean, policies in this area have been focused simply on attracting foreign investment, without using any selectivity criteria or means of channeling it in accordance with national development priorities. Frequently, in fact, it has been seen more as a source of external financing than a means of enhancing competitiveness. Not all TNCs, however, have had the same impact on growth and technological development. There are not many cases among the countries of the region in which foreign investment policies have been integrated with a development strategy based on clearly established objectives. This contrasts with notable examples of such strategies at the global level, including those of Ireland and Singapore. In the absence of such strategies, TNCs tend to prioritize a country's static comparative advantages.

Part of the collective effort to develop technological capabilities to serve as a basis for sustained systemic competitiveness consists of significantly increasing expenditure on R&D and on technology diffusion and creating incentives for private spending in this area. There is a sharp contrast between the industrialized countries and Latin American nations in terms of the priority assigned to R&D. As a proportion of GDP, the former allocate nearly five times as much as the latter to creating new technological knowledge. This lag is a cause for concern and should gradually be corrected. The need is even clearer in view of the support systems used by the developed countries to encourage the creation of new technology-based enterprises.

In addition to increasing total R&D expenditure, the public sector should specifically provide incentives for basic disciplines associated with the sustainable exploitation of the region's natural resources. Fields such as molecular biology and biotechnology, animal and plant genetics, marine sciences, mineralogy and climatology should be given priority in this respect and should be regarded as an indispensable complement to the current pattern of productive specialization in the region.

2. Policies to speed up progress in ICTs

Some developing countries have based their ICT strategies on building a competitive industry for producing computer hardware and telephone facilities. Although this strategy yields a fast-growth economic activity and enhances technological capabilities, it does not necessarily speed up the transition to the digital age. In any case, as the Organisation for Economic Co-operation and Development (OECD) has pointed out, "The key to benefiting from ICT is to focus on policies to foster its use, rather than its production" (OECD, 2001b).

The Latin American and Caribbean countries should follow strategies aimed at using ICTs as facilitators of a broad-ranging process of economic development and systemic competitiveness. The digitalization of production is aimed at boosting productivity, mainly through cutting costs and opening up larger market niches to permit economies of scale. This involves an institutional reorganization process, which helps to bring business practices into the digital era. With the incorporation of ICTs into existing industries, competitive advantages are achieved; this is where the gap in ICT use becomes a central issue.

In contrast to more highly developed economies, digitalization in Latin America is not yet a decisive factor in competitiveness. This is mainly due to the lack of scale. Digitalization is not an individual process. Network models only make sense if they have a critical mass of participants, since the more members a network has, the greater the benefits of joining it. Once a critical mass is reached, network externalities accelerate the process of adaptation, thereby generating a herd effect that forces those who have been left behind to either digitize or withdraw from the market.[4]

It is necessary to apply the "joint requirements" principle in order to speed up the transition. To this end, special attention must be given to creating an awareness of digital opportunities, strengthening human resource skills, obtaining financing, adapting the regulatory environment and, certainly, facilitating access to the Internet (Hilbert, 2001).

The rapid changes in ICTs and the paradigm that is taking shape are shifting the challenges and opportunities for developing countries. The appearance and features of the Internet —as we know it today— are continuing to change at the same headlong pace that marked its initial development. The general trend is towards a convergence of all different types of ICTs into what amounts to a network of networks. The gradual integration of data services in the mobile telephony industry (2G and 3G), together with the advances in the Voice over Internet Protocol (VoIP) and the trend towards digital television or the use of digital powerline communications networking, are early and very promising attempts in the region. The convergence of ICTs is shaping a new type of Internet, which complements the functionality of the "digital nervous system" (Gates, 1999).

But the field in which the region really needs to catch up is in the widespread diffusion of digital practices, which will require a drastic reorganization of the use of human resources. The region is still very much behind in terms of the use and integration of digital practices in economic processes. Fiscal incentives could be useful in this area, together with direct State measures to encourage connectivity, in order to accelerate diffusion rates.

On the other hand, the transition to the digital era should not be thought of solely as a phenomenon related to the production of goods. The potential benefits of the digital era in areas such as e-health, e-education or e-government are immense; digitalizing education and access to pedagogic messages and content in schools (Schnettler, 2001), the dissemination of practices used in the diagnosis and treatment of illness, the expansion of distance education for medical and paramedical personnel (Rodríguez, 2001) and linking governments with their citizens (Orrego, 2001), appear among others, to be fields with inmense future possibilities.

To encourage greater equity in the transition to the information society, measures of various types will be required, both to provide affordable telecommunications services and heighten participation in computerized networks, and to promote access to computer infrastructure. Emphasis must be placed on ensuring universal access, which means, first of all, preventing the emergence of new forms of economic and social exclusion (the "domestic digital divide"), but also speeding up progress towards the critical mass necessary to make the digital organization of production profitable. The concept of digitalization is not limited to the Internet. Less costly solutions to provide alternative access must be found so that the masses of Latin America and the Caribbean can become connected. One policy that embodies this goal, which has already been implemented in a

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4 Network externalities arise for a product when the utility derived by a user from the consumption of a good increases with the number of other agents that consume the same good (Arthur, 1989).

number of countries in the region, involves setting up Internet terminals in schools, community centers and public places.

A factor of particular importance for productive development, systemic competitiveness and job creation is for small and medium-sized enterprises to be sufficiently incorporated into the digital era so that they can participate in internationally competitive networks. As yet there are very few programmes to promote the mass use of computers in the management of small enterprises and the use of the Internet in their technological and commercial management Such programmes could operate through specialized associative networks that would give small and medium-sized enterprises access to information on technology, technical services, credit and markets and make available the tools that have been created to help them in these areas (ECLAC, 2000a, vol. 3, chapter 3).

In addition, in order to ensure the legal security of electronic transactions and generate a greater volume of business through this channel, the legal framework for the protection of such transactions and the consumers who acquire goods and services by this means must be improved.

Lastly, ICTs are a particularly appropriate field for regional cooperation, in particular through the creation of joint mechanisms for developing, consolidating and marketing high-technology products and services (such as software and distance learning) together with region-wide networks. Progress in some of these areas has been blocked by the total absence of regional standards and regulations to support the integration of telecommunications services. This situation is reflected, for example, in the diversity of technologies and standards used in the mobile telephony industry, which are hampering the physical integration of systems and cost reductions associated with the expansion of the regional market. These tasks should therefore be priority lines of action for regional integration processes in the immediate future.

3. Policies on intellectual property rights

The countries of the region should develop their policies in two basic directions (Abarza and Katz, 2002): first, towards *the valuation of national and regional capabilities and assets.* Just as the industrialized countries had clear objectives at the time they negotiated the TRIPs Agreement, the Latin American and Caribbean countries should set clear targets in this area and design a strategy to meet them. Until now, they have simply acted in the expectation of gaining easier access to FDI and developed-country markets, but they have disregarded the possibility of developing their own resources. A priority task with respect to the development of substantive rights is therefore for these countries to take stock and become aware of the importance of the intellectual, genetic and cultural assets they must defend and to determine possible ways of conserving and protecting them.

The second direction is the *renegotiation of the principles and purposes of the TRIPs Agreement.* In this context, it should be clearly understood that respect for intellectual property rights must be compatible with meeting the basic needs of the entire population and with minimal standards of equity in the international diffusion of technical progress that will facilitate the technological upgrading of developing countries. This means, among other things, finding ways to safeguard opportunities for developing technological improvements through reverse engineering and "learning by doing".

It is important to grasp, moreover, that the two legal elements that protect intellectual property in a country —that is, international treaties on the one hand, and the national patent and trademark law, on the other— do not necessarily use the same interpretations or provisions with regard to what can be patented, the duration of patent rights, the principle of territoriality on which patents are issued, the question as to whether or not imports of the patented product are protected, the rules governing the expiration of a patent for "lack of use", compulsory licensing if the patent is not being used, the treatment of nationals or foreigners, and the significance of what has come to be called “exhaustion of patent rights” (Abarza and Katz, 2002). In other words, conflicts between these two juridical elements have always existed, and it is up to each nation’s judiciary system to decide how to deal with this issue. This clearly gives a considerable degree of freedom to developing countries in establishing and promoting their technology policies.

A number of possible areas of adjustment or normative development should be mentioned (see also the discussion of this topic in chapter 4 of this book). One of them derives from the statement by the WTO ad hoc group that was set up in response to the recent conflict between Canada and the European Union. On the basis of the principles and purposes of articles 7 and 8, this ad hoc group recognized that some adjustments need to be made to the first paragraph of article 28, which sets forth the rights conferred upon a patent holder, and has thereby opened the way for a new round of negotiations on these issues. The same ad hoc group has also noted that one of the possible exceptions under article 30 of the TRIPs Agreement would make it possible to use a patented product to conduct scientific experiments during the period covered by the patent, even without the consent of the patent holder. This statement is based on the fact that the purpose of patent legislation is also to facilitate the spread and advance of scientific knowledge rather than solely to protect the patent holder.

The topic of the exhaustion of patent rights opens up a promising opportunity for developing countries. National and regional policy makers in Latin America should re-evaluate, on the basis of sufficient knowledge and information, the most effective or available means for promoting the local development of technology, selecting new plant or animal species, etc. Both reverse engineering and licensing can provide possibilities for local firms to develop their own technologies in the future. This should be sufficient grounds for claiming the exhaustion of a patent in those cases where the development of local technological capabilities could be hindered by the use of foreign patents for the sole purpose of marketing and importing high-technology goods.

Compulsory licensing clearly represents another way in which TRIPs should be made more flexible, as demonstrated by the recent international debate surrounding the pharmaceutical industry.

It seems reasonable to have intellectual property legislation to protect the works of the human intellect. This system should, however, meet three additional requirements: (a) it should grant differential treatment to intellectual property in respect of merit goods such as health, education and basic nutrition; (b) it should provide the less developed countries with effective mechanisms to protect their intellectual, genetic and cultural assets; and (c) it should promote technological development and learning in the developing countries.

Chapter 8

International migration and globalization

In previous eras, population movements have taken place side by side with the development of contacts and flows between different societies and cultures. In particular, large human migrations played a fundamental role during the first phase of globalization, which took place between the late nineteenth and early twentieth centuries. In this respect, the present situation is paradoxical, because in a world which is more interconnected than ever, in which financial and trade flows have been liberalized, the mobility of persons runs up against severe barriers which restrict it (see in this respect chapter 2 of this book).[1] As Tapinos and Delaunay (2000) point out, international migration currently seems to be excluded from the new globalization process. This exclusion is the biggest difference between the new trends in the world economy and the two great previous periods of globalization. This narrow view of "globalization", leaving out the human mobility factor, raises a threefold question of ethics, political realism and economic efficacy, as well as the question of the long-term sustainability of this type of world development strategy (p. 48).

[1] Ignoring the contribution made by migration all over the world to the intensification of relations in the fields of economic activities and labour, social and political links and cultural affairs and values, the present discussions of globalization "rarely consider international migration at all, or if they do they deal with it as a residual category, an afterthought" (Stalker, 2000, p. 1).

The difficulties placed in the way of migration just at a time when real-time exchanges are being promoted —to which end barriers impeding the free circulation of goods and ideas are being demolished— reveal the asymmetrical aspects of a form of globalization which includes some individuals, population groups, countries and regions but at the same time excludes others (Castells, 1999). Although the number of migrants has always been small compared with the world population, at other times in the past —such as that of the boom in trade which accompanied the first phase of globalization— it nevertheless represented a much larger proportion than the present level of 3%. Clear signs of the limited nature of the present degree of globalization of migration —compared with financial globalization— are that free movement of persons between countries is limited almost exclusively to one region of the world (the European Union) and is the subject of debates and case-by-case negotiations on international agreements aimed at permitting only temporary movements of persons with qualifications directly connected with business or the provision of services.

The fact that most migrants move in spite of the persistent barriers to their entry shows up the incompatibility between the restrictive approaches adopted and a world which is advancing towards growing liberalization of other flows. It is this inconsistency which is largely responsible for the big increase in the number of migrants without official papers and the emergence of migrant transit areas, as well as providing fertile ground for one of the most serious crimes against human rights: the trafficking of persons across frontiers. The increase in such situations highlights the need to promote broader agreements among countries to secure better governance of international migration, to recognize the fundamental role of civil society in formulating measures regarding human migrations, and to foster full respect for the rights of migrants.

In recent decades Latin America and the Caribbean has become a source of outward migration to the most varied destinations. At the present moment, one out of every ten of the 150 million international migrants (IOM/United Nations, 2000) was born in a Latin American or Caribbean country, and this is a minimum figure, for it takes no account of the number of persons who migrate (and work) in an irregular capacity, without official papers, and nor does it include temporary, circular or return migrations. The available information indicates that nearly 20 million Latin Americans and Caribbean are living outside their country of birth, and half of them emigrated during the 1990s, especially to the United States, though during the same decade new migration flows to Europe emerged which are on a smaller scale but are registering unprecedented growth rates. The intraregional migration which accompanied the different stages in the development of the Latin American and Caribbean countries in the past still retains some of its traditional features, but it is now on a smaller scale, due partly to the decline in the attractiveness of the main countries of destination (Argentina and Venezuela).

Analyses show that there is an enormous gap between what is generally imagined and what is really the case as regards the magnitude and consequences of immigration. Although sounder and more general evidence is still needed, that which exists is very different from the simple opinions which emphasize the negative repercussions of migration and only serve to heighten prejudices and increase the feeling of rejection against some immigrants. One example of how great this gap is may be found in a study commissioned by the United States Congress from a broad group of specialists (Smith and Edmonston, 1997). Leaving aside the inherent complexity of the wide range of factors involved, this study concludes that the existing evidence shows that immigration has had a relatively minor impact on the wage and job opportunities of the competing local groups ….. Immigration affects above all the well-being of the immigrants themselves ….. (p. 11). In reality, the “condemnation” that popular opinion applies to immigrants has no backing in scientific knowledge (Mármora, 2001). Only very rarely has it been shown that immigrants adversely affect working conditions —this would only appear to be the case in a context favouring illegality— and social services. Why, then, are prejudices persisting and even sometimes getting worse? The answer to this question calls for profound reflection on aspects going beyond the ambit of migrtion itself.

I. The interactive nature of migration and globalization

1. Factors which promote mobility and heterogeneity

The complexity of the present international migration of persons from Latin America and the Caribbean is due to the great diversity of factors which stimulate and characterize it. It is no longer sufficient merely to identify countries as sources or recipients, since it is also necessary to consider those which, because of their geographical position, have become areas of transit towards a final destination, and there has also been a big increase in the number of such destinations. Furthermore, migration is no longer limited to such a clearly identifiable human group as in the past: the range of the types of persons involved —whose migration affects the social reproduction of their families and the development of their communities of origin— is increasingly broad, and in their places of final destination they establish links with diverse social groups, build up networks of contacts which stretch across national borders, and use different strategies and means for their movements.

The basic determinants of international migration lie in the inequalities which exist in levels of development, and the enormous magnitude, persistence and flagrancy of those inequalities in the globalized world of today heighten the so-called pressures for migration (UNFPA, 1998). Thus, in recent decades the Latin American and Caribbean countries have registered an unstable economic performance, and the modest recovery glimpsed in some of them during the 1990s has barely been sufficient to reverse the serious consequences of the "lost decade" of the 1980s (ECLAC, 2001a). The very uneven distribution of the benefits offered by the international economy is very evident in the region, whether in terms of the shortcomings in human capital and knowledge, the changes in the role of the State in the social field or, more generally, the structural insufficiencies of development. At the same time, the precarious nature of employment and the heightening of social tensions have given rise to a generalized feeling of social vulnerability in the region; in view of the widespread perception of insecurity, risks and defenselessness —reflected in public opinion surveys widely disseminated by the mass media—, emigration is being increasingly seen as an option for coping with difficult living conditions, an uncertain employment outlook, and dissatisfaction with the results of the prevailing development pattern. In the final analysis, the reduction of social disparities and convergence of economic conditions are fundamental for reducing the incentives for migration in the long term; meanwhile, the countries of the region will have to live with international migration, facing up to its many consequences, but also taking advantage of the opportunities it offers.

The developed economies have always needed workers from less developed countries. This demand, which is sometimes beyond the immediate influence of business cycles, operates through the establishment of dual labour markets which offer opportunities for the employment of foreign workers at both extremes of the range of skills.[2] In theory, to the extent that the inflow of foreign workers helps to fill the gaps in the domestic supply of labour, migration can be a means of adjustment in the recipient countries, but it can also operate as a factor to keep down wage increases and drive up capital surpluses, and this is basically why local workers are against large-scale immigration.

It is well known that the immigrants with the lowest levels of skills enter the labour markets to occupy jobs that are usually scorned by the local population (in sectors such as primary industries, agriculture or personal services, for example). Through the possibility of reducing labour costs, some employers obtain benefits from such migrant flows. At the same time, the foreign workers may build up social capital and attain upward occupational mobility. Although there is a demand for these workers and many of them carry out activities which are vital for the

[2] Although less consistent, this situation is also observed in the Latin American and Caribbean countries which receive immigrants.

expansion of the economy, they are generally subject to strict regulations on migration —for example, through annual quotas or temporary hiring programmes— and in a number of cases these represent barriers to their entry and permanent residence; this causes some migrants to work without the necessary official papers, thus heightening the negative perception of immigration which often exists in the recipient countries.

The migration of skilled workers has other features. Although it is not a new phenomenon, the growing demand in the developed countries for foreign workers with specific skills means that the barriers impeding their mobility need to be reviewed. Those with high qualifications are in a better position to take an active part in such mobility, as reflected in the General Agreement on Trade in Services (GATS), which, among the ways of providing services, includes their provision by natural persons, with emphasis on the temporary movement of skilled personnel.[3] Although this Agreement provides for quantitative restrictions and additional requirements (such as a work permit), which are a source of controversy in its application —since they involve the consideration of each case separately— the basic idea is that such movements are complementary to trade and allow the developing countries to increase their participation in world trade, which could help in the long run to reduce the incentives for migration (Iredale, 2001; UNFPA, 1998). The developed countries naturally make deliberate efforts to attract scarce specialists —in some cases this forms part of their human resources policies— and these efforts are welcomed in many segments of the societies of origin of the migrants.[4] Particularly striking is the increase in the demand by those countries for immigrants with increasingly specialized skills —such as those connected with engineering and technology in the general field of information processing— which causes them to offer conditions that cannot be matched by the nations of our region.

At the beginning of the 1990s, some 300,000 Latin American and Caribbean professionals and technicians —some 3% of the total number existing in the region— were living in countries other than those of their birth; over two-thirds of that total were concentrated in the United States (Villa and Martínez, 2000), where it is estimated that 12% of all persons with a degree in science or engineering are foreigners, mostly from developing countries (Pellegrino, 2000). The outflow of such human resources has given rise to very serious discussions in the region, because their importance cannot be measured only in quantitative terms. The traditional debate on the brain drain, which stresses its negative repercussions —since it is a factor which helps to widen gaps, undermines the formation of critical masses, and affects income distribution—, is now combined with proposals designed to stimulate the circulation and exchange of highly skilled human resources ("brain circulation" and "brain exchange"), with the aim of making migrants into links between the local and global scientific and technological development networks and agents for the transfer of knowledge and technology (Pellegrino, 2000). From the point of view of the countries of origin, these proposals seek to take advantage of the opportunities opened up by globalization, but their practical application is hindered by the labour flexibilization practices of the big corporations, the retention of the most outstanding students in the universities of the developed world, the enormous disparity between the working conditions and salaries offered by the two types of countries, and the absence of suitable environments for the reinsertion of former migrants.[5]

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3 Under this Agreement, the United States grants a minimum of 65,000 visas for professionals each year, valid for up to three years (IOM-United Nations, 2000); the system of preferences in the United States legislation provides for the admittance of up to 140,000 persons with special qualifications each year (INS, 2000).

4 The big corporations play a fundamental role in this process: for example, a few years ago Bill Gates reacted to a possible reduction in the number of visas for highly skilled workers by saying that if the idea was to prevent firms like his from working in the United States, then such a measure would be "masterly" (Stalker, 2000, p. 135).

5 Analysis of the figures for temporary admittance of migrants in the United States indicates that persons from Latin America and the Caribbean —unlike those from Europe or Asia— are not yet participating on a large scale in the arrangements for the circulation of professionals and technicians (Pellegrino, 2000).

The growing opportunities for individuals abroad are all too obvious compared with the very limited capacity of the developing countries to retain their most highly qualified personnel. However, these opportunities do not always become a reality: many skilled migrants do not succeed in maximizing their benefits because of difficulties in securing official recognition of their qualifications, and in addition to the requirements and limitations on free mobility they face obstacles in finding a suitable place in their countries of destination (such as rules giving priority to local personnel), so that their potential contributions are reduced (ECLAC, 2000g; Iredale, 1998; UNFPA, 1998). In some recipient countries, there is a debate on whether the increase in the immigration of professionals and technicians is a factor tending to depress wages among the most highly qualified groups in the labour force: an association of events which was observed in the 1990s among scientists and engineers in the United States (Espenshade and others, 2001). Although these circumstances bring in a note of caution with regard to the prospects of forming a global market of skilled human resources, they do not detract from the role that these migrants can play in the transfer of technology, and their importance should serve as an incentive to seek best practices —active policies— through which the source countries to make better use of their potential. Some of the integration processes in the region are instructive in this respect, since they envisage measures to facilitate the mobility of professionals[6] and the joint formulation of postgraduate programmes. Thus, the creation of employment opportunities —together with permanent training— for highly skilled workers is a priority task on the regional agenda.

2. Migrant culture and the formation of transnational communities

International migration has always aided in cultural exchanges and —notwithstanding the challenges raised when individuals, groups and communities of different cultures, ethnic groups and religions live together— it is reasonable to expect that it will continue to forge multicultural spaces and spread ideas and values. Globalization involves opposing movements, however: expectations of mobility become widespread, but the restrictions on movement become tighter all the time. The new technologies in the fields of communications and transport facilitate international mobility, and moreover, thanks to better schooling, together with more information on the situation in other countries —with messages on standards of living and codes of values which heighten the perception of the supposed advantages of migration— there are now many more persons interested in migrating. In the final analysis, the *right to migrate* is an option for all those with a minimum of human capital who are not able to materialize their aspirations to social mobility in their countries of origin, whose restrictions on the exercise of economic and social rights end up by undermining the *right to stay*. Thus, international movements of persons and families —in search of something that their own countries only offer them symbolically— are based on increasingly informed decisions, accompanied by the perception that such moves involve decreasing risks and costs. This is the current attitude to migration, the motives for which are now relatively independent of purely economic considerations.

One of the cultural manifestations of globalization is the transition from territorially-based national identities to others which are perhaps less comprehensive but are of a trans-territorial nature. Migration has led to the emergence of new actors who, organized in communities and linked together through networks, maintain close links with their areas of origin (to which they send remittances and information) and represent collective referents of identity in the areas of destination (Portes, 1997a). These transnational communities[7] are a clear example of the interactive

[6] The Andean Community has lengthy experience in instruments for the protection of workers, and there are initiatives under way in MERCOSUR for following up the labour markets and formulating common workers' protection laws (Martínez, 2000).

[7] This transnational status is associated both with the exchanges between migrants and their areas of origin and their continual crossing of political and cultural frontiers (Canales and Zlolniski, 2000).

role of international migration and globalization within the context of the explosion of identity marking the fragmentation of societies today (Castells, 1999, vol. II). Social networks and communities form part of an affirmative strategy of migrants in defence of their cultural features, the expression of their demands for citizenship, and protection both from restrictive attitudes to immigration and practices of social rejection (as exemplified in the working conditions of many migrants and anti-immigration feelings). To a large extent, they act as feedback factors promoting migration flows and further the diversification of human mobility.

The transnational communities benefit from the traditional associations of migrants, but they are more complex than these: they promote cultural events —dances, dinners, festivities and typical products— and they legitimize the diversity of the recipient societies. They are geographically extended social units, with close relations and supportive links, and even sponsor transnational micro-entrepreneurial initiatives (Portes, 1997a and 1997b). They often function with tensions, conflicts and contradictions that recreate the context of structural inequality of their communities of origin, and thereby serve as a matrix for the social reproduction of their members in their destination countries (Canales and Zlolniski, 2000).[8] The heterogeneity of their members, the potential of some of them for resistance and opposition, their different forms of organization, their international links and their complex relations with the market and the State make these transnational communities a mandatory element of reference of indisputable importance for the design of measures to deal with the question of migration. Their interactive relation with globalization is particularly evident in the case of Latin American and Caribbean immigrants in the United States.

3. Persistence of barriers and institutional difficulties which restrict mobility

The restrictive logic underlying the measures applied by many governments with regard to international migration is based on their responsibility for safeguarding national sovereignty, which justifies institutional controls over the entry and continuing presence of foreigners. The extension of this logic to the rules on migration is not in keeping, however, with the international nature of this phenomenon or the factors which stimulate it, both in the countries of origin and those of destination. Entrusting migration policy to the police agencies responsible for guarding the frontiers is undoubtedly an unsuitable option for dealing with a phenomenon of such economic, social and cultural complexity. The result is the aggravation of restrictive practices which are not in line with most governments' declarations on migration[9] and are in contradiction with what is happening with international trade. Thus, States have agreed to eliminate many barriers to the movement of capital and goods and services, without prejudice to negotiations on specific matters, provided that the procedures followed do not run counter to the rules laid down in the global agreements. In the case of international migration, however, such general frameworks do not exist, although the challenges raised by this phenomenon have led States to acknowledge that unilateral action is not enough. How, then, can general agreements be reached on migration, over and above the provisions governing mobility in the field of business and the supply of services which are included in some international instruments?

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8 Their members may have homes in different places, which gives rise to travel circuits that combine variable stays and travel frequencies within clearly transnational living spaces.

9 The Eighth United Nations Inquiry among Governments on Population and Development (1999) shows an increase in the number of governments (28% of the total number of respondents) which consider that the level of immigration is too high; many of them reported that they have control policies (especially in respect of persons without official documentation, refugees and asylum-seekers). Of the governments of Latin America and the Caribbean, 62% said that they had no official position on immigration levels but 15% declared that the level of immigration was too high and 18% said they wanted to reduce it (United Nations, 2001b).

In principle —leaving aside other polemical objectives— strict regulation of migration is usually seen as a means of protecting national labour markets. Only exceptionally, however, do foreigners come to account for a major fraction of the labour force of a country; they are usually only a modest proportion of the total and occupy positions left unoccupied by local workers, so that they rarely displace the latter. It is possible, however, that their participation in the labour market may help to depress wages in their destination country. The probability that this will occur is greater when there is a substantial presence of migrant workers without official papers, who, since they are outside the trade unions and collective bargaining mechanisms, may help to produce a decline in real wages. This has led to allegations that the employment of foreigners without official papers at lower wages than those of local workers will undermine the existing collective agreements, foster the replacement of local workers with foreigners in some sectors, and weaken their contribution to national income (Abella, 2000).

Although the migration policies of most countries continue to be adopted on the basis of their own unilateral criteria, there were some signs in the 1990s of support for regional-level initiatives in this field. In line with this new spirit, it was explicitly recognized at the Symposium on International Migration in the Americas that "international migration is a multi-faceted phenomenon which involves all countries and which calls for international dialogue and cooperation, but that this should in no way impinge upon national sovereignty in establishing the necessary legal and political instruments to deal with international migration" (ECLAC, 2000g, p. 7). This recognition, which does not deny each country's right to regulate immigration, is a promising sign of the gradual adoption of more flexible common principles in the Americas. In order to deal with the many issues involved in international migration it is necessary to move beyond official normative approaches of an essentially restrictive nature, which extend to much of public opinion and feed prejudices on this phenomenon; this means promoting a progressively more flexible approach which facilitates migratory movements and protects the population groups involved.

The task of making the rules on migration more flexible is particularly feasible at the intraregional level (especially in border areas), since restrictions on the flow of foreign workers should begin to slacken as integration processes gain greater depth and it is recognized that migratory exchanges provide a complementary labour component in strategic sectors. It is precisely within the traditional restrictive context that the questions of undocumented migration, "illegal" workers and unfair competition in the labour market become manifest (Mármora, 1997). The opportunity provided by the subregional integration agreements for advancing in these areas must be seized in a decided and systematic manner, recognizing the multisectoral nature of the issues involved in international migration and adopting policies guided by the pursuit of convergence. The restrictive logic, which means closing the door to the possibility of settling in a country other than one's country of origin, leads to serious tensions: many migrants not only find it difficult to exercise their right to live in their country of birth but also to settle in another country or return to their country of origin.[10]

4. Global forces and the future of migration

International migration is a historically important process which forms an indissoluble part of human evolution. In the past, in response to changes in economic, social and political circumstances, it has aided in the expansion of trade and the economy, helped to create new nations and territories, fostered urbanization, opened up new spaces for production, and made decisive

[10] The 1999 United Nations Inquiry shows that most of the governments of the region do not have an official position or policies on emigration (United Nations, 2001b). Although this dilemma has not given rise to much discussion in the region (public initiatives designed to keep emigrants in touch with developments in their countries are weak or non-existent), lately governments have begun to display greater awareness of the important role played by communities of their citizens abroad.

contributions to social and cultural change. In the second half of the nineteenth century and the first decades of the twentieth, the world witnessed a type of migration fundamentally consisting of two opposite flows: the voluntary migration of Europeans, which played a key role in the economic convergence of some regions of the Old and New World, and another flow involving the (often forced) migration of workers of varying origins, but mostly Asians (coolies), to tropical regions, which resulted in the further expansion of the inequality of the international order. These flows, which were promoted by different forces, were readily accepted by the destination countries. Nowadays, however, there is concern over some conflictive aspects of migration affecting not only the countries of origin and destination but also the migrants themselves (such as the risk of heightening inequalities and the risks associated with undocumented status).

Everything seems to indicate that, at least in the short and medium term, migration will continue to be stimulated, in a highly interconnected world in which the profound international economic disparities and the acute structural shortcomings of the developing countries will become increasingly visible. In addition, the developed countries, with their ageing populations, will strengthen their strategies designed to attract skilled human resources and will keep up their demand for less-skilled workers, the new contingents of which cannot easily be absorbed by the labour markets of the developing countries, although in some of the latter the labour supply will gradually diminish as a result of demographic transition processes. In this context, the further spread of values and information, typical of a migrant culture which reasserts the legitimacy of the right to emigrate, together with the consolidation of organized actors in this field, will make it easier to take the decision to migrate.

From a strictly economic standpoint, experience shows that the change of countries from being sources of migrants to recipients of them will only take place in a small number of cases; the developing countries which have made this transition have done so by taking advantage of their low labour and manufacturing costs and exporting labour-intensive products (Richelle, 1998). Most of the developing countries, however, will suffer the disruptive effects associated with development processes and will increase their outward flows of migrants in the short term, especially when better wage levels continue to be the exception rather than the rule in those countries. The strategies of the developed nations and the big corporations aimed at increasing their competitiveness may erode the stock of skilled human resources in the developing countries, thus further widening the economic gaps. In view of this prospect, it would be worth investigating the repercussions that the relocation of production activities could have on employment in the developing countries; transfers of services would appear to be the most promising developments in this respect, and this option could be strengthened in the subregional integration processes, provided that wage differences do not increase still further and the member countries of the agreements make effective progress in assuming the commitments required for deeper integration.

II. International migration patterns of the Latin American and Caribbean population

In the information on the international migration of persons from Latin America and the Caribbean, two main patterns may be identified: emigration to destinations outside the region, and exchanges among countries of the region itself. A third pattern is that corresponding to the traditional immigration from abroad (mainly from Europe), which registered high but variable rates between the second half of the nineteenth century and the years following the Second World War; in recent decades, however, the region has ceased to be so attractive for Europeans and the stock of such immigrants, which has aged through lack of renovation and gone down through death and the return of former immigrants to Europe, went down from some 4 million persons in 1970 to less than 2.5 million in 1990. In recent decades, emigration to destinations outside the region has been the main migration pattern of Latin America and the Caribbean, its most distinctive feature being the marked preference for emigration to the United States, although, on a smaller scale, there has also been an increase in the number of migrants from Latin America and the Caribbean in European countries (such as Spain and Italy), Australia and Japan.

1. Emigration to the United States

The traditional emigration of Mexicans and citizens of Caribbean countries to the United States has been accompanied in recent decades by that of Central and South Americans, reflecting the serious structural limitations many countries have in retaining their population. In addition to the greater incentives to emigrate, this increase has also been due to the greater ease of emigrating as a result of the consolidation of communities of migrants in the recipient countries. After registering a big increase in the 1970s, the stock of Latin American and Caribbean immigrants in the United States as of 1990 stood at 8.4 million persons (Villa and Martínez, 2000). The figures from the 2000 Current Population Survey —although not strictly comparable with the 1990 census data— indicate that there was strong growth in the 1990s too, since the stock came close to 15 million persons, representing over half of the total number of immigrants in the United States (Lollock, 2001; Schmidley and Gibson, 1999). Because of these tendencies, which took place in a context of constant revisions and amendments to the United States rules and policies on migration with the aim of controlling undocumented migration and the illegal trafficking of persons, migration from Latin America and the Caribbean is seen as a very important social phenomenon for the United States, thus fuelling the debate on its repercussions and making it a leading issue in that country's relations with the nations of the region.

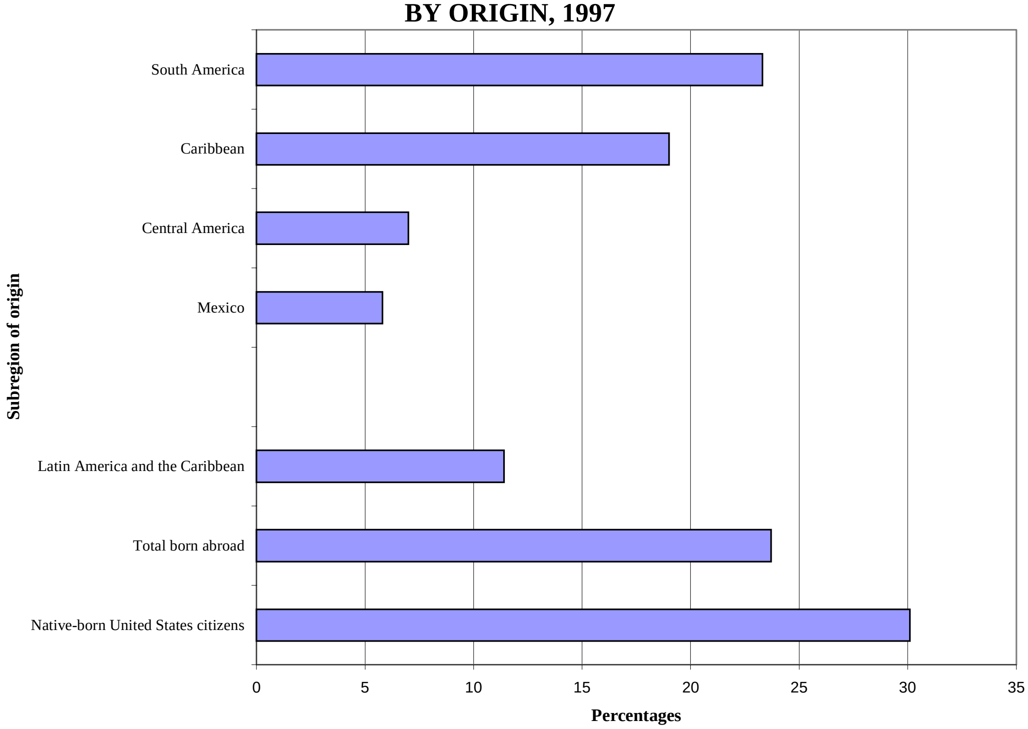
It is in this context that the "new bilateralism" between Mexico and the United States is being designed. From the point of view of Mexico, the regularization of the migratory situation of its undocumented nationals, the increase in admission quotas, the establishment of programmes for temporary workers and the introduction of common border control arrangements are priority issues in the negotiations which were resumed early in 2002. In the words of President Vicente Fox: "Mexico and the United States have agreed that they need to agree … emigration is not simply a problem that must be solved, but also an opportunity that must be taken" (*El Mundo*, 5 September 2001). For the United States, these negotiations are a fundamental step towards their aim of securing "orderly" immigration and combating the trafficking of persons; they also have to do with the importance of the population who identify themselves as "Latino" or "Hispanic" and who, according to the United States census of the year 2000, amount to 35.3 million persons (including both immigrants and citizens): that is to say, 13% of the population of the United States and the largest ethnic minority in the country (Grieco and Cassidy, 2001).

The Latin American and Caribbean immigrants to the United States form a heterogeneous group of varying origins and socio-demographic and socio-economic characteristics. With their total of over 7 million in 1997, Mexicans are a clear majority in the total stock; although they are numerous, no other contingent of natives of the Caribbean (mainly Cubans and Dominicans) or of Central America (especially Salvadorians) amounts to over one million persons. The Mexican immigrants are equivalent to 7% of the population of Mexico, the Cubans and Dominicans amount to almost 8% of their respective populations of origin, and the Salvadorians are equivalent to over 10% of their country's population (Schmidley and Gibson, 1999).

Taken as a whole, a majority of Latin American and Caribbean immigrants in the United States are males: a feature which is highly influenced by the high proportion of Mexicans, which, together with the Central American contingents, among which family groups are common, also influences the socio-economic composition of the immigrants, which is marked by a high proportion of persons with relatively low skill levels. Among the South American and Caribbean immigrants, there is a higher proportion of persons with mid- or high-level qualifications, although this proportion is still below the average for the native-born population of the United States (Villa and Martínez, 2000) (see figure 8.1).

Figure 8.1

UNITED STATES: PERCENTAGE OF PROFESSIONALS IN THE LABOUR FORCE, BY ORIGIN, 1997



Source: A. Schmidley and C. Gibson, "Profile of the Foreign-Born Population in the United States, 1997", *Current Population Reports*, series P23-195, Washington, D.C., United States Bureau of the Census, 1999 (http://www.census.gov).

The occupational breakdown of Latin American and Caribbean immigrants in the United States also varies according to their origin (see table 8.1). Among Mexican workers, a substantial proportion work in agriculture, although the majority (54.4%) are employed in industry, retail trade and construction. Central American immigrants are spread over the various branches of industry, retail trade and services (especially personal services). South Americans are mostly in industry, but a substantial proportion of them work in professional services. The employment profile of Caribbean immigrants comes closer to that of native-born Americans, since almost a quarter of them are in the professional services sector.

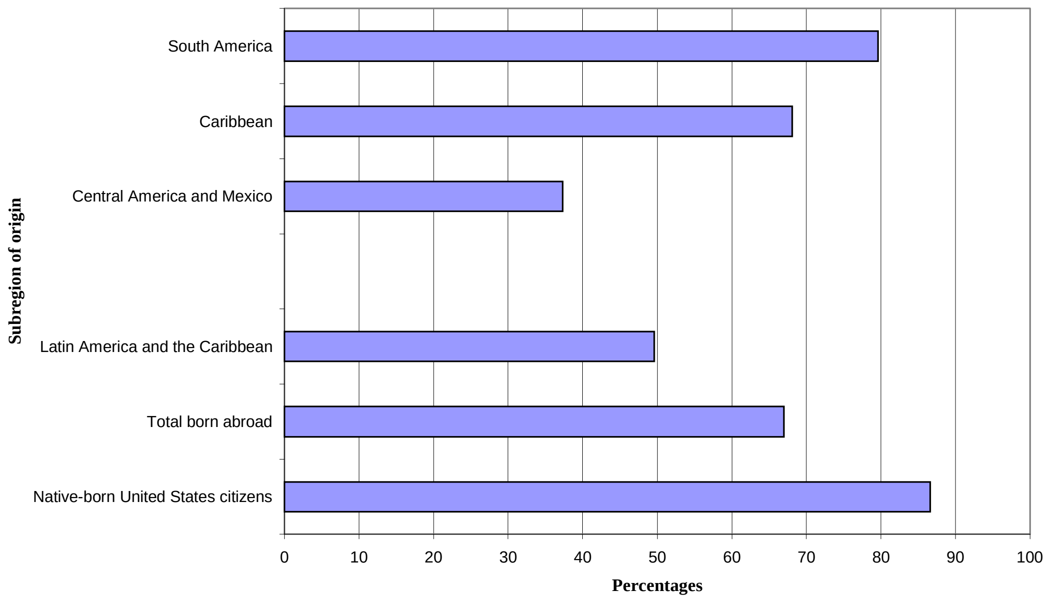
Table 8.1
UNITED STATES: DISTRIBUTION OF THE ECONOMICALLY ACTIVE POPULATION, BOTH NATIVE-BORN AND BORN IN LATIN AMERICA AND THE CARIBBEAN, BY BRANCHES OF ACTIVITY. DATA TAKEN FROM THE 1990 CENSUS
(Thousands)

			Others, by origin							
Branches of activity	**United States Native-born**	**%**	**Mexico**	**%**	**Central America**	**%**	**South America**	**%**	**Caribbean**	**%**
Agriculture	2,694	2.6	312	12.9	16	2.6	4	0.8	13	1.2
Mining	695	0.7	11	0.5	1	0.2	1	0.2	1	0.1
Construction	6,534	6.2	252	10.4	52	8.6	26	5.4	61	5.4
Manufacturing	18,242	17.4	642	26.5	127	21.0	104	21.5	181	16.1
Transport	4,695	4.5	59	2.4	21	3.5	27	5.6	67	6.0
Comunications	2,944	2.8	22	0.9	6	1.0	6	1.2	23	2.0
Wholesale trade	4,592	4.4	120	5.0	26	4.3	23	4.8	52	4.6
Retail trade	17,561	16.7	425	17.5	114	18.8	81	16.7	163	14.5
Finance	7,332	7.0	50	2.1	28	4.6	32	6.6	95	8.5
Small commercial establishments and repair shops	4,970	4.7	139	5.7	55	9.1	40	8.3	71	6.3
Personal services	4,545	4.3	176	7.3	76	12.6	45	9.3	84	7.5
Professional services	24,925	23.7	189	7.8	75	12.4	86	17.8	278	24.8
Public administration	5,287	5.0	25	1.0	8	1.3	9	1.9	34	3.0
Total	**105,016**	**100.0**	**2,422**	**100.0**	**605**	**100.0**	**484**	**100.0**	**1,123**	**100.0**

Source: S. Lapham, *The Foreign-Born Population in the United States. 1990 Census of Population*, Washington, D.C., United States Department of Commerce, 1993 and *Persons of Hispanic Origin in the United States. 1990 Census of Population*, Washington, D.C., United States Department of Commerce, 1993.

The average level of education of Latin American and Caribbean immigrants taken as a whole is lower than that of immigrants from other parts of the world or of the native-born United States population, but the heterogeneity of their educational level is no less than that observed in respect of their other socio-economic characteristics. Thus, taking the percentage of the population aged 25 or older who have completed their secondary education, the difference between South Americans and the native-born United States population is drastically reduced, as also in the case of the discrepancies between Caribbean immigrants and those from other regions (see figure 8.2). In the final analysis, the image of immigrants from the region, taken as a whole, is affected by the high proportion of Mexicans and Central Americans, whose level of education is relatively low. The most significant aspect, however, is that the educational profile of immigrants is associated with their polarization in the field of employment: those with the highest qualifications enter the most dynamic sectors of production or research and academic fields, whereas those with less schooling work in activities that require a low level of qualifications. The fact that the latter are in the majority is linked with the high incidence of poverty among immigrants from Latin America and the Caribbean (Lollock, 2001). Even so, however, immigrants generally have a higher educational level than that of their populations of origin, which shows the selective nature of the migration process. Furthermore, the number of skilled immigrants is very large compared with the supply of human resources of similar educational level in their countries of origin, which backs up the assertions of those who highlight the negative effects of the emigration of such people (Pellegrino, 2000).

Figure 8.2
UNITED STATES: PERCENTAGE OF POPULATION AGED 25 OR MORE WITH AT LEAST FULL HIGH SCHOOL EDUCATION, BY ORIGIN, 2000



Source: L. Lollock, "The Foreign-Born Population in the United States. Population Characteristics", Washington, D.C., United States Bureau of the Census, 2001 (http://www.census.gov).

A further aspect of immigration to the United States concerns the dynamics of admissions (i.e., officially documented immigration). The corresponding data reveal that in the last three decades persons from the region represented over 40% of the total number of all immigrants admitted, and this proportion even exceeded 50% in the first half of the 1990s (see table 8.2). In line with the figures on the total stock of immigrants, Mexicans occupy the first place among admissions of persons from the region, followed by persons from the Caribbean (mostly Dominicans, Cubans, Jamaicans and Haitians), while in the 1980s Salvadorians also occupied a noteworthy place (see table 8.3).

Table 8.2
UNITED STATES: TOTAL NUMBER OF IMMIGRANTS ADMITTED, AND TOTAL COMING FROM LATIN AMERICA AND THE CARIBBEAN, 1971-1998
(Thousands)

Period	Total	Latin America and the Caribbean	Percentage of total
1971-1980	4,493	1,813	40.4
1981-1990	7,338	3,458	47.1
1991-1994	4,510	2,341	51.9
1995-1998	3,095	1,278	41.3

Source: United States Immigration and Naturalization Service (INS), *1998 Statistical Yearbook of the Immigration and Naturalization Service*, Washington, D.C., United States Department of Justice, 2000.

Table 8.3

UNITED STATES: IMMIGRANTS ADMITTED FROM SELECTED COUNTRIES OF LATIN AMERICA AND THE CARIBBEAN, 1971-1998

(Thousands)

Country of origin	Period			
	1971-1980	1981-1990	1991-1994	1995-1998
Mexico	640	1656	1400	531
Caribbean	741	872	437	385
Cuba	265	145	48	89
Dominican Republic	148	252	180	120
Haiti	56	138	81	60
Jamaica	138	208	72	67
Other Caribbean countries	134	129	56	49
Central America	135	469	267	156
El Salvador	35	214	117	62
Other Central American countries	100	255	150	94
South America	297	461	237	206
Argentina	30	27	14	9
Colombia	78	123	54	50
Ecuador	50	56	31	29
Other South American countries	139	255	138	118
Total, whole region	**1,813**	**3,458**	**2,341**	**1,278**

Source: United States Immigration and Naturalization Service (INS), *1998 Statistical Yearbook of the Immigration and Naturalization Service*, Washington, D.C., United States Department of Justice, 2000.

What are the main reasons why immigration to the United States is allowed? According to that country's rules on migration, most admissions are granted on family grounds (kinship with United States citizens and family reunification), which suggests that the decision to migrate is not always due directly to reasons of employment (see table 8.4).

Table 8.4

UNITED STATES: IMMIGRANTS ADMITTED FROM LATIN AMERICA AND THE CARIBBEAN, BY SUBREGION OF ORIGIN AND ADMISSION CLASS, 1998

Subregion of origin	Total	Admission class				
		Kinship with United States citizens	Family reunification	Employment	Refuge and asylum	Other
Mexico	131,575	71,731	55,140	3,586	41	1,077
Central America	35,679	20,814	9,470	4,048	843	504
Caribbean	75,521	31,665	24,908	2,361	15,480	1,107
South America	45,394	26,765	11,116	5,706	712	1,095
Total, whole region	**288,169**	**150,975**	**100,634**	**15,701**	**17,076**	**3,783**

Source: United States Immigration and Naturalization Service (INS), *1998 Statistical Yearbook of the Immigration and Naturalization Service*, Washington, D.C., United States Department of Justice, 2000.

2. Emigration to other destinations

The information on emigration from Latin America and the Caribbean to destinations outside the region other than the United States is incomplete and suffers from problems of comparability in both concepts and time; even so, the total stock of such emigrants in the year 2000 may be estimated at a little over 2 million persons (see table 8.5). The search for destinations other than those traditionally used began to take on greater importance in the 1970s and 1980s, when the overthrow of democratic regimes in many countries and the profound economic crisis of the "lost decade" increased the propensity to migrate. In the 1990s, the shortcomings of labour markets and the incipient support networks for migration led to the maintenance (or even the intensification) of some migration flows established in previous decades. Apart from the impulse given by these factors, migration was also boosted by the return of former emigrants from abroad and the return of those who obtained recognition of their right to citizenship of the countries of origin of their parents and ancestors (Villa and Martínez, 2001).

Table 8.5

LATIN AMERICAN AND CARIBBEAN IMMIGRANTS IN EUROPE AND IN OTHER COUNTRIES FOR WHICH INFORMATION IS AVAILABLE, AROUND THE YEAR 2000

(Thousands)

Country where present	Total
Austria a/	2
Belgium	5
Denmark	1
France a/	42
Germany	88
Italy	116
Netherlands	158
Norway	15
Portugal	26
Spain	150
Sweden	20
United Kingdom b/	500
Total Europe	1,123
Australia	75
Canada	553
Israel	78
Japan	285
Total, all countries with available information	**2,114**

Source: CELADE IMILA Project.

a/ Figure corresponds to 1990.
b/ Thomas-Hope (2000).

In Canada, the stock of immigrants from the region —which was extremely small up to the 1960s— rose from a little over 320,000 persons in 1986 to nearly 555,000 in 1996. The traditional flow of immigrants from the Caribbean (mainly from Jamaica, Guyana, Trinidad and Tobago and Haiti), which accounted for half of that stock, has been supplemented in recent decades with an inflow of immigrants from Central America (mainly Salvadorians), whose rapid growth was reflected in a total of almost 70,000 persons in 1996.

Various European countries have received immigrants from Latin America and the Caribbean, the main concentrations being observed in the old colonial metropolitan countries (the United Kingdom, the Netherlands and Spain) and Italy. There was a very heavy inflow of Caribbean immigrants into the United Kingdom from its former colonies from the end of the Second World War up to 1962, when that country decided to put an end to its policy of free admission for citizens of the Caribbean Commonwealth; although the inflow of such immigrants still amounted to 625,000 persons in 1980, the number had gone down to less than 500,000 by 1991 (data from the OPCS, censuses and labour force surveys, cited by Thomas-Hope, 2000). Two thirds of the almost 150,000 immigrants from the region registered in the Netherlands in the year 2000 came from the Netherlands Antilles (www.statline.cbs.nl). In contrast, Spain mostly receives natives of Latin American countries, and it may be estimated from the data of the regularization campaign for migrants recently carried out in that country that the stock of Latin American immigrants, which amounted to 50,000 persons in 1981 (Palazón, 1996), had increased to 150,000 by the year 2000 (www.mir.es), the bulk of that total being made up of Ecuadorians (29,000), Peruvians (28,000), Dominicans (27,000) and Colombians (25,000). Latin Americans also predominated among the 116,000 immigrants from the region present in Italy in the year 2000, with Peruvians (33,000), Brazilians (19,000) and Ecuadorians (10,000) making up the largest groups (www.istat.it).

The stock of Latin American and Caribbean immigrants in Australia amounts to rather more than 70,000 persons, among whom Chileans predominate (www.immi.gov.au). The stock of such immigrants in Israel is of similar size, the majority of them from Argentina (www.cbs.gov.il). Finally, according to information from the Immigration Office of the Ministry of Justice of Japan, in the year 2000 over 300,000 non-native residents in that country were Latin Americans (http://jim.jcic.or.jap/stat/stats/21MIG22.html); the fact that 80% of these were Brazilians and another 14% Peruvians suggests that most of these persons (born in Brazil and Peru) are descendants of Japanese immigrants (*nisei*) who arrived in those countries in the early decades of the twentieth century.

3. Intraregional migration

Migration among the countries of the region has deep historical roots and is associated both with labour market factors and factors of a conjunctural nature (including local socio-political conflicts). This migration pattern registered a marked increase in the 1970s, when the number of migrants doubled, reaching almost two million persons, but in the 1980s, because of the economic crisis, it slackened, as reflected in the modest increase in the stock of migrants to only 2.2 million (Villa and Martínez, 2000). Almost two thirds of these migrants were concentrated in Argentina and Venezuela (see table 8.6): countries which have registered a marked decline in immigration and, recently, an increase in emigration to countries outside the region.

Argentina, whose stock of intraregional immigrants came to rather more than 800,000 persons in 1990 (equivalent to almost 3% of the country's population), is the traditional destination for migrants from neighbouring countries, who mostly work in agriculture, industry, construction and services. Under the stimulus of the petroleum boom of the 1970s, Venezuela received large numbers of immigrants from Colombia, as well as persons from the Southern Cone who had been forced to leave their countries, and by 1990 it had 660,000 immigrants from inside the region (3.4% of the national population). In Central America, the socio-political upsets of the 1970s and 1980s, together with structural shortcomings in development, gave rise to a considerable increase in the stock of immigrants (mainly Nicaraguans and Salvadorians) in Costa Rica, where the total stock came to 300,000 persons in 2000 (8% of the country's population) (INEC, 2001). In the 1970s and 1980s, Mexico received substantial immigration from Guatemala and El Salvador and also became established as a transit zone for migrants on the way north. Something similar —with smaller figures but even greater economic, social and cultural effects— occurred in the case of Belize. Various other Central American countries also act as transit zones for migrants from South American countries and other regions.

Table 8.6

LATIN AMERICA: NUMBER OF PERSONS BORN ABROAD, BY REGION OF ORIGIN AND COUNTRY WHERE PRESENT, AROUND 1990

(Thousands)

Country where present	Year	Region of origin					
		Latin America	%	Rest of world	%	Total	%
Argentina	1991	807	50.2	799	49.8	1,606	100.0
Bolivia	1992	46	24.7	140	75.3	186	100.0
Brazil	1991	115	15.0	652	85.0	767	100.0
Chile	1992	66	57.9	48	42.1	114	100.0
Colombia	1993	67	62.6	40	37.4	107	100.0
Costa Rica		…		…			
Cuba		…		…			
Dominican Republic	1993	…		…			
Ecuador	1990	53	69.7	23	30.3	76	100.0
El Salvador	1992	19	73.1	7	26.9	26	100.0
Guatemala	1994	31	75.6	10	24.4	41	100.0
Haiti		…		…			
Honduras	1988	30	88.2	4	11.8	34	100.0
Mexico	1990	85	24.9	256	75.1	341	100.0
Nicaragua	1995	20	76.9	6	23.1	26	
Panama	1990	38	61.3	24	38.7	62	100.0
Paraguay	1992	166	88.8	21	11.2	187	100.0
Peru	1993	23	43.4	30	56.6	53	100.0
Uruguay	1995	46	53.5	40	46.5	86	100.0
Venezuela	1990	660	64.5	364	35.5	1 024	100.0
Total		**2,272**	**48.0**	**2,464**	**52.0**	**4,736**	**100.0**

Source: CELADE, IMILA Project.

Note: The information available from the 2000 censuses gives a proportion of 16% of immigrants from the region (out of a total of 520,000 persons) in Mexico and a proportion of 63% (out of a total of 82,000 persons) in Panama.

There is intensive circulation of persons in the Caribbean: apart from the already long-standing migration from Haiti to the Dominican Republic, the expansion of tourism activities in a number of island countries has generated employment opportunities which encourage territorial mobility. In 1990, over half of the Caribbean immigrants came from that same subregion, and the proportion was even greater in the case of Trinidad and Tobago, the United States Virgin Islands and Barbados (see table 8.7). The effect of this intra-Caribbean migration has a marked effect on the populations of origin, since in Grenada and Saint Vincent and the Grenadines between one sixth and one fifth of the population have emigrated elsewhere in the region. An important aspect of migration in the Caribbean is the return of former emigrants, which has multiple socio-economic repercussions, such as the transfer of savings (including retirement pensions), investment in local social welfare projects, and the organization of activities involving high skill levels (Thomas-Hope, 2000).

Table 8.7
CARIBBEAN: NUMBER OF PERSONS BORN ABROAD, BY REGION OF ORIGIN AND COUNTRY WHERE PRESENT, AROUND 1990
(Thousands)

Country where present	Year	Region of origin					
		Caribbean	%	Rest of world	%	Total	%
Antigua and Barbuda	1991	8.3	67.5	4.0	32.5	12.3	100.0
Bahamas	1990	4.0	15.0	22.6	85.0	26.6	100.0
Barbados	1990	12.9	60.3	8.5	39.7	21.4	100.0
British Virgin Islands	1991	5.8	71.6	2.3	28.4	8.1	100.0
Dominica	1991	0.9	33.3	1.8	66.7	2.7	100.0
Grenada	1991	2.8	62.2	1.7	37.8	4.5	100.0
Guyana	1990	1.0	27.0	2.7	73.0	3.7	100.0
Jamaica	1990	3.3	11.5	25.3	88.5	28.6	100.0
Montserrat	1991	1.4	66.7	0.7	33.3	2.1	100.0
Saint Kitts and Nevis	1991	1.6	48.5	1.7	51.5	3.3	100.0
Saint Lucia	1991	3.0	53.6	2.6	46.4	5.6	100.0
Saint Vincent and the Grenadines	1991	2.7	64.3	1.5	35.7	4.2	100.0
Trinidad and Tobago	1990	37.1	73.8	13.2	26.2	50.3	100.0
United States Virgin Islands	1990	23.3	70.8	9.6	29.2	32.9	100.0
Total		**108.1**	**52.4**	**98.2**	**47.6**	**206.3**	**100.0**

Source: F. Mills, 1990-1991 *Population and Housing Census of the Commonwealth Caribbean*. Regional Monograph, *Intraregional and Extraregional Mobility, the New Caribbean Migration*, Trinidad and Tobago, Caribbean Community (CARICOM), 1997.

One of the features of intraregional migration is the growing proportion of women and highly qualified persons. Although the flows display considerable heterogeneity, this "feminization" of migration is due both to the possibilities offered by the labour markets and to considerations of family reunification, while the increased migration of highly qualified persons, for its part, although due to the unequal employment conditions between countries, also helps to improve the profile of intraregional migration (Villa and Martínez, 2000). Another feature of intraregional migration which has been becoming more marked with time is the increase in forms of temporary migration for varying periods which do not involve moving house; this expansion of "living spaces" is associated with subregional integration initiatives, greater economic openness and the territorial restructuring of the economies of the region (see box 8.1).

Box 8.1

CHANGES IN THE MOBILITY OF PERSONS IN ONE AREA OF MERCOSUR

Interaction between the metropolitan area of Buenos Aires and Uruguay has always been favoured by geographical, economic and cultural proximity, so Buenos Aires has a substantial concentration of Uruguayan immigrants. What details are available on other forms of mobility as components of this interaction? The information on the movement of persons —all types of movements, without distinguishing length of stay— provides some valid clues for the formulation of hypotheses on what happens with respect to the movement of persons in an integration area. Thus, movements to and from Uruguay (mainly Montevideo) represent some 40% of the total entries and exits of persons in the Buenos Aires metropolitan area. The persons in question stated that the reasons for their journeys were visits to friends and relatives, the use of services and commerce, and work connected with business and government activities, and many of them said they travelled very frequently. Among those going to Uruguay —mostly from Buenos Aires— by far the main reason given for their travel was summer tourism, followed to a much smaller extent by business matters (commerce, meetings, services).

This information gives grounds for formulating the hypothesis that traditional migratory movements, involving a change in the habitual place of residence of the persons in question, is only a part of the intense mobility observed. Leaving aside tourism —which follows long-established circuits— the novel feature is that some of the reasons for travelling given by frequent travellers are the same as those associated with traditional migration, which suggests that there has been an expansion of living spaces and that there is a close association with the functioning of social, business and institutional networks operating in both territories which extend across national borders and mainly involve highly qualified workers. How far these new forms of mobility are encouraged by formal integration processes and how far they simply represent the continuation of existing dynamics are open questions; what is clear is that, with increasingly low transport costs, these movements allow some persons to attain objectives which could previously only be achieved through traditional migration.

Source: Rodolfo Bertoncello, "Migración, movilidad e integración: desplazamientos poblacionales entre el Área Metropolitana de Buenos Aires y Uruguay", document presented at the Third International Colloquium on Geo Crítica, Migración y Cambio Social (Barcelona, Spain, 28-31 May), 2001 (www.ub.es/geocrit).

III. Potential and problems of migration

1. Remittances

Monetary transfers by emigrants to their countries of origin form a close link between migration and development. Although there is no doubt that these remittances are an important source of foreign exchange, factors such as the varying forms of the transfers (family or collective), the channels of transmission (formal or informal), the costs of transmission and the ways the money is used (consumption, saving or investment) make it difficult to evaluate their actual and potential impact on the development of the recipient communities. Because of the informal nature of many transfers —an unknown proportion travel in the pockets of emigrants, relatives or friends— the central banks are unable to estimate their amount accurately. Even so, it is calculated that in the region they totalled over US$ 17 billion in the year 2000 (see table 8.8). Mexico, with almost US$ 7 billion, is the main recipient in the region and the second largest recipient in the world, after India; although their incidence in the national economy is relatively low (1.1% of GDP), remittances nevertheless bring in more money than that generated by most export branches. Their impact is much greater on the economies of El Salvador, Nicaragua, the Dominican Republic, Ecuador and Jamaica (where they represent between 8% and 14% of the GDP of those countries and, in the case of El Salvador, are equivalent to 48% of the value of total exports). The amounts remitted to Brazil, Colombia and Peru are also considerable, although their impact on GDP is small

(0.2%, 1.3% and 1.3% respectively). In the 1990s there was rapid growth in the amount of remittances, especially in Nicaragua, Ecuador, Peru and Honduras.

Table 8.8

LATIN AMERICA AND THE CARIBBEAN: MAIN COUNTRIES RECEIVING REMITTANCES, 1990 AND 2000 a/

	Millons of dollars		**Average annual variation**	**% of GDP**		**% of exports**	
	1990	**2000**	**1990-2000 (%)**	**1990**	**2000**	**1990**	**2000**
Latin America and the Caribbean	**4,766**	**17,334**	**13.8**	**0.4**	**0.9**	**2.7**	**4.2**
Mexico	2,492	6,573	10.2	0.9	1.1	5.1	3.6
El Salvador	357	1,751	17.2	7.9	13.6	36.7	47.8
Dominican Republic	315	1,689	18.3	4.5	8.5	17.2	18.8
Colombia	488	1,118	8.6	1.2	1.3	5.6	7.2
Brazil	527	1,113	7.8	0.1	0.2	1.5	1.7
Ecuador	50	1,084b/	36.0	0.5	8.0	1.5	18.7
Jamaica	136	789	19.2	3.2	10.8	6.1	23.3c/
Cuba	…	720	…	…	2.5	…	15.0
Peru	87	718	23.5	0.2	1.3	2.1	8.4
Guatemala	107	563	18.1	1.4	3.0	6.8	14.9
Honduras	50	410	23.4	1.6	6.9	4.8	16.3
Nicaragua	10d/	320	41.4	0.9	13.4	2.6	34.0
Other	147	487	12.7	0.1	0.1	0.2	0.4

Source: ECLAC, on the basis of figures from the International Monetary Fund (IMF), *Balance of Payments Statistics. 2001 Yearbook*, Washington, D.C., 2001; Cuba: estimates by the country.

a/ Only the inflows of remittances declared by the country in question are taken into account.
b/ Figure for 1999.
c/ Figure for 1998.
d/ Figure for 1992.

A report by the Inter-American Development Bank states that on average Latin American and Caribbean migrants send their families US$ 250 between eight and ten times a year (IDB, 2001), which highlights the great saving effort made by many emigrants. This is particularly so in the case of Central American migrants: although the kind of employment they obtain in their countries of destination only provides them with quite low incomes, they nevertheless give substantial support to their families, a high proportion of which are living in poverty;[11] according to surveys made by ECLAC, over 80% of the family remittances received in El Salvador, Guatemala and Nicaragua are used to buy food (ECLAC, 1993 and 2000b). The counterpart to this is that the personal and social costs of emigration are reflected in numerous cases of broken families and children left in the care of relatives or friends.

The use of remittances for productive purposes is restricted by the fact that the recipient families do not have many options for forgoing their use for consumption; furthermore, interest rates on the bank accounts of small savers are usually negative, and the lack of credit and technical assistance programmes inhibits the development of business skills; thus, a large part of the family businesses set up with remittances are tiny businesses for the sale of food, tailors' shops or retail trade. Many micro-enterprises run by returning emigrants or their families have very limited horizons and register high rates of failure. Some of the most enterprising emigrants set up

11 According to the household survey carried out in Honduras in 1997, 83% of the households receiving remittances were below the poverty line and 58% were indigent (Perdomo, 1999).

prosperous businesses in the United States or other countries of destination, but only rarely do they establish production or trade links with their countries of origin, for example in order to import "nostalgic" or "idiosyncratic" goods (local foods or handicraft goods). Other emigrants, especially those of retirement age who intend to return to their homeland, acquire land, animals and agricultural implements there. Generally speaking, there are few examples of successful promotion of the productive use of remittances through public policies.

The potential of family remittances is expanded through those generated by migrants' organizations; although these resources are much smaller than those of family transfers, they serve to finance social and community infrastructure works such as the construction of sanitary, educational, sporting and religious installations, the provision of basic services, and road construction (Alarcón (no date); Orozco, 2000). Although the productive links between emigrants' organizations and their communities are still only incipient, there are promising examples in Mexico (see box 8.2), while the National Competitiveness Programme of El Salvador proposes, through the establishment of bank branches and national credit unions in the United States, to strengthen financial links with emigrants and offer tax incentives to Salvadorian investors who live outside the country.

Box 8.2

GOVERNMENT PROGRAMMES IN MEXICO IN SUPPORT OF COLLECTIVE REMITTANCES

There are many associations of Latin American and Caribbean migrants in the United States; in 1998, for example, Mexicans had 170 clubs in Los Angeles and 120 in Chicago. These associations very often send collective remittances to their places of origin, mainly for social infrastructure works. One example of a government programme which seeks to complement these contributions is the *Tres por Uno* ("Three for One") programme which the Mexican state of Zacatecas began to operate in 1986 and reformulated in 1996. The programme provides that for every dollar received from associations of Zacatecans abroad for community improvements, the federal, state and municipal governments will contribute a further dollar each. In 1997, one year after the programme had been reformulated, nearly 100 projects totalling some US$ 5 million were carried out in 27 municipalities. The programme promotes infrastructure and development works in rural areas and involves the community in the taking of decisions and the contribution of municipal resources, thus creating positive synergies in the investments which help to give them deeper community roots. Its success is due to the noteworthy level of organization of emigrants' clubs in the United States.

Other successful programmes are *Mi Comunidad* ("My Community"), which is connected with in-bond assembly industries in the state of Guanajuato, and the *Afinidad Jalisco Banamex* debit card, which is designed to bring down the commissions charged by electronic transfer firms. All these determined efforts to give support to emigrants, their families and their communities come under the Programme for Attention to Mexican Communities Abroad, set up in 1990 by the Ministry of Foreign Affairs, which is based on the efficacious action of Mexican consulates. Within this same field, health programmes for the families left behind by emigrants in Mexico are being carried out, as well as some production projects for micro-enterprises, in coordination with the National Solidarity Enterprise Fund.

Source: R. Alarcón, *The Development of Hometown Associations in the United States and the use of Social Remittances in Mexico*, Tijuana, El Colegio de la Frontera Norte (no date).

Little is known about the various costs that emigrants must pay in order to save the money they send to their countries of origin; in addition to those connected with the move itself and disruptions in family structures, there are others relating to working conditions, the adaptation to different cultures (starting with the need to learn another language) and, in general, the conditions of everyday life. There are also transfer costs —the combined effect of the commissions charged by specialized firms and unfavourable exchange rates— which are relatively higher the smaller the remittances are (ECLAC, 2000b). The gradual generalization of electronic transfers (instead of the postal services and informal couriers) and the growing competition in the provision of this service are helping to bring down those costs, however (Orozco, 2000).[12] Another aspect requiring greater analysis is the dependency effect that remittances have for the recipient families and communities; the size and regularity of the flows of resources are subject to fluctuations —some of them linked to the economic and social environment in the countries of origin and destination, and others to the behaviour and situation of individuals after some time has elapsed since their emigration— which can have serious repercussions on the recipients. As for promoting the productive use of remittances, there is still a wide field to explore, ranging from the provision of incentives —through measures to give technical and credit support, to reduce risks or to exempt from taxes— to the formation of associations among emigrants, recipients, communities, national and local public bodies and private agents; such measures must be considered as complementary to the countries' development efforts and must respect the decisions of the persons involved.

2. Lack of protection and vulnerability of migrants

Apart from the gravity of the trafficking of persons —a crime that countries and the international community should punish most severely— migration also involves other forms of lack of protection and vulnerability. These occur when migration is not a voluntary action but is due to compelling political or environmental reasons and exposes the migrants to the precarious status of being refugees and the complex problems of resettlement and reinsertion.[13] As these movements are due to sudden unforeseen circumstances, it is hard to make conjectures about their future evolution, but their incidence will probably go down insofar as countries advance in their democratization processes and become better prepared to cope with natural disasters. Undocumented status, due to overstaying the authorized period of presence in a country, and consequent deportation, are two common features of present-day migration (see box 8.3). Both of them may involve the violation of human rights —as for example through arbitrary arrest, extortion and abuse of authority— which is usually accompanied by discriminatory treatment of migrants on account of their origin, qualifications or ethnic background. Although irregular forms of hiring workers are very widespread because of the more flexible labour rules now current, foreigners are particularly exposed to abuses because they lack legal protection, especially in the case of undocumented migrants.

[12] Data for Mexico indicate that between 1994 and 2000 electronic transfers increased from 43% to 70% of the total number of transfers, while thanks to greater competition it has been possible to reduce transaction costs. Thus, for example, Western Union, one of the best-known agencies in this field, has reduced the cost of sending up to US$ 200 to Latin American or Caribbean countries from US$ 22 in 1999 to US$ 15 in 2001. The effects of competition are also to be seen in the reduction of the profit margins of firms providing electronic transfer services. The data for Mexico show a decline in those margins from 11.1% in 1999 to 4.1% in the year 2000.

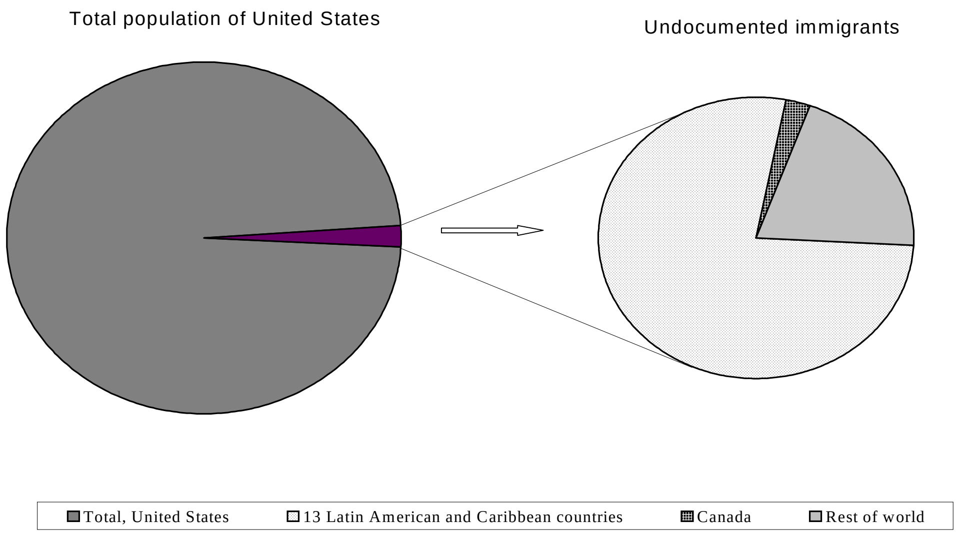
[13] According to the World Refugee Survey, 2000, there are some 14 million refugees in the world and an even larger number of displaced persons within their own countries (IOM/United Nations, 2000; Crisp, 2000).

Box. 8.3

UNITED STATES: ESTIMATES OF THE NUMBER OF PERSONS WITHOUT OFFICIAL DOCUMENTS

Using a combination of demographic and statistical procedures, it was estimated that in 1996 there were some five million undocumented immigrants in the United States; this is equivalent to almost one-fifth of the total number of foreigners present in the country. Mexicans formed 54% of this stock, followed by Salvadorians and Guatemalans (less than 10% in each case). The reason for the undocumented status of most of these immigrants was "entry without inspection"; in the case of natives of other regions, the reason was usually "nonimmigrant overstays".

MAGNITUDE OF THE PROBLEM OF UNDOCUMENTED IMMIGRANTS



Source: United States Immigration and Naturalization Service (INS), *1998 Statistical Yearbook of the Immigration and Naturalization Service*, Washington, D.C., United States Department of Justice, 2000.

The rigorous entry controls and strict supervision of length of stay adopted by many countries in order to try to reduce undocumented immigration have proved ineffective. As they take little account of the factors which lead people to migrate, they only scratch the surface of a phenomenon which has very deep roots. Experience indicates that the problem of undocumented migration is an elusive phenomenon which increases when controls over migration are made stricter: when this happens, migrants —sometimes encouraged by the demand of unscrupulous entrepreneurs for cheap labour— develop strategies for staying longer than the officially authorized time at any cost. The control measures, based on restrictive rules, ignore the potential contribution of migrants to the economic prosperity of the recipient societies, provide fertile ground for the generation of extremely negative public images of migration, and foment xenophobic and racist reactions (UNFPA, 1998), as well as having to do with the emergence and expansion of criminal organizations that manipulate the migration industry and make big money from the traffic in persons.[14]

[14] Although these organizations concentrate on migration to the developed countries, concern over their existence is shared by the countries of the region: thus, in the Declaration of Quebec City, adopted at the Third Summit of the Americas in April 2001, it is

3. Citizenship and human rights

Protection of the fundamental human rights of migrants in the countries of destination is a matter of great concern at present. Awareness of the abuses and hostile and discriminatory treatment suffered by many persons because they are foreigners (non-citizens) has given rise to intensive discussions in civil society whose content gradually seeps up to government circles. Effective recognition of the instruments on migration which form part of international law is essential in order to guide this discussion, but the reluctance of many governments to ratify those instruments prevents their principles from being incorporated into national legislation and policies.

There is an extensive range of international instruments on migrants. Under the leadership of the International Labour Organization (ILO), numerous international labour standards have been formulated, a number of which have received the approval of the international community and been incorporated in conventions and agreements on the rights of migrant workers, but in view of the marked disparity observed between the letter of the treaties and their actual application, the great challenge at present is to ensure that States obey the agreements they have signed (Perruchoud, 2000). Although some instruments probably need to be redesigned in order to adapt them to the prevailing situations, there are others whose validity is beyond doubt. Among these are the International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families, which recognizes that many migrant workers and their families are not protected by national legislation, establishes international definitions of migrant workers, and lays down rules for respecting the specific human rights of all migrants, whatever their origin or status. Since it is aimed at putting an end to exploitation and to all irregular situations in migration, its application would represent a decisive step forward towards incorporating the question of the human rights of migrants in all initiatives dealing with current international migration (see box 8.4). The Convention was adopted by the United Nations General Assembly on 18 December 1990, and in order for it to come into force it needs to be ratified by at least 20 States. Up to the beginning of 2002, this Convention had been ratified by 19 States, including six from the region (Belize, Bolivia, Colombia, Ecuador, Mexico and Uruguay), while another three countries (Chile, Guatemala and Paraguay) have signed it (www.december18.net). The large number of provisions of the Convention, which mean that it must be analysed very carefully before its ratification, and the concern of some States that its application might encourage the arrival of still more persons in irregular situations, have militated against its entry into force.

Strict adherence to the rules —and determination to follow the arduous road to ensuring their strict application— is a necessary but not of itself sufficient condition for advancing in the fulfilment of the agenda on migrants' rights. Transnationalization and the new forms of citizenship made necessary by international migration raise unprecedented challenges for the present globalization process: among other aspects, they call for recognition of the role of transnational migrant communities and promotion of the conscious intervention of civil society. In the case of the communities, their action should not be allowed to become a de facto policy for the defence of fundamental rights, since this could eliminate the incentive of the fulfilment of obligations which are the responsibility of governments, while with regard to civil society in the countries of destination, redoubled efforts should be made to educate society in the field of non-discrimination, which is a long-term task.

proposed to strengthen mechanisms for hemispheric cooperation to take effective measures against trafficking in human beings (www.summit-americas.org).

Box 8.4

THE INTERNATIONAL CONVENTION ON THE PROTECTION OF THE RIGHTS OF ALL MIGRANT WORKERS AND MEMBERS OF THEIR FAMILIES

The International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families, adopted by the United Nations General Assembly in its resolution 45/158 of 1990, reaffirms the fundamental rights of migrant workers and their families, without distinction, and offers States a uniform system of national legislation, for the effects of which both officially documented and undocumented immigrants are recognized as such workers. The rights envisaged in the Convention include:

- Freedom to leave any State, including their State of origin, and freedom to enter and remain in their State of origin (article 8);
- The right to life (article 9);
- Prohibition of being subjected to torture or to cruel, inhuman or degrading treatment or punishment (article 10);
- Prohibition of being held in slavery or servitude or being required to perform forced or compulsory labour (article 11);
- The right to freedom of thought, conscience and religion (article 12);
- Prohibition of being subjected to arbitrary or unlawful interference with his or her privacy, family, home, correspondence or other communications (article 14);
- Prohibition of being arbitrarily deprived of property (article 15);
- The right to liberty and security of person and prohibition of being subjected to arbitrary arrest or detention; in the event of their detention, they have the right to be informed at the time of arrest, as far as possible in a language they understand, of the reasons for their arrest (article 16);
- Prohibition of being subjected to measures of collective expulsion (article 22).

Special emphasis is placed on the right to equality with nationals of the State concerned before the courts and tribunals (article 18) and with regard to remuneration and other conditions of work (article 25). Such equality shall also extend to urgent medical attention (article 28) and access to education (article 30). Upon the termination of their stay in the State of employment, migrant workers and members of their families shall have the right to transfer their earnings and savings and their personal effects and belongings (article 32). The Convention also enumerates other rights of migrant workers, whether or not documented, and their families: the right to liberty of movement in the territory of the State of employment (article 39), the right to form associations and trade unions (article 40), and equality of treatment with nationals of the State concerned as regards access to housing, vocational training and social services. The Convention also seeks to prevent the entry and illegal employment of migrant workers in an irregular situation; the measures suggested include the imposition of sanctions on persons who organize illegal or clandestine movements of migrant workers and on employers of undocumented workers (article 68). States shall maintain appropriate services to deal with questions concerning migration through the formulation of relevant policies, exchange of information, the provision of information to migrant workers, and the provision of consular services (article 65).

Source: Office of the United Nations High Commissioner for Refugees (UNHCR) (http://www.unhcr.ch); R. Perruchoud, “Legal standards for the protection of migrant workers”, paper presented at the Symposium on International Migration in the Americas, San José, Costa Rica, 4-6 September 2000.

IV. Proposals for a regional agenda on international migration

The foregoing considerations provide grounds for the identification of at least three main items for a regional agenda on international migration: governance of migration, links with emigrants, and measures to prevent some of the risks associated with migration.

1. Governance of international migration

The current forms taken by mobility represent opportunities for development, but also definite risks of different kinds —such as the traffic in persons, xenophobia, problems of undocumented status, and the lack of protection for migrants— which must be addressed through an integral approach. Most countries are at once countries of destination and of origin, while a considerable number of other countries are transit zones, so that actions on migration, if they are to be realistic and efficient, cannot be limited to unilateral measures. All this explains why the governance of international migration must be tackled through dialogue and cooperation, taking a multilateral view which recognizes the complexity of the phenomenon and provides for areas of national autonomy in policy design and implementation. This is an issue which should be given the highest priority, since it seeks to enhance the benefits of migration while reducing the risks for migrants and the countries involved. While it is essential to seek mechanisms for concerted action among States, provision must also be made for the active participation of civil society, a number of whose organizations play a fundamental role in the defence of migrants. The governance of current migration is a necessity for all countries, and its bases go beyond the merely quantitative dimension, since they involve recognition of the fact that migrations are part and parcel of social, economic and individual processes and acceptance of the need to progress towards more objective and modern forms of management (Mármora, 1997).

Most of the countries of the region actively participate in intergovernmental forums on migration, which shows their political will to agree on a concerted strategy in this matter. Such forums —especially the Regional Conference on Migration and the South American Conference on Migration— form the core of a strategy of shared governance, so their consolidation can help in the establishment of mechanisms which are binding on all parties. In order to progress in this direction, various measures need to be taken, including:

- promoting the deliberate incorporation of migration and its governance into the agenda of the international community in order to reach increasingly broad agreement on this matter;
- signing and ratifying the international instruments on the protection of migrants and also taking steps to ensure that the provisions of those instruments are effectively fulfilled;
- consolidating and extending the areas of authority on migration in the various regional and subregional multilateral agreements;
- establishing explicit bilateral agreements both between Latin American and Caribbean countries and between those countries and others outside the region which are recipients of migration flows from the region.

With regard to policies on migration, globalization will make it increasingly necessary to progress from "migration control" to "migration management" in the broad sense, which does not mean that States must give up their right to regulate the entry of foreigners and their conditions of residence, but rather that they should agree to formulate reasoned admission policies (CELADE, 1995; Meissner, 1992) which cover residence, return, family reunification, restoration of links, cross-border transit and the transit of persons to third countries. A global agreement on migration policies could serve as a framework for general agreement on the international movement of persons, establishing general principles and guidelines on various aspects which require international consensus (CELADE, 1995). A global agreement of this type calls for successive rounds of negotiations and means progressing from unilateralism to international consensus. "But if the main aim of this discussion is simply how many controls and restrictions are to be added, this would be as if the rounds on international trade had been organized merely to increase the existing barriers, instead of reducing them in the light of a world which is more open and integrated for the free circulation of goods" (Mármora, 1997, p. 12). In proportion as the incipient initiatives for dialogue and cooperation on migration prosper, the present restrictions on mobility in general will gradually lose their backing and legitimacy.

Ratification of the International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families is imperative for all the governments of the region, because of its inclusive and comprehensive nature. Likewise, on the basis of the strength deriving from the commitment thus established, those governments could likewise call upon the countries which receive migration from the region to ratify that instrument as well. The Convention would thus not only technically enter into force but would also gain greater legitimacy. The next step would be to ensure its due fulfillment in every country.

Multilateral consensus initiatives include the integration blocs, intergovernmental forums on migration, and other mechanisms of a subregional nature. The integration blocs —MERCOSUR, the Andean Community, the Central American Integration System, the Central American Common Market, and the Caribbean Community— have already made substantial progress towards extending their field of operations beyond specific agreements on matters of trade and are beginning to advance in matters connected with their social agenda, which must include specific recognition of the importance of migration. In this sense, the subregional integration agreements offer opportunities that must be taken, since they represent particularly suitable spaces for dealing with migration as a vital component of partnerships between members whose asymmetries are smaller than in the case of developed countries. The main intergovernmental forums on migration are the Regional Conference on Migration —set up in 1996 by the countries of North America and Central America— and the South American Conference on Migration, which was established more recently and is made up of 11 South American countries.[15] The participants in these forums must maintain an ongoing exchange of experiences in order to gain a full understanding of the phenomenon of migration and strengthen the benefits derived from it. Action must also continue to be promoted in order to address common problems and make determined progress towards the achievement of consensuses, forms of cooperation —as for example in the areas of management and legislation— and binding commitments, with their fulfilment being evaluated in the light of each country's needs. The governments of the region must give their fullest backing to these initiatives, which should be copied by the Caribbean countries. There are also other subregional-level mechanisms (such as the Puebla-Panama Plan and the Rio Group) which emphasize concern with matters of migration; in this case links should be established with the appropriate specialized forums (the Regional Conference on Migration and the South American Conference on Migration), which can provide fundamental background information for debates and initiatives which complement their own fields of operation.

Another area of multilateral initiatives is the Summit of the Americas. In the Declaration of Quebec City, signed in April 2001 in Canada by the heads of 34 States of the Americas, the countries

[15] The Regional Conference on Migration, which brings together countries with strong emigration, immigration and transit flows, has an operational instrument (the Plan of Action) which includes joint action on matters of migration and development, human rights of migrants, and migration management; one of the most promising features of this forum is that it has opened up a dialogue with organizations of civil society. The South American initiative is in the process of institutionalization and has begun to outline a short- and medium-term programme of work.

recognize the economic and cultural contributions made by migrants to receiving societies as well as to their communities of origin and commit themselves to ensure dignified, humane treatment with appropriate legal protections, defence of human rights, and safe and healthy labour conditions for migrants, as well as to strengthen mechanisms for hemispheric cooperation to address the legitimate needs of migrants and take effective measures against trafficking in human beings. The Plan of Action includes explicit commitments on migration, human rights and equity, which the countries assume as their responsibility for the coming years. This Plan calls for the strengthening of cooperation among States to address, with a comprehensive, objective and long-term focus, the manifestations, origins and effects of migration in the region; it also provides for close cooperation among countries of origin, transit and destination in order to ensure protection of the human rights of migrants (www.summit-americas.org).[16]

The multilateral agenda of the region must include efforts to systematically address questions of migration in other processes, such as those relating to cooperation programmes between the European Union and Latin America; it is worth recalling that these programmes include six areas recognized as having close links with migration: development, the environment, democracy, regional integration, education and humanitarian aid. The Ibero-American Summit of Heads of State and Government is likewise a suitable forum for the consideration of these matters, as at its eleventh meeting (held in Lima in 2001) it not only recognized the contribution made by migrants both to their countries of origin and of destination but also declared that it is necessary to strengthen bilateral and multilateral dialogues in order to address the question of migration in an integral manner and take measures to ensure equal treatment for migrants, fully respecting their human rights and eliminating all forms of discrimination that affect their dignity and integrity (www.oei.es).

Likewise within the context of multilateral initiatives, the countries of the region must make a determined effort to secure a review of the conditions and limitations which, under the terms of the General Agreement on Trade in Services, affect the temporary movement of qualified personnel. The aim is to secure genuine, effective liberalization of labour markets by eliminating the factors that restrict such movement: the imposition of standards regarding qualifications which favour the mobility of persons among the developed countries but hamper that of nationals of developing countries is a restriction which is incompatible with the opening of markets. In this respect, the World Trade Organization could be an appropriate forum for promoting more flexible movement of qualified personnel at the global level, taking advantage of the comparative advantages which the Latin American and Caribbean countries have in various specific branches (such as construction and tourism). Within the region, a new appraisal must be made of the limitations affecting their own horizontal commitments (such as the requirement that foreigners must be registered in professional associations and their subjection to certain provisions of the laws on migration); the integration agreements are a suitable option for progressing in this respect.

Bilateral agreements cover matters of mutual interest for countries, such as cross-border transit, circulation of workers, social security, and the recognition of courses of study and professional qualifications; although the negotiation of these agreements is usually less complicated than in the case of multilateral agreements, the aspects covered are dealt with in greater depth. A recent promising example is the "new bilateralism" between Mexico and the United States, which, apart from short-term considerations, opens up a space for discussion and agreement on the measures the two countries propose to adopt. Although there are many examples of bilateral agreements in the region, many are not operational or have become out of date; redoubled efforts should therefore be

[16] Among other actions included in the Plan of Action are: establishment of an inter-American programme for the promotion and protection of the human rights of migrants, including migrant workers and their families; cooperation and exchange of information among States concerning illegal trafficking networks, including the development of preventative campaigns on the dangers and risks faced by migrants; and the establishment of linkages with subregional processes, such as the Regional Conference on Migration and the South American Conference on Migration (www.summit-americas.org).

made to renew their validity. To this end, the countries should seek to strengthen their arrangements for bilateral dialogue, following the principle of seeking policy convergence —such as the harmonization of rules and procedures— on international migration.

2. Links with emigrants

Recognition of the economic, social and cultural potential that emigrants represent for their countries and communities of origin can help countries to take due advantage of one of the externalities of migration; the strengthening of stable links with fellow-citizens and their communities abroad will increase the direct benefits of emigration. In order to do this, it is necessary to identify the most suitable types of links and develop mechanisms to make them more stable. Other initiatives that countries could consider include:

- facilitating remittances of money (with emphasis on the most successful experiences of some countries in this respect) and encouraging their use for community and productive purposes (without prejudice to the right of persons and families to use these resources as they see fit);
- using links with emigrants as a means for permitting the legitimate exercise of those persons' right to participate in the political processes of their countries of origin;
- taking advantage of the contributions that scientists, professionals and technicians who have emigrated can make to their countries of origin;
- using contacts with emigrant communities abroad to promote idiosyncratic products.

Functional regulation of remittances would make it possible to obviate the excessive commissions charged by some firms specializing in making transfers. Ways should also be sought to allow the recipients of remittances to enjoy favourable exchange rates on terms which are appropriate to their needs (as regards the monetary value of the transactions). Measures should also be taken to encourage investment by emigrants in projects of common interest (as in the case of the state of Zacatecas in Mexico, for example), micro-enterprises, and other sustainable ventures, through the provision of credit support and technical assistance.

Every effort should also be made to guarantee that citizens residing abroad can still exercise their civic rights in their country of origin.[17] The exclusively national nature of political rights is seriously open to question in view of the present intense mobility of persons, so democratic systems should guarantee the participation in electoral processes of all those who comply with the relevant requisites, without obliging them to be physically present in their country of origin. In order to dispel any prejudices that such participation could arouse, initiatives in this direction should be subject to broad discussion and should be integrated with other actions designed to deepen democratic systems: a proposal which has found support in a number of countries of the region. Furthermore, although many developed countries have progressed in their discussions on the partial political inclusion of foreigners —as part of the general granting of social and economic rights— the traditional idea that citizenship only gives political rights to the nationals of a country still predominates (Calderón, 2000). This debate must necessarily take account of the trends towards the transnationalization of the rights of the individual and fundamental values, especially those of democracy.

Links with emigrants also contain high potential for scientific and technological development, which is a matter of fundamental importance at a time when the progress of societies is linked to access to and incorporation of knowledge and information. Everything indicates that the demand for

[17] Only one country of the region has a Constitution which expressly prohibits those living abroad from voting; in all the others it is possible to vote by returning to the country to do so. Argentina, Brazil, Colombia, Honduras and Peru have legislation which permits votes to be cast from abroad.

highly qualified human resources will continue in the developed countries, so that —barring coercive measures— keeping such persons in their countries of origin will be by no means easy, as well as being a source of controversy. One alternative would be to develop and strengthen academic links, promoting communication by electronic means and temporary visits and giving determined support and encouragement to the formation of networks of researchers and shared research programmes; in addition, measures should be taken for the effective incorporation of technicians and scientists who have emigrated into national science and technology projects. The inclusion of these initiatives in national human resources training policies would help the countries of the region to cope with the losses of human capital they have suffered (which are even more difficult to tackle in the case of emigrants who work for transnational corporations) and would make it possible to take advantage of their experience without it being necessary for them to return on a permanent basis. Countries should reject the idea that the emigration of highly qualified personnel is an irreversible fact and should acknowledge, instead, that this phenomenon goes beyond purely quantitative dimensions.

Taking advantage of their organizational potential, communities of emigrants abroad could serve to introduce and spread the use of idiosyncratic national products, thus helping to form potential markets for their sale. Such products —foodstuffs and craft articles— have proved to have great acceptance in communities of Latin Americans and Caribbean nationals living in the United States.

3. Measures to prevent the risks associated with migration

The risks faced by persons who migrate to other countries in search of better opportunities or in order to rejoin their families or escape from persecution are increasingly evident, so the design of preventative measures is of fundamental importance. As a starting point, international agreements and States must recognize a basic principle: the use of police procedures should be reserved only for combating actions which really do constitute crimes, especially those committed by criminal organizations engaged in the trafficking of migrants. Although the criminal nature of such actions is beyond dispute, prosecution of them should not extend also to the victims of such traffic, and in the application of the relevant international instruments (the United Nations Convention against Transnational Organized Crime and its two protocols) a clear distinction should be made from the common minor offences of failing to possess the necessary official documents, since undocumented migrants are not criminals. Care should also be taken to ensure that punitive actions do not have adverse effects on migrant communities and networks. Another complex issue is that of deportation, which sometimes extends even to the interception of migrants in transit; in order to avoid arbitrary actions in the application of such rules, international agreements should be promoted which clearly identify the cases subject to punishment.[18]

It is well known that undocumented or irregular migration involves serious risks for the migrants in question. Although this is a matter which gives rise to great controversy, there can be no doubt that the countries of origin should develop measures of an "educational" nature designed to minimize those risks and put migrants in a stronger position to cope with the legal and social vulnerability to which they are exposed. Some efforts have already been made in this respect, such as the educational campaigns promoted by the International Organization for Migration, but these need to be put on a much larger scale in order to inform potential migrants —and the population in general— of the fact that their entry and presence in another country means assuming legal responsibilities, facing difficulties in gaining access to employment and services, and knowing that they may have to accept living conditions that are not in keeping with their traditions. This information could be provided through programmes shared by the countries of origin, transit and destination of migrants.

[18] The Regional Conference on Migration has made important progress with regard to procedures on the trafficking of migrants and deportation, which can serve as an example for other countries of the region.

The foregoing also has to do with facilities for the integration of immigrants. Although most democratic countries of the world have inclusion mechanisms —such as the right and obligation of children to go to school, or the right to family reunification— measures need to be agreed upon for ensuring the expansion of the social and economic rights of immigrants, which includes the necessity to respect the culture of their recipient country, since all countries must seek to protect their social cohesion. The establishment of mechanisms for the possible granting of full political rights for foreigners and the possible recognition of forms of dual citizenship are also matters worth analyzing, both in the societies of origin and of destination.

From a different angle, measures should also be considered to reduce the dangers associated with discrimination and xenophobia. A first step in this direction would be for States to ratify the relevant international instruments and undertake to give full rights to immigrants. In the Declaration of the World Conference against Racism, Racial Discrimination, Xenophobia and Related Intolerance, held in Durban in the year 2001, governments acknowledge that xenophobia is one of the main sources of contemporary racism and that violations of migrants' human rights are part of discriminatory and racist practices; they also reaffirm that while every country has the sovereign right to formulate and apply migration policies, these must be consistent with the rules and standards laid down in international instruments on human rights (www.unhcr.ch). Among the concrete actions associated with this objective is the development of forms of education furthering non-discrimination, which involve both the inclusion of special modules in regular school education and sensitization programmes aimed at business associations, professional associations, trade unions, departments responsible for administering migration, and persons responsible for shaping public opinion. It is important that efforts should be made in the region to review the contents of some educational programmes so as to help foster peaceful coexistence and respect for persons of other origins.

Chapter 9

Globalization and environmental sustainability

Economic globalization has multiple implications for environmental sustainability. The interactions are so numerous and so complex that it would be simplistic to affirm that the two are in conflict. Indeed, there are neither theoretical reasons nor adequate or conclusive empirical evidence to show that the relationship between globalization and environmental sustainability is unidirectional or unidimensional (ECLAC/UNEP, 2001).

One thing that is unquestionable, as the scientific evidence makes clear, is that the growing and cumulative scale of human activities has produced environmental effects of a global nature ("global public bads") that are not reflected in the markets but that affect global common interests transcending national perspectives. There has clearly been an increase in environmental interdependence and vulnerability among countries, whatever their degree of development. This gives a special character to the third phase of globalization, which took place in the last quarter of the twentieth century.

This chapter presents some of the major changes in environmental management and sustainability in the region associated with globalization, recognizing that the main channels through which globalization affects the environment are shifts in trade, investment and technology flows. It identifies the new challenges for international cooperation that stem from the recognition of this increased environmental interdependence among countries.

The new and shifting imperatives of global environmental management were brought to light by the various world summits and conferences held and the multilateral environmental agreements signed in the 1990s. These processes and agreements have had two main effects: they have prompted national governments to take a more proactive international approach to cooperation with a view to protecting and administering global public goods on the basis of innovative multilateral systems, and they have fostered greater equity in the way the responsibilities and costs of reversing environmental damage are shared out between rich and poor States.

In the 1990s, a new ethical and political framework emerged, embracing new international legal principles for the environment and development. The most relevant of these is Principle 7 of the Rio Declaration on Environment and Development regarding “common but differentiated responsibilities”, which implicitly acknowledges the environmental debt that the developed countries have accrued with the rest of the international community by submitting the environment to an array of cumulative global externalities during the industrialization process. It reflects the differences between countries as regards their historical participation in the generation of these environmental externalities and, most importantly, it provides the political basis for remedial action in which each country’s involvement is matched to its financial and technological capacities. This means that industrialized countries have to take on greater commitments than developing ones under multilateral environmental agreements.

Accordingly, the environment will be increasingly important as an issue for negotiations between Latin America and the Caribbean and the industrialized countries. The importance of the global environmental services that the region provides, such as the storage of carbon dioxide (the main generator of climate change through the greenhouse effect) in its large forests, and its enormous wealth of terrestrial and marine biodiversity, mean that the region has the potential and the opportunity to play a key role in helping to solve global problems.

I. The impact of productive restructuring on sustainable development

The environmental effects of productive and technological restructuring may be direct or indirect. The environmental implications of globalization are different from the economic ones, in both time and space. The environmental consequences are generally longer-term, with dynamic, cumulative characteristics that are difficult to measure because they are associated in some cases with qualitative parameters. Furthermore, many of these implications are not necessarily reflected in markets. Some examples of such implications are cross-border pollution, effects on global goods, effects on landscape and the loss of scenic beauty, the extinction of species and the loss of biodiversity (ECLAC/UNEP, 2001).

Direct environmental effects are generated by the use of new technologies for agriculture industry and energy, by the exploitation of hitherto untapped renewable and non-renewable natural resources, by the creation and dispersion of new biological forms and by the release of new substances into the environment. Indirect environmental effects are generated by the social, economic, political and demographic adjustments driven by the wave of new technology, which has resulted in changes in prices and demand, the social organization of work, production systems, employment, the international division of labour, services and the location and nature of human activities and settlements.

Environmental implications associated with a general redefinition of comparative advantages are difficult to anticipate, given the possibility that new and unsuspected advantages may arise and the likelihood that the factors that determine comparative advantages and their volatility will multiply (Gallopín and Chichilinsky, 2001). The decline in the raw material/output ratio, and the replacement of traditional materials by new ones as part of the new technological and economic paradigm, will affect more directly those countries that have based their capital accumulation process on their mineral or forestry resources. New technologies, and particularly biotechnology, are already affecting traditional farmers by transferring revenue and the control of production and marketing to the major transnational chemical and pharmaceutical corporations and large marketing firms. The increases in agricultural yields in the advanced countries due to the new technological development, together with agricultural subsidy policies, are reducing the edaphic and climatic comparative advantages of Latin America and the Caribbean.

A range of comparative advantages could emerge in the countries of the region, with widely varying environmental consequences. These advantages include those deriving from access to cheap energy sources, those associated with lower transport costs because of proximity to natural resources, those of location offered by lax environmental or health legislation (a perverse advantage) and those represented by the opportunity to benefit from local environmental or climatic conditions or components. In ecological terms, this shifting mosaic of comparative advantages in the region's countries could pose the risks of increased pressure on fragile or remote areas or ecosystems with little human intervention, the sudden increase in the value of particular ecological elements or functions (and a decline in the value of others) and the introduction of new biological forms or even exotic ecosystems in the region. In the absence of social regulation, these developments may lead to overexploitation and degradation of regional ecosystems (and the loss of such comparative advantages as may be associated with them), but if well managed they could generate new sustainable sources of prosperity and lead to a positive redefinition of comparative advantages in the global context.

The development and spread of new technologies in the region, particularly biotechnology, has the potential to produce significant environmental implications (Gallopín, 1995). It is possible to anticipate that these changes will have a significant impact on Latin American and Caribbean ecosystems. These alterations could entail, for example, major effects on the environmental sustainability of production activities, alterations in subregional water and nutrient cycles, changes in agricultural yields, the disappearance of some ecosystems and the appearance of new ones, changes in the environmental supply of natural resources and alterations in limiting factors and ecological restrictions.

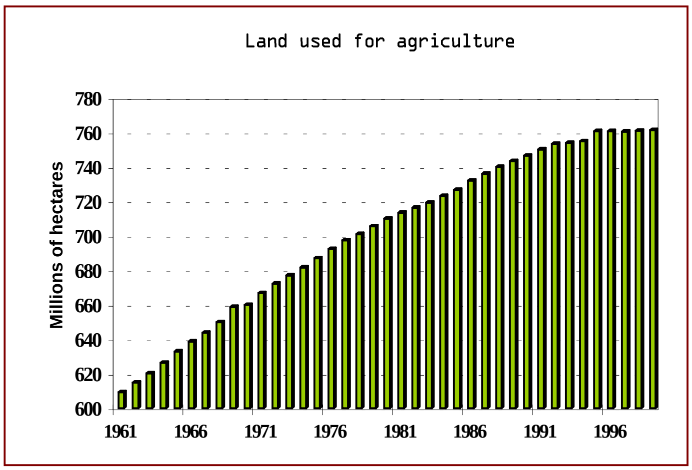
In any event, there is now greater technical potential than ever before to move towards the sustainable management of ecosystems in the long term. This includes better control, monitoring and reduction of environmental pollution, diversification of the uses of ecological resources and development that is environmentally sustainable in the long term.

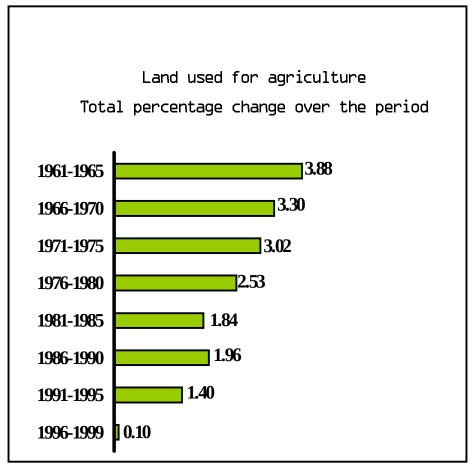
Nonetheless, the direction in which the new technological and economic paradigm is moving suggests that this technical potential will tend to be realized only in the more advanced countries. That is, the region will risk becoming a focal point for the perverse effects of the technological and economic revolution, unless the countries pursue the structural changes that are needed in the social, economic and technological spheres by adopting active, sustained, endogenously determined, shared strategies that command support among social actors.

II. Changes in the production structure and their effects on environmental sustainability

The changes undertaken by the economies of Latin America and the Caribbean in recent decades have resulted in a sectoral recomposition whereby services have increased their relative weight in the economic structure, while that of primary and industrial production has diminished proportionately. The implications of these trends for sustainable development need to be assessed. The relative decline in the value of primary and industrial production has not alleviated direct environmental pressure on the resource base or environmental damage, as the agricultural frontier has continued to expand and the volume of mineral, forestry and fishery resources extracted has maintained an upward trend (see figures 9.1 and 9.2).

Figure 9.1
EXPANSION OF THE AGRICULTURAL FRONTIER, 1961-1999

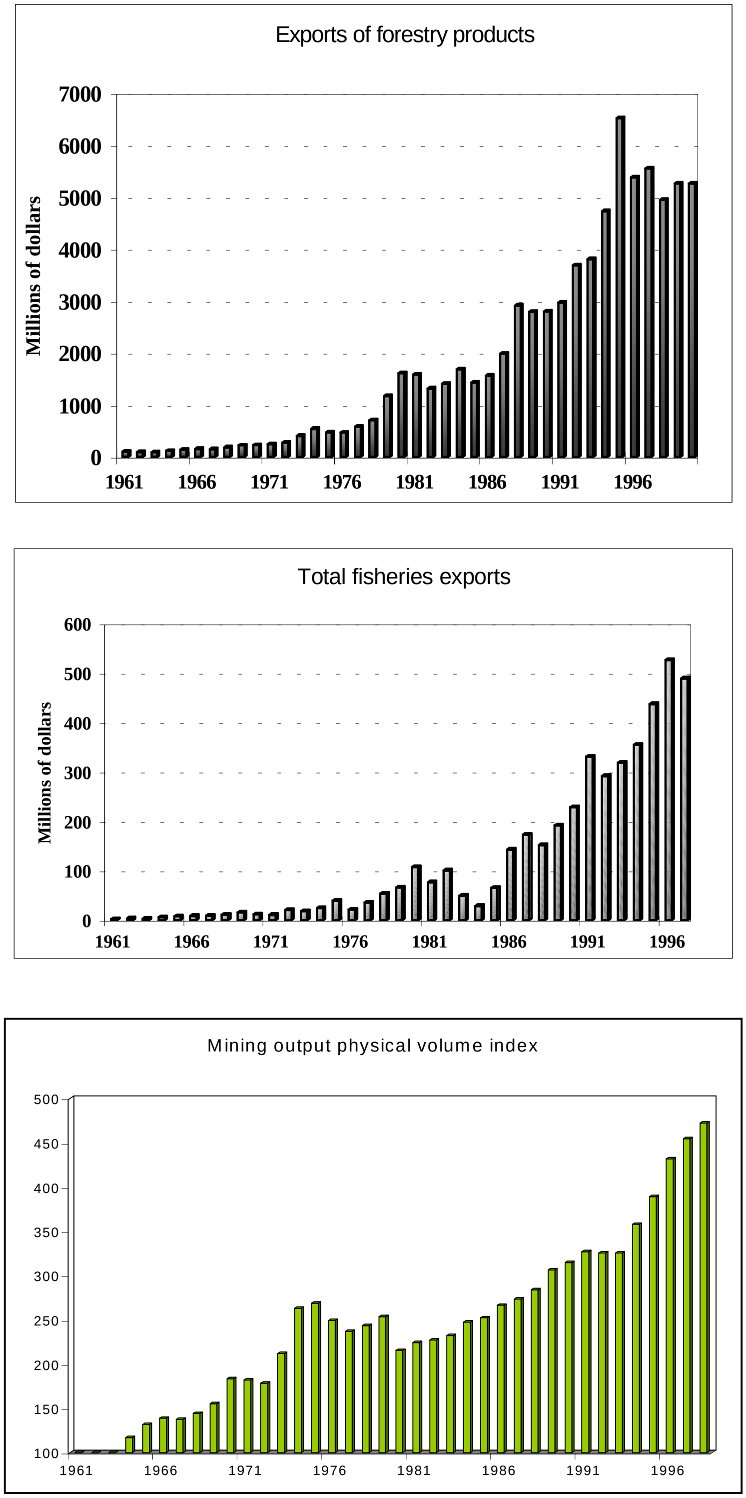




Source: Food and Agriculture Organization of the United Nations (FAO), "FAO Statistical Databases (FAOSTAT)" (www.fao.org), 2001.

The traditional effects of primary activities, particularly changes in land use, are now being concentrated in smaller, more fragile areas that are of greater ecological significance, inasmuch as the ecosystems concerned are critical to the conservation of national, regional or world biological diversity. In other words, they are becoming concentrated in places that are environmentally more sensitive, and perhaps more vulnerable. This is compounded by the fact that the region’s rural population is not expected to fall significantly over the coming decades, despite continuing urbanization trends, which means that the degree of population pressure on resources is unlikely to change.

Figure 9.2
TRENDS IN SELECTED NATURAL RESOURCE SECTORS IN LATIN AMERICA AND THE CARIBBEAN



Source: Food and Agriculture Organization of the United Nations (FAO), "FAO Statistical Databases (FAOSTAT)" (www.fao.org), 2001; ECLAC, *Foreign Investment in Latin America and the Caribbean, 2000 Report* (LC/G.2125-P), Santiago, Chile, April 2001. United Nations publication, Sales No. E.01.II.G.12.

Many of the region's key environmental problems are linked to land use changes, especially the conversion of forests to agricultural land uses.[1] As figure 9.1 shows, between 1961 and 1999 over 150 million hectares were incorporated into agricultural production in the region, and much of this land was converted from forest. Although the agricultural land area is still increasing, the rate has slowed, especially in the last few years. Two thirds of the land brought into agricultural use corresponds to increased production of livestock, mainly cattle. In the region, the livestock boom has been the most decisive factor behind the decline in forest cover that has occurred, especially in the humid tropical zones (Tudela, 1990). This process, which first became significant in the 1950s, was encouraged by governments through infrastructure, subsidized credit and land titles.

Where livestock expansion is concerned, the economic reforms carried out in the region over recent decades have involved the elimination of subsidies and of colonization projects that induced human settlement in new areas. Even so, the deforestation rate has dropped only slightly in South America in recent years, according to FAO data.[2] It is interesting to note that, contrary to what might be expected in the light of growing specialization in manufacturing, the pressure on forested areas in Mexico and Central America has not diminished. The FAO data show an annualdeforestation rate of 1.2% in the period 1990-2000, which is much higher than the South American rate.

Economic reform has also had the effect of modernizing the region's agriculture, making it more intensive, with the positive result of reducing pressure on natural areas. It does, however, mean greater use of fertilizers and pesticides, which also cause environmental problems. Furthermore, in some cases, expansion of the agricultural frontier is directly linked to strong growth in external markets, with a tendency towards specialization and monoculture in the most favoured areas. This is the case with soya, whose growing area and export volumes have risen steadily over the last 30 years (Vera, 2001).

The period 1980-1999 also saw an increase in the volume of exports from sectors with a recognized environmental impact. Figure 9.2 shows the evolution of exports derived from the region's forestry, fishery and mining sectors. In addition, there has been growth in external sales of products from polluting manufacturing industries, as the next section details. Cleaner production processes mean that primary activities may now be causing less environmental damage per unit of output. For this reason, there may be wide variations in environmental performance in each sector depending on the characteristics of producers, environmental regulation in the countries and the environmental requirements of markets. In any event, the resource base has been steadily declining, especially in countries whose international trade has been based on natural resource-intensive exports. In some activities, the overexploitation of resources has already had direct impacts on output. This is the case with sea fishing, as catches have continued to decline, and efforts to switch to alternative activities are still posing risks to fragile ecosystems (see table 9.1).

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[1] Deforestation is the main cause of biodiversity loss and land degradation in the region. It affects the availability and regulation of water resources, and represents the region's main contribution to global warming.

[2] The FAO data show that the forested area was reduced at a rate of 0.5% a year in South America between 1990 and 1995, and 0.4% a year over the decade as a whole (1990-2000). The annual deforestation rate in Central America held steady at 1.2%, while in the Caribbean an annual loss rate of 1.7% in the first period was reversed, with forest cover increasing by some 0.3% a year in the second period (FAO, 2001a).

Table 9.1
LATIN AMERICA AND THE CARIBBEAN: SELECTED ENVIRONMENTAL INDICATORS
(Cumulative percentage growth rates)

Physical indicators	1989/1980	1999/1990
Arable farmland area	7.3	6.3 a/
Volume of agricultural output	26.8	28.3
Total fertilizer consumption	5.3	42.2 a/
Livestock	7.4	0.8
Volume of industrial roundwood production	25.4	18.1 a/
Firewood and coal production	12.3	0.4 a/
Marine fisheries production	17.9 (1985-1990)	-24.3 a/
Marine fish farming production	165.0 (1985-1990)	116.0
Physical volume of mineral production, including oil	25.9	43.1
Physical volume of mineral production, excluding oil	46.2	67.6
Carbon dioxide (CO_2) emissions	22.9	37.1
Carbon monoxide (CO) emissions	23.5	28.4
Cumulative percentage population growth	21.93	17.0 b/
Cumulative increase in gross domestic product (dollars)	13.95	33.22

Source: Based on ECLAC, *Statistical Yearbook for Latin America and the Caribbean, 2000* (LC/G.2118-P), Santiago, Chile, February 2001. United Nations publication, Sales No. E.01.II.G.1; and United Nations Environment Programme (UNEP), "GEO. Estadísticas ambientales de América Latina y el Caribe", San José, Costa Rica, University of Costa Rica, 2001, forthcoming.

a/ 1998/1990.
b/ 2000/1990.

It is undoubtedly in the secondary sector of the economy that a structural change with positive implications for the environment, and thence for production quality, is taking place. In most branches of industry, better processes, quality requirements, environmental administration systems, certification mechanisms, staff training and other features associated with technological change and globalization have acted in synergy with the consolidation of national environmental policies, better enforcement of laws and regulations, the operation of new management instruments, growing awareness among businesses, greater demands from society and other factors to reduce the environmental impact of industry.

This change is mainly taking place in large firms, particularly those that have links to transnational corporations or are involved in their production chains. Foreign direct investment may thus have positive implications for the environment, insofar as foreign firms tend to employ cleaner technologies in their production processes. The spread of these to small and medium-sized enterprises (SMEs) is barely beginning, although many SMEs are already modernizing and introducing environmental quality practices. There are gaps in the information available, however, which could be remedied by better assessment mechanisms.

This process is clearly having positive repercussions, but it has not yet gone far enough to reverse some worrisome trends. For example, certain greenhouse gas emissions are now growing faster than before. The need to expand production over the coming decades, in a regional context in which participation in the world economy is growing and more employment needs to be created, makes it more urgent to devise sustainable energy policies that can address these disturbing trends (see the fourth section of this chapter).

In the service sector, some highly dynamic activities that are quite relevant, particularly in certain subregions, are contributing to economic growth but are also adding to environmental pressures. This is the case with large-scale beach tourism, especially in the Caribbean. Meanwhile, the reorientation of certain services has emerged as an opportunity to find more sustainable ways of profiting from natural resources, such as ecotourism. The increasing dissemination of information services is likely to provide the basis not just for enhanced knowledge and improved communication, but for more effective environmental management systems as well.

If accurate, systematic knowledge of these trends and pressures and their interrelationships with economic processes is to be obtained, it is imperative to continue to collect and systematize data, devise operating systems to ascertain the economic value of natural resources and environmental services, develop integrated economic and environmental accounting systems and improve natural resource accounts, as a basis for policy integration.

To sum up, the region is at a contradictory stage where the environment is concerned. Some economic and technological trends are beginning to be favourable for the environment, especially in manufacturing and services, but also in some emerging activities in the primary sector. At the same time, pressure from old production and land-use processes is continuing to build up, while the rapid expansion of production remains a pressing need. These problems are compounded by emerging environmental tensions resulting from increased vulnerability to global environmental processes and the growing environmental demands of export markets. The region needs to act more urgently to adopt sustainable production and consumption patterns and less environmentally vulnerable ways of participating in the world economy.

III. Economic globalization and the environment

1. The environmental impact of exports and foreign direct investment

The reallocation of resources that took place in most of the region's countries as a result of the economic reforms of recent decades has in many cases boosted investment, production and exports of natural resource-intensive products. In addition, the increasing competitiveness of world exports is raising the opportunity cost of leaving natural resources unexploited at faster rates than their natural regeneration. This has led to the emergence of strong economic forces that are driving a number of countries to exploit their natural resources.

According to ECLAC studies, the changing composition of the export structure is a sign that the reallocation of resources has tended to steer a large group of countries, especially in South America, towards more natural resource-intensive areas of specialization. In this context, it is worth noting that natural resource-based branches of manufacturing producing highly standardized intermediate industrial goods such as iron and steel, petrochemicals, non-ferrous minerals, pulp and paper, copper and aluminium turned in a better economic performance in the South American countries during the period analysed. These are industries that the World Bank categorizes as environmentally sensitive,[3] consisting of branches where pollution abatement expenditures exceeded 1% of total sales in the United States in 1988 (Schaper, 2000; Schaper and Onffroy, 2001).[4]

The results of the studies also suggest that there is no direct link between trade liberalization policies and environmental protection. The enormous diversity shown by the indicators and data for each of the national economies is evidence of the extreme complexity of this relationship. The environmental implications will depend on each country's situation in terms of its institutional

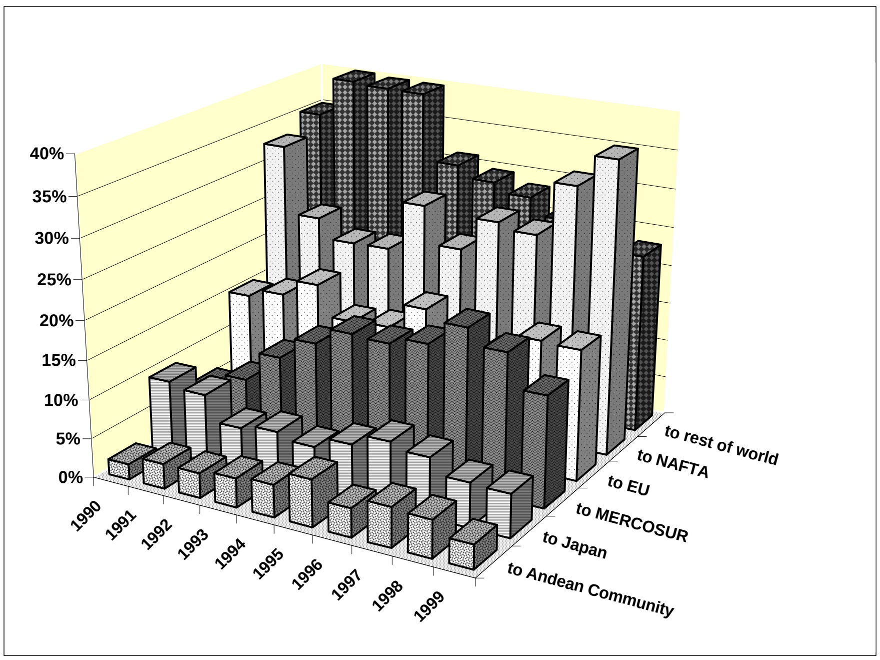
[3] Essentially, this is a group of 40 industries at the three-digit level of the Standard International Trade Classification (SITC, Rev.1).
[4] The studies concerned cover Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Jamaica, Mexico, Paraguay, Peru, Uruguay and Venezuela. Of these, only Mexico showed a contrary tendency.

structure, its trade composition, its income distribution, the enforcement of environmental regulations, the power of interest groups, the geographical density of its economic activity, the education levels of its population and the income elasticity of the demand for environmental quality.

For the Andean Community and the Southern Common Market (MERCOSUR), for example, the results suggest that in the 1990s there was a significant rise in the export volume of products with an obvious environmental impact.

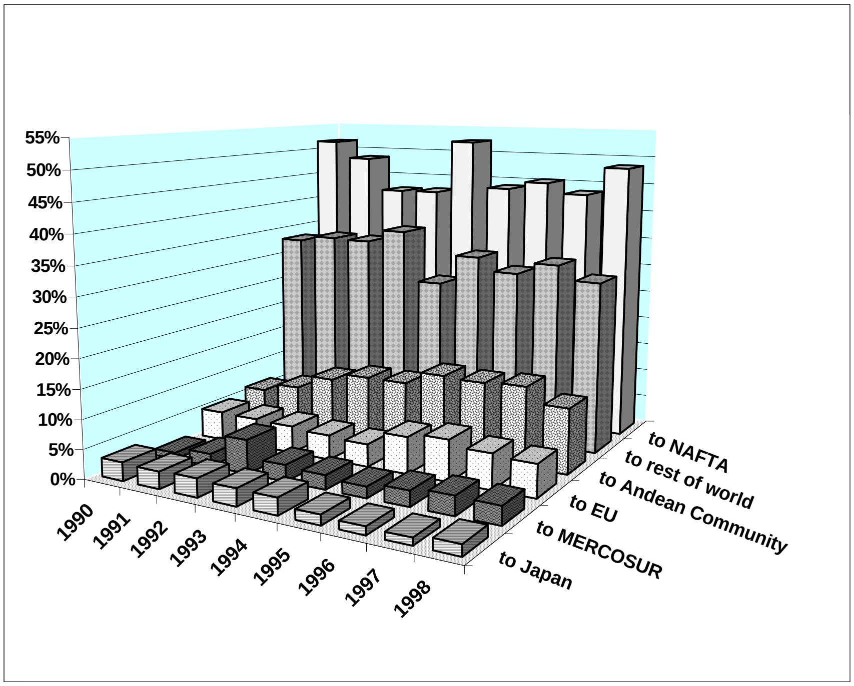
Figures 9.3 and 9.4 show the distribution by destination of the total volume of environmentally sensitive exports. It is interesting to note not only the increase in the volume of exports, but also the fact that for both the Andean Community and MERCOSUR, the main destinations by volume for environmentally sensitive exports were the three countries of the North American Free Trade Agreement (NAFTA), namely Canada, Mexico and the United States. For Chile, by contrast, the predominant destination for environmentally sensitive exports is Japan. Although this was still the largest market towards the end of the 1990s, its share fell from 50% in 1991 to 28% in 1999, with destination markets such as the European Union and NAFTA becoming more important.

Figure 9.3
MERCOSUR: EXPORT VOLUMES OF ENVIRONMENTALLY SENSITIVE INDUSTRIES, BY DESTINATION MARKET



Source: Based on information from the ECLAC Foreign Trade Data Bank for Latin America and the Caribbean (BADECEL).

Figure 9.4
ANDEAN COMMUNITY: EXPORT VOLUMES OF ENVIRONMENTALLY SENSITIVE INDUSTRIES, BY DESTINATION MARKET



Source: Based on information from the ECLAC Foreign Trade Data Bank for Latin America and the Caribbean (BADECEL).

Another important finding is that, in the 1990s, export volumes in environmentally sensitive industries within the MERCOSUR and Andean Community areas grew at faster rates than flows to countries outside the region (see table 9.2). However, the level of these exports in the early 1990s, started at very low levels, compared to the volume exported to other regions.

Table 9.2
AVERAGE ANNUAL GROWTH IN ENVIRONMENTALLY SENSITIVE EXPORT VOLUMES, BY DESTINATION
(*Percentages*)

	From MERCOSUR 1990-1999	**From Andean Community 1990-1998**
To MERCOSUR	19.6	34.2
To Andean Community	16.5	15.9
To NAFTA	4.9	7.0
To EU	4.0	12.6
To Japan	-3.0	1.8
To rest of world	1.9	6.9

Source: Based on information from the ECLAC Foreign Trade Data Bank for Latin America and the Caribbean (BADECEL).

Overall, while most of the countries show an increase in the volume of environmentally sensitive exports during the 1990s, it is interesting to note that the relative share of such exports diminished in terms of value, and also experienced a relative loss of competitiveness in international markets. The latter is reflected by the revealed comparative advantage (RCA) indices that are shown in table 9.3 for the Andean Community and MERCOSUR countries and Chile.

Table 9.3
REVEALED COMPARATIVE ADVANTAGE (RCA) INDICES FOR THE GROUP OF ENVIRONMENTALLY SENSITIVE INDUSTRIES

Region/country	1990	1998
MERCOSUR	**1.37**	**1.11**
Argentina	1.19	0.72
Brazil	1.55	1.35
Paraguay	0.11	0.24
Uruguay	0.29	0.41
Andean Community	**1.69**	**1.58**
Bolivia	0.89	0.58
Colombia	0.66	0.71
Ecuador	0.36	0.37
Peru	2.14	1.71
Venezuela	**2.26**	2.48
Chile	**2.94**	**2.71**

Source: The author, on the basis of information from the ECLAC Foreign Trade Data Bank for Latin America and the Caribbean (BADECEL) and the United Nations International Commodity Trade Database (COMTRADE).

Note: The RCA index is calculated as RCAij = (Xji/Xjt)/(Xit/Xtw), where j = a product or industry (SITC code, revision l), i = country, w = the world and t = total. It measures changes in a country's exports of a product j as a share of world exports of that same product j, comparing them to changes in the country's total exports; as a share of total world exports; i.e., considering the country's relative weight as determined by its size. If the RCA index >1, the country has a comparative advantage in the product; i.e., its share of the world market for this product is higher than its overall share of world exports. If the RCA index <1, the country does not have a comparative advantage in the product.

The results in table 9.3 show that environmentally sensitive industries in both MERCOSUR and the Andean Community have lost export market share, but remain competitive (RCA>1). These aggregate figures, however, mask large differences among groupings, countries and products. While MERCOSUR exports stand out as very competitive (RCA of between 2 and 5) in pulp and paper, iron and steel and aluminium, for Andean Community exports this is the case in copper, aluminium and petroleum products (RCA of between 2 and 10). Chile's competitiveness, on the other hand, has declined slightly across this whole group of industries. It is, however, very competitive in pulp and paper (RCA>14) and inorganic chemicals (RCA>4). Although it is very competitive in copper, its RCA shows a downward trade over the decade.

In these circumstances, the countries face a number of challenges. The most important one has to do with their specialization in potentially polluting, natural resource-intensive industries, which places them in a very vulnerable position as regards the environmental requirements and demands they will have to meet in developed-country markets.

From the scanty available information it is difficult to get a precise idea of the environmental impact of foreign direct investment (FDI), which depends on multiple factors, such as the corporate strategies of individual firms, the sectors in which they operate, their relative efficiency, corporate environmental policy, the technologies they use and the characteristics of the recipient country's environmental regulations and institutions. On the one hand, FDI plays an important role in defining major natural resource projects for export (Mortimore and Peres, 2001),[5] which may result in greater pressure on natural resources. On the other hand, transnational corporations can facilitate the transfer and use of environmentally friendly technologies and improvements in environmental management (OECD, 1999).

In any event, the few studies that do exist indicate that the presence of foreign-owned firms, together with a large share of exports in total sales, increase the likelihood of firms carrying out environmental investment (Young and Roncisvalle, 2001). Furthermore, the larger a firm, as measured by its number of employees, the longer-established it is, the stricter the environmental controls applied and the greater the pressure from local society, the more environmental investment is likely to rise (Ferraz and Seroa da Motta, 2001). According to reasonable estimates, private-sector environmental spending in Argentina reaches 0.17% of GDP, while environmental investment spending in Brazil is estimated to have averaged 0.8% of net operating revenue in 1998.

Table 9.4 is derived from a survey held in 1996 among a wide range of firms in the state of São Paulo, Brazil. As can be seen, in this case the level of concern of firms for environmental considerations is determined by external demand.

Table 9.4
FIRMS INVESTING IN THEIR PRODUCTION PROCESSES FOR ENVIRONMENTAL REASONS, 1996

	Ownership of capital (as of 31/12/1996)			
Investment in production	Domestic	Foreign	Mixed	Total
Processes for environmental reasons				
Yes (%)	18.2	43.10	35.50	18.70
Exports/revenues (%)	1.54	12.91	8.83	2.00
No (%)	81.80	56.90	64.5	81.30
Exports/revenues (%)	0.60	6.14	5.53	0.68
Number of firms	39,968.00	582.00	259.0	40,809.00
Exports/revenues (%)	0.77	9.06	6.69	0.93

Source: Carlos Eduardo Young and María Cecilia Junqueira Lustosa, "Meio ambiente e competitividade na indústria brasileira", *Revista de Economia Contemporânea*, vol. 5, special issue, 2001.

In the case of Argentina, (Chudnovsky, López and Freylejer, 1997), while recognizing the difficulty of accurately classifying the reasons for investment, the findings indicate that while some investment is carried out to comply with national environmental regulations, the need to comply with export market requirements, the existence of more stringent internal company policies (transnationals), the environmental "image" of the firm or the scope for reducing operating costs through environmental management are determining factors in environmental investment decisions.

Furthermore, the growing international competition resulting from globalization has led to greater concern about and efforts to comply with international environmental standards and to a quest to differentiate products and processes; this is the thrust of the ISO 14001 standards and the concept of eco-efficiency in production processes. Subsidiaries of transnational corporations have

5 In the primary sector, investment by transnational corporations has gone mainly into oil and gas exploration in Argentina, Bolivia, Brazil, Colombia and Venezuela and mineral prospecting in Argentina, Chile and Peru.

greater opportunities to incorporate uniform environmental management standards into their strategies, especially in operations aimed at the international market. These environmental management systems at the company level are now covered by the ISO 14001 scheme. This certification, like the ISO 9000 quality management certification, has gradually become established as a necessary credential for leading firms, particularly exporters. In line with this trend, a growing number of the region's large firms, whether foreign or locally owned, have invested to obtain ISO 14001 certification for their environmental management systems.

In the last three years, the number of firms with ISO 14001 certification has increased substantially. In 1998, 7,887 firms in 72 countries around the world had ISO 14001 certification. By March 2001, the number of firms had more than tripled to reach 27,509 in 96 countries. In the region, although the absolute number of firms certified is still small, it rose by 44% over the same period. The first place is held by Brazil with 270 firms certified, followed by Mexico with 188 and Argentina with 114 (between 2000 and 2001, the numbers increased by 81%, 27% and 14%, respectively). As of March 2001, Colombia and Costa Rica had 20 firms certified; Chile, 11; Peru and Uruguay, 10; Venezuela, 7; Barbados, 3; Honduras, 2; and the Dominican Republic, Ecuador, Guatemala, Paraguay, Saint Lucia and Trinidad and Tobago, 1 apiece.

2. Changes in the international economic context and the environment

Globalization has brought to light the interdependence between international trade and the environment. This has happened in an international context where concerns about the environment are becoming encreasingly strong, particularly in the developed countries. In Latin America and the Caribbean, by contrast, slow economic growth and the problems of poverty that represent a more immediate threat to human life and health have given precedence to short-term priorities, to the detriment of environmental considerations or slower-maturing production efforts that take account of environmental quality.

However, insofar as the countries of the region have opted for a strategy of trade liberalization and export-led growth, they do not have much flexibility for adapting their production systems to the environmental requirements of their main export markets. The way in which this adjustment is bound to take place is largely determined by the type of technological and environmental management prevailing in the developed countries, because they are the ones that dominate world trade and export the largest share of goods and services among themselves (including even raw materials). Accordingly, they will also most likely be determining the pattern of production and technology that will prevail in the rest of the world.

As the countries of Latin America and the Caribbean seek higher and better participation in international markets, trade will become increasingly important in shaping patterns of economic activity and the use of resources. However, widespread tariff reductions have increased the importance of national regulatory policies, including environmental policies, owing to their perceived potential to distort international trade. Multilateral trade negotiations have also changed, and are increasingly focusing on national policies that determine conditions of competition. These can be affected when costs vary among countries due to subsidies, intellectual property protection policies or environmental policies, among other things.

Another feature of the international context is that environmental requirements are linked to economic considerations and interests. One example illustrating this link is related to the opportunity to increase exports of the environmental goods and services industry, a new sector whose growth is driven by the world wide adoption of environmental rules, laws and standards. In the United States, for example, the 1992 Energy Policy Act promotes, among other things, the creation of a technology transfer programme to reduce the trade deficit through exports of environmentally innovative technologies. Similarly, the 1992 Export Enhancement Act was intended to encourage exports of environmental goods and services.

Another phenomenon that combines economic interests with concerns about the environment in developed countries is the rising cost of disposing of waste and products that have reached the end of their life cycle. This creates environmental obligations that are reorienting the ways in which goods and services are produced and marketed. Firms are aiming to implement product life cycle management systems. This concept is creating conflicts in international trade, as it is difficult to put into practice when products are marketed across national borders. Eco-labelling programmes, eco-packaging rules and recycling programmes are examples of this life cycle concept in practice. It is often perceived by outsiders as a potential barrier to international trade, given the heterogeneity of environmental standards.

Furthermore, consumer habits and demands have turned environmental excellence into a new factor of competitiveness among firms and products, and the same is true of environmental assessment of the entire product life cycle. Consumers are increasingly opting for so-called “green products”; i.e., those they regard as environmentally sounder in respect of their contents and the way they are produced. Thus, businesses are also under pressure from consumers to improve the environmental characteristics of their products and processes. Environmental performance is not just important for firms’ marketing efforts, but has also become a relevant factor in capital markets, which reward firms with a proven environmentally responsible attitude.

For Latin America and the Caribbean, these developments mean that stringent environmental criteria will be applied in their main export markets in the coming years. It will be increasingly difficult to argue that environmental restrictions in the developed countries are trade tactics or unfair sanctions. The global nature of environmental problems will in any event give a *de facto* legitimacy to the environmental requirements imposed on exports. These trends will force the region to make major changes in its environmental practices and regimes, not just to heed the signals being given out by international markets, but to ensure the very survival of the production base in the countries of Latin America and the Caribbean.

IV. The environmental repercussions of productive and technological restructuring in the energy sector

In the 1990s, liberalization and deregulation in sectors such as energy and telecommunications unleashed a process in which new technologies were rapidly introduced and businesses were restructured. This process influenced the region’s energy sector in two ways: (a) directly, through a far-reaching process of structural transformation in the infrastructure sectors (particularly energy) involving the entry of new agents, mainly transnational corporations and some large locally owned conglomerates, that gave rise to major changes in the hydrocarbon and electricity production chains; and (b) indirectly, as the energy sector had to adapt constantly and rapidly to changes in the final demand for energy on the part of other production and social sectors (ECLAC, 2001e). These changes affected the evolving energy-environment relationship, through both economic factors (energy intensity) and environmental ones (emissions, energy efficiency and the share of renewable energy sources).

1. Energy intensity

Much of the literature on this subject identifies sustainable development as one of the principles underlying the energy sector reforms implemented in recent decades. Despite this general affirmation and the slow growth of per capita electricity consumption, however, the region’s level of efficiency in energy transformation and use is far from adequate.

Energy intensity is linked to a country's economic development process. It increases in the early stages of development (mechanization and the development of energy-intensive industries), then flattens out (stabilization of these processes) and finally decreases (introduction of technological improvements, know-how, improved yields in energy transformation and consumption).

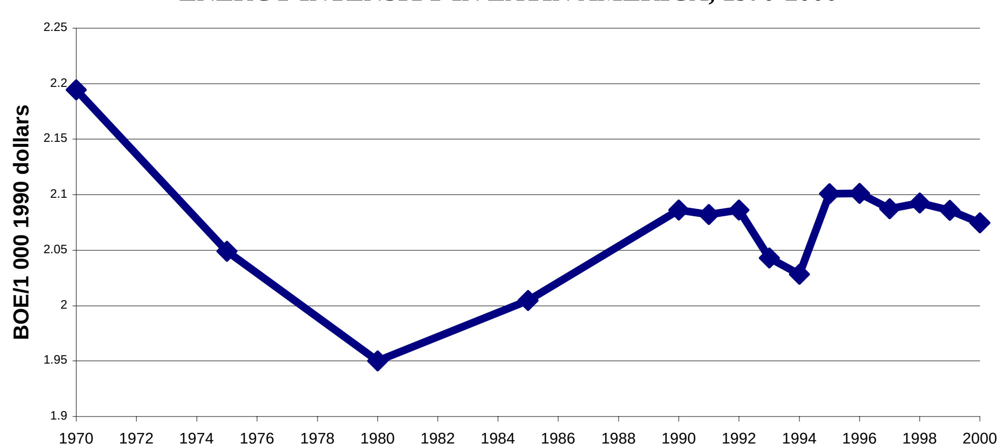
As table 9.5 and figure 9.5 show, the evidence indicates that the reforms did not have the hoped-for effect on energy efficiency. As a result, the subject became the crux of initiatives to achieve more rational use of energy resources in the late 1990s. The data show, in fact, that energy intensity has behaved erratically: after dropping sharply between 1970 and 1980, it began to rise steadily, so that 7% more energy is now consumed to generate the same unit of ouput than in 1980.

Table 9.5
INDICATORS OF ENERGY CONSUMPTION AND ENERGY INTENSITY IN LATIN AMERICA AND THE CARIBBEAN

Sectoral share of total consumption		**1970**	**1975**	**1980**	**1985**	**1990**	**1995**	**2000**
Transport		27.07%	30.90%	32.43%	31.77%	33.04%	35.27%	35.64%
Industry		31.19%	32.00%	34.28%	35.41%	35.63%	34.05%	35.54%
Residential		33.46%	28.17%	24.30%	23.97%	22.18%	20.88%	18.53%
Others		8.28%	8.93%	9.00%	8.85%	9.14%	9.79%	10.28%
Total consumption (KBOE)		1,178,409	1,500,466	1,870,950	1,972,564	2,218,536	2,589,219	2,983,607
Energy intensity (BOE/1000 1990 dollars)		2,195	2,049	1,950	2,005	2,086	2,101	2,075
Index 1980=1		1,125	1,051	1,000	1,028	1,070	1,077	1,064
Per capita GDP (1990 dollars)		1,909	2,303	2,688	2,484	2,442	2,596	2,798
Index 1980=1		0.710	0.857	1.000	0.924	0.908	0.966	1 041
Growth	1970-1980	4.73						
	1980-1990	1.72						
	1990-2000	3.01						
	1970-2000	3.15						

Source: Based on data from the OLADE Energy Economic Information System and ECLAC.

Figure 9.5
ENERGY INTENSITY IN LATIN AMERICA, 1970-2000

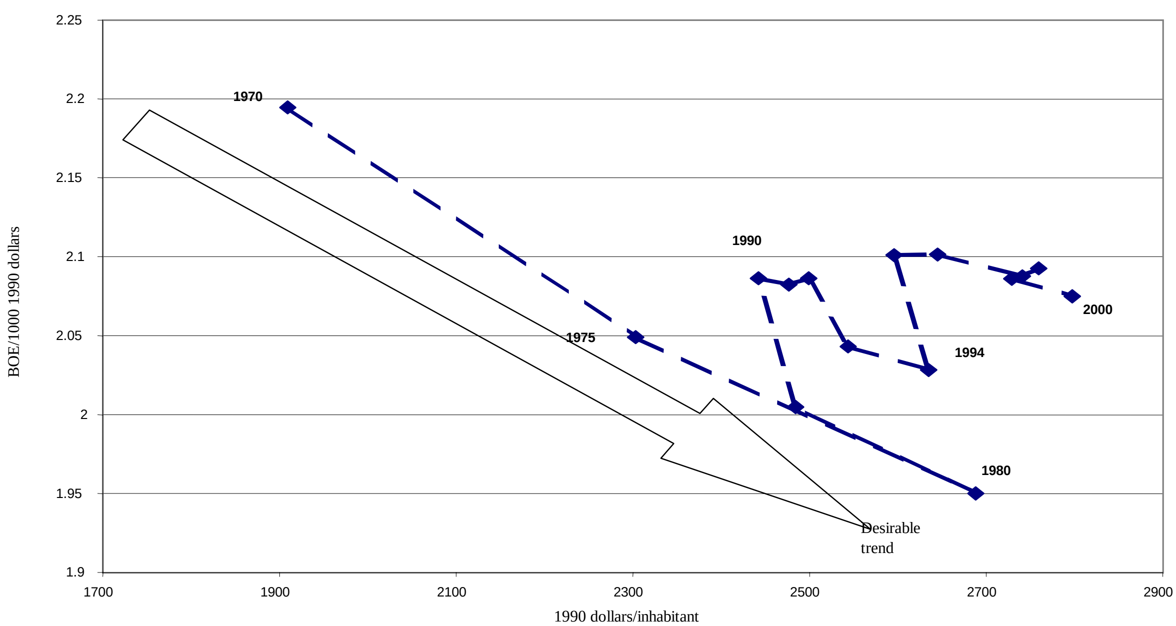


Source: Based on data from the OLADE Energy Economic Information System and ECLAC.

Some components of energy intensity have changed considerably. While the share accounted for by household consumption declined from more than a third of the total in 1970 to just 18% in 2000, the share of the transport sector rose strongly and steadily over the whole period (from 32% to more than 35%), as did that of industry, though to a lesser extent and mainly during the 1970s rather than later (see table 9.5). A shift in the industrial structure of certain countries in the region (particularly Brazil) towards energy-intensive industries, or (again in Brazil) a shift in the composition of exports towards energy-intensive products such as cellulose, led to strong growth in the energy content of the industrial sector, and with it a rise in total energy intensity.

Figure 9.6 plots energy intensity against per capita output. Between 1970 and 1980, a desirable trend is apparent: economic growth accompanied by lower energy use per unit of output (lower energy intensity), indicating improved efficiency and better use of energy resources. This trend was reversed, however, between 1980 and 1985, when per capita income fell back and energy intensity rose, and again between 1987 and 1990, indicating that economic recession in the "lost decade" was not accompanied by better energy use. In the early 1990s a favourable trend was re-established, but this broke off again in mid-decade. The behaviour of the energy intensity/per capita output ratio in the last two decades of the twentieth century was erratic, but the net effect was an overall worsening of the situation.

Figure 9.6
ENERGY INTENSITY AND PER CAPITA INCOME IN LATIN AMERICA AND THE CARIBBEAN, 1970-2000



Source: Based on data from OLADE/ECLAC.

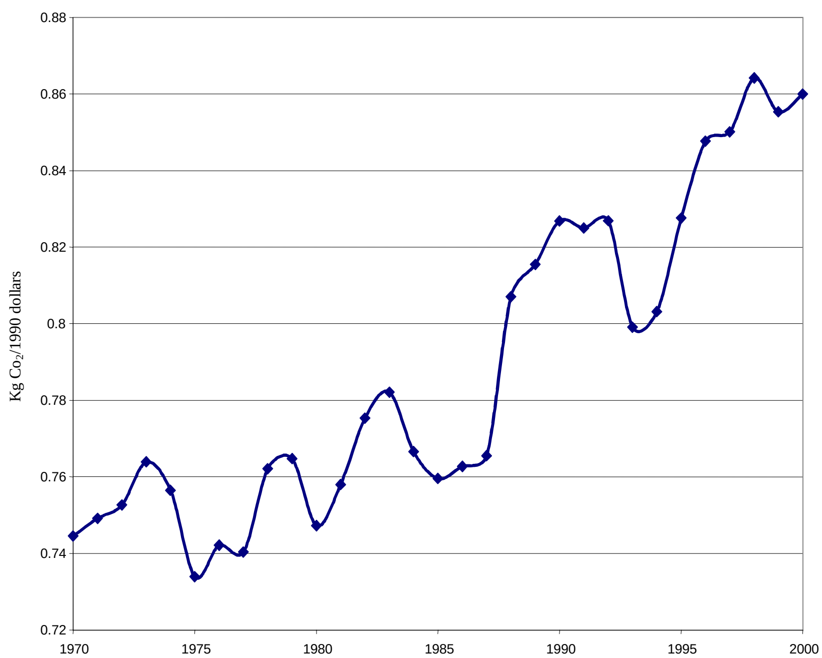
To sum up, in terms of energy intensity, the achievements of the Latin American and Caribbean countries in the last three decades have been modest, and trends in the last two decades have taken an undesirable turn. This outcome contrasts with the progress made by the OECD countries as a group over the past 20 years, with energy intensity falling by 20% thanks to energy policies designed to diversify supply and make energy use more effective by cutting out waste and increasing usage efficiency. This has involved the development of institutions to regulate energy consumption by applying temperature standards in public premises, measuring the consumption of hot water for personal use and household heating and setting technical standards for new buildings.

It has also involved publicity campaigns to combat excessive energy consumption and encourage energy-saving investments through promotional mechanisms such as free diagnosis and financial help for the implementation of improvements, and the allocation of significant research and development funding to programmes to increase energy efficiency and develop new and renewable sources. Latin America and the Caribbean have significant scope for action along the same lines.

2. CO_2 emissions

As a result of the factors described above, the total CO_2 emissions of the Latin American and Caribbean energy sector (not including emissions of biotic origin) have risen steadily since 1970. If this increase is correlated with economic growth using the index of emissions per unit of GDP, it transpires that the 2000 level was 16% higher than the 1970 one, largely because of the steady increase observed since 1985 (see figure 9.7).

Figure 9.7
RATIO OF CO_2 EMISSIONS TO GDP IN LATIN AMERICA AND THE CARIBBEAN



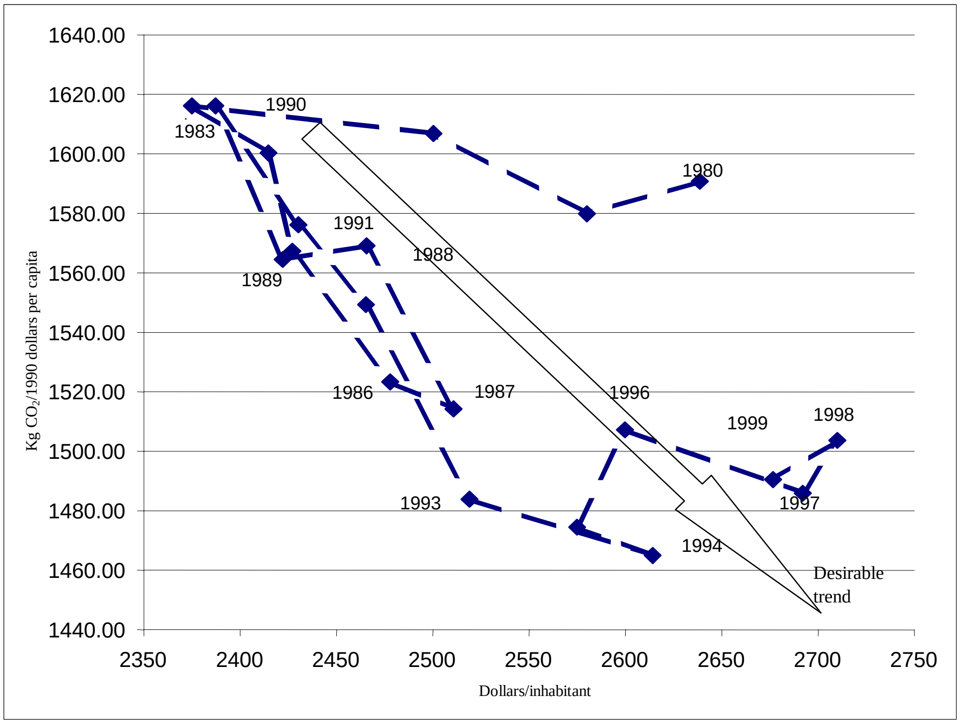
Source: Based on OLADE/ECLAC.

Figure 9.8 plots the emissions intensity indicator (kg of CO_2 per unit of output) against per capita output. As can be seen, the evolution of this emissions indicator does not show any specific tendency, but in recent years the trend has been clearly adverse.

As in the case of energy intensity, the behaviour of this indicator is associated with changes in the region's energy consumption structures (both by sector and by source) and production structures. Perhaps the best way of appreciating the changes that have taken place in the energy sector, and their impact on the environment, is to analyse emissions from electricity generation (see figure 9.9). The push to build hydroelectric generating capacity is reflected by the steady decline in

CO_2 emissions per unit of energy generated, a decline that was virtually unbroken from 1970 to 1993 (with a subperiod of stagnation between 1985 and 1988), but which went clearly into reverse thereafter. In 1993, when the last hydroelectric facilities built over the previous decades were still in full operation, emissions levels were almost 50% lower than they had been in 1970. By 2000, however, levels had risen 17% above that minimum.

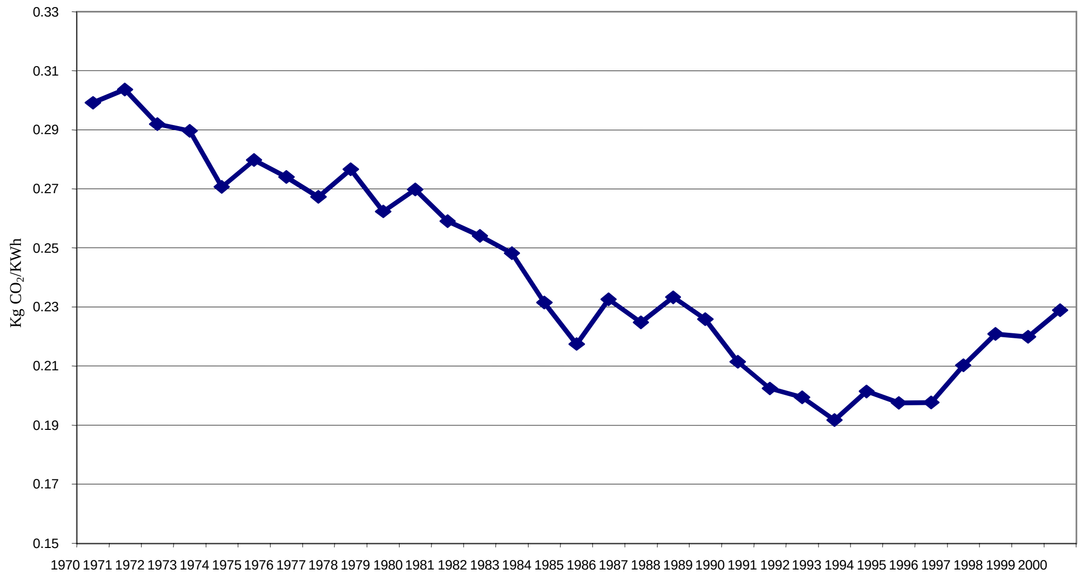
Figure 9.8
CO_2 EMISSIONS, 1980-1999



Source: Based on OLADE/ECLAC.

This substantial increase is connected with the reform process, which resulted in a move to expand generating systems based primarily on conventional thermal power stations. As part of this trend, countries with natural gas reserves built combined cycle power stations that were more efficient and less polluting than the old ones.

Figure 9.9
CO_2 EMISSIONS FROM POWER STATIONS, 1970-2000

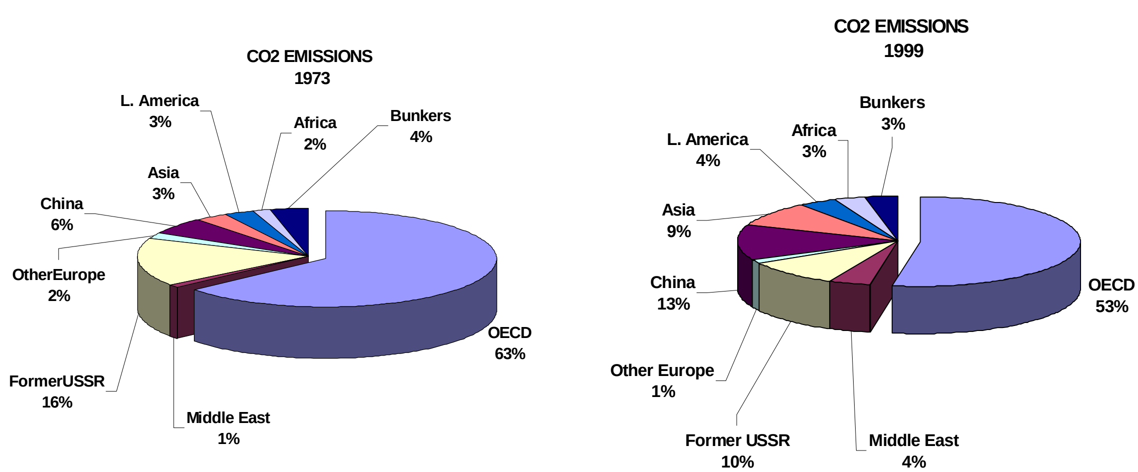


Source: Based on OLADE/ECLAC.

3. The Latin American and Caribbean energy sector and global climate change

In the late 1990s, Latin America and the Caribbean accounted for 8.5% of the world's population and 4.5% of world GDP. As regards greenhouse gas emissions, total world CO_2 emissions grew by 6.5 billion tons in absolute terms over the 25 years that followed the first oil shock. The contribution of Latin America and the Caribbean to total world CO_2 emissions is still low, but the region's share of this total grew from 2.6% in 1973 to 3.8% in 1999. The share of other regions has increased more, with that of China doubling from 6% to 12.7% in the same period, while that of the rest of Asia tripled (see figure 9.10).

Figure 9.10
EMISSIONS BY WORLD REGION, 1973-1999



Source: International Energy Agency (IEA), *Key World Energy Statistics*, Paris, 2000.

The forecasts available for the next two decades do not suggest that the situation will change significantly.[6] It is projected that growth in world energy consumption will be largely confined to developing countries, particularly in Asia and Latin America. Despite this rapid growth, Latin America and the Caribbean will account for only 7.4% of total energy consumption by 2020. As for CO_2 emissions, the developing countries are expected to be producing some 70% of the total by 2020. China accounts for almost 33% of the projected increase.

With 8.5% of the world's population, Latin America now produces 5.4% of world greenhouse gas emissions. The region's largest emitter is Mexico, with 356 million tons a year. The emissions of Mexico and Brazil represent 53% of the regional total. Although the combined population of the two countries is close to that of the United States, Mexico and Brazil together emit just 12% as much as that country.

Two thirds of the region's emissions come from the burning of liquid fuels (petroleum and derivatives), with coal accounting for less than 8%. The region's emissions per unit of output are relatively low: 0.41 kg of CO_2 per unit of GDP at purchasing power parity, as against a world average of 0.67 and a figure of 0.61 for the OECD countries. In relation to the total primary energy (TPE) supply, the region emits 2.1 tons of CO_2/TPE. The level of this indicator, which is below the world average, is due to the extensive use made of renewable energy, particularly hydraulic energy, in the regional energy structure. The per capita emissions indicator for Latin America and the Caribbean is very low, at 2.45 tons per inhabitant.

These considerations provide a starting point for formulating some regional energy policy priorities in the light of the world climate change agenda. Although Latin America and the Caribbean make a relatively small contribution to total greenhouse gas emissions, trends in the region have not been favourable in recent decades, and can certainly be improved on. There are opportunities to improve the trend of regional energy intensity through policies to promote energy efficiency and diversify the energy supply. As of 2000, only 15% of the region's hydroelectric potential was being tapped. There has been little development of other renewable energy sources, including geothermal ones.

There is clearly a long-term synergy between the region's energy policies on the one hand, the objectives of which are to improve energy efficiency and the absorption of new renewable and low-emissions technologies, and the consolidation of international efforts to combat climate change on the other. The region also has the potential to be a net supplier of global environmental services in the form of atmospheric CO_2 sequestration projects that could be marketed to countries facing high mitigation costs to offset their greenhouse gas emissions. There is also synergy between these energy policies and the objective of improving local environmental quality, particularly in urban areas; this would have real public health benefits in the region's cities.

In the political sphere, lastly, the region's countries have shown a real commitment to global efforts to coordinate climate change mitigation measures. As of May 2001, 12 Latin American and Caribbean countries had already submitted their first national communications to the authorities of the United Nations Framework Convention on Climate Change. As of late 2001, 17 of the 46 countries to have ratified the Kyoto Protocol were Latin American or Caribbean.[7]

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6 See International Energy Agency (IEA, 2000). The data are for emissions from the burning of fossil fuels. This publication does not count Mexico as part of Latin America, as the country is included in the OECD category. Mexico's share has been reclassified here as belonging to Latin America and the Caribbean.

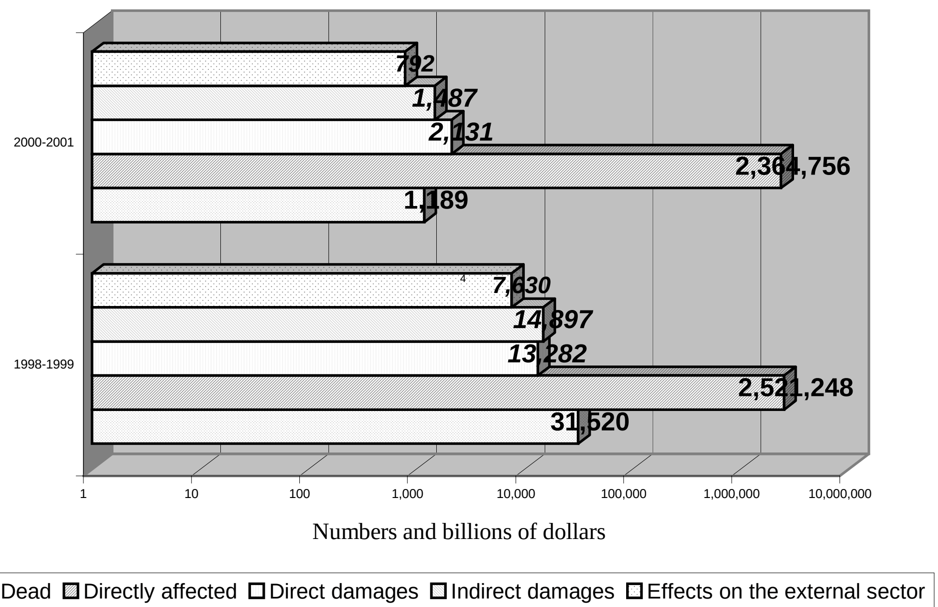
7 Antigua and Barbuda, Argentina, Bahamas, Barbados, Bolivia, Colombia, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Trinidad and Tobago and Uruguay.

V. Changes in the region's vulnerability

Vulnerability, in the sense of a system's internal susceptibility to changes that negatively affect its equilibrium in the face of an external event, is a concept in growing use.[8] The main fields of application of vulnerability analyses that deal with environmental issues are natural disasters and the research being done by the Intergovernmental Panel on Climate Change (IPCC). The acknowledgement that the damage caused by a given physical phenomenon may vary greatly depending on the development level of the countries affected,[9] and other variables such as environmental sustainability, is resulting in a new approach to natural disasters in which the idea of vulnerability is a key element.

The Latin American and Caribbean region is highly exposed to potentially destructive natural phenomena such as floods, earthquakes and volcanic eruptions. In combination with the region's high degree of sensitivity and limited capacity for adaptation, this exposure has resulted in a high and rising incidence of disasters caused by natural phenomena (see figure 9.11).

Figure 9.11
LATIN AMERICA AND THE CARIBBEAN: EFFECTS OF DISASTERS CAUSED BY NATURAL PHENOMENA, 1998-2001



Source: ECLAC.

Note: The chart summarizes the effects of disasters that have been evaluated by ECLAC. There is an indeterminate number of events that have not been evaluated by ECLAC, either because the countries did not request it (as in the case of disasters, particularly floods, that have affected Argentina, Bolivia, Brazil and Chile) or because they were "minor" seasonal events. The damage caused by these events could well be double the figure for the damage caused by the events evaluated.

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8 The vulnerability of a system is determined by: (i) the degree of exposure (the amount of time for which the system is subjected to an external change and the way in which it is so subjected), (ii) its sensitivity (the degree to which the system is affected by an external change) and (iii) its adaptability (ability of the system to adjust to the external change, moderate potential harm and take advantage of the opportunities or cope with the consequences it creates) (IPCC, 2001).

9 Of all disaster victims in the world, 90% live in developing countries where poverty and population pressure force growing numbers of the poor to live in dangerous locations (Annan, 1999).

While the reasons for the high level of vulnerability in Latin America and the Caribbean are complex and varied, the pattern of development followed by most of the countries, with high levels of poverty, inadequate infrastructure, socio-economic exclusion and environmental degradation, is a decisive factor (ECLAC/IDB, 2000). Over the past four years, disasters caused by climatic phenomena have been particularly devastating in the region. They have revealed how vulnerable many countries are because of inadequate preparation and limited response capabilities, particularly small island developing States and other small developing countries.

In Central America, which is one of the most vulnerable subregions, the estimates of economic damage (quite apart from the loss of human life) caused by natural disasters that ECLAC has been carrying out since 1972 put the average annual cost at 2% of subregional GDP. In the Caribbean, one of the main variables explaining the volatility of the countries' output is the occurrence of natural disasters (Commonwealth Secretariat, 1997). Because they are islands and small in size, the countries of this subregion suffer from a high degree of economic and environmental vulnerability (ECLAC, 2000a, vol. 3, chap. 4).

These problems have been compounded by the emergence of new threats linked to global warming, such as changes in the distribution and intensity of precipitation and the possible intensification of droughts and flooding associated with El Niño and rising sea levels.

The vulnerability analyses carried out for Latin America and the Caribbean by IPCC allude to the difficulty of identifying common patterns of vulnerability to climate change, mainly because of the region's diversity in terms of climate, ecosystems, population distribution and cultural traditions.

In the Caribbean, low-lying islands and atolls are regarded as vulnerable, as are many of the countries, since much of their population, infrastructure and agricultural land are located in coastal areas. Natural ecosystems such as coral reefs, which are very sensitive to temperature increases, and mangrove swamps may also be adversely affected. It is expected that tourism, which accounts for over 50% of GDP in some of these countries, will be directly and indirectly affected. The loss of beaches (to erosion and flooding), the salinization of freshwater aquifers, damage to infrastructure and the loss of recreational activities (such as diving among coral reefs) could jeopardize the sector's viability and long-term sustainability. Health care systems may be put under greater pressure by the spread of heat-related diseases such as cholera and dengue.

In Latin America and the Caribbean, possible changes in the El Niño cycle may have negative effects on agriculture and fisheries in a number of the region's countries. Changes in precipitation patterns could reduce the availability of water resources in some areas that already face shortages, with negative implications for agriculture, the drinking-water supply and energy production. Other effects mentioned by IPCC include possible declines in the yields of important crops, which would jeopardize subsistence agriculture in some countries, and the spread of certain infectious diseases (malaria, dengue, cholera), with all the extra stress this would put on the countries' health care systems.

Vulnerability may be increased by cumulative events, such as recurrent or cyclical disasters, or when multiple pressures reduce the ability of human or environmental systems to withstand or adapt to change (Clark and others, 2000). Considering the poverty and inequality that characterize the region, and the importance of natural resources for its production and exports, the effects of the economic globalization process will be key in reducing vulnerability to environmental threats. If this process results in less poverty, exclusion and inequity in the countries and enables the region to use its natural resource endowment sustainably, Latin America and the Caribbean will be better able to adapt to the environmental changes it will face in this century, and vulnerability may diminish as a result. If the region's economic, social and environmental conditions worsen, however, environmental change may have very adverse effects on the most vulnerable communities, which are the most sensitive to such events and the least able to adapt and respond to them.

VI. Changes in national and regional environmental management institutions and governance

1. Institution-building

Efforts to create modern environmental institutions in the region were given their initial impetus by the 1992 United Nations Conference on Environment and Development, or Earth Summit. Subsequently, the countries felt the need to establish higher-ranking environmental authorities in the form of ministries or authorities of a similar level created from existing coordinating committees (ECLAC/UNEP, 2001). This need for a national institutional framework to oversee compliance with sustainable development commitments also influenced existing subregional partnership and integration arrangements, as well as emerging ones. As a result, the quest for environmental protection and sustainability has gradually been adopted as a political objective of regional and subregional processes, under different institutional structures.

The 1980s were a period of great difficulty for environmental management. The adjustments resulting from the economic crisis that struck the region affected its recently created environmental institutions, which were weak to begin with, leaving them with great responsibilities but few resources with which to address them. In the 1990s, the region underwent an intense democratization process in parallel with economic reform.[10] In almost all the countries, furthermore, civil society became an important counterpart for government institutions in areas such as health, the environment and human rights. The environment became a grass-roots social issue involving many volunteer groups at the local, national, regional and world levels. As a result of this ever-increasing environmental awareness, national approaches to the issue were reviewed and adapted. The Earth Summit strengthened internal debate about the different aspects of sustainable development, in the light of the negotiations on Agenda 21, the Convention on Biological Diversity, the United Nations Framework Convention on Climate Change and the United Nations Convention to Combat Desertification in those Countries Experiencing Serious Drought and/or Desertification, particularly in Africa. Scientists and public-sector, private-sector and social organizations mobilized and participated to an unprecedented degree (ECLAC, 2000a).

The global conventions concluded since 1992 have also resulted in a number of important institutional changes and innovative cooperation mechanisms. For example, most of the countries have set up specific bodies such as commissions, institutes or national programmes on biodiversity in response to the convention on this subject. New types of environmental assessment are being carried out, such as the national communications on greenhouse gas inventories submitted by each country in accordance with the United Nations Framework Convention on Climate Change.

Regionally, the countries' environmental authorities have set up the Forum of Ministers of the Environment of Latin America and the Caribbean, which consists of the 33 ministries or equivalent authorities. The work of the Forum of Ministers is strengthened by the support of the Inter-Agency Technical Committee created in 1999 by ECLAC, UNDP, UNEP, the World Bank and IDB, whose main task is to support the recommendations and objectives that the member countries of the Forum have accepted under the Regional Plan of Action agreed upon in Lima in 1998.

Subregionally, three processes can be distinguished. The first is the inclusion of sustainable development in economic integration agreements, as reflected in the resolutions of the Andean

[10] Acuña (2000) reveals that in nine of the region's countries no direct relationship of cause and effect can be identified between economic reform and changes in environmental regulations. Nonetheless, there are some instances of positive change in the regulatory and institutional frameworks governing environmental issues. These occurred primarily in countries that began reforming later or where democratic government was restored.

Community, MERCOSUR, the Central American Integration System and the Caribbean Community (CARICOM).

Secondly, there are the subregional treaties whose aim is the conservation of shared natural resources and which include sustainable development considerations; examples of these include the Regional Seas Programme, the Treaty for Amazonian Cooperation and the agreements arrived at by the Central American Commission on Environment and Development (CACED) (ECLAC, 2000a).

Thirdly, the Programme of Action for the Sustainable Development of Small Island Developing States, adopted in Barbados in 1994, deserves particular attention. The special characteristics of these States prompted the United Nations to draw up a programme of action for making sustainable development viable in such countries. The Caribbean countries gave strong support to this new instrument and established their own model for applying the Programme of Action, giving substance to the agreements adopted at the 1997 Caribbean Ministerial Meeting on the Implementation of the Programme of Action for the Sustainable Development of Small Island Developing States. The subregion thus decided to develop and implement mechanisms that would help overcome the financial, technical and other barriers identified as obstacles to the achievement of sustainable development in the island States of the Caribbean, with particular attention to vulnerability.

2. Challenges for the future

The institutional development and environmental management capabilities achieved by the countries so far, however, have not been enough to contain the environmental costs of economic expansion and urban concentration on the scale and of the nature seen in the region over recent decades. The countries still need to enhance their institutional platforms and capabilities considerably if they are to achieve effective control of the negative externalities affecting the regional environment as a result of the current development style. This observation should sound a warning about the challenges involved in building the political consensus needed to underpin stable economic growth. This consensus should embrace the need for greater investment, resource allocation, improvements to policy instruments and innovations in public-sector management to rectify the major shortcomings identified above and to halt existing patterns of environmental degradation. In view of the trends that have been documented, the countries of the region will be unable to prevent a steady decline in the quality of their environment and natural resources unless they make a systematic effort, and allocate more resources, to improve the effectiveness of environmental management in the years ahead.

Given these institutional shortcomings in the environmental sphere, it is disturbing to note, at the same time, the tendency of some countries towards policy failures such as tax competition[11] to attract investment in primary sectors such as mining. This competition has even led some countries to give tax relief on economic rents associated with the exploitation of non-renewable resources, matching the tax treatment of these primary sectors with that of the rest of the economy. Tax relief for rents associated with the exploitation of non-renewable resources is a distortion that may exacerbate the concentration of economic activity in primary and natural resource sectors. Distortions of this nature may have perverse environmental effects for the region, as they could lead to yet greater specialization in environmentally sensitive sectors at a time when the region still does not have a system of environmental institutions that is fully able to deal with the negative externalities of this phenomenon.

[11] "Tax competition" may occur among countries, among states in a federal system or even among municipalities, when they compete to attract investment by offering favourable tax treatment.

3. Changes in environmental financing

Although there are differences among countries, total environmental spending by both the public and private sectors generally does not exceed 1% of GDP, and national public-sector environmental spending rarely tops 3% of total public spending. As a result of administrative decentralization, many environmental expenses are now met by provinces or states, whose environmental budgets may represent a slightly higher percentage of the total than is the case nationally. It is at the municipal level, however, that the environmental budget is particularly important, as it is usually municipalities that are responsible for collecting household waste, treating sewage, etc. (ECLAC/UNDP, 2001).

Public-sector environmental budgets have fluctuated sharply over the past decade and in many cases have shown a tendency to fall, mostly because of the position of public finances and the weakness and discontinuity of environmental governance. Budget deficits and the need to generate resources to meet external obligations have generally resulted in budget cuts, to which environment-related areas are extremely vulnerable. Dependence on credit for financing has also lowered the quality of the environmental budget by increasing the proportion of financing costs in the total.

Furthermore, the need to obtain fresh resources to finance environmental spending means that the environmental agenda is permeated by the interests of donor or lender countries or institutions. Thus, the “green” agenda in Brazil receives far more funding than programmes to solve urban environmental problems. In Argentina, the five jurisdictions most favoured for environmental investment are the ones that attract the most international tourism.

The impact of international donations and loans on the public-sector environmental budget varies greatly among the region’s countries. In the largest ones, their amount is generally very small in comparison to locally generated resources, and is tending to decline (Colombia is an exception, however). In smaller countries, though, and particularly in the Caribbean, external assistance is essential both for public-sector environmental agencies and for the non-governmental organizations that often play a vital role in environmental initiatives.

An important development in the region, lastly, is the appearance of private funds specializing in environmentally friendly projects that combine economic or monetary interests with “green” ones.

VII. Changes in international environmental governance

Economic globalization is creating a new relationship between the market and the State, and this is having major effects on world environmental management by creating new imperatives that oblige States to cooperate in administering global public goods and to improve the coordination of their regional and national environmental policies. Furthermore, “global civil society” and transnational corporations are playing a more prominent role in some of these multilateral processes.

Two types of international environmental regulations can be distinguished: those aimed at protecting the supply of global public goods and those aimed at incorporating environmental clauses into other types of international agreements. In the first group are multilateral environmental agreements (MEAs) on various issues, such as biological diversity, climate change and protection of the ozone layer. The second group includes environmental regulations associated with free trade and integration agreements, such as the environmental agreement linked to NAFTA and the environmental rules of the European Union.

In contrast to the multilateral trading system, the management of international environmental affairs is weakly structured and lacks coherence. In the past 20 years there has been a huge proliferation of intergovernmental institutions within and outside the United Nations system. This process accelerated after the Earth Summit, when new bodies were established within the system. These included the Commission on Sustainable Development and the secretariats of the conferences of the parties to at least five multilateral conventions (the Convention on Biological Diversity, the United Nations Framework Convention on Climate Change, the United Nations Convention to Combat Desertification in those Countries Experiencing Serious Drought and/or Desertification, particularly in Africa, the Rotterdam Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade and the Stockholm Convention on Persistent Organic Pollutants), as well as the Global Environment Facility[12]. The expansion of multilateral environmental treaties and the proliferation of forums and secretariats for these treaties and of intergovernmental bodies set up to monitor them underscore the need to rationalize the international governance of sustainable development.

To this end, countries are considering the advisability of carrying out a gradual evaluation with a view to harmonizing different processes that have similar subjects and objectives, such as biodiversity, the chemicals agenda and the ozone layer, among others. Analyses of the scope for linking together environmental agreements negotiated prior to the Rio Summit (such as the Convention on International Trade in Endangered Species of Wild Fauna and Flora, the Convention on Wetlands of International Importance Especially as Waterfowl Habitat and the Convention on the Conservation of Migratory Species of Wild Animals) within broader frames of reference (the Convention on Biological Diversity) have been carried out and should be considered as one approach to achieving greater consistency and avoiding duplication among agreements with converging objectives. The agreements on the protection of biodiversity (species and ecosystems) are a particularly clear instance, since they all overlap in geographical terms as well (ECLAC/UNEP, 2001).

One of the most controversial proposals is for the creation of a world environment organization with powers of sanction like those of the World Trade Organization (WTO). Proponents of this idea claim that an organization of this type would ensure compliance with international environmental agreements and relieve the growing pressure on WTO to take responsibility for environmental matters. Arguments against the proposal include, on the one hand, the lack of international political will to undertake an initiative of this kind and, on the other, the risk that such an organization might widen the gap between environmental issues and economic and social ones, which is the opposite of what the international sustainable development agenda has been seeking since the first half of the 1990s.

The international financial support and domestic resources mobilized for sustainable development have clearly been inadequate. The concessionary contributions made by GEF and the Multilateral Fund of the Montreal Protocol obviously provide only a fraction of the resources needed to solve global environmental problems. Moreover, the official development assistance pledged at the Earth Summit to support the most vulnerable countries has dwindled greatly. It consequently needs to be reaffirmed that the transition to sustainable development will require new and additional resources and innovative and stable financial mechanisms that can facilitate the development of endogenous capacity and the transfer of innovative technologies to developing countries.

The negotiation and implementation of international environmental agreements has also been heavily influenced by economic factors. The cost of implementing them, the way this cost is distributed and the effects it may have on the competitiveness of particular countries have hindered the full implementation of the Kyoto Protocol to the United Nations Framework Convention on

[12] The Global Environment Facility (GEF) was set up in 1991 to enable developing countries to fund the additional expenses they must incur to address environmental problems of worldwide impact (loss of biodiversity, climate change, depletion of the ozone layer and other problems connected with international waters and desertification).

Climate Change. The relationship between environmental agreements and trade agreements is also a source of problems. During the negotiations on the Cartagena Protocol on Biosafety, which regulates cross-border movements of genetically modified organisms, one of the most controversial subjects was the relationship between the Protocol and global free trade agreements, and the question of which would prevail if they were incompatible. Neither this Protocol nor other international environmental agreements have any global mechanism for resolving the conflicts with trade agreements that are arising with increasing frequency (Brañes and Rey, 2001).

Developing countries are also under growing pressure to incorporate environmental components into trade agreements. In the region, this tendency has manifested itself most clearly in the environmental agreement paired with NAFTA and in the Canada-Chile Free Trade Agreement; despite resistance from the Latin American countries, it has also emerged in the Free Trade Area of the Americas (FTAA) negotiations. As mentioned in an earlier section, environmental issues are now strongly represented in subregional integration agreements.

The main objectives of including environmental issues in trade and integration agreements are to prevent the emergence of competitive advantages deriving from lax environmental standards ("environmental dumping") and to ensure that environmental legislation is not used for protectionist purposes. In relation to the first of these issues, it has been argued that the pressure to sustain competitiveness, to which countries are subjected by globalization, may prevent governments from taking steps to internalize environmental costs and improve environmental performance if this entails higher costs for domestic producers (Zarsky, 1997). These disputes are of long standing.[13]

The only international organization competent to deal with the interaction between trade and the environment is the WTO Committee on Trade and Environment. Since its establishment in 1995, however, its environmental debates have remained purely analytical —and even defensive— in nature, to prevent the emergence of trade barriers based on environmental issues,[14] and it has not fostered any initiatives to achieve positive synergies between trade, the environment and the promotion of sustainable development (Panayotou, 2000).

Nonetheless, the recent adoption of the Doha Ministerial Declaration launching a new round of WTO trade negotiations has increased the scope and depth of the environmental issues that will be considered within WTO. In fact, unprecedentedly for WTO, the new Declaration provides for immediate negotiations on three environmental issues: (a) the relationship between WTO rules and specific trade obligations under MEAs; (b) the development of procedures for regular information exchanges between MEA secretariats and the relevant WTO committees; and (c) the reduction or, as appropriate, elimination of tariff and non-tariff barriers to environmental goods and services.

Meanwhile, the Committee on Trade and Environment and the Committee on Trade and Development were mandated to act as a forum to identify and debate development and environmental aspects of the negotiations "to help achieve the objective of having sustainable development appropriately reflected" in the negotiations. The members also agreed to broaden the mandate of the Committee on Trade and Environment to authorize it to make recommendations to the next Ministerial Conference with respect to future action and possible negotiations on the effect of environmental measures on market access, relevant intellectual property rights issues and eco-labelling requirements.

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[13] For example, in 1971, during the preparations for the United Nations Conference on the Human Environment, held in Stockholm in 1972, a study which the secretariat of the General Agreement on Tariffs and Trade (GATT) was asked to prepare revealed the concern among trade authorities that environmental policies would become obstacles to trade.

[14] Under this "defensive" strategy, one of the Committee's main areas of work is the analysis of MEA-related trade restrictions.

VIII. An agenda for action

1. Consolidating national environmental management mechanisms and strengthening institutional capacity to cope with the trends observed

Although the region has made significant progress in developing environmental institutions and laws, there is still a need to further strengthen environmental management capabilities and instruments. As has been argued in this chapter, the countries' efforts to strengthen their environmental management capacity and instrumentation have not kept pace with the challenges raised by Agenda 21 (United Nations Conference on Environment and Development, 1992). This gap is reflected in the persistence of trends towards environmental deterioration in the region. In the 1990s, it became even more urgent to find responses to the new challenges resulting from the productive restructuring driven by globalization. These new challenges are related to the need to develop environmental management capacity to deal with the externalities of growing specialization in natural resource sectors, to control pollution in the fastest-growing sectors, and to introduce new management practices and cleaner production technologies. The countries therefore face the twofold challenge of modernizing their institutional platforms, instruments and management capacity both to achieve the targets set out in Agenda 21 and, at the same time, to face up to the new challenges created by increased participation in the global economy.

To respond effectively to these challenges, the countries will have to invest in improving the capacity of their environmental authorities to implement cost-effective environmental management options, inter alia by formulating clear national agendas, identifying priorities, mobilizing resources and consolidating mechanisms to ensure that environmental management operates on a cross-sectoral basis at all levels of government. There are also opportunities to expand the application of economic and fiscal instruments that give out more realistic price signals to economic agents for the use of natural resources (see below). This requires investment to improve the technical and analytical capacities of environmental authorities to take the lead in designing economic and fiscal environmental management instruments within the government apparatus. Continued efforts are also needed to improve oversight to ensure that existing regulations are complied with and to generate better environmental information and statistics with a view to identifying and prioritizing the problem areas to which national environmental management resources should be channelled, detecting signs of deterioration in environmental quality and anticipating productive restructuring processes that require specific environmental management measures.

2. Developing institutional capacity and mechanisms to reduce the region's vulnerability to natural disasters

Another challenge faced by the region, and particularly the countries of Central America and the Caribbean Basin, is the need to develop institutional capacity and mechanisms to reduce vulnerability to natural disasters. The frequency of extreme hydrological and climatic events has increased over the past two decades. Although there is no scientific certainty that this recent rise in climatic volatility is associated with the increased concentration of greenhouse gases in the atmosphere, the countries must prepare to face scenarios in which events of this type are more frequent, and take steps to reduce their vulnerability accordingly.

Some of the measures that the countries can take are: establishing national vulnerability reduction mechanisms that include monitoring, early warning and response capabilities for extreme natural events; developing the capacity to identify and map areas that are at risk from different types of natural events owing to their socio-economic, hydrological and geographical characteristics; and taking land-use planning and other measures to reduce vulnerability and properly manage identified risk areas. The countries of the region also need to take a more proactive approach to multilateral negotiations in pursuit of stronger international action to mitigate and adapt to climate change, including the ability to access funds and technical assistance for adaptation and mitigation projects.

3. Developing institutional capacity and mechanisms for the sustainable management of natural and energy resources

Latin America and the Caribbean face the prospect of increasing deregulation in a number of economic sectors. Without prejudice to the objectives pursued by deregulation, in the natural resource and energy sectors there are sound reasons for the countries to undertake analyses of possible scenarios and long-term trends. Some trends will be more desirable than others, depending on each country's sustainable development priorities. Policy directions that are credibly aimed at long-term goals may be useful in giving the desired shape to the current dynamic and subsequent development of these markets.

Actions that the countries could take include developing national capacity and mechanisms to complement the current deregulation processes in natural resource and energy sectors with scenario analyses and assessments of long-term sustainability trends. Developing analytical capacity and formulating long-term policy guidelines nationally and regionally would be particularly useful in sectors such as water management and supply, the region's energy future and the fishing and forestry sectors. Some of the models adopted by the industrialized countries may be helpful for this purpose,[15] but there are also experiences in the region that can provide the basis for a collective learning process.

4. Innovative ways to finance the attainment of sustainable development goals

The achievement of sustainable development goals[16] requires the investment of an enormous amount of resources, which the countries have not succeeded in mobilizing over the past decade. In the current economic environment, the countries will have to launch innovative initiatives to close this financing gap.

Where the mobilization of domestic resources for sustainable development is concerned, the countries must come up with a growing volume of internal funding to finance their goals. If this is to happen, changes to the tax regime to further these goals, as exemplified by the "green" tax reforms already being implemented by a number of countries,[17] will have to play a preponderant role in these efforts in the coming years. The countries of Latin America and the Caribbean have the opportunity to introduce specifically environmental components into future tax reforms. Various options are available: (a) using environmental taxes, charges and tariffs as incentives to prevent environmental damage and internalize the social cost of activities that have an environmental impact; (b) levying environmental taxes and charges for the use of natural resources, for revenue-generating purposes;[18] and (c) designing the tax system in such a way as to encourage optimum use of natural resources.

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[15] The European Union has drawn up guidelines for the energy structure that it plans to achieve in 10 years, as a means of encouraging investment in technological development among firms seeking to supply the innovation necessary to meet these policy goals. A similar technological development process took place in the United States in the 1970s and 1980s in response to the goals contained in the Clean Air Act, which led to the development of the catalytic converter.

[16] At the United Nations Conference on Environment and Development, held in Rio de Janeiro in 1992, it was estimated that to achieve the goals laid down in Agenda 21, the developing countries would have to mobilize an extra US$ 560 billion a year (United Nations, 1993).

[17] Denmark, Finland, Germany, Italy, Netherlands, Norway, Sweden, Switzerland and the United Kingdom (OECD, 2000, p. 4).

[18] Or earmarking the revenue for environmental infrastructure investment and management activities, in countries that implement tax hypothecation policies.

The experience of the region's countries with environmental taxes and charges is only incipient as yet. The identification of concrete opportunities to introduce and apply these new instruments as part of fiscal and administrative systems will undoubtedly command more attention in the near future.

As regards the mobilization of international resources for sustainable development objectives, the countries could join forces to relaunch the debt-for-nature swap initiative or some other mechanism that eases the financial burden of external debt and frees up resources for uses that create positive global externalities. There is also potential in collective negotiations to give greater political priority to increasing transfers of concessional resources to fund the objectives laid down in Agenda 21, in accordance with the official development assistance (ODA) targets set by the United Nations. Likewise, the countries should work towards common positions in order to participate effectively in multilateral negotiations to consolidate mechanisms for capturing the economic value of the global public goods and environmental services provided by the region, as detailed below.

5. Consolidating international markets for global environmental services and building regional capacity to participate actively in them

Latin America possesses natural resources and ecosystems of global importance, and this makes the region a very important supplier of global environmental services. Examples of global environmental services include the major contribution made by the huge Amazonian forest mass and other regional ecosystems to stabilizing the climatic system by acting as sinks for atmospheric CO_2 in the biogeophysical carbon cycle, as well as the contribution made by Latin American ecosystems, several of which are characterized by the highest level of biodiversity, to the preservation of genetic resources. To date, the absence of markets through which the economic value of these global environmental services can be captured has jeopardized the region's ability to reverse the degradation of its natural capital and secure a flow of resources to offset the opportunity cost of preserving it.[19]

The region needs to find mechanisms that will yield a steady flow of international resources to finance efforts to preserve and manage its natural resources and ecosystems of global importance. Without a stable flow of resources it will not be possible to make the investments needed to guarantee the continued provision of these global environmental services. The Clean Development Mechanism is the first international initiative to create an international market of this type. From a strategic point of view, the region should actively work to consolidate this first global initiative to create a market enabling the capture of the economic value from the climate stabilization services the region provides to the international community. This would set an important precedent for future progress in the same direction and for the inclusion of similar measures in new international agreements, particularly those on the conservation of biodiversity.

Countries should play a proactive role in the multilateral negotiations associated with the United Nations Framework Convention on Climate Change and the Convention on Biological Diversity, with a view to consolidating suitable mechanisms for capturing the economic value of global environmental services. They should also build their capacity to capitalize on the opportunities opened up by these new market mechanisms through domestic promotion and training efforts focusing on those sectors that have the greatest potential for generating the projects concerned. These efforts require that the State should play an active role, as the economic

[19] When it is not possible to capture economic value from the conservation of these natural resources, the pattern of microeconomic incentives induces countries to devote natural ecosystems to low-profit economic uses such as extensive stockbreeding and subsistence agriculture (see the second section of this chapter). These changes in land use are often irreversible and tend to deplete the natural capital base.

opportunities created by an incipient market of this type are not apparent to national economic agents or to traditional financial institutions. The promotional and catalytic role of seed funding from multilateral and regional organizations[20] will be critical in the early start-up and consolidation phases of these markets, until they acquire enough momentum to mobilize funds on their own.

6. Increasing the absorption of cleaner production technologies through existing foreign investment and trade links and domestic investment in research and development

The recent wave of technological innovation represented by new cleaner production technologies, low-emissions transport technologies, energy efficiency technologies and renewable sources, and the new markets to which they have given rise, will exhibit significant dynamism over the coming decades. If the Latin American and Caribbean countries are to be promptly inserted into these markets, they need to seek mechanisms for accelerating the absorption and spread of these new technologies.

Countries can seize opportunities for absorbing clean technologies through existing investment processes and new links with countries at the forefront of these technologies. These objectives should be an integral part of trade and FDI strategies, which should combine environmental impact assessments for new investments with commitments to introduce and diffusion clean technologies. In broader terms, measures should be taken to encourage the diffusion of new cleaner production processes and technologies from the leading firms through each country's production chains (e.g., SMEs, suppliers and consumers). The establishment of cleaner production centres to disseminate information and promote local technological development and pilot demonstration projects in different sectors is another line of action that could be pursued in support of these objectives. A number of countries in the region already have successful models of this type.

7. Strengthening political commitment to sustainable development goals among all social actors nationally, regionally and globally

Finally, it must be recognized that, unless an unremitting effort is made to inform and educate all social actors, the goals of sustainable development will not become a priority on the political agenda of our countries. Progress in meeting sustainable development goals can only be made if the public is informed and civil society is proactive in the pursuit of its right to live in a healthy environment and to halt existing environmental degradation trends. Much effort is still needed to give sustainable development goals greater relevance and importance in the Latin American and Caribbean political arena.

Some of the measures that the countries can take to strengthen domestic political commitment to sustainable development goals are: introducing the concept of sustainable development at all levels of national educational systems; widely publicizing national sustainable development goals and indicators of progress or setbacks in relation to them; giving national sustainable development goals greater weight in the public consciousness as a political objective and a citizen entitlement; investing in research, data generation and analysis of national trends in relation to sustainable development goals, so that public opinion has a factual basis on which to assess national trends and form its own judgements; and continuing to strengthen democracy and channels of communication through which all social groups can assert their priorities and, in a broad sense of the term, their rights.

[20] For example, the World Bank's Prototype Carbon Fund and the Andean Development Corporation's financing line for Clean Development Mechanism projects.

Chapter 10

Globalization and social development

The recent phase of globalization has drawn increasing attention to the region's persistent social deficits, particularly in education, employment and social protection. These are the three critical areas in which virtuous circles can be generated that enhance capacity for participating in the globalized world and for constructing and benefiting from economic development. Globalization also poses new challenges, stemming mainly from technological change and the volatility of labour market conditions. Thus, education, employment and social protection are the pillars of a proactive social policy aimed at the implementation, in the new context of globalization, of the universal principles enshrined in human rights declarations and United Nations world summits.

I. Educational deficits and gaps in the region

At a time of increasing innovation and an expanding knowledge frontier, education presages the destiny of both individuals and societies. In social terms, the changes generated by globalization and new production patterns call for human resources capable of participating in the new modes of production, work and competition. Education is essential not only to enable people to share in the benefits of progress, but also to enable economies to ensure sustained development through competitiveness based on more intensive knowledge use. Education is also an entitlement enshrined in international declarations on human rights.

ECLAC has argued that education is one of the best ways to ensure productive growth with social equity, and to strengthen democracies based on the broad and non-exclusive exercise of citizenship (ECLAC, 1992b and 2000a). Education is the key to reducing inequalities, and the best way to prevent the intergenerational reproduction of poverty. Education affords access to quality jobs, participation in knowledge networks and involvement in the information revolution, and it offers escape from the vicious circle of poverty. Education also provides the tools for a critical reassessment of reality, design of new collective projects, learning to live in a multicultural world, and the formation and exercise of citizenship, particularly in the knowledge society (ECLAC, 2000a, chap. 3).

Although some progress has been made, education in Latin America and the Caribbean continues to display wide gaps in achievement (quantity and quality) and returns. These are largely based on income level and geographical location, whereas the gender gap, especially in terms of access, has almost completely been overcome. Highly stratified access to education reproduces income inequalities, instead of correcting them; and this, together with its effects on labour market participation and potential for upward mobility, partly explains the high degree of rigidity that exists in the region's current social structure. Internationally, the education gap between Latin America and the Caribbean and both developed and emerging economies in Asia has widened.

1. Progress in terms of coverage

Primary school enrolment rates have risen to over 90%, but rates remain low at other educational levels (70% in secondary and 26% in post-secondary education; see table 10.1).[1] Gender differences are minor at all levels, and in fact coverage rates nowadays tend to favour the female population. Among income groups, enrolment is highest in the wealthiest quartile at all education levels. In every country enrolment is greater in urban areas than in rural ones —regardless of age group, sex or income quartile— and the differences increase as the education level rises.

Primary school enrolment rates vary from 95% or more (Chile, Panama and Venezuela) to below 75% (Guatemala). Coverage tends to be similar between boys and girls, with differences no larger than two percentage points in most countries, with no definite pattern. On average, enrolment is five percentage points higher in urban areas than in rural ones, although differences exceed 10 percentage points in El Salvador, Guatemala and Honduras. Enrolment differentials across income groups are smallest at the primary level (seven percentage points), ranging from two percentage points between the highest and lowest quartiles in Chile to 15-19 points in El Salvador, Guatemala and Honduras. There is greater uniformity between income groups at the primary level, with enrolment gaps generally narrowing over the last decade, especially in Brazil, although they have widened in Colombia, Honduras and Venezuela.

[1] All the statistical information presented below has been calculated by ECLAC on the basis of national household surveys. Age ranges and educational levels are assimilated as follows: 6-13-year-olds with primary education; 14-17-year-olds with secondary education; and 18-25-year-olds with higher education. The averages presented are calculated as simple means of national figures. As information for some countries, is incomplete, it is impossible to estimate, for example, rural data or a year at the start of a decade to serve as a basis for comparison. The text mainly mentions trends in countries that have nationwide data.

Table 10.1
LATIN AMERICA AND THE CARIBBEAN (17 COUNTRIES): SCHOOL ENROLMENT BY AGE GROUP AND SEX, AND BY AGE GROUP AND FAMILY INCOME a/**, 1990 AND 1999**
(*Percentages*)

Country	Year	Age group									Age group					
		6 - 13 years			14 - 17 years			18 - 25 years			6 - 13 years		14 - 17 years		18 - 25 years	
		Total	Men	Women	Total	Men	Women	Total	Men	Women	C1	C4	C1	C4	C1	C4
Argentina	1990															
	Urban	97.2	97.7	96.9	-	-	-	-	-	-	96.6	99.6	-	-	-	-
	1999															
	Urban	99.2	99.0	99.3	85.1	83.4	86.9	42.4	39.4	45.3	98.8	99.7	80.1	95.9	28.2	58.3
Bolivia	1989															
	Urban b/	94.8	94.9	94.7	87.1	90.4	84.1	46.6	52.5	41.6	93.9	96.0	88.5	82.5	49.5	48.7
	1997															
	Nationwide	93.0	93.5	92.6	77.5	79.1	75.9	37.2	39.2	35.3	90.4	97.0	73.8	82.1	31.9	44.0
	Urban	96.0	96.0	96.1	88.4	89.2	87.7	48.6	50.7	46.7	94.3	99.1	89.7	87.6	45.1	54.9
	Rural	88.6	89.7	87.5	55.3	60.0	50.3	9.1	12.3	5.9	84.5	94.0	46.3	70.3	8.1	15.2
Brazil	1990															
	Nationwide	83.0	82.1	84.0	61.9	58.6	65.2	20.9	19.4	22.4	75.9	94.4	54.6	77.0	13.8	32.7
	Urban	88.1	87.4	88.8	69.0	66.4	71.6	24.1	22.9	25.3	80.7	94.4	59.4	77.0	15.6	32.7
	Rural	69.5	68.2	70.8	41.0	37.5	44.9	9.2	7.8	10.9	63.4	85.4	39.6	51.6	6.9	13.8
	1999															
	Nationwide	94.6	94.2	95.1	81.7	81.5	81.9	31.6	31.0	32.2	92.5	98.5	76.8	92.8	25.0	47.5
	Urban	95.6	95.3	95.9	84.2	83.8	84.5	33.5	33.1	33.9	93.3	98.9	77.3	95.4	26.0	51.3
	Rural	91.6	90.9	92.3	73.2	73.8	72.5	23.1	22.5	23.8	89.8	96.2	75.2	80.2	19.9	29.0
Chile	1990															
	Nationwide	96.7	96.4	96.9	80.4	80.3	80.4	22.0	24.2	19.9	95.6	98.6	76.0	89.5	15.9	34.2
	Urban	97.8	97.6	98.0	86.0	86.0	86.0	25.1	28.2	22.2	96.8	99.2	80.7	94.7	17.6	39.0
	Rural	92.0	91.7	92.3	56.4	56.7	56.2	7.8	7.2	8.4	90.8	95.8	53.1	64.6	7.6	9.7
	2000															
	Nationwide	98.6	98.6	98.5	90.0	90.0	90.1	33.9	35.6	32.3	97.9	99.7	85.7	97.2	21.8	53.1
	Urban	98.9	99.0	98.9	91.9	91.8	92.1	36.2	38.5	34.1	98.3	99.8	87.3	98.0	22.5	55.9
	Rural	96.4	96.2	96.5	78.7	79.1	78.3	18.7	17.7	19.7	95.3	98.2	76.5	89.2	16.7	27.5
Colombia	1991															
	Nationwide	83.4	82.4	84.4	62.7	60.3	65.0	22.6	22.8	22.5	81.0	86.8	62.5	63.0	19.4	28.4
	Urban	91.4	90.7	92.1	76.7	77.9	75.5	29.5	30.4	28.9	87.8	95.4	74.6	77.8	22.7	41.4
	Rural	74.4	73.2	75.7	45.9	40.8	51.4	11.9	12.1	11.7	72.1	77.8	45.2	48.7	14.1	11.6
	1999															
	Nationwide	90.5	89.6	91.4	69.7	68.6	70.8	24.5	24.9	24.2	87.9	94.5	67.8	75.1	18.4	37.7
	Urban	93.6	92.7	94.5	77.8	77.9	77.7	29.3	30.1	28.7	89.9	98.0	73.3	86.6	19.3	50.2
	Rural	86.5	85.8	87.3	57.8	55.6	60.1	15.1	15.9	14.3	85.0	89.9	58.0	60.9	16.5	15.4
Costa Rica	1990															
	Nationwide	86.5	86.5	86.5	52.0	53.1	50.6	19.4	19.9	18.9	84.0	92.2	45.8	63.3	14.3	28.2
	Urban	90.4	89.9	90.8	72.5	72.7	72.2	32.2	34.4	30.0	88.1	95.6	62.0	88.8	21.7	50.4
	Rural	83.6	84.1	83.1	36.7	38.3	35.0	9.7	9.3	10.3	80.9	89.5	32.5	46.2	7.7	14.9

Table 10.1 (continued)

Country	Year	Age group									Age group					
		6 - 13 years			14 - 17 years			18 - 25 years			6 - 13 years		14 - 17 years		18 - 25 years	
		Total	Men	Women	Total	Men	Women	Total	Men	Women	C1	C4	C1	C4	C1	C4
	1999															
	Nationwide	94.2	94.4	94.0	64.5	61.9	67.0	29.8	28.0	31.5	92.6	98.2	59.3	78.2	19.7	42.5
	Urban	97.5	97.4	97.6	76.3	73.4	79.1	40.6	38.2	42.9	97.0	99.6	68.4	94.7	27.6	57.3
	Rural	91.9	92.3	91.5	54.2	52.2	56.2	19.5	18.6	20.3	89.2	97.2	48.7	68.0	10.8	30.6
Ecuador	1990															
	Urban	96.3	95.9	96.7	81.1	79.2	83.0	40.2	39.9	40.4	95.9	98.3	81.3	84.1	40.1	45.1
	1999															
	Urban	92.5	92.4	92.6	77.2	76.6	77.8	33.1	33.6	32.6	90.9	97.6	70.6	88.7	24.2	50.0
El Salvador	1990															
	Urban	89.0	89.1	88.9	73.0	73.4	72.7	28.6	31.3	26.6						
	1999															
	Nationwide	85.2	85.2	85.1	65.3	67.1	63.5	22.3	23.3	21.3	78.9	94.7	60.1	76.1	13.9	33.3
	Urban	91.5	91.2	91.8	77.3	77.4	77.1	30.2	31.5	29.0	84.5	97.9	70.0	90.8	18.0	48.5
	Rural	78.4	78.8	77.8	51.2	55.9	45.9	10.6	11.5	9.7	72.3	90.9	46.7	61.5	7.2	14.6
Guatemala	1998															
	Nationwide	69.4	70.3	68.3	41.9	45.1	38.7	15.9	17.7	14.3	63.2	80.2	32.7	55.4	7.5	27.2
	Urban	77.9	78.9	76.9	63.5	66.0	61.1	27.5	30.1	25.2	70.1	86.0	45.3	83.3	11.6	45.0
	Rural	64.8	65.8	63.6	29.1	33.2	24.7	6.1	7.4	5.1	58.6	77.4	23.4	40.2	4.0	12.2
Honduras	1990															
	Nationwide	74.1	73.4	74.8	39.8	37.0	42.7	13.7	12.9	14.5	68.9	84.5	35.2	48.3	8.9	22.0
	Urban	83.3	82.9	83.8	58.1	57.1	58.9	25.3	25.1		77.6	93.6	49.4	72.7	17.1	
	Rural	68.5	67.6	69.3	26.9	24.1	29.9	3.3	3.3	3.3	63.2	78.8	25.5	30.0	2.3	6.3
	1999															
	Nationwide	81.6	79.7	83.5	44.7	41.2	48.5	16.3	14.4	17.9	75.9	91.9	38.7	54.8	9.6	24.9
	Urban	87.4	85.9	89.0	60.0	57.4	62.5	26.2	24.4	27.6	81.5	95.1	49.5	73.8	17.8	40.0
	Rural	77.7	75.7	79.7	32.4	29.0	36.3	5.9	5.0	6.7	71.9	90.0	28.4	41.1	1.6	9.5
Mexico	1992															
	Nationwide	91.8	92.6	90.9	56.0	57.0	55.0	19.5	21.7	17.5	89.0	97.3	48.8	69.5	9.4	30.7
	Urban	95.2	95.5	94.9	67.1	69.2	65.0	26.2	29.3	23.3	93.5	98.8	58.9	85.4	11.7	43.8
	Rural	87.9	89.7	85.8	41.0	40.8	41.1	8.2	8.3	8.1	83.5	95.3	31.4	52.1	5.1	11.0
	1998															
	Nationwide	94.6	95.6	93.7	60.1	62.0	58.3	21.0	23.5	18.7	91.2	98.8	47.7	78.0	11.0	35.2
	Urban	96.1	96.7	95.4	69.1	69.8	68.4	26.9	29.3	24.5	93.0	99.1	54.7	86.9	14.2	45.3
	Rural	93.0	94.2	91.7	48.5	52.4	44.4	11.0	13.2	9.0	89.3	98.4	38.3	65.7	5.0	19.4
Nicaragua	1993															
	Nationwide	74.3	72.2	76.5	54.9	54.0	55.8	20.6	22.6	18.7	68.3	86.9	44.7	63.8	16.1	27.8
	Urban	85.3	84.4	86.3	72.6	71.0	74.3	29.5	32.5	26.8	79.6	95.6	56.4	87.3	19.3	40.0
	Rural	62.4	59.1	65.9	32.2	32.6	31.8	8.9	10.4	7.5	56.1	77.5	27.1	43.5	10.6	13.8
Panama	1991															
	Nationwide	93.7	93.4	94.1	71.3	69.5	73.3	28.8	26.5	31.2	90.5	97.7	62.6	82.3	18.5	45.5
	Urban	95.6	95.1	96.0	77.5	76.4	78.6	33.6	31.9	35.2	92.8	98.9	68.4	86.2	21.9	52.3
	Rural	89.7	89.6	89.8	57.0	53.3	60.8	15.8	13.5	18.7	85.7	95.0	48.1	73.8	9.1	27.2

Table 10.1 (concluded)

Country	Year	Age group									Age group					
		6 - 13 years			14 - 17 years			18 - 25 years			6 - 13 years		14 - 17 years		18 - 25 years	
		Total	Men	Women	Total	Men	Women	Total	Men	Women	C1	C4	C1	C4	C1	C4
	1999															
	Nationwide	96.5	96.2	96.8	77.1	74.4	79.9	32.8	29.7	35.9	94.3	99.4	70.8	87.3	19.3	51.8
	Urban	97.4	97.5	97.3	80.9	79.2	82.6	37.0	33.3	40.6	95.1	99.6	74.1	89.3	21.6	56.9
	Rural	94.6	93.5	95.7	67.8	63.6	72.7	18.7	17.5	19.9	92.8	99.1	61.9	83.2	11.8	33.0
Paraguay	1999															
	Nationwide	93.1	92.8	93.3	66.6	65.2	67.9	25.4	24.7	26.1	90.9	97.3	58.3	77.9	14.4	42.3
	Urban	96.3	95.5	97.1	77.9	77.1	78.6	33.2	32.6	33.6	93.6	99.0	71.8	86.5	18.8	53.0
	Rural	90.0	90.4	89.6	55.2	55.4	55.0	13.9	14.6	13.0	88.5	95.6	46.0	67.6	8.9	25.1
Dominican Republic	1997															
	Nationwide	91.3	90.2	92.4	82.7	81.7	83.6	34.2	33.5	34.8	89.7	94.6	83.2	84.7	35.6	39.0
	Urban	93.0	92.2	93.9	85.6	82.2	88.4	38.8	38.5	39.1	90.4	96.9	87.3	87.8	35.8	43.9
	Rural	89.6	88.2	91.0	79.0	81.0	76.9	26.7	26.5	26.9	89.1	91.8	78.4	79.9	35.4	31.2
Uruguay	1990															
	Urban	98.0	98.0	98.1	75.0	71.8	78.3	30.7	27.7	33.3	96.9	99.7	64.2	90.8	15.2	53.2
	1999															
	Urban	97.9	97.9	98.0	76.5	72.9	80.0	31.7	27.3	36.2	97.0	99.8	65.3	96.1	15.0	60.1
Venezuela	1990															
	Nationwide	92.0	91.2	92.7	68.5	65.3	71.9	27.6	25.3	29.9	90.5	94.7	68.2	75.3	27.7	33.9
	Urban	93.9	93.3	94.6	72.8	70.4	75.2	30.6	28.5	32.8	92.5	96.4	71.5	81.0	30.4	38.1
	Rural	83.9	83.0	85.0	47.0	41.9	53.3	8.7	7.5	10.1	82.8	86.1	50.8	48.2	8.1	10.3
	1999															
	Nationwide	95.6	95.1	96.2	70.5	67.1	73.8	19.0	16.9	21.2	93.3	99.2	64.1	81.0	16.8	26.0
Average c/	1990 d/															
	Nationwide	87.6	87.3	88.0	61.6	60.1	63.0	21.8	21.6	22.1	84.4	93.3	56.7	71.1	16.0	31.9
	Urban	93.1	92.8	93.4	75.0	74.7	75.3	31.3	32.2	31.1	90.4	97.0	68.7	84.0	23.3	45.2
	Rural	80.8	80.6	81.0	43.6	41.6	45.6	9.4	8.8	10.2	77.1	88.2	39.3	52.4	7.5	13.5
	1999 e/															
	Nationwide	93.3	92.9	93.6	69.8	68.3	71.3	26.1	25.5	26.7	90.7	97.5	63.8	80.6	17.7	39.8
	Urban	95.3	95.1	95.5	78.2	77.2	79.2	34.3	33.9	34.8	93.0	98.6	71.0	89.7	23.3	53.5
	Rural	90.2	89.8	90.7	58.9	58.0	60.1	16.0	15.8	16.2	87.6	95.6	55.3	69.7	11.7	23.5

Source: ECLAC, on the basis of special tabulations of household surveys conducted in the respective countries.

a/ C1 and C4 correspond to the first and fourth quartile of the per capita household income distribution, respectively.
b/ Eight main cities.
c/ Averages calculated with figures from countries that have comparable data for the two years considered. Thus, the nationwide average excludes Bolivia, Dominican Republic, Ecuador, El Salvador, Guatemala, Nicaragua, Paraguay and Uruguay; the urban average excludes Argentina, Dominican Republic, El Salvador, Guatemala, Nicaragua, Paraguay and Venezuela; and the rural average excludes Bolivia, Dominican Republic, Ecuador, El Salvador, Guatemala, Nicaragua, Paraguay, Uruguay and Venezuela.
d/ The average was calculated taking the years closest to 1990.
e/ The average was calculated taking the years closest to 1999.

In the 1990s, enrolment rates expanded most at the secondary school level (8 percentage points), to attain an average of 70%, albeit with wide dispersion ranging from 90% in Chile to below 45% in Guatemala and Honduras. Unlike other levels of education, where enrolment differences between the sexes tend to balance out, girls' enrolment is generally higher than boys' at this level (by about three percentage points). Although the rural-urban enrolment gap at the secondary school level narrowed during the decade, at 19 percentage points it is still larger than at any other level. In terms of income groups, enrolment differences between the highest and lowest quartiles average 16 percentage points, ranging from under 10 points (Bolivia and Colombia) to over 30 (Mexico and Uruguay). This gap has generally widened during the decade, except in Bolivia, Brazil, Chile and Panama. In other words, gains in coverage benefited low-income groups relatively less.

Financial and regulatory efforts during the decade to expand the coverage of basic education throughout the region resulted in the near-universalization of primary education, with gaps generally tending to close at this level. The notable progress in secondary education coverage, however, was concentrated in urban areas, while benefiting lower-income social groups relatively less. Thus, in efforts to universalize basic education, there have been major institutional difficulties in closing the existing rural-urban and income-group gaps. Hence, achieving universal coverage up to the end of secondary education will require sustained and intensified efforts to close these gaps which widened during the transition from low to universal coverage levels. The quicker this can be done, the sooner education systems will be able to make a positive contribution to equity.

In the 18-25-year age group, which is assimilated here to higher education, enrolment expanded by four percentage points in the 1990s to reach an average of 26%, ranging from over 33% (Bolivia, Chile, Dominican Republic and Panama)[2] down to 6% (Guatemala and Honduras). The largest differences reported between the sexes (over four percentage points) favour men in Bolivia and Mexico, and women in Panama, Uruguay and Venezuela. The urban-rural gap at the tertiary level (18 points) is similar to that seen in secondary education, and has also been narrowing. Between the highest and lowest income quartiles, differences vary from less than 10 percentage points (Dominican Republic and Venezuela) to over 30 (Chile, Panama and Uruguay). This income quartile gap widened in all the countries in the 1990s. Thus, unlike primary education during this period of expanding coverage, secondary and higher education have tended to become more elitist.

Despite the progress made, differences remain when comparing Latin American countries with those of the OECD and Sout-East Asia. Deficits persist not only in terms of coverage, but also in the pace of expansion of secondary and higher education and in learning outcomes. The duration of both compulsory and secondary education, and the length of the school day, are much shorter in the region. Between 1985 and 1997, the countries of South-East Asia took the lead in terms of secondary and higher education coverage, despite having started with major deficits. During the same period, the OECD countries moved even further ahead, as nearly all young people living there take secondary education courses and the majority complete them (85%). The share of technical education in total secondary education is also smaller in the region than in OECD or South-East Asian countries (see table 10.2).

2 In some of these countries, the coverage rates reported for this age group may include some secondary-school students.

Table 10.2
ENROLMENT IN SECONDARY AND HIGHER EDUCATION, 1985 TO 1997

	Gross enrolment ratios					
	Secondary education			Tertiary education		
Country groups	**1985**	**1997**	**Increase in enrolment ratios (% points)**	**1985**	**1997**	**Increase in enrolment ratios (% points)**
Latin America and the Caribbean	50.2	62.2	12.0	15.8	19.4	3.6
OECD countries	92.3	108.0	15.7	39.3	61.1	21.8
NIAE countries a/	57.3	73.1	15.8	14.8	30.5	15.7
East and South-East Asia b/	41.5	66.3	24.8	5.4	10.8	5.4

Educational performance 1998

	Duration of education (years)		Tertiary education in natural sciences, engineering and agriculture as % of total tertiary	
Country groups	**Compulsory**	**Secondary**	**Enrolment**	**Graduates**
Latin America and the Caribbean	7.1	5.1	26.0	26.6
OECD countries	9.8	6.4	27.2	25.2
NIAE countries a/	7.7	6.3	36.0	38.2
East and South-East Asia b/	7.3	6.1	31.6	32.2

Source: Beverly Carlson, "Education and the Labour Market in Latin America: Confronting Globalization", Working Paper, Santiago, Chile, 2001, unpublished, based on data from United Nations Educational, Scientific and Cultural Organization (UNESCO), *Statistical Yearbook 1999*, 1999; and *World Education Report, 2000*, 2000.

a/ Newly industrialized Asian economies: Hong Kong, Republic of Korea, Singapore, China, Malaysia and Thailand.
b/ Developing countries only, including NIAE countries.

The behaviour of the UNESCO school life expectancy indicator[3] also shows that efforts in the region to raise the population's education level have been insufficient. This indicator remained constant at 10.2 school years between 1980 and 1990, before edging up to 10.6 years in the first half of the 1990s. Apart from being modest in absolute terms, this increase of 0.4 years actually implies a decline in relative human capital development, because between 1980 and 1995, the OECD countries saw school life expectancy rise by 2.3 years, while the equivalent figure for Korea rose by 2.5. These trends caused the gap to widen: the difference of 2.4 years between the OECD countries and Latin America in 1980 had practically doubled to 4.3 years by the mid-1990s (see table 10.3), although, naturally, the trend varies from country to country. Taking the decade as a whole, according to ECLAC estimates based on coverage data reported in household surveys, educational progress seems to have continued, and by 1999 the region had probably advanced a further few tenths of a point, with the greatest progress being made in Brazil, Chile, Colombia and Costa Rica with increases of a year or more.[4] Despite the emphasis given to education in social policies, there are still countries where the average student entering the education system today will fail to complete the basic cycle that allows escape from poverty (ECLAC, 1998e).

[3] School life expectancy is defined as the total number of years of schooling which a child can be expected to receive in the future, assuming that the probability of his or her being enrolled in school at any particular age is equal to the current enrolment rate for that age.

[4] As shown in table 10.3, these calculations put school life expectancy at just over one year higher, on average, than UNESCO estimates, but the rate of progress is equally slow.

Table 10.3
SCHOOL LIFE EXPECTANCY IN SELECTED COUNTRIES, 1980, 1990 AND 1995
(*Both sexes, nationwide*)

		UNESCO			ECLAC	
Region	**Country**	**1980**	**1990**	**1995**	**1990**	**1999**
Latin America	Argentina (urban)					14.7
	Bolivia	8.6	9.9		14.8	13.4
	Brazil	9.5	10.4	11.1 (1994)	10.7	13.3
	Chile	11.5 (1983)	12.0 (1991)	12.6 (1996)	12.8	14.1
	Colombia		9.0 (1991)	10.0	10.9	11.9
	Costa Rica	9.7	9.6	10.1 (1994)	10.5	12.3
	Ecuador (urban)				14.1	13.1
	El Salvador		9.2 (1989)	9.8		11.1
	Guatemala					8.4
	Honduras	8.4 (1983)	8.7 (1991)		8.6	9.5
	Mexico		10.6	11.1	11.1	11.6
	Nicaragua				9.8	
	Panama	11.4	11.3		12.6	13.4
	Paraguay		8.6	9.8		12.0
	Dominican Republic					13.3
	Peru	11.0 (1981)	11.9 (1988)	12.4		
	Uruguay (urban)				13.2	13.4
	Venezuela	10.0	10.8		12.2	11.9
	Average a/	**10.2**	**10.2**	**10.6**	**11.4**	**12.0**
NIAE b/	Hong Kong	11.4				
	Korea	11.7	13.3	14.2		
OECD	Austria		14.5 (1992)	14.5 (1996)		
	Belgium	13 (1981)	14.2	16.8		
	Denmark	13.4	14.2	14.8		
	France	12.6	14.5 (1991)	15.5		
	Greece	12.0	13.3	13.5		
	Netherlands	13.0	14.9	16.6		
	Ireland	11.4	12.6	13.7		
	Japan	13.1	13.2	13.2 (1994)		
	Norway	12.9	14.2	15.2		
	Poland	12.0	12.2	13.0 (1994)		
	United Kingdom	12.9	13.7	16.5		
	Sweden	12.6 (1981)	13.0	14.7		
	Switzerland	12.6	13.6	14.1		
	Average a/	**12.6**	**13.7**	**14.9**		

Source: UNESCO, "Education at a Glance", and database; ECLAC estimates on the basis of household surveys

a/ Average excludes urban data.
b/ Newly industrialized Asian economies.

The priority of education in public policies is best shown by the increase in public education expenditure in the 1990s. In relation to GDP, expenditure grew from 2.9% in 1990-1991 to 4.0% in 1998-1999, while annual per capita expenditure, expressed as a simple country average in 1997 dollars, rose by US$ 51 to US$ 137 between 1990-1991 and 1998-1999 (see table 10.4; ECLAC, 2001c). Although the increase was greater than the equivalent figure for health expenditure (US$ 28 over the same period), it is clearly insufficient in comparison to educational investment in the OECD countries (which amounts to about 5% of GDP), and in relation to the amount needed to raise educational levels sufficiently to have a major impact on equality of opportunity and competitiveness. The level of public expenditure, rather than its recent increases, is what explains differences in school enrolment rates in the primary and secondary cycles; hence the importance of raising the level of resources allocated to education and maintaining it in times of crisis.

Table 10.4
LATIN AMERICA AND THE CARIBBEAN (17 COUNTRIES): SOCIAL PUBLIC EXPENDITURE ON EDUCATION

Country	In 1997 dollars			As a percentage of GDP		
	1990-1991	1994-1995	1998-1999	1990-1991	1994-1995	1998-1999
Argentina	226	318	383	3.3	4.2	4.7
Bolivia	…	52	62	…	5.3	6.0
Brazil	162	226	187	3.7	4.9	3.9
Chile	87	129	202	2.6	2.9	3.9
Colombia	63	86	120	3.2	3.4	4.7
Costa Rica	115	136	163	3.8	4.1	4.4
El Salvador	…	35	52	…	2.0	2.7
Guatemala	25	29	40	1.6	1.8	2.3
Honduras	32	31	32	4.3	4.1	4.1
Mexico	104	157	167	2.6	3.8	3.8
Nicaragua	22	20	26	5.0	4.9	5.7
Panama	125	151	198	4.7	5.0	6.0
Paraguay	22	61	66	1.2	3.2	3.7
Peru	28	56	62	1.3	2.3	2.2
Dominican Republic	18	34	57	1.2	2.1	2.8
Uruguay	130	151	218	2.5	2.5	3.3
Venezuela	129	139	140	3.5	3.7	3.8
Simple average	86	106	128	2.9	3.5	4.0
Simple average a/	86	115	137	2.9	3.5	3.9

Source: ECLAC, *Social panorama of Latin America, 2000-2001* (LC/G.2138-P), Santiago, Chile, October 2001. United Nations publication, Sales No. E.01.II.G.141.

a/ Excludes Bolivia and El Salvador.

2. Quality deficits

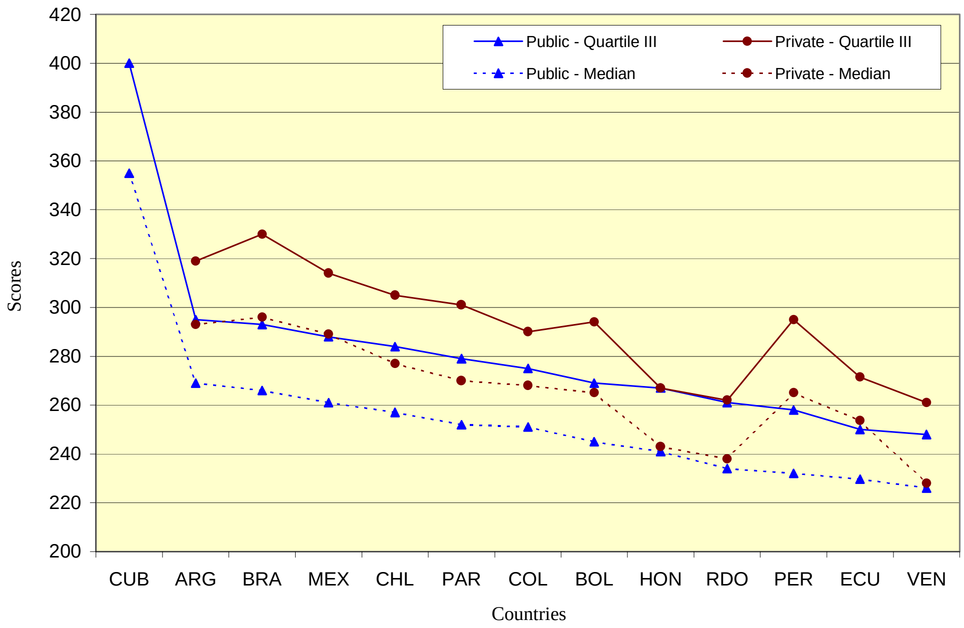
Education quality in Latin America and the Caribbean displays major segmentation, to the detriment of students from low-income families. In 1994, attainment in language skills among fourth-grade pupils in basic education (scored out of a maximum of 100 points) averaged 71.9 among pupils from high-income families, 58.4 for middle-income children and 47.9 for children from low-income families. In mathematics, the corresponding averages were 59.0, 49.8 and 43.8 respectively.[5] Pupils attending private schools, which are generally expensive, achieve better results in mathematics and language skills than their public-school peers (see figure 10.1). Measurements of learning outcomes in reading, writing, mathematics and science also reveal the performance of Latin American students to be inferior to that of their counterparts in industrialized countries (see table 10.5)

5 OREALC, 1994. Figures for Argentina, Bolivia, Chile, Costa Rica, Dominican Republic, Ecuador and Venezuela.

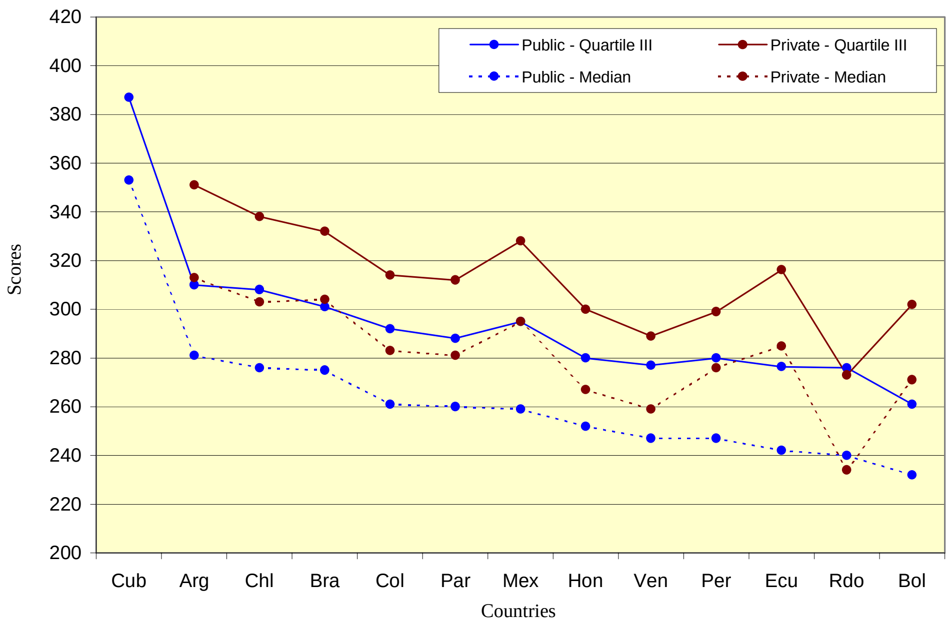
Figure 10.1

MEDIAN AND 75TH PERCENTILE SCORE IN STANDARDIZED TESTS APPLIED TO 4TH GRADE STUDENTS IN PUBLIC AND PRIVATE SCHOOLS

Mathematics



Language



Source: Latin American Education Quality Evaluation Laboratory (LLECE), UNESCO Regional Office for Education in Latin America and the Caribbean (OREALC), 1997 data.

Table 10.5
RELATIVE POSITION OF IBERO-AMERICAN COUNTRIES IN INTERNATIONAL STUDIES OF EDUCATION QUALITY

Study	Participating countries	Ibero-American countries	Relative position
Laboratory, 1997 a/	13	13	The average scores of the highest-ranked country are between 1.5 and 2.0 standard deviations from the scores obtained by the other 12 countries
TIMSS, 1996 b/	41	3	31, 37 and 40
TIMSS, 1999 b/	38	1	35
IALS, 1998 c/	22	2	19 and 22
IALS, 1998 d/	22	2	21 and 22

Source: Latin American Education Quality Evaluation Laboratory (LLECE), International Association for the Evaluation of Educational Achievement (IEA), Third International Mathematics and Science Study (TIMSS); and Organization for Economic Cooperation and Development (OECD), International Adult Literacy Survey (IALS). (http)://222.unesco.org/education/uie/confintea/pdf/3d_span.pdf), 2001.

a/ Language and mathematics, 3rd and 4th grades.
b/ Mathematics, 8th grade.
c/ Literacy skills in young people between 16 and 25 years of age.
d/ Literacy skills in adults between 26 and 65 years of age.

These inequalities are compounded by unequal access to (and use of) computer networks and audiovisual media, where the production of knowledge and, to a large extent, culture, constantly circulates and renews itself. Although efforts are being made to endow school infrastructure with computer equipment for students and teachers alike, its pace of diffusion and use are both insufficient. As a result, there is a significant "digital divide" between children and young people who are accustomed to using computer networks and languages interactively and those from low- and low-middle-income families for whom access is much more limited. As suggested in chapter 7. this "domestic digital divide" in Latin America and the Caribbean is more of a threat than its international counterpart.

Emerging economic activities in the culture industry, along with the new information and communication technologies, are producing major changes in the way schoolchildren develop their intellectual capacities and gain access to knowledge. As schools install audiovisual and interactive media, priority starts to shift from knowledge acquisition towards developing learning skills. Mass diffusion of video (in both production and consumption), computer software, cable television and interactive long-distance information exchange, are restructuring the channels of knowledge formation and transmission. Use of mass communications media and information technologies in Latin America and the Caribbean is deficient (UNESCO, 2000a). Radio and television are still seldom used for educational purposes, although there are a number of audiovisual and informatics experiments taking place. Caribbean countries have expanded their use of printed and electronic media, using radio and exhibitions to promote reading and improve language use, with television as an important vehicle for curricular content. In Brazil, television is being used for teacher training programmes, while the *Enlaces* network has connected nearly all of Chile's schools to the Internet and provides technical assistance to students and teachers in its use for educational purposes (UNESCO, 2000b).

Higher education is going through a prolonged crisis that is affecting all of its various missions: professional staff are finding it harder to do their job; universities are increasingly losing their central role as generators of knowledge; and, as a focal point for citizenship formation —in which Latin American universities played a particularly important rol— much of higher education fluctuates between political rigidity and the more technocratic alternative. Current levels of scientific and technological research and development are clearly insufficient and uneven, and there is a clear divorce between academic research and productive activity.

In addition, public and private universities are both facing serious problems. The former are overpopulated and overprotected; they lack systematic evaluation, misuse funds and have excessively bureaucratic and ritualistic structures. Private universities, meanwhile, range from the very bad (which cater for students who fail to obtain or hold on to places in public universities) to the highly technified (which are restricted to elites). In both cases there is a lack of regulation.

Adult education and training is also insufficient and inadequate. The training institutes that accompanied industrialization processes in the early post-war decades have been rendered irrelevant by ongoing changes in production patterns, yet in-house training within firms is still embryonic.

3. Education, employment and income

Schooling levels among the workforce (i.e, the economically active population) increased in every country of the region in the 1990s: in total (from 6.1 to 7.0 years); among men (from 5.8 to 6.8 years) and women (from 6.3 to 7.2 years); in urban and rural areas (from 7.8 to 8.6 and from 4.5 to 5.3 years, respectively); among the employed (from 5.5 to 6.4 years) and the unemployed (from 6.7 to 7.6 years); and in all age groups (from 7.4 to 8.2 years among 15-29-year-olds; from 6.6 to 7.6 years in the 30-49 age group; and from four to five years in the case of the over-50s), as shown in table 10.6. There are large variations between countries, ranging from nine years of schooling in Chile and Panama to less than six in Brazil, Guatemala and Nicaragua. The countries that have made the most progress in this area were El Salvador, Mexico and Venezuela. The absolute gap between rural and urban areas remains considerable, though it has narrowed slightly. The difference between men and women remains relatively constant in favour of women, but with relative gains for female students in Colombia, Guatemala, Panama and Venezuela, and relative gains for men in Brazil, Chile, Honduras, Mexico and Nicaragua. Similarly, with few exceptions, average years of schooling among the unemployed are greater than among the employed in all age groups, with the largest differences in Brazil, Guatemala, Honduras, and Panama, but very small ones in Chile and Costa Rica. These gaps have tended to widen in Brazil, El Salvador and Guatemala, but have narrowed in Costa Rica and Panama.

Seen from a longer-term perspective, progress in this field has varied greatly across countries and different periods of time. A comparison of the educational levels of workers who began their education in the 1950s (the over-50s in 1990) and those who started in 1975 (the 15-29 age group in 1999) shows that the greatest progress was achieved by Chile, Mexico and Venezuela (increases of more than four years). The least progress (under 2.5 years) was made by Honduras and Guatemala and by countries that had already achieved high education levels by the mid-twentieth century (Argentina and Uruguay). In terms of time periods, there was significant progress between 1955 and 1975, enabling today’s 30-49-year-old workers (who were of school age then) to increase their level of schooling from five years (the educational level of workers aged 50 or over today) to 7.6, or by 2.6 extra years. Nicaragua, Mexico and Panama achieved the largest increase (over 3.5 years), Progress made since 1975, when today’s 15-29-year-olds were being educated, has enabled them to attain an average of 8.2 years of schooling. This betters the educational level of workers between 30 and 49 years of age by 0.6 years. The largest increases were seen in Mexico, Bolivia, El Salvador and Brazil, in that order. On the other hand, the crisis of the 1980s caused education losses in Costa Rica, Ecuador, Honduras and Panama, along with slower rates of progress in the other countries (see figure 10.2).

Table 10.6
LATIN AMERICA AND THE CARIBBEAN (17 COUNTRIES): AVERAGE NUMBER OF YEARS OF SCHOOLING OF ECONOMICALLY ACTIVE POPULATION (EAP), BY AGE GROUP AND EMPLOYMENT STATUS, 1990 AND 1999
(*Percentages*)

Country	Year		Age group											
			Total			15-29 years			30-49 years			50 years or older		
			EAP	Employed	Unemployed	EAP	Employed	Unemployed	EAP	Employed	Unemployed	EAP	Employed	Unemployed
Argentina	1999	Urban	10.1	10.0	10.2	10.9	10.9	10.9	10.9	10.7	11.0	8.7	8.5	8.8
Bolivia	1989a/													
		Urban	8.5	7.9	9.1	10.1	9.5	10.6	8.8	8.7	9.0	6.4	5.4	7.6
	1999													
		Total	7.2	6.3	8.5	8.7	8.1	9.3	7.3	6.7	8.1	5.2	4.0	7.6
		Men	8.0	7.2	9.2	9.2	8.6	9.8	8.5	7.7	9.7	6.2	5.1	7.8
		Women	6.3	5.4	7.7	8.1	7.6	8.8	6.3	5.7	6.9	4.1	2.8	7.4
		Urban	9.3	8.7	9.9	10.5	10.1	10.8	10.1	9.8	10.5	7.2	6.3	8.1
		Rural	4.2	3.8	5.2	6.4	6.1	6.9	3.5	3.6	3.3	1.9	1.6	4.0
Brazil	1990													
		Total	4.9	4.2	5.5	5.9	5.5	6.3	5.4	4.6	6.1	3.2	2.6	3.9
		Men	4.5	4.0	5.1	5.4	5.0	5.8	5.2	4.5	5.9	2.9	2.6	3.2
		Women	5.2	4.4	6.1	6.4	5.9	6.8	5.6	4.8	6.3	3.5	2.6	4.7
		Urban	6.3	5.8	6.9	7.4	7.2	7.7	7.1	6.5	7.7	4.5	3.9	5.2
		Rural	3.3	2.6	4.0	4.4	3.8	5.0	3.6	2.8	4.4	1.5	1.3	1.9
	1999													
		Total	5.5	5.1	6.0	7.1	6.6	7.6	6.0	5.7	6.4	3.5	3.0	4.0
		Men	5.4	4.8	6.0	6.6	6.0	7.2	5.9	5.4	6.3	3.7	3.0	4.5
		Women	5.7	5.3	6.0	7.5	7.1	8.0	6.2	5.9	6.5	3.2	3.0	3.5
		Urban	7.0	6.8	7.3	8.3	8.2	8.4	7.7	7.5	7.8	5.0	4.5	5.5
		Rural	4.1	3.4	4.7	5.9	5.0	6.8	4.4	3.8	5.0	1.9	1.5	2.4
Chile	1990													
		Total	8.2	8.0	8.4	9.8	9.5	10.1	8.7	8.7	8.7	6.1	5.8	6.3
		Men	7.9	7.8	7.9	9.2	9.1	9.4	8.5	8.5	8.5	5.9	5.8	5.9
		Women	8.6	8.2	8.9	10.4	10.0	10.8	8.9	8.9	9.0	6.3	5.9	6.7
		Urban	9.6	9.6	9.7	11.1	10.9	11.4	10.4	10.2	10.5	7.3	7.6	7.1
		Rural	7.1	6.5	7.1	8.8	8.2	8.8	7.0	7.1	7.0	5.3	4.1	5.3
	2000													
		Total	9.0	8.8	9.1	10.7	10.5	10.9	9.7	9.5	9.9	6.5	6.5	6.5
		Men	8.7	8.6	8.7	10.2	10.0	10.4	9.4	9.4	9.4	6.4	6.4	6.5
		Women	9.3	9.0	9.5	11.2	10.9	11.5	10.1	9.7	10.4	6.6	6.5	6.6
		Urban	10.5	10.5	10.5	11.8	11.8	11.8	11.3	11.4	11.3	8.5	8.4	8.5
		Rural	7.4	7.1	7.7	9.6	9.1	10.0	8.1	7.7	8.5	4.5	4.5	4.5
Colombia	1991													
		Total	6.2	5.8	6.7	7.6	6.9	8.3	6.9	6.4	7.4	4.1	3.9	4.4
		Men	6.4	5.7	7.1	7.4	6.6	8.2	7.1		7.8	4.8	4.1	5.4
		Women	6.0	5.8	6.3	7.8	7.3	8.3	6.8	6.4	7.1	3.5	3.7	3.3
		Urban	7.7	7.5	7.9	9.1	8.6	9.6	8.7	8.4	9.0	5.3	5.5	5.1
		Rural	4.7	4.0	5.5	6.1	5.3	6.9	5.2	4.5	5.9	3.0	2.3	3.6
	1999													
		Total	6.9	6.5	7.4	8.3	7.6	9.0	7.5	7.2	7.8	4.9	4.6	5.2
		Men	6.8	6.3	7.3	8.0	7.2	8.8	7.4	6.9	7.9	5.0	4.7	5.3

Table 10.6 (continued)

Country	Year		Total EAP	Total Employed	Total Unemployed	15 - 29 years EAP	15 - 29 years Employed	15 - 29 years Unemployed	30 a- 49 years EAP	30 a- 49 years Employed	30 a- 49 years Unemployed	50 years or over EAP	50 years or over Employed	50 years or over Unemployed
		Women	7.0	6.7	7.4	8.6	8.1	9.2	7.6	7.4	7.8	4.8	4.5	5.2
		Urban	8.5	8.2	8.9	9.6	9.2	10.1	9.2	9.0	9.5	6.7	6.3	7.1
		Rural	5.3	4.8	5.8	7.0	6.1	7.9	5.8	5.3	6.2	3.2	3.0	3.4
Costa Rica	1990													
		Total	6.9	6.7	7.1	8.1	7.9	8.4	7.9	7.7	8.1	4.0	4.6	2.9
		Men	6.6	6.5	6.8	7.8	7.5	8.0	7.7	7.5	8.0	3.9	4.6	2.9
		Women	7.1	6.9	7.4	8.5	8.2	8.8	8.0	7.8	8.2	4.0	4.6	2.9
		Urban	8.3	8.1	8.5	9.3	9.0	9.6	9.5	9.1	9.9	5.3	6.2	3.4
		Rural	5.5	5.3	5.8	7.0	6.7	7.3	6.2	6.2	6.3	2.8	3.0	2.6
	1999													
		Total	7.4	7.3	7.4	8.1	8.1	8.1	8.2	8.3	8.0	5.7	5.5	5.8
		Men	7.2	7.1	7.2	7.7	7.6	7.7	8.1	8.2	8.0	5.6	5.4	5.8
		Women	7.6	7.5	7.6	8.6	8.6	8.6	8.2	8.5	8.0	5.7	5.6	5.8
		Urban	8.7	8.7	8.8	9.2	9.3	9.1	9.8	9.6	10.0	7.1	7.1	7.2
		Rural	6.0	6.0	6.0	7.0	6.9	7.2	6.5	7.0	6.1	4.1	4.0	4.2
Ecuador	1990													
		Urban	9.0	8.2	9.9	10.2	9.4	11.0	9.9	9.1	10.7	7.1	6.0	8.2
	1999													
		Urban	9.4	9.0	9.9	10.3	9.9	10.8	10.7	10.1	11.3	7.3	7.0	7.6
El Salvador	1990													
		Urban	6.3	6.4	6.1	8.2	7.9	8.4	7.1	7.3	6.9	3.5	3.9	3.1
	1999													
		Total	5.9	5.3	6.5	7.7	7.0	8.5	6.5	5.9	7.1	3.2	3.1	3.4
		Men	5.8	5.6	6.1	7.2	6.9	7.6	6.5	6.3	6.7	3.8	3.4	4.1
		Women	6.0	5.1	6.9	8.2	7.0	9.4	6.5	5.6	7.4	2.6	2.8	2.2
		Urban	8.2	7.5	8.9	9.8	9.0	10.5	9.2	8.5	10.0	5.1	4.9	5.3
		Rural	3.7	3.2	4.2	5.7	5.0	6.4	3.8	3.4	4.1	1.5	1.3	1.8
Guatemala	1989													
		Total	4.5	3.4	5.7	5.7	4.6	6.9	4.3	3.7	4.9	3.1	1.9	4.9
		Men	4.7	3.8	5.6	5.8	4.9	6.7	4.2	4.2	4.3	4.1	2.2	5.9
		Women	4.2	3.1	5.7	5.7	4.3	7.0	4.4	3.3	5.6	1.8	1.6	2.3
		Urban	6.3	5.1	7.6	7.3	6.4	8.1	6.3	5.8	6.8	5.0	3.1	8.1
		Rural	2.6	1.7	3.7	4.2	2.8	5.6	2.2	1.7	2.7	1.4	0.7	2.3
	1998													
		Total	5.5	4.1	7.3	6.7	5.5	8.0	5.7	4.4	7.1	3.9	2.5	6.4
		Men	5.2	4.5	6.1	6.4	5.7	7.1	5.9	4.9	7.1	3.0	2.9	3.1
		Women	5.8	3.7	8.6	7.0	5.2	9.1	5.4	4.0	7.0	4.9	2.0	10.5
		Urban	7.3	6.2	8.4	8.5	7.5	9.5	7.5	6.8	8.2	5.7	4.2	7.4
		Rural	3.4	2.1	5.6	4.8	3.4	6.3	3.5	2.1	5.5	1.2	0.7	3.0
Honduras	1990													
		Total	5.0	4.1	5.9	6.2	5.3	7.1	5.3	4.5	6.1	3.0	2.5	3.6
		Men	4.7	4.1	5.2	5.9	5.1	6.7	5.0	4.5	5.5	3.0	2.6	3.4
		Women	5.3	4.2	6.8	6.5	5.5	7.5	5.6	4.5	6.7	2.9	2.5	4.6
		Urban	6.5	5.6	7.5	7.7	6.7	8.6	7.4	6.3	8.6	4.2	3.8	4.7
		Rural	3.3	2.7	4.1	4.8	3.9	5.6	3.2	2.8	3.6	1.5	1.3	2.0

Table 10.6 (continued)

Country	Year		Total PEA	Total Em-ployed	Total Unem-ployed	15-29 years PEA	15-29 years Em-ployed	15-29 years Unem-ployed	30-49 years PEA	30-49 years Em-ployed	30-49 years Unem-ployed	50 years or older PEA	50 years or older Em-ployed	50 years or older Unem-ployed
	1999													
		Total	5.9	5.0	7.0	6.4	6.1	6.7	6.6	5.7	7.4	4.2	3.1	6.6
		Men	6.1	4.9	7.5	6.1	5.8	6.4	6.7	5.7	7.7	5.3	3.2	8.7
		Women	5.7	5.1	6.4	6.7	6.4	7.0	6.4	5.7	7.2	2.7	3.1	1.2
		Urban	7.2	6.5	8.1	7.7	7.5	8.0	8.3	7.5	9.0	5.3	4.4	6.8
		Rural	4.4	3.5	5.7	5.1	4.8	5.4	4.8	3.8	5.8	2.7	1.9	6.0
Mexico	1989													
		Total	6.0	5.5	6.6	7.7	7.5	7.9	6.2	5.9	6.4	3.6	3.2	4.3
		Men	5.7	5.6	5.9	7.2	7.3	7.1	6.1	6.0	6.3	3.9	3.6	4.3
		Women	6.3	5.5	7.6	8.3	7.8	8.7	6.2	5.8	6.6	2.9	2.9	-
		Urban	7.7	7.2	8.4	9.0	9.0	9.0	8.2	7.8	8.5	5.5	4.8	6.9
		Rural	4.3	3.9	4.8	6.4	6.0	6.8	4.1	4.0	4.3	1.7	1.7	1.7
	1998													
		Total	7.4	6.8	8.1	9.2	8.7	9.7	7.8	7.4	8.4	4.2	4.3	4.0
		Men	7.3	7.0	7.6	9.1	8.7	9.6	8.2	7.7	8.7	4.4	4.7	4.0
		Women	7.5	6.5	9.0	9.3	8.8	9.9	7.4	7.0	7.9	3.8	3.8	-
		Urban	8.9	8.3	9.8	10.3	9.8	10.8	9.6	9.0	10.2	6.1	6.1	6.0
		Rural	5.8	5.3	6.4	8.2	7.7	8.7	5.8	5.8	5.9	2.5	2.4	2.6
Nicaragua	1993													
		Total	4.4	4.0	4.7	6.0	5.4	6.5	4.7	4.5	4.9	2.2	2.2	2.2
		Men	4.1	3.9	4.4	5.7	4.8	6.5	4.9	4.5	5.3	1.8	2.2	1.4
		Women	4.6	4.2	5.1	6.2	5.9	6.6	4.4	4.5	4.3	2.7	2.2	3.6
		Urban	5.8	5.7	5.9	7.2	7.2	7.2	6.8	6.5	7.1	3.2	3.3	3.1
		Rural	2.8	2.4	3.4	4.7	3.5	5.8	2.4	2.5	2.3	1.1	1.2	0.9
	1998													
		Total	5.0	4.6	5.3	6.3	5.8	6.7	5.7	5.3	6.2	2.7	2.6	2.9
		Men	5.0	4.4	5.6	5.6	5.3	6.0	6.2	5.2	7.1	3.1	2.8	3.6
		Women	4.9	4.8	5.0	6.9	6.4	7.4	5.3	5.4	5.2	2.4	2.5	2.2
		Urban	6.6	6.2	7.1	7.7	7.3	8.1	7.9	7.2	8.6	4.3	4.0	4.6
		Rural	3.2	3.0	3.4	4.8	4.4	5.3	3.6	3.4	3.7	0.9	1.2	0.5
Panama	1991													
		Total	8.4	7.5	9.4	9.6	8.9	10.3	9.2	8.3	10.1	6.3	5.3	7.4
		Men	7.8	7.0	8.7	9.0	8.3	9.7	8.7	7.8	9.5	5.8	4.9	6.7
		Women	9.0	8.0	10.2	10.3	9.6	11.0	9.7	8.7	10.7	6.8	5.7	8.3
		Urban	9.5	9.0	10.1	10.5	10.1	10.9	10.4	9.9	11.0	7.6	7.0	8.2
		Rural	7.3	6.0	8.6	8.7	7.7	9.7	8.0	6.7	9.3	4.8	3.6	6.3
	1999													
		Total	9.2	8.4	10.0	10.1	9.5	10.6	9.9	9.4	10.5	7.3	6.3	8.5
		Men	8.5	7.9	9.1	9.4	8.9	9.9	9.3	8.9	9.7	6.9	6.0	7.7
		Women	9.9	8.9	11.0	10.8	10.2	11.4	10.6	9.8	11.3	7.9	6.6	9.8
		Urban	10.4	10.0	10.8	11.1	10.8	11.4	10.9	10.9	10.9	9.1	8.2	10.0
		Rural	7.9	6.8	9.1	9.1	8.3	9.9	9.0	7.8	10.1	5.1	4.4	6.2

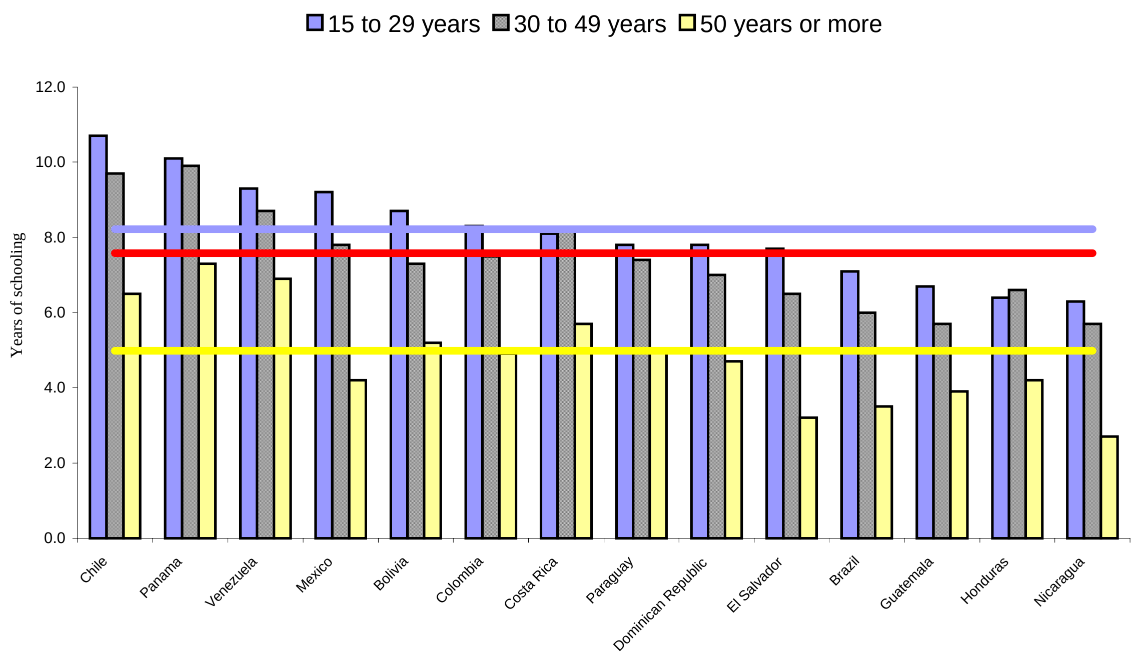
Table 10.6 (concluded)

Country	Year		Total PEA	Total Employed	Total Unemployed	15-29 years PEA	15-29 years Employed	15-29 years Unemployed	30-49 years PEA	30-49 years Employed	30-49 years Unemployed	50 years or older PEA	50 years or older Employed	50 years or older Unemployed
Paraguay	1990 b/													
		Urban	9.3	8.6	10.3	9.9	9.3	10.4	10.0	9.3	10.9	7.1	7.3	5.3
	1999													
		Total	6.8	6.5	7.1	7.8	7.8	7.8	7.4	7.0	7.8	5.0	4.6	5.5
		Men	7.0	6.6	7.5	7.7	7.7	7.6	7.9	7.1	8.6	5.5	5.0	6.1
		Women	6.5	6.3	6.7	8.0	7.9	8.1	6.9	6.9	6.9	4.6	4.2	4.9
		Urban	8.4	8.1	8.7	9.3	9.3	9.3	9.2	8.9	9.4	6.7	6.1	7.4
		Rural	5.1	4.8	5.4	6.3	6.3	6.3	5.6	5.1	6.2	3.1	3.1	3.0
Dominican Republic	1997													
		Total	6.6	6.1	7.1	7.8	7.7	8.0	7.0	6.8	7.3	4.7	3.9	5.7
		Men	6.5	5.8	7.3	7.2	6.9	7.5	7.4	6.5	8.4	4.9	4.0	5.9
		Women	6.6	6.4	6.9	8.4	8.4	8.5	6.7	7.0	6.4	4.6	3.8	5.6
		Urban	8.1	7.6	8.6	8.9	8.9	8.9	9.0	8.7	9.3	6.3	5.1	7.5
		Rural	5.0	4.6	5.4	6.8	6.4	7.1	5.0	4.8	5.2	2.9	2.6	3.3
Uruguay	1990													
		Urban	8.6	8.5	8.7	9.8	9.6	10.0	9.2	9.2	9.2	6.7	6.5	6.8
	1999													
		Urban	9.3	9.3	9.2	10.3	10.2	10.4	9.8	10.0	9.6	7.7	7.7	7.7
Venezuela	1990													
		Total	6.3	5.7	6.9	7.5	7.1	7.8	7.3	6.5	8.1	4.1	3.6	4.7
		Men	5.8	5.5	6.2	6.7	6.4	6.9	6.7	6.2	7.2	4.1	3.8	4.4
		Women	6.8	5.9	7.7	8.3	7.8	8.7	7.9	6.7	9.0	4.1	3.3	5.1
		Urban	7.8	7.5	8.1	8.7	8.6	8.7	8.8	8.5	9.1	6.0	5.5	6.5
		Rural	4.8	3.9	5.7	6.2	5.6	6.9	5.7	4.4	7.1	2.2	1.7	2.7
	1999													
		Total	8.3	7.8	8.8	9.3	9.0	9.5	8.7	8.3	9.1	6.9	6.0	7.8
		Men	7.6	7.3	7.9	8.4	8.0	8.8	8.1	8.0	8.3	6.4	6.0	6.8
		Women	8.9	8.2	9.7	10.1	10.0	10.3	9.3	8.5	10.0	7.4	6.0	8.8
Average c/	1990 d/													
		Total	6.1	5.5	6.7	7.4	6.9	8.0	6.6	6.1	7.1	4.0	3.6	4.5
		Men	5.8	5.4	6.3	7.0	6.5	7.5	6.4	6.0	6.8	4.0	3.6	4.4
		Women	6.3	5.6	7.2	7.8	7.2	8.4	6.8	6.1	7.4	3.9	3.5	4.6
		Urban	7.8	7.4	8.3	9.1	8.6	9.5	8.6	8.2	9.0	5.6	5.3	5.9
		Rural	4.5	3.9	5.2	6.1	5.3	6.8	4.7	4.3	5.1	2.6	2.1	3.0
	1999 e/													
		Total	7.0	6.4	7.6	8.2	7.7	8.7	7.6	7.1	8.1	5.0	4.4	5.8
		Men	6.8	6.3	7.3	7.8	7.3	8.2	7.5	7.0	8.0	5.0	4.5	5.6
		Women	7.2	6.6	8.0	8.7	8.2	9.2	7.7	7.2	8.1	4.9	4.4	6.0
		Urban	8.6	8.1	9.0	9.6	9.3	9.9	9.4	9.0	9.7	6.6	6.1	7.1
		Rural	5.3	4.7	6.0	6.8	6.2	7.5	5.7	5.2	6.3	2.9	2.6	3.6

Source: ECLAC, on the basis of special tabulations of household surveys conducted in the respective countries.

a/ Eight main cities.
b/ Asunción metropolitan area.
c/ Averages calculated from figures from countries that have comparable data for the two years considered.
d/ The average was calculated taking the years closest to 1990.
e/ The average was calculated taking the years closest to 1999.

Figure 10.2
AVERAGE YEARS OF SCHOOLING OF TOTAL ECONOMICALLY ACTIVE POPULATION (EAP), BY AGE GROUPS, 1999



Source: ECLAC, on the basis of special tabulations of household surveys conducted in the respective countries.

Inequalities in the returns to education have also suffered significant segmentation in recent years.[6] Returns are high (education premium) for those with university education and also, but to a lesser extent, for those who complete secondary school (compared to those who do not). The increase in income among the youngest group (25-34-year-olds) with most years of schooling is less than for the population as a whole, partly because of their lower returns to experience, but also because of educational "devaluation".[7] Gender differences here are large, but they also vary considerably, and are greater when secondary education is incomplete.

II. Globalization and employment

Employment is the main link between economic and social development, since it is the major source (80%) of household income. Many of the social effects of closer integration into the world economy, and of adjustment processes to achieve macroeconomic balance and adapt to changes in the international economy, are transmitted through the organization and functioning of the labour market. This is what establishes the number and quality of jobs generated and the wages and incomes that people earn. The chances of finding a job, the level of coverage and social protection for employed people and the earnings they obtain have a decisive effect on the level and distribution of material welfare among the population. Social exclusion and segmentation, caused by inadequate

6 See, for example, the analysis by Carlson (2001), based on five of the region's countries (Argentina, Brazil, Chile, Paraguay and Uruguay) for the period 1993-1999. See also Morley (2000b) for a discussion of the widening of income differentials by education level.

7 The term "educational devaluation" has been used to describe the fact that today higher levels of education are needed to generate given levels of income than in the past. See ECLAC (1998e).

access to good jobs, generate poverty and social inequalities that are reproduced over time. This is manifested in the highly concentrated income distribution that continues to characterize the region (ECLAC, 2000a and 2000b).

Employment effects stemming from technological change, oppenness to international trade and the integration of Latin America and the Caribbean into the world economy are compounded by the effects of structural adjustment and those stemming from business cycles. The consequences of the changing employment patterns shared by the vast majority of the region's countries include: (i) high and rising job insecurity and instability caused by high levels of unemployment and job mobility; (ii) increasing inequality resulting from the trend of wages between sectors and between different productivity and skill levels; and (iii) exclusion generated by a shortage of good jobs, low coverage of social safety nets and the increasing precariousness of employment. An analysis of available information also reveals specific features associated with the patterns of productive specialization and participation in world trade flows that began to show through in the closing decade of the twentieth century.

1. Dynamics of the production and employment structure

An analysis of changes in the production and employment structure reveals the differential effects of the two dominant patterns of specialization in Latin America.[8] The first of these patterns involves the production of raw materials and industrial commodities, with intensive use of capital and natural resources; this is characteristic of South American countries in particular. The second pattern entails production of manufactured goods with a high imported input content (the extreme case being mere assembly of such inputs, or "maquila"). This is characteristic of Mexico and some of the Central American and Caribbean economies. This second specialization pattern comprises several labour-intensive segments, and a large proportion of the corresponding exports are sent to the North American market (see chapter 6 of this volume). These two specialization patterns broadly coincide with the countries' geographical location, so the ensuing discussion will divide the region into northern and southern countries.

The uneven rates of economic growth recorded during the decade (averaging 4.5% or more per year in Argentina, Chile, Costa Rica, Panama and Peru) were accompanied by widely differing changes in the sectoral structure of production, reflecting the different specialization patterns. Generally speaking, countries in the northern part of the region, particularly Mexico, Costa Rica, El Salvador and Honduras, saw their industrial sectors expand faster than those producing non-tradable goods and services, and the share of exports in GDP grew rapidly[9] (see table 10.7). In the southern countries, on the other hand, tradable-goods-producing activities tended to grow more slowly, especially in the industrial segments. This was the pattern in Argentina, Brazil, Chile, Colombia, Paraguay and Uruguay; while Bolivia broadly maintained its output structure. Countries that diverged from subregional trends were Ecuador, and particularly Peru, in the south, and Guatemala in the north.

[8] A third pattern, characteristic of some Caribbean countries, involves specialization in services. As mentioned in chapter 11, countries with this pattern have a clear advantage over those specializing in raw materials.

[9] Between 1990 and 2000, the exports/GDP ratio rose from 31% to 52% in Costa Rica, from 15% to 36% in Mexico and from 17% to 36% in El Salvador. In South America, the corresponding levels and increases are both lower: Argentina saw its exports/GDP ratio rise from 10% to 12%; Brazil, from 8% to 11%; and Colombia, from 14% to 19%. A notable exception was Chile, where exports expanded from 21% to 37% of GDP.

Table 10.7
LATIN AMERICA (17 COUNTRIES): OUTPUT TRENDS IN THE 1990s a/

	Tradable and non-tradable goods and services								
	Total b/			**Tradable sector** c/			**Non-tradable sector** d/		
Country	**1990-1994**	**1994-1999**	**1990-1999**	**1990-1994**	**1994-1999**	**1990-1999**	**1990-1994**	**1994-1999**	**1990-1999**
Argentina	13.6	2.3	7.2	6.9	1.2	3.7	15.8	2.6	8.2
				(7.7)	(0.4)	(3.6)	(10.9)	(1.5)	(5.6)
Bolivia	3.9	4.1	4.0	4.4	3.8	4.1	3.7	4.7	4.2
				(4.4)	(3.9)	(4.2)	(2.2)	(2.8)	(2.5)
Brazil	3.0	1.4	2.2	4.0	0.6	2.3	2.7	1.6	2.2
				(3.8)	-(0.5)	(1.7)	(1.3)	(1.4)	(1.4)
Chile	6.7	5.8	6.3	6.3	4.9	5.6	7.0	6.3	6.6
				(7.0)	(3.6)	(5.3)	(3.4)	(2.9)	(3.2)
Colombia	4.7	-0.9	1.2	1.3	0.5	0.8	6.2	-1.5	1.3
				(2.6)	-(1.9)	-(0.2)	(4.4)	(7.6)	(6.4)
Costa Rica	5.2	5.1	5.1	5.3	7.4	6.5	5.1	3.8	4.4
				(5.7)	(9.1)	(7.6)	(3.0)	(1.9)	(2.4)
Ecuador	3.4	-0.3	1.3	4.7	0.5	2.4	2.6	-1.2	0.5
				(5.3)	(0.7)	(2.7)	(0.2)	-(2.9)	-(1.5)
El Salvador	4.2	3.0	3.7	6.0	4.9	5.5	4.3	2.7	3.6
				(5.6)	(5.0)	(5.3)	(1.8)	(2.2)	(2.0)
Guatemala	4.0	4.4	4.2	2.9	4.6	3.7	4.5	4.7	4.6
				(2.7)	(2.9)	(2.8)	(5.0)	(3.9)	(4.5)
Honduras	3.1	3.1	3.1	3.0	2.8	2.9	3.2	3.3	3.2
				(3.4)	(4.4)	(4.0)	(0.9)	(1.6)	(1.3)
Mexico	4.1	2.5	3.4	3.1	4.8	3.9	4.4	1.7	3.2
				(3.5)	(5.6)	(4.4)	(2.7)	(1.2)	(2.0)
Nicaragua	-0.4	4.1	2.4	0.5	5.7	3.4	-1.0	2.7	1.3
				(0.3)	(2.4)	(1.6)	-(3.9)	-(2.0)	-(2.7)
Panama	5.4	3.6	4.5	15.0	2.4	8.5	5.4	3.9	4.6
				(8.7)	(0.9)	(4.7)	-(0.3)	(3.0)	(1.3)
Paraguay	2.9	1.7	2.2	1.9	0.9	1.3	4.1	1.3	2.5
				(1.2)	(0.3)	(0.7)	(4.1)	(4.2)	(4.2)
Peru	4.6	4.3	4.5	7.7	3.8	5.5	4.1	4.4	4.3
				(6.3)	(3.8)	(4.9)	(1.1)	(2.8)	(2.0)
Uruguay	3.0	1.9	2.4	1.5	0.0	0.6	3.8	2.3	2.9
				-(1.1)	(0.1)	-(0.5)	(0.8)	(1.2)	(1.0)
Venezuela	2.8	-0.1	1.2	3.6	1.2	2.3	2.5	-0.7	0.7
				(2.1)	-(0.3)	(0.8)	(2.2)	-(0.1)	(0.9)

Source: ECLAC, on the basis of official figures from the respective countries.

a/ The years considered for each country were as follows: Argentina, 1990, 1994 and 1999; Bolivia, 1989, 1994 and 1999; Brazil, 1993, 1996 and 1999; Chile, 1990, 1994 and 1998; Colombia, 1991, 1994 and 1999; Costa Rica, 1990, 1994 and 1999; Ecuador, 1990, 1994 and 1999; El Salvador, 1990, 1995 and 1999; Guatemala, 1989, 1994 and 1998; Honduras, 1990, 1994 and 1999; Mexico, 1989, 1994 and 1998; Nicaragua, 1990, 1993 and 1998; Panama, 1989, 1994 and 1999; Paraguay, 1990, 1994 and 1999; Peru, 1990, 1994 and 1999; Uruguay, 1990, 1994 and 1999; and Venezuela, 1990, 1994 and 1999. These correspond to the years for which employment data based on household surveys are available.

b/ This total corresponds to the sum of outputs generated by tradable and non-tradable goods and services. It differs from GDP because it does not include adjustments for banking services, value-added tax or import duties.

c/ Manufacturing industry figures are shown in brackets.

d/ Figures for government, social, community and personal services are shown in brackets.

The different patterns of specialization and linkage with international trade flows were reflected in the behaviour of employment. Total employment grew faster in countries where the new industrial production tended to dominate as a model for productive organization than in countries where expansion was based more on activities connected to the processing of natural resources. Overall, total employment expanded by 2.9% per year in South American countries, compared to 3.7% in countries to the north of the region; in both cases employment growth was relatively stronger in non-tradable activities. Wage-earning employment expanded in line with total employment in the region as a whole —more rapidly than total employment in Argentina, Chile, Costa Rica, El Salvador, Panama, Paraguay and Uruguay, but more slowly in Bolivia, Colombia, Guatemala, Honduras, Mexico and Venezuela, where self-employment tended to grow in importance (see table 10.8). Curiously, while total employment growth follows a north-south pattern, the same cannot be said about the relative importance of wage employment, which tends to mirror economic growth trends in the respective countries.

Nevertheless, international specialization patterns had a major impact on wage-earning job creation. In South American countries, wage employment grew much more slowly in tradable activities than in non-tradable activities, whereas in northern countries wage-paying jobs expanded at similar rates in both sectors. The difference is even clearer in terms of wage-paying manufacturing jobs. This category of employment expanded by just 0.7% per year in South American countries, and even shrank in Argentina, Brazil, Chile, Colombia and Uruguay, whereas in the north of the region, manufacturing jobs grew at a rate of 4.8% per year, with particularly rapid growth in El Salvador, Honduras and Mexico (see table 10.8).

The economically active population (EAP) continued to grow relatively strongly in the 1990s. In the southern countries, although EAP growth was slower (2.5% per year), weaker job creation pushed open unemployment higher at various times during the decade, depending on the country (see figure 10.3). In the northern countries, despite vigorous expansion of the active population (4.0% per year), average annual employment expanded at a similar or slightly higher rate during the decade, and urban unemployment tended to remain stable or even fall.

In the northern countries, employment in non-tradable sectors grew by 4.8% per year, which was again faster than in South American countries (3.6%). In this case, however, the stronger job creation in the north was concentrated in non-wage sectors. Social, community and personal services continued to be the activities that absorbed the most low-skilled workers, mainly self-employed, with the result that levels of informality were maintained or increased. This explains the fact that for the region as a whole, about 70% of the jobs created in the past decade were in the informal sector (ECLAC, 2001d).

Job creation opportunities have therefore clearly depended on the specialization patterns of the different countries of the region. Table 10.9 provides an overview of this phenomenon. The elasticity of employment with respect to output has been clearly higher in the countries of the north, where, in addition, wage-earning jobs expanded faster than self-employment. These patterns contrast with the weakness of labour demand in countries to the south, where most job creation has involved self-employment. The difference is particularly clear in the manufacturing sector, where employment shrank in the countries of the south, but grew strongly in the north.

Table 10.8
LATIN AMERICA (16 COUNTRIES): TREND OF TOTAL AND WAGE EMPLOYMENT, 1990-1999
(*Average annual rates of variation*)

	Total employment			Wage employment		
Country b/	**Total**	**Tradable goods and services** c/	**Non-tradable goods and services** d/	**Total**	**Tradable goods and services** c/	**Non-tradable goods and services** d/
Costa Rica	3.5	1.1	5.0	4.3	3.0	5.0
		(1.9)	(3.6)		(2.7)	(3.3)
El Salvador	4.0	3.2	4.3	4.5	3.7	4.8
		(3.8)	(1.9)		(5.0)	(3.4)
Guatemala	0.1	-1.2	2.1	-0.7	-0.5	-0.8
		(2.5)	-(1.1)		(0.9)	-(3.6)
Honduras	4.9	3.9	6.2	4.0	3.3	4.4
		(7.6)	(5.4)		(8.3)	(4.9)
Mexico	3.8	2.5	4.8	3.4	2.5	3.9
		(4.8)	(5.4)		(4.2)	(4.7)
Nicaragua	6.5	7.1	5.9	6.6	10.7	4.5
		(2.2)	(2.9)		(7.4)	(5.8)
Panama	3.2	-0.5	5.1	3.7	1.6	4.4
		(3.2)	(2.4)		(3.2)	(2.2)
Group average	**3.7**	**2.3**	**4.8**	**3.7**	**3.5**	**3.7**
		(4.0)	**(2.8)**		**(4.8)**	**(2.9)**
Argentina	2.0	-2.4	2.9	2.9	-2.6	4.3
		-(2.7)	(3.8)		-(3.0)	(4.3)
Bolivia	5.6	7.9	5.0	4.4	4.2	4.5
		(8.4)	(0.2)		(5.4)	(2.4)
Brazil	1.6	-0.4	2.8	1.8	-0.5	2.9
		-(0.3)	(2.7)		-(0.6)	(3.3)
Chile	2.4	-0.6	4.0	3.0	-0.2	4.7
		-(0.4)	(4.7)		-(0.1)	(6.6)
Colombia	1.7	-0.3	3.0	1.2	0.0	1.9
		-(0.7)	(3.3)		-(0.7)	(2.1)
Ecuador	4.2	2.7	4.6	4.0	2.1	4.7
		(1.9)	(4.7)		(1.1)	(3.7)
Paraguay	3.7	3.6	3.8	4.4	4.3	4.4
		(3.2)	(2.9)		(5.2)	(3.1)
Uruguay	1.1	-1.1	1.8	1.5	-0.3	2.0
		-(1.8)	(1.0)		-(2.0)	(1.1)
Venezuela	3.8	1.8	4.5	2.6	1.2	3.1
		(2.6)	(3.6)		(0.8)	(2.4)
Group average	**2.9**	**1.2**	**3.6**	**2.9**	**0.9**	**3.6**
		(1.1)	**(3.0)**		**(0.7)**	**(3.2)**
Overall average	**3.3**	**1.7**	**4.1**	**3.2**	**2.0**	**3.7**
		(2.3)	**(3.0)**		**(2.4)**	**(3.1)**

Source: ECLAC, on the basis of special tabuations of household surveys conducted in the respective countries.

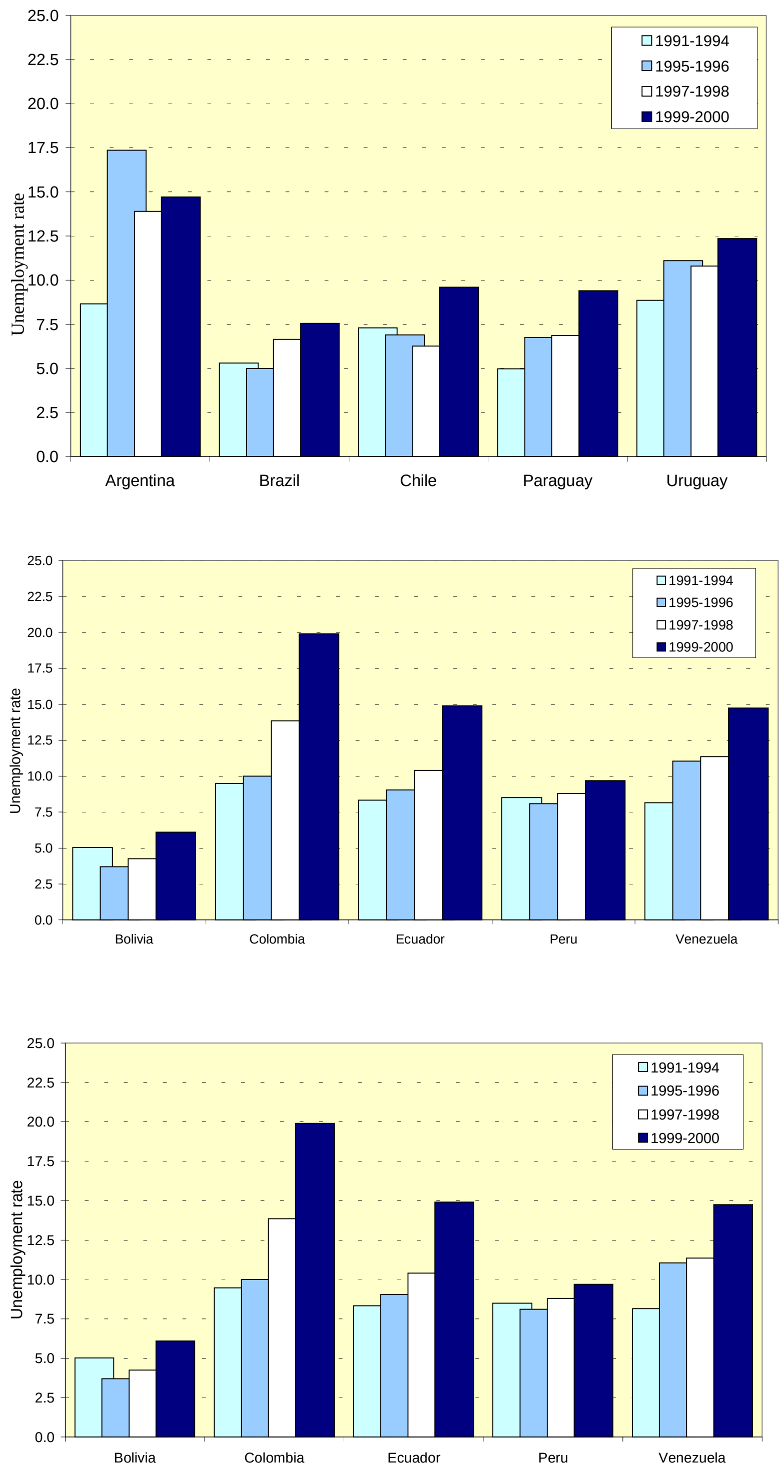
a/ The years considered were as follows: Argentina, 1990 and 1999; Bolivia, 1989 and 1999; Brazil, 1993 and 1999; Chile, 1990 and 1998; Colombia, 1991 and 1999; Costa Rica, 1990 and 1999; Ecuador, 1990 and 1999; El Salvador, 1990 and 1999; Guatemala, 1989 and 1998, Honduras, 1990 and 1999; Mexico, 1989 and 1998; Nicaragua., 1993 and 1998; Panama, 1989 and 1999, Paraguay, 1990 and 1999; Uruguay, 1990 and 1999; and Venezuela, 1990 and 1999.

b/ Geographic coverage is as follows: Argentina, Greater Buenos Aires; Bolivia, eight main cities; Ecuador, El Salvador and Uruguay, urban areas; Paraguay, Asunción and Central Department. In the other countries, the figures correspond to the nationwide total.

c/ Manufacturing industry figures are shown in brackets.

d/ Figures for government, social, community and personal services are shown in brackets.

Figure 10.3
LATIN AMERICA (17 COUNTRIES): URBAN UNEMPLOYMENT RATES BY PERIOD, 1991-1994, 1995-1996, 1997-1998 AND 1999-2000



Source: ECLAC, on the basis of official figures from the respective countries.

Table 10.9
LATIN AMERICA AND THE CARIBBEAN: INDICATORS OF EMPLOYMENT TRENDS IN THE 1990s
(*Median values of average annual growth rates*)

	Northern part of the region a/	**Southern part of the region** b/
Elasticity of employment-output	0.83	0.53
Wage employment	4.2	1.8
Own-account employment	3.6	4.0
Manufacturing industry	4.3	-0.1
Unemployment c/	10.5 8.4	7.8 12.2

Source: Barbara Stallings and Jürgen Weller, *Job Creation in Latin America in the 1990s: The Foundation for Social Policy*, Macroeconomía del desarrollo series, No. 5 (LC/L.1572-P), Santiago, Chile, Economic Commission for Latin America and the Caribbean (ECLAC), 2001. United Nations publication, Sales No. E.01.II.G.115.

a/ Costa Rica, Dominican Republic, El Salvador, Honduras, Mexico and Panama.
b/ Argentina, Bolivia, Brazil, Chile, Colombia, Paraguay, Peru, Uruguay and Venezuela.
c/ Open urban unemployment rate. The first figure is the average for 1990-1991 and the second is the average for 1999-2000.

These changing employment patterns were accompanied by a widening of wage differentials between workers with high and low levels of education. This was relatively general, however, and did not reflect specialization structures. According to information available for wage-earners in 16 of the region's countries (10 of which have nationwide data), the education-based wage gap widened significantly in Argentina (Greater Buenos Aires), Chile, Colombia, urban areas of Ecuador, Guatemala, Mexico, Paraguay, Uruguay and Venezuela. It also widened, albeit more slowly, in Costa Rica, El Salvador, Nicaragua and Panama; and it narrowed only in Bolivia, Brazil and Honduras. This relatively widespread trend towards wider earnings differentials did not reflect clearly differentiated behaviour between the tradable and non-tradable sectors. In some countries the wage gap widened more in the tradable sector than in those producing non-tradable goods and services (Colombia, Paraguay and Venezuela); elsewhere it widened by similar amounts in both sectors (Greater Buenos Aires and Guatemala); and in other countries the gap widened more among non-tradable activities (Chile, urban areas of Ecuador, Mexico and Uruguay). In countries displaying smaller overall differentials, a widening gap in the tradable sector tended to be offset by a narrowing one in non-tradable activities. Lastly, in Honduras and urban areas of Bolivia, the wage gap closed sharply in the non-tradable sector, while the opposite occurred in Brazil (see table 10.10).

Many studies have pointed out that a widening of wage differentials is contrary to predictions that trade liberalization, in countries with a relative abundance of unskilled labour, would increase the demand for such workers, and hence their relative incomes.[10] Insofar as this is a general phenomenon that does not reflect different specialization patterns, it is partly explained by technological changes, especially those related to the expansion of information and communication technologies, and by other changes in production patterns. These include the restructuring and expansion of certain services (especially financial and business, but also social, community and personal services), which generated a demand for highly skilled workers. It is also the product of shortcomings in national education systems, which have resulted in the underexploitation of new technologies[11] and greater inequality in the labour market.

[10] See Tokman and Martínez (1999), Robbins (1994 and 1996), Pissarides (1997), Wood (1997), Lora and Olivera (1998) and Weller (2001).
[11] On this topic, see Acemoglu and Ziliobotti (2001).

Table 10.10
LATIN AMERICA (16 COUNTRIES): TREND OF WAGE DIFFERENTIALS IN THE 1990s a/

Countries	Year	Total wage-earners (public and private)	Private-sector wage-earners		
			Total	Tradable goods and services	Non-tradable goods and services
Argentina b/ c/	1990	…	2.14	2.19	2.15
(Greater Buenos Aires)	1999	…	2.47	2.55	2.49
Bolivia c/	1989	…	3.46	2.66	3.73
(Urban areas) d/	1999	…	2.90	2.67	2.89
Brazil	1993	5.67	6.58	8.40	5.58
	1999	5.42	5.46	6.22	5.25
Chile c/	1990	…	4.05	4.86	3.97
	1998	…	4.87	5.51	4.70
Colombia	1991	2.57	2.59	2.69	2.63
	1999	4.12	3.82	4.85	3.76
Costa Rica	1990	2.53	2.46	1.94	2.71
	1999	2.89	2.53	2.68	2.50
Ecuador	1990	2.39	2.85	2.74	2.90
(Urban areas)	1999	2.97	3.72	3.42	3.85
El Salvador	1990	2.92	3.79	4.20	3.65
(Urban areas)	1999	3.46	3.60	4.77	3.29
Guatemala	1989	3.13	3.79	3.77	3.74
	1998	3.92	4.45	4.73	4.32
Honduras	1990	4.05	5.13	4.30	5.56
	1999	3.24	3.34	3.10	3.55
Mexico b/ c/	1989	…	2.19	2.57	2.07
	1998	…	3.32	3.25	3.35
Nicaragua c/ b/	1993	…	2.53	3.03	2.47
	1998	…	2.76	3.24	2.59
Panama	1989	2.83	2.93	2.70	3.17
	1999	3.12	3.14	3.39	3.09
Paraguay	1990	2.64	2.75	1.80	2.79
(Asunción and Central Dept.)	1999	3.22	3.62	3.45	3.46
Uruguay	1990	2.27	2.45	3.33	2.28
(Urban areas)	1999	2.73	3.14	3.83	2.96
Venezuela	1990	2.01	2.12	2.47	2.01
	1999	2.87	3.32	4.71	2.94

Source: ECLAC, on the basis of special tabulations of household surveys conducted in the respective countries.

a/ The figures represent the ratio of average incomes earned by 25-59-year-old wage-earners working 20 or more hours per week to (a) those who have 17 or more years of schooling, and (b) those with between six and nine years of schooling.

b/ Workers with 13 or more years of schooling compared to those with 6-9 years.

c/ It was impossible to distinguish between public- and private-sector wage-earners in the survey, so the figures refer to total wage-earners.

d/ Coverage in 1989 corresponds to the eight main cities, and in 1999, to the urban total.

2. Globalization and greater labour flexibility and precariousness

One of the key features of the recent phase of globalization in Latin America and the Caribbean has been the intensity of the structural adjustment policies that have been widely adopted since the mid-1980s. In this context, labour-market deregulation was seen as a necessary condition for sustaining and enhancing competitiveness, especially in the sectors most directly involved in the economic globalization process. But labour flexibility is also a consequence of globalization, since productive restructuring and new ways of organizing production processes have resulted in a wide variety of employment modalities. Greater flexibility has been a widespread feature in the region, even though countries have entered the international trade arena with different specialization patterns.

The heightened international competition and faster technological change resulting from globalization have increased the need for productive restructuring to maintain competitiveness. This produces expansion and contraction among sectors and firms, accompanied by job creation and destruction, with workers moving from those in decline to those that are in the ascendant. Moreover, the need for greater productive efficiency, in a context of unstable external demand, requires greater flexibility in production and work processes. One of the consequences of this, at the firm level, has been a proliferation of different modes of productive organization, including the formation of enterprise networks, both vertical and horizontal, and the outsourcing of tasks and processes to avoid overheads in activities that are unlikely to be maintained in the longer run or that are not central to production. These phenomena have been partly responsible for the replacement of traditional manufacturing jobs by employment in services. This situation exerts strong pressure for more flexible hiring and firing conditions.

The State’s progressive abandonment of its role as market regulator, together with the need to encourage productive restructuring to achieve integration, paved the way for a review of labour legislation with a view to reducing labour overheads, and, at the limit, transforming labour into a strictly variable cost. To some extent, labour flexibility may benefit workers, since it allows them to take advantage of opportunities generated by sectors and firms that are expanding and gives them the chance to choose among different working conditions.

Nonetheless, the acknowledged downside of greater labour-market flexibility is mainly that it has spawned low-quality jobs, characterized by instability, low pay, lack of social protection or inadequate working conditions. Thus, the higher unemployment that several countries have experienced has been accompanied by a more general process of increasing labour instability and insecurity. This stems from more flexible hiring practices and the increasing weight of informal, inherently precarious activities involving self-employment or wage-earning jobs in microenterprises or very small firms.

This process has resulted in a significant erosion of social protection in many countries. Excluding Uruguay, two thirds of wage-earners in microenterprises are not covered by social security, and there is evidence that the social security deficit among small firms also has increased significantly over the past decade. Given the increasing importance of job creation in such firms, in several cases this has reduced social-security coverage in the economy as a whole. Although the problem is mainly and increasingly concentrated in the microenterprise sector, a significant percentage of wage-earners in small and medium-sized businesses are also not covered. Even more alarmingly, a rising percentage of urban wage-earners in several countries do not have employment contracts (see table 10.11).

Table 10.11
LATIN AMERICA (12 COUNTRIES): WAGE-EARNERS WITH NO EMPLOYMENT CONTRACT AND WITHOUT SOCIAL SECURITY IN URBAN AREAS
(*Percentage of total wage-earners*)

			Workers without social security		
			Size of establishment		
Country	**Year**	**Workers without job contract**	**Total**	**Up to 5 employees**	**Over 5 employees**
Argentina	1990	21.9	29.9	64.8	18.2
	1997	33.0	37.3	74.1	22.7
Bolivia	1989	…	57.3	88.5	40.3
	1997	…	61.8	90.7	46.9
Brazil	1990	35.1	26.9	…	…
	1996	46.3	34.9	68.4	22.4
Chile	1990	15.1	20.1	42.5	13.2
	1996	22.2	19.6	43.6	13.1
Colombia	1989	37.5	…	…	…
	1996	31.0	28.5	62.5	19.0
Costa Rica	1990	…	22.5	66.2	11.8
	1997	…	26.2	71.2	14.0
El Salvador	1997	…	45.6	85.2	28.4
Mexico	1989	32.4	36.3	…	…
	1996	37.7	35.6	79.1	20.3
Paraguay	1995	64.9	64.4	94.3	47.2
Peru	1989	29.9	…	…	…
	1997	41.1	…	…	…
Uruguay	1981	…	2.8	5.9	1.9
	1997	…	3.9	7.0	2.8
Venezuela	1997	…	38.8	79.1	24.5

Source: ECLAC, *Social panorama of Latin America, 1999-2000* (LC/G.2068-P), Santiago, Chile, 2000. United Nations publication, Sales No. E.00.II.G.18. For the column "workers without job contract", the supplementary source is Daniel Martínez and Víctor Tokman, "Efectos de las reformas laborales: entre el empleo y la desprotección", *Flexibilización en el margen: la reforma del contrato de trabajo*, Paris, International Labour Organisation (ILO), 1999.

Changes in the configuration of production systems have led to the revision of labour regulations to allow greater flexibility, mainly in terms of types of contracts. More flexible hiring includes legal acceptance of contracts with fewer guarantees, aimed at encouraging temporary and occasional employment, together with measures to facilitate dismissal and reduce its cost. In the vast majority of cases, temporary jobs, or those without a contract, mean more precarious employment; this leads to less protection, fewer incentives for investing in training and weaker commitment to increasing productivity. All of this has fuelled the shrinking coverage of social protection mentioned above. For most countries, temporary wage-earning employment has grown in relative importance (ECLAC, 2001b). Except in Chile, these hiring arrangements are much more common among microenterprises and small businesses, where they tend to be over twice as prevalent as in establishments employing more than five workers (see table 10.12).

Table 10.12
LATIN AMERICA (7 COUNTRIES): INCIDENCE OF NON-PERMANENT WAGE-EARNING WORK IN URBAN AREAS
(*Percentage of total wage earners*)

			Size of establishment	
Country	**Year**	**Total**	**Up to 5 employees**	**Over 5 employees**
Argentina	1997	17.9	27.0	14.0
Chile	1990	11.0	…	…
	1998	16.9	17.7	16.6
Colombia	1984	13.4	25.9	10.1
	1990	15.5	25.1	12.6
	1998	21.6	32.3	18.4
Costa Rica	1981	1.1	3.0	0.6
	1990	9.4	20.6	6.6
	1997	9.5	20.3	6.5
Ecuador	1997	45.1	69.5	35.6
El Salvador	1995	26.3	68.2	18.2
Venezuela	1997	15.4	20.9	13.7

Source: ECLAC, *Social panorama of Latin America, 1999-2000* (LC/G.2068-P) Santiago, Chile, 2000. United Nations publication, Sales No. E.00.II.G.18.

Nonetheless, greater labour flexibility has also partly been a matter of acknowledging the way the labour market really operates and adapting the regulations accordingly. In this sense, regulatory adjustments may have helped to formalize labour and contractual relations for broad groups of workers who previously were not explicitly "covered" by the regulations. Regulations have also been introduced to defend union rights, protect women from discriminatory practices, eradicate child labour and regulate youth employment (ECLAC, 2000b).

III. Social protection

1. Social insurance and protection: dealing with risk and volatility

Social protection is intended to cover a variety of risks (obstacles to personal development, illness, loss of income) through a number of different strategies (prevention, mitigation). It consists of a set of measures relating to social security contribution regimes (illness, disability and pensions) and social assistance financed with fiscal revenues (medical attention, nutrition, employment programmes, disaster relief, transfers and subsidies).[12] Within this framework, only just over a third of the region's countries have programmes providing unemployment protection, comprehensive support in case of disability and family assistance. Also relevant in a broader sense are programmes to facilitate access to assets for low-income populations (low-income housing, access to land, microcredit and training). High levels of social vulnerability stem not only from technological deficit, poverty or highly concentrated income distribution, but also from the absence of vigorous

[12] See the work of Repetto and Sanguinetti (2001) on poverty-reduction and social safety net programmes in 14 of the region's countries; see also Castro (2000).

universal social policies (ECLAC, 2000a). The major coverage deficit is probably the largest outstanding problem among social protection systems.

It has been said that Latin America has avoided, rather than assumed, the new risk-management responsibilities required of market-oriented societies. By contrast, in industrialized countries, where growth and consumption rates are less volatile, the post-war expansion of the role of markets went hand in hand with a strengthening of social security, growth of the public sector and construction of the welfare state[13] (Rodrik, 2001c; Porter, 1999). In the region, the need for change today stems simultaneously from the historic failures and difficulties that social safety nets have encountered and from the new challenges being imposed by demographic and epidemiological dynamics and a globalization process that causes macroeconomic volatility compounded by unstable and precarious employment and earned incomes. Heightened macro- and microeconomic risks have thus spawned greater social risks and increasing demands for social protection; but these have been met by underdeveloped systems that have still not fully recovered from the crisis that engulfed them in the 1980s.

Families living below or close to the poverty line are highly vulnerable owing to the precariousness of employment and household income. Not only does poverty encompass 35% of all households and 44% of the population, but in most of the countries (between 25% and 30%) a significant portion of households have per capita incomes that vary between one and two times the poverty line. Families in this category face a high risk of falling into poverty (ECLAC, 2001c, p. 225). The generally negative income-distribution trends that persist in the region have in some cases affected poor sectors, in some cases middle-income groups, and in a few cases both.[14] This reality has called into question the increasing upward social and economic mobility seen in the region until the 1970s, which established a time horizon and a logic that led many families to delay consumption in order to invest in human capital, housing, pensions and health care.

The extent and depth of social and economic risk in the region raises doubts about its fiscal capacity to meet the requirements of social risk management. As fiscal constraints are tighter in an open-economy context, social protection has tended increasingly to be financed through arrangements aimed at maximizing the benefit-contribution ratio (insurance schemes). When this is done by undermining the system's redistributive potential, it has a negative effect on equity, Although insurance systems are good for actuarial equilibrium and financial solvency, large amounts of public funds are needed to finance the access and solidarity attributes that are fundamental for reconciling actuarial requirements with universality and equity. Moreover, redistributive tools enhance the capacity and sustainability of financing by diversifying risk.

In addition, despite the widespread existence of programmes aimed at preventing and reducing risk (nutrition, training and social investment funds), coping with crisis (emergency employment, subsidies for basic goods and services, transfers in cash and in kind) and mitigating vulnerability (contributory health and pension schemes, unemployment and disability insurance), their impact is small because of limited coverage in most countries.

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[13] As Rodrik (1998) has shown, there is a positive correlation between the extent of an economy's integration with the rest of the world and the level of public expenditure, whether on public-sector consumption or social security.

[14] Trends in the region have been highly varied during the last decade. While in some countries both middle- and low-income groups increased their income share (Bolivia and Uruguay), elsewhere both groups have lost (Costa Rica, Ecuador and Nicaragua). In other cases low-income sectors have seen their share increase while that of middle-income groups has either remained constant (Chile, Mexico and Panama) or has declined (Guatemala); or else low-income sectors have maintained their share while middle-income groups have lost ground (Brazil and Paraguay). Alternatively, middle-income groups have gained share while the poor have either maintained (Colombia, Honduras) or lost theirs (El Salvador) (ECLAC 2001c, p. 235).

In comparison to OECD countries, the absence of protection against risks stemming from greater labour-market precariousness in Latin America and the Caribbean is compounded by weakness in reducing poverty.[15] Employment protection strategies and family organization differ between the two groups, but Latin America provides less protection against employment problems and for specific groups (Uthoff and Ruedi, 2001). Family protection systems in OECD countries enable poverty to be overcome with just one household member employed full-time. In Latin America, it is generally only possible to escape poverty when two members of the family are earning income. In many families, the shortage of job opportunities and the lack of institutions to reconcile household chores with responsibilities outside the home prevent both spouses from earning incomes, with the result that they are unable to break out of poverty.

Although three quarters of households in Latin America include both spouses, only in one out of three are both employed. In such cases, the incidence of relative poverty (defined as disposable family income under 50% of the median) is 12%; when only one spouse is employed, poverty reaches 31%, and when neither receives labour income, the figure rises to 80% (see table 10.13). In OECD countries, lack of full-time employment among heads of household and spouses significantly increases the incidence of poverty in terms of primary income (i.e., before the redistributive effects of social protection systems): from below 5% to over 35% if they only work part-time, and to over 89% when there are no income earners.

In Latin America transfers under social protection programmes reduce the incidence of poverty from 31% to 26% in households where one spouse is employed, and from 80% to 62% where neither spouse works. In OECD countries, the social safety net reduces the incidence of poverty by relatively much larger amounts: from 35% to 18% among families with employment problems but where there are income earners, and from 89% to 42% when there are none. Family structures (whether nuclear or extended) also reduce poverty more effectively in OECD countries than in the region (see table 10.13).

2. Social safety nets, employment and poverty

In crisis situations, the countries of the region have tended to reinforce their strategies for reducing and dealing with risks through emergency nutrition and employment programmes, backed by in-kind transfers. Micro-lending has also been used, but to a lesser extent. Nonetheless, the coverage of such programmes is undermined by a lack of fiscal resources —a shortage that tends to become more acute when demands are greatest; i.e., at times of crisis. Groups affected by crises give high priority to risk mitigation programmes.

The low impact of protection systems, especially for those without links to the formal sector, generates a close relation between employment conditions and trends and poverty. Given the repercussions of fragile and volatile growth compounded by insufficient resources, employment measures are crucial in dealing with social risks.

In most countries, formal employment has been shrinking, but self-employed workers remain outside the social security system because their incomes are too small to pay the contribution (ILO, 2000). The urban open unemployment rate has been trending upwards in a large group of countries in the region, with 15-24-year-olds and women most likely to be unemployed (ECLAC, 2001c). Women’s employment and pay are still subject to gender discrimination (ILO, 2000).

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[15] The following analysis considers seven countries of the region (Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico and Uruguay) and seven OECD countries (Australia, Canada, Germany, the Netherlands, Sweden, United Kingdom and United States). For comparative purposes, the OECD relative poverty measure was used, estimated as 50% of median per capita disposable family income.

Table 10.13
POVERTY IN HOUSEHOLDS HEADED BY 25-64-YEAR-OLDS, BY EMPLOYMENT STATUS
(*Simple average for poverty measured as 50% of the median and family size adjusted by e=0.5*) a/

Category	Percentage of households	Relative poverty (e=0.5)		
		Measured on the basis of primary income	Measured on the basis of disposable income	Relative reduction
Latin America	100			
Households with spouse	75.0			
Without problems b/	27.6	12.0	10.2	- 15%
With problems c/	42.7	30.5	26.1	- 15 %
Total problem d/	1.5	80.4	62.3	- 23 %
Inactive e/	3.2	64.6	23.2	- 65 %
Households without spouse	25.0			
Without problems b/	17.4	26.3	19.5	- 26 %
Total problem d/	1.2	79.5	57.8	- 28 %
Inactive e/	6.4	63.6	32.6	- 49 %
OECD	100.0			
Without problems b/	62.2	3.8	2.5	- 34 %
With problems c/	27.1	35.0	18.1	- 48 %
Inactive e/	15.7	88.6	41.6	- 53 %

Source: ECLAC, on the basis of data from household surveys.

a/ Poverty estimated as 50% of median per capita family disposable income, assuming economies of scale in consumption expressed as an elasticity of consumption with respect to family size equal to 0.5.

b/ In Latin America in households with spouses when both are employed, or households without spouses when the head of household is employed; in OECD when at least one of the two has a full-time job.

c/ In Latin America in households with spouses when one of the two spouses is inactive or unemployed. In the OECD when neither of the spouses has a full-time job.

d/ In Latin America in households with spouses when both spouses are unemployed or one of them is inactive or unemployed, or households without spouses when the head of household is inactive or unemployed.

e/ When there are no income-earners in the household.

In a globalized world with rapid technological innovation, employment bears a major share of the burden of adjustment. The latter is magnified by the loss of autonomy to use monetary, exchange-rate and fiscal tools to adjust to external real or financial shocks, or by the use of such instruments in procyclical fashion. As long as high degrees of wage rigidity persist (in nominal terms at least), adjustments operate through unemployment. The requirements of competitiveness and technological change call for greater labour mobility between sectors in order to adapt to new productive requirements and mitigate the costs of external shocks.

Job stability is no longer a dominant feature of the way work is organized, and there are magnified impacts on wage uncertainty (Rodrik, 2001c). Unemployment insurance, supported by special job creation and income generation programmes, involving a net resource transfer to laid-off workers to cushion general, group or individual crisis situations, are the most common mechanisms for protecting incomes earned from employment. In some cases, they help smooth out consumption or simply replace informal self-insurance mechanisms. But despite their importance for offsetting the micro- and macroeconomic effects of labour instability, they have very limited coverage in the region.[16]

[16] A typology of programmes currently operating in five of the region's countries has been evaluated by Ferranti et al. (2000). The programmes evaluated are: the *"Trabajar"* public works programme in Argentina, which provides small incomes for a few months; the *"Probecat"* training programme in Mexico for unskilled but not necessarily unemployed youth; mandatory compensation for unfair dismissal in Peru; unemployment insurance in Brazil, financed through a contribution shared between the employer and the employee, which pays a declining percentage of the wage; and individual accounts (known as *"cesantías"*) in Colombia, financed through employer contributions, which can be drawn on in the case of loss or change of job, and to meet educational or housing expenses.

The coverage of unemployment insurance schemes in the region varies from 4% to 29% of the unemployed population; they are financed through employer and employee contributions, topped up with public funding to cover the deficit.[17] The size, conditions and sources of transfers vary considerably, and their equity and efficiency effects depend on their financial and benefit structure; in general, however, they only favour middle- and high-income groups. The individual severance payment scheme covers a small group with low risk coverage. These systems generally face major challenges, because the amounts they pay out usually exceed their established financing capacity, and they only cater to more stable workers. On the other hand, they do not discourage workers from seeking new jobs, given their low benefit level.

Special emergency job creation and training programmes target the poorest groups and are really poverty alleviation programmes, although they combine a variety of objectives (apart from income support, employment and training, they also contribute to the provision of infrastructure and regional development). Their target populations are defined on the basis of legal regulations or programme aims (age, education, level of poverty, family status, sex, geographic location, economic sector or a combination thereof). Usually they are established with time-bound objectives, although they have a tendency to become permanent. As they are financed out of public budgets funded by general taxation or borrowing, they are highly dependent on the fiscal situation at any given time. These programmes are expensive in terms of related elements and services (materials and skilled staff in charge of the programmes, remuneration for training, etc.), which erodes the real transfer to the beneficiary population.

IV. The social agenda

1. Closing educational gaps

Closing the educational deficits and gaps that exist in the region requires three simultaneous strategies: recognition of the universal right to education, strengthening of incentives for students to stay in school and institutional and pedagogic adaptation to cultural and technological change. In order to reconcile equity with multiculturalism and differentiation of identities, education needs to temper its egalitarian vocation with attention to difference. Equity requires progressively expanding coverage throughout the school cycle until secondary education is universalized and narrowing educational attainment gaps based on socio-economic origin and geographical location. These objectives need to be complemented by special programmes for specific groups, a curriculum that is more relevant to geographic realities and intensive action in situations displaying high vulnerability and social and economic precariousness.

Education development in Latin America and the Caribbean is still in a transition between basic and other, more complex levels. It faces two common challenges: the traditional and the basic, on the one hand, and new challenges related to emerging technologies, competitiveness and citizenship formation, on the other. Over the past decade, educational reforms have triggered profound changes, with a variety of emphases. The reforms were aimed at enhancing the quality of learning processes, improving the efficiency and efficacy of resource use and making access to education more equitable. The reforms have had repercussions throughout the system: teaching content and processes; funding and resource-allocation mechanisms; distribution of functions between the State and private enterprise and between the different levels of the State

[17] The employer's contribution, whether or not shared with the employee, is the most common of all forms of financing. Argentina, Barbados, Ecuador and Venezuela, together with Canada, Greece, the Netherlands, Sweden and the United States, have systems involving contributions shared between the worker and the employer. In some European countries, including Belgium, Denmark, Ireland and Norway, and in some Central and Eastern European countries, the contribution is paid by the employer and the worker, but the Government makes up any deficit. Only in Uruguay, along with Austria, France, Germany, Luxembourg, Spain, Switzerland and the United Kingdom, is the cost of unemployment insurance shared between worker, employer and government.

(decentralization); quality control exercised through a review of teaching practices and achievement appraisal; and, in more incipient form, adaptation of the curriculum to students' sociocultural conditions and labour-market requirements. The framework and the objectives of these reforms remain relevant today, and need to be based on a collective awareness of the right to education.

Making good on such commitments requires political will on the part of the governments and multiple social stakeholders, together with a diversified set of policies that each country must tailor to its own challenges and objectives. It also requires a consensus on available resources —human, economic and technological— and on the rules for their allocation. National commitments should include raising public investment in education to OECD standards at least (5% of GDP). Educational innovations should be ranked by their contribution to greater equity, primarily through their impact on continuity (ensuring students actually attend classes, improving their progression through the system and keeping young people in school) and on student achievement, especially in low-income sectors and rural areas (ECLAC, 2000a).

Efforts should aim firstly at strengthening educational continuity. The training of individuals to perform as citizens and workers in an increasingly open, interdependent and competitive world, based on intensive use of knowledge, requires the strengthening of various links in the educational process, specifically targeting the phases in which the region has deficits. This means extending the coverage of pre-primary education,[18] which today is comparatively low, and raising secondary school graduation rates so as to universalize 12 years of basic education. At this stage of the region's educational development, rates of return and opportunities for labour market entry are improved radically by the completion of secondary education. The latter years of secondary school are therefore key ones for raising the general status of workers and generating virtuous effects on equity and social mobility for the future. The pursuit of ambitious and necessary coverage targets also requires (comprehensive) cross-sectoral programmes with broad impact on access to formal education among low-income sectors, mobilizing and empowering the community to become a stakeholder in the process of expanding and improving the educational system.

In order to improve educational quality and achievement and to narrow existing gaps, the curriculum needs to be made more relevant —adapting educational content, practices and institutions to specific social, cultural, linguistic and geographic situations— and making mass use of information and communication technology (ICT) resources to enhance learning outcomes and socialize the basic tools of the knowledge society. Improving the quality of life requires the provision of knowledge with synergetic effects in areas such as health, citizenship and basic economic tools (sex education, personal care, accounting and productive knowledge for family use, use of basic technologies, and so forth). Efforts to improve quality also require additional investments and institutional changes (UNESCO, 2000a): school libraries with sufficient books and materials; teachers with post-secondary training and adequate pay working in a single school; formal appraisal of student performance; non-homogeneous student groupings and a classroom atmosphere that engenders respect and harmony among students; parental participation in the life of the school community; and special efforts among groups and in zones that display major educational deficits.

The rapid cultural and technological changes being imposed by the information society call for equally rapid and radical changes in knowledge transmission. Thus, apart from curricular content, there is a need for a general willingness to make changes in modes of learning,

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[18] The importance of preschool education is increasingly being recognized, because early stimulation is a key to educational achievement in the subsequent cycles and because socialization in school complements and often compensates for precarious socialization available in the home. Over the last decade, preschool coverage reached 40% of all children (3-6-years-olds), which is still very low, and access is precarious for low-income families. Moreover, in many cases attendance is limited to one year.

communicating and producing.[19] Cultural changes, together with a growing awareness of diversity and cultural rights, requires education to specially recognize and respect different groups and outlooks on life based on ethnicity, gender or sociocultural origin.[20] This should be a daily practice that promotes a sense of dignity among people, instils confidence in oneself and in others and gives credibility to the commitments made between different parties, promoting their appreciation of each other's capacities and confidence in the future, In this sense, it constitutes an important form of social capital for political harmony, enabling the various stakeholders to become actively involved in collective projects.

Social inclusion today necessarily involves access to knowledge, participation in networks and use of up-to-date information and communication technologies, all of which must be disseminated through the formal education system. The goals of educational equity and quality are also related to the globalization of communication and information and to new production patterns. The ever-faster circulation of existing and new knowledge, and its appropriation, have highlighted the need for changes in educational content, practices and infrastructure. This requires sustained and rapid progress towards new modes of learning and the incorporation of innovative technical supports for learning, based essentially on communication and information media —either unidirectional and audiovisual (television, video, radio) or interactive (software, teleconferencing and Internet). Greater exploitation of the culture industry, using audiovisual media to disseminate educational content, makes it possible to harmonize media-based cultural consumption and school learning, as the two feed on each other.[21] In schools located in poor or rural areas, it is essential to provide facilities for students to familiarize themselves with interactive media to which they have no access at home, nor will have in the short run. The school therefore represents the most suitable place to ensure, distribute and democratize contact with and use of the new interactive media and contents.[22] Moreover, use of the new media should encourage the design and use of educational content portals, training for education stakeholders (students, teachers, school directors and families) and progressive expansion of connectivity in the school system.[23]

Nonetheless, in keeping with these new learning supports, there is an even greater need to develop higher cognitive functions by directing learning activities towards problem solving, capacity for reflection, creativity, deep understanding, information selection, discrimination between the

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19 According to Touraine (1997, p. 326), the professional future is so unpredictable and is likely to diverge so widely from what most people attending school today will have learned that schools above all should be required to educate individuals for change, instead of developing specific competencies that will probably be obsolete or useless for most of them within a short time.

20 Cubides (1998); Hopenhayn and Ottone (2000).

21 School pupils' attention span, motivation and absorption capacity increase when audiovisual media are used, and learning activities assume a more horizontal and conversational structure on the basis of such material. As such media become more widely introduced and reflected upon critically, the school may be able to overcome the conflict between school learning and media consumption by stimulating a more selective and judicious use of cultural consumption.

22 Such equipment need not be very expensive, given falling computer and network connection costs and the possibility of obtaining contributions from private enterprise, foundations and international cooperation and of taking advantage of economies of scale in telecommunications. The most significant costs may be the maintenance and updating of equipment. Programmes such as *Red Enlaces* in Chile, the National Programme for Informatics in Education in Brazil, the Informatics Education Program in Costa Rica run by the Ministry of Public Education and the Omar Dengo Foundation, and the School Educational Informatics Network and EDUSAT in Mexico show that it is possible to make rapid progress in diffusing access to computer skills in schools (ECLAC, 2000a, chap. 3). Between 1994 and 2000 in the United States, the number of schools with network connections grew from 14% to nearly 100%, and the number of classrooms from 3% to almost two thirds, including nearly 95% of the poorest schools (Clinton, 2001).

23 In Argentina, the Educ.ar programme was set up in 2000, to give the entire educational system access to the Internet and to the most recent technological developments. The programme received initial funding from the Martín Varsavsky Foundation and subsequent support from a variety of firms, institutions and professional teams. It established itself as a corporation and has since expanded its initial capital. The project is built on three basic pillars: an educational content portal, a teacher training plan and a connectivity plan. Content that until now had been restricted to privileged environments is delivered through the portal, disaggregated by the age of the target population, to students, teachers and families. The national government directs and finances a teacher training programme throughout the country. The State will provide tools for the connectivity plan (computers and Internet connection), firstly in secondary schools, quadrupling the current number of people connected to the Internet throughout the country. Subsequently, primary schools will be connected. Funding includes loans from international organizations, the national budget, local and provincial budgets, income generated from Educ.ar, corporate sponsors and grants (http://www.educ.ar/educar/home/elproyecto.jsp).

relevant and the irrelevant and the ability to plan and investigate (Gardner, 1999). These functions are indispensable in an information-saturated environment such as that provided by interactive and audiovisual media.

Notwithstanding the achievement shortcomings in basic education, overcoming the deficits and closing the gaps at this level make it possible to visualize similar targets for post-secondary, technical and university education. There are various challenges at this level: making access more equitable, which is a powerful factor behind social differentiation; extending the supply of vocational, technical and professional alternatives in the post-secondary years; regulating quality standards;[24] and forging closer ties between technical/university education and employment/competitiveness needs, drawing the university domain closer to the world of business and public administration.

Despite the wide range of public expenditure priorities, public funding for universities cannot be renounced. It should be complemented by the various contributions of users and promoters, and the management of university funding and resources should be made more efficient through effective public-private partnerships. Public support for the development of private universities is crucial for a number of reasons: because it enables additional private resources to be channelled into higher education; because diversity of supply guarantees diversity of approach; and because healthy regulated emulation leads to better quality. Moreover, in order to substantially increase research and development activities with a view to closing the technological gap with the industrialized world, the university system should operate as a network, or network hub, so that it becomes one of the pillars of innovation systems (see chapter 7).

2. The main challenges in employment

The challenge of economic and social development at a time when the region is participating in the globalization process requires the countries to enhance productivity and international competitiveness and raise incomes for firms and workers, while at the same time developing labour security and social protection systems for workers and their families. This poses challenges in employment and wage policy design and regulation and in the new employment arrangements that are emerging from globalization. In particular, this involves preventing employment from becoming more precarious; improving the employability, adaptability and protection of workers in a context of greater occupational mobility; and adapting the role of labour administrations.[25]

Globalization has not ensured a fair distribution of the economic benefits of trade liberalization and capital mobility. Accordingly, the first challenge is to lay the foundations for complementing liberalization with social progress and less inequality. The relevant international agreements have established precise definitions of fundamental labour rights, which have been incorporated into key ILO conventions. These include freedom of association and collective bargaining, prohibition of slave and forced labour, progressive eradication of child labour and non-discrimination. The ILO Declaration on Fundamental Principles and Rights at Work and its follow-up (International Labour Conference, 1998) reaffirms the commitment of countries, entrepreneurs and labour unions to upholding the values and principles stated in the conventions and to working towards their progressive and definitive fulfilment.

Job creation, as an economic and social goal, needs to be given high priority in the design and implementation of public policies, in view of its repercussions for social cohesion and protection. Economic policies therefore need to be evaluated in terms of their contribution to job creation. In addition, recent experience at the sectoral and firm level highlights the need to vigorously expand support for the microenterprises and small and medium-sized firms that generate most of the jobs in

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[24] Public monitoring should guarantee quality with the same criteria and evaluation systems in both private and public universities (standards in programmes, teacher quality, research, knowledge-access infrastructure and administrative and financial management).

[25] For further details on the issues discussed in this section, see Tokman and Martínez (1999) and Tokman (2001).

the region, and also to improve the quality of the jobs they have already created. Achieving this aim entails the design of appropriate macroeconomic policies and policies on credit, public investment in technology transfer and business and technology training, and the promotion of productive conglomerates and linkages between large and small firms.

Participation in the world economy has substantially eroded the capacity of individual countries to implement autonomous economic policies (whether monetary or fiscal) to act on employment and wages, without undermining long-term competitiveness and job creation. The creation of new jobs is only sustainable when economic activities are competitive in the long run. This means raising productivity and reducing production costs; but to prevent the burden from falling exclusively on labour costs, progress should be based on productivity increases achieved through investment in human resources and technological development.

To bring domestic costs into line with the behaviour of productivity and improve international competitiveness, the region has attempted to reduce hiring and firing costs and non-wage labour levies[26] by adopting flexible hiring modalities. While labour costs are important, the fact that they are high or that employment contracts are rigid cannot take the blame for all problems of competition, since labour costs in Latin America and the Caribbean are well below those in developed countries.[27] Accordingly, while recognizing the potential benefits of reforming the social security regime and reducing the cost of hiring unskilled workers, the effort should focus not solely or even mainly on reducing labour costs, but on increasing productivity. Wage increases in line with productivity improvements should also be introduced into collective bargaining processes, partially linking wages to results through mechanisms enabling workers to share in company profits.

In the new context where the traditional employment career based on a “job for life” has given way to one involving frequent changes of job, firm and skill requirements, the workers affected face very high costs. For many people, restructuring leads to unemployment (of increasing duration in many countries, with significant loss of income, protection and productive capacities for those who do not get rehired). Given that restructuring is largely inevitable to ensure dynamic participation in the new international economy, workers cannot afford to be radically affected by increasing mobility, and need the ability and opportunity to adapt to new conditions and occupations while retaining social protection during periods of unemployment. This means developing workers’ employability by modernizing training and education systems and maintaining social protection (see sections below). This prospect raises the need to expand the coverage of protection systems to broad groups of workers who are currently excluded (informal and unemployed).

Lastly, increasing integration into the world economy makes it necessary to review and adapt the role of labour administrations to harmonize it with labour legislation (migration, skill certification and social security) and to adapt public administration to a labour-market policy based more on self-regulation by stakeholders and less on supervision by public authorities, which should assume a more pedagogic role. Such a policy should reach beyond the business and economic sectors to achieve national scope, and extend beyond the confines of wages or labour relations (social dialogue). Modernization should be accompanied by the political and administrative repositioning of the relevant ministries so that they can participate in the economic cabinet and overall government action; in many cases, they will have to reclaim labour-market policy and legitimize their capacity as interlocutors with labour unions.

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26 Social security contributions, payroll taxes to finance housing, education, training and child protection.

27 On average, minimum wages in Latin American countries are below their levels of 17 years ago, while manufacturing wages are practically at the same level as in 1980. The hourly wage in manufacturing in 1997 was less than US$ 1.5 in Colombia, Mexico and Peru, US$ 2.5 in Chile, US$ 3 in Brazil and just over US$ 4 in Argentina, compared to nearly US$ 7 in Korea, US$ 13 in the United States and US$ 15 in Germany. Labour costs are lower still in the case of wage-earners working without a contract or with a temporary one. See Tokman and Martínez (1999).

3. Education, training and employment (employability)

Skills for work now need to be developed on a more continuous basis, and possibly in a different institutional framework. Educational requirements for employment are rising, yet average schooling among workers in Latin America and the Caribbean currently stands at just seven years. Accordingly, to enhance future workers' capacity to raise productivity and embrace the world of new technologies, their education (number of years' schooling) urgently needs to be increased. This would clearly also include changes in the educational profile of school leavers (quality).

The new technologies and work processes increasingly demand greater creativity, initiative and versatility, and less specialization. It is therefore necessary to develop basic competencies, rather than specific skills, to provide workers with a knowledge base enabling them to better adapt to new jobs. These considerations have implications for basic education and for post-secondary and vocational education systems. The contents of formal education need to be related to skill demands emerging from the labour market, and the quality of basic education, where basic capacities are developed, needs to be improved.

International disparities in learning, achievements and technical training alternatives urgently need to be overcome in order to narrow the productivity gap. Experience in developed countries suggests that a larger and better-quality supply of technical and professional education at the secondary and higher levels has highly positive effects on labour-market participation, making it possible to raise general productivity. To expand the coverage of technical and professional education in Latin America and the Caribbean, and also to make it more relevant to changing labour requirements, the business world needs to be involved (curricular programmes, internships, longitudinal surveys and mutual consultation). This would enhance the appropriation of technology in the workplace and is a suitable field for disseminating new technologies.

4. Social protection systems

The persistence of high levels of poverty and inequality in Latin America and the Caribbean calls for a political reorientation of institutional frameworks and collective commitments. Social protection in the region still suffers from major deficiencies both in its traditional coverage and with regard to the new risks arising from globalization, such as greater mobility and job instability, Income inequality in the region, together with the level of unemployment and the high incidence of poverty, call for new schemes of protection, on a par with traditional health, education, old age, disability, housing and child protection programmes.

In addition to changes originating in labour markets, structural changes are also occurring in the region, and these impose new demands on the funding requirements and coverage of social protection. These changes presage substantial increases and transformations in the demand for social services in the future; they include population ageing, epidemiological change and smaller household size. The improvement of social protection should be guided by the principles of universality, solidarity, efficiency and comprehensiveness. This approach will guarantee progress in fulfilling internationally established economic, social and cultural rights, thereby strengthening citizenship (ECLAC, 2000a, vol. 2).

In the first place, significant progress needs to be made towards universal social protection, reducing the glaring inequities that exist in the quality of the services provided and in access to them. In addition, resources must be used in a more effective and socially efficient way. Their management and allocation must be improved and funding mechanisms must be strengthened through appropriate combinations of public resources with mandatory social and private insurance. Given the type and magnitude of poverty and risks in the region, protection systems need to combine risk grouping and diversification. Policies strictly targeting the poorest sectors of the population are not sufficient, nor do they allow appropriate and stable differentiation of risk.

Solidarity, achieved through compulsory contributions and public transfers to universal forms of insurance, makes it possible to establish cross-subsidies between different income strata and risk groups. Public funding, to bear the cost of protecting those who are unable to pay, guarantees solidarity while also strengthening the financial soundness of saving and insurance systems. To overcome the current segmentation of the population between different social protection subsystems, insurance functions need to be integrated with those aimed at redistribution and solidarity. Emphasis should be placed on systems of mandatory insurance with high collectivization of risks, since they ease fiscal pressure and enhance equity.

Contemporary globalization has made both consumers and factors of production more mobile, and is forging new arrangements between the public- and private-sector economies. Most reforms in the 1990s included active private-sector participation in the provision and financing of services; this has tended to favour the insurance function over redistribution, thereby placing the burden of redistribution and solidarity on general taxation. Although, in principle, such insurance results in better actuarial balance and better time adjustment, it does not guarantee universality and social inclusion when underconsumption and inequality of insurance affects broad social sectors of the population and not just the poor.[28] Apart from solidarity, the public function in protection also includes regulating risk selection in insurance policies and preventing high transaction costs.

Naturally, both the quantity and quality of social protection are conditioned by the level of economic development that makes them possible, and also by existing fiscal covenants containing political and social agreements on the level of welfare that should be guaranteed to citizens (ECLAC, 1998c and 2000a). The necessary increase in social spending should occur in the context of fiscal situations that are sustainable over time, while strengthening the actuarial balance of social protection systems. Allocating the necessary funding requires the definition of the breadth and levels of protection to be provided, up to the limit of countries’ structural fiscal capacity. This approach is not static: the fiscal covenant to protect rights should include rules on progressivity, such as a rising marginal public contribution to social protection and to poverty alleviation in line with economic growth. Also, in this case, social protection programmes should not be allowed to become vulnerable; it is therefore essential to design their development, financing and operation in the context of countercyclical policies that have real capacity to cushion the economy against situations that generate vulnerability and impoverishment.

Lastly, building inclusive social protection[29] means giving particular importance to the value that affected groups place on the State’s responsibility to guarantee a decent standard of living and social welfare. Those affected put a higher value on programmes that guarantee minimum subsistence levels for the family group (subsidies, microcredit, nutrition and free access to health care and education services); and they place a lower value on food subsidies, emergency employment programmes and training, unemployment insurance and transfers, whether in cash or in kind (Repetto and Sanguinetti, 2001). It is therefore important to provide permanent and intensive information services in order to spread awareness of the forms of protection available and of mechanisms for gaining access to them.

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[28] This criticism alludes to the paradigm of “social risk management”, the foundations of which are developed in World Bank (2000b and 2001e), and in Ferranti and others (2000). A critical synthesis is provided in Sojo (2001). Dealing with risks through insurance hinders universality for several reasons: (i) insurance markets are underdeveloped; (ii) the population’s need for protection does not translate into effective demand for insurance when wages are unequal, low, unstable and uncertain; and (iii) generally speaking, insurance is mandatory and feasible only for full-time wage-earners with permanent jobs.

[29] The social cohesion and integration fostered by social protection no longer affect the local or national level alone, but have come to be seen as global public goods. Social protection should form part of the global strategy to combat the violence, desperation and fanaticism that are used to justify terror; and it is essential to address the deep social inequalities that exist in order to build confidence in a more peaceful and predictable world (Kaldor, 2001; Savater, 2001).

5. Social protection and employment

While access to social protection is highly dependent on people's labour market participation, the changes occurring in labour markets affect the demands placed on social services and their funding sources. Thus, the high incidence of informality (70% of all new jobs created in urban areas of the region's countries over the last decade), together with unemployment, impose constraints on the universalization of social protection under current schemes and the ability of the latter to base their funding on payroll contributions.

Increasing social protection in accordance with labour market structures requires development in two related but different domains: (i) in view of the highly precarious nature of employment, extending the main protection systems (those aimed at upholding economic, social and cultural rights) to ensure that access to them is determined by citizenship and not exclusively by formal labour-market participation; and (ii) addressing the risks associated with employment and income. Current social security systems need to be adapted to maintain protection in the face of more frequent job changes, to prevent workers from suffering a drastic loss of benefits and to increase incentives for them to embrace productive restructuring. This means that reforms of social protection systems in general, and social security in particular,[30] should introduce mechanisms to guarantee protection in a climate of greater labour mobility. If social protection systems function so as to support labour mobility, the capacity of the labour market to respond to external shocks will be greatly enhanced. This requires portability of social security benefits, in particular health, pension and unemployment benefits, and guaranteed permanent access to a basic safety net (health, education and food), regardless of the beneficiaries' mode of labour-market participation.

The higher social and economic risk generated by more volatile income levels should be addressed with social protection mechanisms to stabilize the level of individual and national income, which means allocating a significant fraction of public expenditure in the form of social insurance against external shocks. However, it must be recognized that the demands imposed by an unemployment insurance programme of broad coverage represent a severe strain on the region's resources. Perhaps the most reasonable course of action in the years to come would be to establish individual forced saving mechanisms, generally funded through employer and employee contributions, but with partial solidarity mechanisms.[31]

Since some groups of workers are not protected by such systems, special employment programmes should be deployed at times of overt crisis (whether national, sectoral or local), although not as a universal scheme. Such programmes should have a permanent and flexible institutional structure so that they can be deployed quickly at critical times.

6. Social agenda for regional integration and cooperation

The major challenges of human and social development need to be assumed by each nation. Nonetheless, in the context of an increasingly intensive process of economic, social and cultural globalization, projection towards a regional and world agenda for education, employment and social protection is of decisive importance.

The relative unity of language that exists in Latin America, on the one hand, and the English-speaking Caribbean, on the other, provides favourable conditions for creating or strengthening regional integration initiatives in education. Through meetings of experts, governments, academics and organizations, and with electronic network communication, it is perfectly possible to share

[30] On trends, progress and constraints in relation to reforms of social security systems in the region, see ECLAC (1998e and 2000a).

[31] The systems that exist in a number of countries (Brazil, Colombia and Peru), and those proposed in Argentina and Chile, aim to replace severance pay with individual funds based on contributions made by employers and employees, which can be drawn on in the event of dismissal or resignation. They enable workers to maintain protection while finding a new job, without losing what has already been acquired.

information on topics such as best practices, the results and weaknesses of reforms, successful and imaginative experiences in making the most of scarce resources, new teaching methods and school computerization programmes. The more this information is shared, the richer education policy can become; the socialization of experience and creative imagination is the first step towards integrating progress in education region-wide.

Curricular integration is another area in which progress should be made. Joint exploitation of developments is feasible in areas such as educational content, software, portals and textbooks;[32] comparison and standardization in the evaluation of educational achievement; setting of standards by level; and shared criteria in teacher professionalization and in-service training. All of this strengthens national education systems while facilitating progress towards the introduction of regional accreditation systems, international recognition of qualifications awarded by educational institutions and subregional or regional regulatory agreements to streamline mutual recognition of qualifications.

In a different domain, it is also important to educate for regional integration. This means strengthening awareness of belonging not only to a nation but also to a broad region with a shared language, culture, history and possible destiny. Basic education affords the best means of instilling a deeper sense of regional belonging and reversing xenophobic attitudes.[33] Given education's mass coverage, schools are the most appropriate place from which to transmit values systematically to the community.

On employment issues, two general principles have guided international action since the World Summit for Social Development (Copenhagen, 1995), and should continue to do so: (i) preventing the expansion of world trade from violating workers' fundamental rights; and (ii) avoiding a levelling-down of wages and working conditions between countries with different development levels. International action should continue to be based on promoting and evaluating progress in applying these basic principles and upholding the labour rights enshrined in the relevant agreements, as ILO has been doing pursuant to its received mandates. Naturally, the agenda includes regional joint ventures on productive projects, professional training and labour migration.

Internationalization requires rapid regional convergence among social protection systems. Globalization has promoted greater mobility of labour, factors of production and consumers, but this has only generated opportunities for a small fraction of highly skilled workers. Tight restrictions remain on the free mobility of unskilled workers, and current systems of social protection and recognition of qualifications do nothing to encourage such mobility. Protection for migrants requires international coordination to tackle discrimination and ensure the transferability of qualifications and social protection entitlements.[34] Integration agreements dealing with international labour mobility require harmonization of social security policies based on three fundamental principles: (i) equal social security treatment between nationals and non-nationals; (ii) continuity of coverage (that is, portability of accumulated benefits and the ability to continue making contributions); and (iii) formal determination of applicable social security legislation. In the medium term this should lead to greater standardization of social protection systems across

32 Scale and/or network economies make the production of such materials much more viable and profitable if they are developed region wide rather than on a national scale. It would therefore be useful to explore the potential for alliances and joint actions between countries and organizations in the region.

33 This requires reviewing the content of teaching and its possible connotations, especially in relation to the history, geography or politics of other nations and cultures living in the region and whose populations move across borders. Unfortunately, part of taught history recounts military triumphs against neighbouring countries, but makes very little reference to cooperation between countries, the contribution made by foreign citizens to national cultural wealth or regional integration.

34 The specific problems faced by illegal migrants need to be considered in this context. Illegal migrants form a significant excluded group, either because their jobs are precarious and unprotected or because they do not have guaranteed access to minimum social services provided by the State to all its citizens; moreover, their pay is generally below prevailing wage rates. Regularizing their migratory status is therefore a prerequisite for social and labour-market inclusion. Migration issues are analysed in detail in chapter 8 of this volume.

countries, at least at the regional and subregional levels, with a view to developing international portability of social protection benefits and academic and job credentials. Workers would then be able to make contributions in one country and demand services in another, and accumulate benefits in different countries.

The evolution of social security systems towards individual contribution schemes (individually owned accounts) with variable benefits may facilitate contribution and benefit portability, as well as progress towards universal insurance.[35] Accordingly, one of the obligations is to work towards establishing minimum shared standards and structures, and unified patterns of costs and benefits. Nonetheless, individual insurance systems impose financial constraints, and others relating to risk segmentation and coverage, which make national and international portability of benefits difficult.

In addition, greater integration with the world economy means that the region's countries will face heightened demands for social spending to alleviate the greater economic and social risks arising from such integration. In view of domestic financial constraints on the capacity to expand social expenditure, it would be useful to explore the possibility of setting up international, regional or subregional social funds to support national efforts (see chapter 4).

[35] This is especially valid in the case of pensions involving individual capitalization systems, which provide mechanisms allowing contribution and benefit portability.

Chapter 11

The effects of globalization on CARICOM Caribbean economies

The recent globalization process poses significant challenges to small developing economies such as those in the Caribbean, which are already dealing with a number of issues in their pursuit of sustainable development. For Caribbean countries, the impact of globalization on trade has been reflected in increased liberalization and market-opening policies, especially during the latter part of the 1980s and the 1990s. Influenced by the paradigm shift in policies at the global level, Caribbean countries responded with a package of policies geared towards limiting the role of the State in the economy and reinvigorating stagnant production systems, which were reoriented towards export markets. Trade reforms were implemented and regional integration gained new impetus.

The reduction of trade barriers and the increasing openness of these economies have not led to a significant increase in intraregional trade or helped them to obtain a growing share of the extraregional export market; as a result, these countries' growth potential has been limited. Caribbean economies lack trade-product complementarity to foster intraregional trade and have not substantially changed the composition of their exports. In fact, they are dependent on preferential market access schemes granted by developed countries. In addition, Caribbean economies are characterized by differences in per capita income and stage of development that are hard to reconcile with deeper integration schemes.

Globalization has both fostered and brought to light a process of sectoral change in the composition of output in favour of the services sector and to the detriment of agriculture and manufacturing. This process accentuates the differences among Caribbean economies by creating a dual pattern of specialization, so that the countries are divided between service-based and goods-producing economies. It also highlights the dependence and vulnerability of these economies. While export growth has been subject to the vicissitudes of the agricultural and manufacturing sectors, import growth, driven mostly by consumer goods, has not receded. This has created a need to attract foreign capital to further stimulate the growth and development of sectors that have been successful under globalization. Trends in employment and migration have mimicked these changes in output and capital flows.

Within this scenario, in most countries macroeconomic policy has been geared towards maintaining macroeconomic stability by adhering to pegged or fixed exchange-rate regimes. The result is that inflation has been lowered to single-digit levels. In small open economies such as the Caribbean ones, which are constrained by their external sector, fiscal and monetary policy control absorption, which is the main adjustment lever. This strategy precludes the use of countercyclical fiscal policies. This may ultimately give rise to a tendency towards low growth levels and hinder the achievement of a full-employment potential level of output.

In this chapter, the impact of the globalization process on countries in the Caribbean community is discussed. The chapter comprises six sections. The first examines regional integration issues; the second focuses on structural change under globalization; and the third centres on the evolution of capital flows in the Caribbean. The fourth section deals with labour issues and migration; the fifth focuses on macroeconomic performance and policy; and the last section addresses sustainable development issue.

I. Caribbean integration as a positive response to globalization

During the 1990s, the trade regime in the Caribbean region underwent important changes, signaling a desire to move away from the inward-looking policies of the past towards a policy of open regionalism. This meant not only diversifying its trade links with extraregional trading partners,[1] but also, and most importantly, deepening and perfecting the current intraregional integration regime and institutions. As with other trade agreements that proliferated in the 1990s, the Caribbean response was aimed at guaranteeing and protecting regional access to markets in the face of a process of globalization which, in principle, was supposed to provide equal market access for all.

The subregion took steps to strengthen the Caribbean Community (CARICOM) integration grouping. In 1989, member States of the Community agreed “to advance beyond the Common Market[2] towards more comprehensive integration, recognizing that while it had achieved significant liberalization of the market for goods, the further development of the regional economy was constrained by restrictive Treaty provisions limiting the free movement of services and capital and skilled labour” (CARICOM, 2000a).

This was the genesis of the CARICOM Single Market and Economy (CSME). It was intended to achieve a much broader and deeper integration than had been possible under the existing treaty and, through the development of economies of scale, to increase the competitiveness of these countries in the global economy. The creation of CSME was also meant to enhance the

[1] In the 1990s, CARICOM signed free trade agreements with Venezuela (1992), Colombia (1994) and the Dominican Republic (1998).

[2] The treaty establishing CARICOM (1973) provided for the creation of two distinct entities: the Caribbean Community and the Common Market.

bargaining position of CARICOM countries in international negotiations such as those at the level of the World Trade Organization (WTO) and the future Free Trade Area of the Americas (FTAA).

Its objectives included the free movement of goods, services, capital and persons; more intensive coordination of macroeconomic policies and economic relations (see box 11.1); and the harmonization of laws governing trade and other economic activities within the common market area. It also provided for full application of the Common External Tariff (CET). This entailed simplifying the CET structure and reducing its level, with a view to diminishing its protectionist content. The structure of CET made a distinction between competing and non-competing imports, as well as between inputs, intermediate inputs and final goods, forming a hierarchy in which non-competing inputs bear the lowest tariff and competing goods the highest tariff.[3]

The CET structure comprised four tariff rates (0%, 5%, 10% and 15%) and a maximum tariff rate of 40% for primary agricultural products. The schedule for the phased reduction of the tariff was established in 1992 and provided for the reduction of tariff rates over a period of five years, with effect from January 1993 to June 1998. Tariff reform was also complemented by changes in quantitative measures.

Box 11.1

MACROECONOMIC CONVERGENCE IN CARICOM

At the regional level, CARICOM member States continue to strive to achieve macroeconomic convergence. Open regionalism, inspired largely by the European Union and the ECLAC model, has acted as a catalyst for macroeconomic surveillance. CARICOM has also put in place convergence criteria to facilitate macroeconomic coordination. These include advancing the Single Market and Economy, joint management of the adverse impacts of globalization and the creation of a monetary union (CARICOM 2000). The CARICOM criteria are modelled on those of the European Union. They aim to foster stability and consistency in policy making by targeting key macroeconomic variables. At a deeper level macroeconomic convergence is geared towards fiscal discipline, a favourable balance of payments, stable prices, stable and competitive exchange rates, and high levels of quality employment.

At present, the convergence criteria are based on the following performance indicators:

- A reserve-cover rule based on the maintenance of three months of import cover or 80% of demand liabilities, for a period of at least 12 months.
- An exchange-rate rule that stipulates the maintenance of a stable exchange rate within a band of 1.5% for a period of 36 months.
- An external-debt rule that requires members to maintain a debt-service ratio not exceeding 15%.

Given their persistent current imbalance, the exchange-rate rule has been the most difficult criterion for countries with flexible regimes to achieve. The Guyana dollar has been above the upper limit of the band since 1998, while the Jamaican dollar has met the band limits only once since 1995 (in 1997). Most countries have had more success with the other criteria. The average import cover surpassed the three-month target between 1995 and 1999, while the average debt-service ratio has stayed within the band of 15% of exports of goods and non-factor services.

A number of other variables, including growth rates, inflation, unemployment, fiscal balance ratios —overall fiscal balance as a percentage of GDP— and interest rates have also been monitored. The indicators show significant variability and volatility. Variability was highest in inflation rates, interest rates and growth rates. The high level of volatility and the different paces of structural adjustment indicate that the countries are unlikely to converge in the near future. Plans for monetary union may therefore have to be put on hold.

Source: CARICOM Secretariat (2001).

[3] Competing goods are those in regard to which regional production satisfies 75% of regional demand.

Implementation of the CSME called for the creation of new institutions to manage the deepening of the integration process. The original treaty has therefore been amended by nine protocols affecting the structure of the organization, the movement of capital and labour, and policies regarding trade, agriculture and transport in the region.

The new integration framework maintains the recognition of differences in size and development contained in the treaty establishing the Caribbean Community (Treaty of Chaguaramas, 1973). The treaty's Common Market Annex differentiates between less developed countries (LDCs) and more developed countries (MDCs) (Barbados, Guyana, Jamaica and Trinidad and Tobago) among CARICOM members.

Its provisions consist of a special regime for LDCs so as to provide support and minimize the possible negative effects arising from the competition of MDCs. This takes the form of derogations from the obligations established by the original free trade agreement. These derogations include the right to apply duty and/or quota restrictions on certain products for a specified period and to maintain duties on specific goods for revenue purposes. They also allow for a longer period in which to comply with the implementation of CET and for lower value added requirements for certain products under the applicable rules of origin.

This renewed impetus to foster integration among Caribbean countries has not been totally successful. Progress towards regional integration has been slow and incomplete. Almost 10 years after the decision to implement the Common External Tariff, eight out of the 13 CARICOM members are in the final phase of implementation. Some non-tariff barriers, including the application of duties, licensing requirements and others, remain a pervasive feature of CARICOM. Quantitative restrictions and non-automatic licensing requirements on beverages and agricultural and food products have been also widely used. In addition, import quotas, import prohibitions, price controls, safeguards and countervailing measures are still in place.

Thus, CARICOM remains a fragile regional trade arrangement. Intraregional trade represents only 10% of total trade (see table 11.1), which is a lower share than in other regional trade agreements such as the Central American Common Market, the Andean Community or MERCOSUR. This underscores the fact that many economies produce a narrow range of commodities that are near-perfect substitutes and highlights the dependence of CARICOM on extraregional markets.

Intraregional trade is also highly concentrated. Trinidad and Tobago accounts for more than half of all intraregional imports, while other countries contribute a minimal amount to trade flows (see table 11.2). This ultimately means that the workings of an integration scheme depend on the willingness of a few members to maintain the existing arrangements.

In addition to a low degree of trade complementarity, part of the difficulty in fully implementing a single market and economy stems from the differences among CARICOM members. Caribbean countries exhibit disparities not only in terms of size, per capita income and stage of development, but also in terms of their production structures. Despite the fact that these differences are recognized in the Treaty of Chaguaramas and that the Caribbean countries support open integration schemes and market-oriented policies, the differences among them have not receded. These differences are a legacy of their history (Williams, 1984) and remain to this date a pervasive feature of their economies.

Table 11.1
CARICOM: EXPORTS AND MARKET SHARE, 1985-1999

Regional bloc	**CARICOM: Exports by regional trading bloc and market share**			
	1985	**1990**	**1995**	**1999**
NAFTA	47.4	48.1	50.1	47.4
Europe	18.8	17.4	16.6	16.3
CARICOM	7.7	7.9	9.1	9.7
Andean Community	5.9	6.7	6.2	8.7
MERCOSUR	2.3	3.9	2.4	1.9
CACM	1.1	0.7	0.8	1.1
Regional bloc	**CARICOM: Market share in other regional trading blocs**			
	1985	**1990**	**1995**	**1999**
NAFTA	0.71	0.43	0.32	0.26
Europe	0.15	0.13	0.12	0.10
Andean Community	0.40	0.96	0.41	0.30
MERCOSUR	0.30	0. 34	0.19	0.07
CACM	0.20	0.18	0.38	0.66

Source: ECLAC, *Competitive Analysis of Nations*, 2001 edition. Estimated on the basis of purchases of importing countries.

Table 11.2
CARICOM: DISTRIBUTION OF INTRAREGIONAL IMPORT MARKET SHARE, BY MEMBER COUNTRY, SELECTED YEARS BETWEEN 1985 AND 1999
(Percentages)

Country of origin	**1985**	**1990**	**1995**	**1999**
Trinidad and Tobago	2.81	4.08	5.32	5.49
Barbados	1.01	0.84	0.9	1.14
Suriname	0.06	0.14	0.42	0.81
Jamaica	1.3	1.15	0.79	0.7
Guyana	0.62	0.35	0.53	0.56
Saint Vincent and the Grenadines	0.73	0.35	0.3	0.27
Saint Lucia	0.26	0.27	0.21	0.19
Dominica	0.26	0.23	0.24	0.19
Belize	0.22	0.18	0.09	0.11
Grenada	0.13	0.13	0.09	0.1
Bahamas	0.13	0.14	0.09	0.04
Antigua and Barbuda	0.11	0.08	0.05	0.03
Saint Kitts and Nevis	0.07	0.04	0.03	0.01
Total	7.71	7.98	9.06	9.64

Source: ECLAC, *Competitive Analysis of Nations*, 2001 edition.

II. The process of structural change under globalization

The process of globalization has been a linchpin for the development of specific sectors but has not provided the means to overcome the weaknesses and stumbling blocks that have marked the development of some of the more traditional sectors. In this regard, it has reinforced a process of change in sectoral output and, in so doing, has made the existing disparities among CARICOM countries more visible and transparent.

During the 1990s, many Caribbean economies experienced a shift in the sectoral composition of output from agriculture and mining to the service sector, while the manufacturing sector remained stagnant. In terms of weighted averages, agriculture accounted for 13.5% of output in 1990 and 9.5% in 1999 (excluding Guyana).[4] For the same years, manufactures represented 12.7% and 11.6%. The service sector increased its contribution to output from 39.1% to 46.6% (see table 11.3).

In the case of the agricultural sector, this change in the composition of output has reflected a loss of competitiveness resulting from high production costs, external shocks and a heavy dependence on trade preferences granted by the European Union. High production costs impinge on profit margins, thereby reducing the incentive to expand production, while external shocks such as those caused by natural disasters have destroyed both infrastructure and crops in cultivated areas. Finally, Caribbean countries have remained dependent on preferential trade access schemes such as those granted by the Lomé Convention agreements and their successor, the Cotonou Agreement.[5] Preferential schemes that benefit traditional products —extended temporarily at the fourth WTO Ministerial Conference (9-13 November, 2001, Doha, Qatar)— may help to postpone an adjustment that is bound to occur under globalization.

The trends and performance of the banana sector during the 1990s illustrate some of the shortcomings affecting a traditional agricultural sector. Banana production and exports from Caribbean countries, particularly the Windward Islands (Dominica, Grenada, Saint Lucia, and Saint Vincent and the Grenadines), experienced a sharp decline.

At the beginning of the 1990s, banana production represented more than 12% of GDP for the Windward Islands; by 1999, the figure had decreased to 7%. In addition, between 1993 and 1999, the overall export volume declined by more than 50% (238,878 tons in 1993 and 130,419 tons in 1999). During the same period, the number of active growers declined from 24,111 to 11,665. The banana sector has also been affected by the WTO dispute concerning the legitimacy of the European Union import regime for bananas.[6]

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4 The data on agriculture exclude Guyana. This country experienced a 300% increase in sugar cane production from 1990 to 2000, which, as shown in table 3, distorts the average for the region.

5 The Lomé Convention provides the framework for trade and cooperation between the European Union and ACP (Asian, Caribbean and Pacific) States. The first Lomé Convention was signed in 1975 (with 45 ACP countries) following the accession of the United Kingdom to the European Community. Lomé II followed, in 1975 (with 58 ACP countries); Lomé III, in 1984 (with 65 ACP countries); and Lomé IV, in 1989 (with 68 countries in 1989 and 70 in 1995). Under Lomé IV, all CARICOM exports enter the European Union duty free, and the agreement also establishes special regimes for bananas, rum, beef and sugar. The Cotonou Agreement (Cotonou, Benin, 23 June 2000) replaces the Lomé Agreement and is valid for a period of 20 years, with periodic reviews every five years. The Cotonou Agreement overhauls trade relations between the European Community and ACP States.

6 In 1997, Ecuador, Guatemala, Honduras, Mexico and the United States challenged the European Community regime for the import, sale and distribution of bananas that had been established in 1993. This regime consisted in the establishment of a tariff quota of 2 million tons allocated to Latin American countries and non-traditional ACP bananas. A solution was finally reached in 2001. The agreement provided for the adoption of a tariff-only regime by the European Union, to be implemented no later than 1 January 2006. In the interim, the regime to be applied consists of a two-phase quota scheme. At the fourth Ministerial Conference in Doha, WTO waivers were approved, permitting continued temporary tariff preferences for ACP imports. European Community Council Regulations No. 2587/2001 (19 December 2001); No. 896/2001 (May 2001). (WTO) WT/MIN(01)/15 and WT/MIN/(01)/15 (14 november, 2001).

Table 11.3
SECTORAL SHARE OF OUTPUT, 1990 AND 2000
(Percentages)

	Agriculture		Mining		Manufacturing		Tourism		Financial services		Other services	
	1990	2000	1990	2000	1990	2000	1990	2000	1990	2000	1990	2000
Antigua and Barbuda	4.2	4.9	2.0	2.2	3.4	2.8	14.4	14.4	7.2	11.2	18.9	25.1
Barbados	7.3	6.1	0.8	0.9	10.0	9.3	13.9	15.0	0.0	0.0	7.8	8.3
Belize	18.4	21.0	0.7	0.8	17.2	17.2	19.2	19.8	5.1	5.2	25.2	24.8
Dominica	25.0	18.2	0.8	0.8	7.1	7.2	2.1	2.4	11.3	13.2	16.2	20.9
Grenada	13.4	10.1	0.4	0.6	6.6	9.9	5.8	11.8	7.8	12.9	20.1	30.5
Guyana	23.6	35.4	9.5	10.9	11.1	11.7			6.0	5.7	8.7	8.5
Jamaica	6.2	7.1	8.7	9.1	21.1	15.8			9.2	14.9	9.4	16.9
Saint Kitts and Nevis	6.5	3.8	0.4	0.5	12.9	14.3	7.6	9.0	8.0	19.3	15.0	17.6
Saint Lucia	14.6	7.7	0.4	0.5	8.2	5.9	9.6	13.3	7.3	10.6	16.8	20.0
Saint Vincent and the Grenadines	21.1	12.0	0.3	0.3	8.5	5.8	2.2	2.5	7.6	9.6	20.5	25.2
Suriname	9.3	11.1	9.1	17.8	13.0	10.6	12.1	10.6	17.8	9.3	5.4	8.9
Trinidad and Tobago	1.9	1.8	57.7	56.5	4.5	6.0	5.7	7.3	5.0	4.7	5.9	6.2
Weighted average a/	17.2	18.6	39.4	36.8	12.7	11.6	39.1a/	46.6a/	.....	......	......	......
Weighted average for agriculture (excluding Guyana)	13.5	9.5	.....	.....	.....	......	......	.....	......	......	......	.....

Source: ECLAC, Selected statistical indicators of Caribbean countries, vol. 14 (LC/CAR/G.666), Port of Spain, ECLAC Subregional Headquarters for the Caribbean, November 2001.

Note: "Other services" includes communications and transport.

a/ The weighted average was estimated for agriculture, manufacturing and the service sector as a whole (including tourism, transport and Communications).

Other commodities, such as rice and sugar, have not been hit as hard as the banana sector. In the case of Guyana, sugar and rice have benefited from measures designed to improve the organization of production, infrastructure and access to better technology. In particular, sugar cane production increased its contribution to Guyana's GDP from 9% to 17% between 1990 and 2000.

In the 1990s, the manufacturing sector, with a few exceptions (Grenada and Saint Kitts and Nevis), declined or remained at a standstill (see table 11.3). This result is the outcome of the performance of its different components. In the Caribbean, the growth and development of manufacturing has been shaped by agricultural development (Guyana) and natural resource exploitation (Trinidad). It has also responded to the successes or failures of economic policies aimed at promoting inwardly or outwardly directed integration (Jamaica). Thus, the impact of globalization on the manufacturing sector is linked to its effect on agriculture, on natural resources or on the variables that determine the outcome of a given policy orientation.

While recent globalization has made the decline of agriculture and the associated manufacturing sectors visible, it has —given the quest for new sources of raw materials— favoured natural resource exploitation. Trinidad has traditionally benefited from the large amounts of foreign investment and resources that have been geared to the development and exploitation of its oil reserves. In the past five years, it has taken advantage of its market position and natural gas reserves to change the composition of its hydrocarbons sector. The production and utilization of natural gas has replaced that of crude oil. As a result of the growth and development of the natural resource industry, Trinidad has become a leading producer and exporter of methanol and ammonia. Guyana has attracted foreign direct investment (FDI) in timber production, as well as gold and diamond extraction. Although these activities have become significant foreign exchange earners, their value added content remains relatively low.

Besides agriculture- or natural-resource-based manufacturing, the 1990s witnessed the development of apparel manufacturing, albeit with declining success. A case in point is that of Jamaica. This country's manufacturing sector is the second-largest sector of economic activity following distribution. Manufacturing activities include the processing of sugar, beverages and tobacco, and the production of chemicals, metals and construction materials. Until the 1980s, the manufacturing sector had been promoted as an import-substituting sector. Under market-oriented structural adjustment programmes in the 1990s, Jamaica switched its trade orientation to focus on developing its textile, apparel and manufacturing and garment assembly industries. Most garment exports entered the United States market under the offshore assembly programme.

In spite of these efforts to change its trade orientation and the preferential access to the United States market granted by the Caribbean Basin Economic Recovery Act (CBERA, 1983), manufacturing has declined. In 1990, it represented 21% of GDP, but by 2000, it had fallen to 16%. This can be attributed partly to the North American Free Trade Agreement (NAFTA), which has given Mexico a competitive edge over the Caribbean countries.[7]

It is interesting to note that, unlike the Dominican Republic and several small Central American countries, CARICOM countries have not developed labour-intensive *maquila* industries on a large scale. This is so despite the fact that these countries benefit from the offshore assembly provisions of United States tariff code 9802, under which apparel exports assembled from fabric wholly made and cut in the United States enter that market at reduced duty. One major factor that may have contributed to the Dominican Republic's relative success in setting up *maquila* industries compared to the experience of CARICOM countries is the difference in factor (labour) endowment. The scarcity and relatively high cost of labour in many CARICOM countries as compared with the Dominican Republic may have made them less attractive destinations for efficiency-seeking FDI in the textile and apparel sectors. In addition, the tradition of strong labour unions in the CARICOM countries has deterred investment in labour-intensive industries, where low labour cost is critical to comparative advantage.

It has been argued that since the firms operating in the export processing zones (EPZs) are exempted from domestic laws, they tend to pay workers less than the minimum wage. This may have been the case in the past, particularly in the early 1980s, but the situation has changed with the passage of a new law requiring firms in the *maquila* sectors of EPZs to adhere to minimum wage laws. Indeed, evidence from Barbados, Dominica, Grenada, Saint Lucia, and Saint Vincent and the Grenadines indicates that wages in the EPZ apparel and textile segment have been relatively higher than in the rest of the industry.

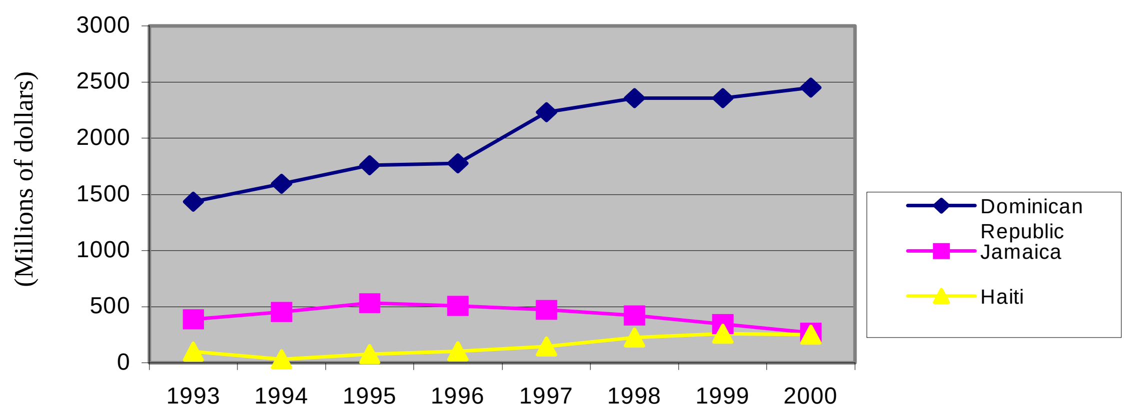
Apart from variations in factor endowment and the cost of labour, the differences in how countries have responded to competition might also partly explain the differences among countries as regards their experience with EPZs. The Dominican Republic took strong measures to attract more foreign investment into the textile and apparel sectors by expanding its free trade zones, offering better tax incentives and providing manpower training programmes, as well as streamlining customs procedures. These measures have paid off in the form of a significant increase in apparel exports to the United States.

[7] For example, under NAFTA, Mexico's exports of apparel assembled from fabric wholly made and cut in the United States enjoy duty- and quota-free access to the United States. In contrast, although United States imports of apparel from the CBI countries made with United States-manufactured and cut fabric enjoy preferential quotas under guaranteed access levels (GALs), they are subject to duties on the value added. In addition to duty and quota preferences, Mexican apparel exporters also benefit from generous rules of origin.

As shown in figure 11.1, the Dominican Republic has been the Caribbean's largest exporter of textile and apparel products to the United States. Haiti's total apparel exports to the United States, although still a small percentage of total Caribbean apparel exports to that country, grew from US$ 98 million in 1993 to US$ 249 million in 2000. In contrast, Jamaica's apparel exports declined through the entire second half of the 1990s. After growing from US$ 388 million in 1993 to US$ 537 million in 1995, they began to fall, reaching a low of US$ 268 million in 2000.

Figure 11.1

UNITED STATES APPAREL IMPORTS FROM SELECTED CARIBBEAN COUNTRIES



Source: United States International Trade Commission (USITC), 2001.

The main destinations for Caribbean exports of goods are North America and Europe, with these markets accounting, in some cases, for more than 70% of total merchandise exports. Exports are concentrated in food products (20% of total merchandise exports), raw materials (17%), mineral fuels (17%), chemical products (12%), manufactured goods (8%) and beverages and tobacco (7%).[8] Owing to the difficulties faced by the agricultural and manufacturing sectors, the Caribbean Community's competitive edge in third markets was eroded during the 1990s. Its share of world exports of goods averaged 0.28% in 1985 and 0.13% in 1999. CARICOM lost market share in North America (from 0.71% in 1985 to 0.26% in 1999), Europe (from 0.15% in 1985 to 0.10% in 1999), the Andean Community (from 0.40% in 1985 to 0.30% in 1999) and MERCOSUR (from 0.30% in 1985 to 0.07% in 1999) (see table 11.1).

While agriculture declined and manufacturing remained stagnant, the service sector increased its relative contribution to GDP. In 2000, hotels and restaurants, which account for a portion of tourism services, represented, on average, 13% of GDP; financial services, 12%; and communications and transport, 17%.

Tourism services have become an increasingly important sector of the Caribbean economies. During 1990-2000, the subregion's number of visitors and total receipts from tourism increased, on average, by 71% and 59%, respectively. Visitor expenditures represent close to 35% of external earnings and 18% of GDP. Moreover, the Caribbean is the most important destination in the world for cruise ships, as it accounts for 50% of world cruise ship passengers (see table 11.4).

8 Estimates based on ECLAC, *Competitive Analysis of Nations*, 2001 edition.

Table 11.4
TOURIST ARRIVALS AND RECEIPTS IN SELECTED CARIBBEAN COUNTRIES, 1980-1998

Country	Number of tourist arrivals (1000)			Tourism receipts Millions (United States dollars)			Tourism earnings as % of total export earnings		
	1985	1990	1999	1985	1990	1999	1985	1990	1999
OECS countries									
Antigua and Barbuda	149	197	232	133	298	291	74.3	86.4	...
Dominica	21	45	74	9	20	49	18.1	19.4	27.5
Grenada	52	76	125	26	38	63	48.1	36	35.8
Montserrat	…	13	19	...	7	3			
Saint Kitts and Nevis	48	73	84	31	63	70	69.5	61.2	52.3
Saint Lucia	95	141	261	56	154	311	46.1	51.1	75.4
Saint Vincent and the Grenadines	42	54	68	23	56	77	27.8	37.7	45.1
Non-OECS CARICOM countries									
Bahamas	1,368	1,562	1,577	995	1,324	1,503	66	87.9	74.3
Barbados	359	432	515	309	494	677	38.9	59.1	50
Belize	93	88	300 a/	12	51	99 a/	7.9	19	28.1
Guyana	46	64	76 a/	18	27	60 a/	6.9	10.7	8.6
Jamaica	572	841	1,248	407	740	1,333	30	30.1	28.5
Suriname	32	28	55 a/	9	1	45 a/	2.5	0.2	...
Trinidad and Tobago	187	195	336	97	95	210	3.7	4.1	6.6

Source: World Tourism Organization (WTO), *Yearbook of Tourism Statistics, 2000 and 2001*, Madrid; ECLAC, *World Development Finance*, Santiago, Chile, 2000.

Note: "…" means no data are available.

a/ Data available for 1998.

Its importance notwithstanding, the tourism sector has not followed a balanced pattern of development, as its growth has not been homogeneous throughout the region. In particular, it has not opened up any major opportunities in the goods-producing economies (Guyana, Belize, Dominica and Trinidad and Tobago). Also, in the 1990s a combination of factors, including weakening competitiveness of Caribbean tourism, reluctance to undertake structural reforms and increasing external competition, eroded the comparative advantage of some of the tourism-based economies. This was particularly so in the smaller and more vulnerable countries of the Organization of Eastern Caribbean States (OECS), where the tourism industry has become somewhat saturated.

Some Caribbean countries have also sought to develop other service activities, particularly offshore banking and new enterprises in the field of information and communications technologies (ICT). Offshore banking has run into difficulties in recent years owing to money laundering and other illegal practices, and this has made a major restructuring effort necessary.[9] Barbados and Jamaica have had some success in ICT sectors, but they have also encountered difficulties because of the monopolistic provision of telecommunications services in the subregion and the recent worldwide volatility of the industry (see box 11.2).

[9] Money laundering and other illegal practices have recently dominated offshore banking issues. The Financial Action Task Force (FATF) estimates that the scale of money-laundering transactions is substantial in several countries of the region. Individual Caribbean countries continue to face mixed perceptions with respect to their efforts to combat money laundering and their use as clandestine tax havens. Currently, four countries in the subregion —Dominica, Grenada, Saint Kitts and Nevis, and Saint Vincent and the Grenadines— are still on the FATF blacklist; all of them belong to the Organization of Eastern Caribbean States (OECS). Meanwhile, Bahamas and the Cayman Islands were removed from the list after undertaking required reforms. In spite of the fact that some of its members are listed, the Caribbean Financial Action Task Force (CFATF) continues to work to upgrade supervision, regulation and disclosure requirements in its subregional jurisdictions.

Box 11.2
THE NEW TECHNOLOGIES IN THE CARIBBEAN

Countries in the region have been actively pursuing policies to attract investment to develop the ICT sector. Jamaica and Barbados are the leaders in this endeavour. Jamaica has developed a national strategic plan for information technology, which has as its main objectives the creation of a knowledge-based society and the development of IT firms. The government provides office facilities and infrastructure for IT firms, loans from a venture capital loan fund for ICT projects and telecommunications infrastructure, among other things. What it gains in return are jobs, skills training and rental income. Loans from the technology fund helped to establish three call centres in 2000. One of them, NetServ, collapsed in December 2001 (six months after it had started operations) after having received loans of about US$ 4 million from the government. The company has since been placed in receivership. The collapse of this call centre has raised the issue of the viability of the IT sector, which is associated with high risks and volatility.

The main constraints in developing high-value-added segments of the IT industry are the shortage of workers skilled in specific areas, such as software and data conversion; the shortage of workers that are multi-skilled in information and communications technologies; and the monopoly provision and resulting high cost of telecommunications services. The latter is particularly important because of the significant role that telecommunications infrastructure plays in facilitating economic development.

Telecommunications services in the region have been provided by monopolies, in particular Cable and Wireless (C&W). Caribbean governments entered into negotiations with this company to liberalize the telecommunications market. Jamaica concluded an agreement in 1999 which opened up value-added services to some competition while allowing the company to retain a monopoly in voice telephony for a fixed period. Cellular telephone services have expanded rapidly thanks to the competition allowed. The number of Internet service providers has also increased, but the majority of the population does not have access to the service because of relatively high rates. Access is provided on the basis of a monthly payment for a fixed number of hours of access rather than at a flat rate. Rates vary across the subregion but are generally beyond the reach of low-income earners, who make up the bulk of the population. In addition, the authorities do not regulate Internet access rates, although they do require the service providers to be licensed or registered.

Internet access is also constrained by the control exercised by telecommunications monopolies such as Cable & Wireless over connectivity and broadband access. Broadband has become necessary for data-intensive communications in which large data files have to be uploaded as well as downloaded by businesses. It is particularly important for firms engaged in e-commerce and those using CAD/CAM applications. E-commerce is an infant service industry in the Caribbean. There is evidence of business-to-consumer (B2C) service in the airline industry, for example, where electronic tickets are purchased online. Little information is available on business-to-business (B2B) e-commerce. However, monopoly provision of broadband access by C&W does not facilitate cheaper transaction costs through B2B commerce.

The OECS countries secured an agreement with C&W early in 2001 for the rapid liberalization of the telecommunications market. Liberalization will be phased in from April 2001 to October 2003, when full liberation is to be achieved. To win this concession, OECS governments had to agree to prevent bypassing of C&W network and to allow rebalancing of telephone rates to reflect the true cost of local calls. C&W will still provide the same networks and services in each country where it operates at present, albeit under non-exclusive licenses. Full competition is still at least a couple of years away, which means that development of high-value IT services will not be realized in the short or medium term.

The development of services has reinforced a pattern of dual trade specialization in the Caribbean economies consisting of goods-producing and service-based economies. The two types of economies have reacted differently to globalization. Generally, the service-based economies (including Antigua and Barbuda, the Bahamas, Barbados, Jamaica, Saint Lucia and Saint Kitts and Nevis) have shown a more robust response to globalization. This is reflected in the fact that, on average, their trade and growth performances have surpassed those of the goods-producing economies, with the exception of Trinidad and Tobago. The difference in performance is related to the international product cycle and the elasticity of demand for tourism services. Tourism services have remained on the upswing of the global product cycle for a longer time. In addition, tourism demand is income elastic, which allows countries to earn more relative to traditional commodities. On the other hand, the poor performance of agriculture and manufacturing has impacted negatively on export growth in several goods-producing economies.

At the same time, the patterns that determine the composition and level of imports have not changed. Imports are driven by consumer spending. In most countries, consumer goods account for more than 40% of total imports. Also, manufacturing and agriculture have a high import content.

This scenario has created not only a perpetual tendency towards balance-of-payments constraints but also a constant need to attract foreign capital and a continued dependence on official aid. This limits the manoeuvring capacity of the authorities while stimulating the growth of those activities that require foreign capital. In turn, this reinforces the present pattern of structural change and trade specialization.

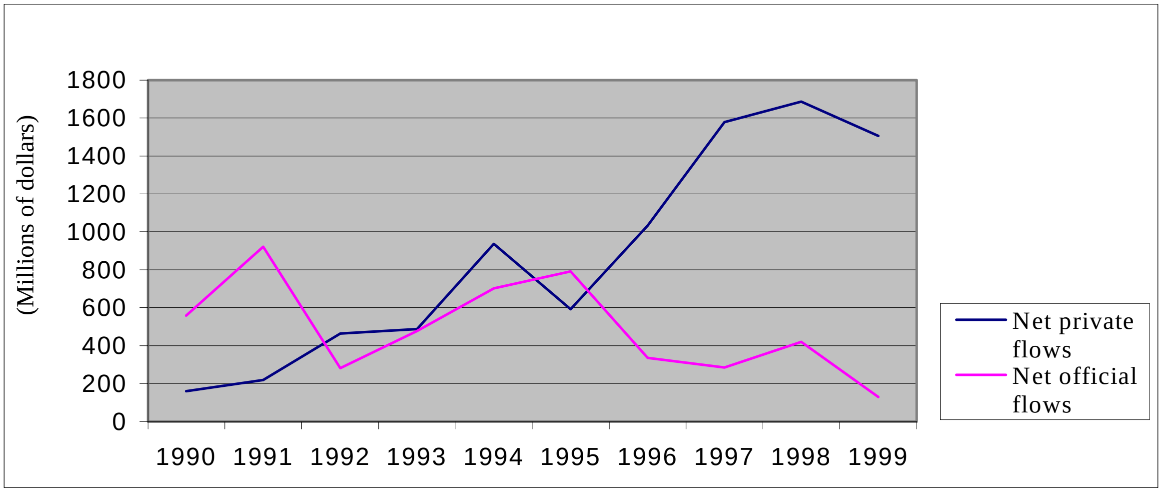
III. Capital flows

Structural reforms facilitated a significant increase in private capital flows to the Caribbean countries during the last decade, albeit at a slower pace than in the case of other developing countries. Total net financial flows to the Caribbean grew from US$ 722.7 million in 1990 to US$ 1.635 billion in 1998. A breakdown of financial flows into private and official flows shows two contrasting trends. The less developed countries in the subregion have had relatively little access to private international financial markets and have therefore tended to rely more on official and multilateral flows. However, the volume of these types of flows diminished considerably during the 1990s. Net official flows of resources, including grants, declined from US$ 561 million in 1990 to US$ 130.2 million in 1999.

There has been a greater reliance on private capital flows to finance development projects. Such flows increased fivefold, from US$ 161.6 million in 1990 to US$ 1.505 billion in 1999 (see figure 11.2). In terms of relative importance, private capital flows outpace official flows by a wide margin. This constitutes a remarkable shift, since in 1990 official flows were more than twice the size of private flows. The least developed countries, such as Haiti and Suriname and some smaller OECS countries, most notably Antigua and Barbuda and Dominica, have been unable to attract significant amounts of private flows because of their small size and limited resources (the OECS countries) or political instability (Haiti and Suriname). The combined effect of declining official flows and limited access to private international financial markets has affected the ability of smaller islands to finance viable development projects. It therefore seems reasonable to conclude that the benefits of financial globalization have been sharply skewed in favour of the larger, resource-based economies as well as those that are relatively more developed.

FDI is the main component of private capital flows in the Caribbean, but the subregion managed to attract only 3.7% of the total FDI received by the Latin American and Caribbean region. This is partly due to the high cost of doing business in the subregion, especially in relation to telecommunications and insurance (see table 11.5).

Figure 11.2
CAPITAL FLOWS TO THE CARIBBEAN, 1990-1999



Source: World Bank, *Global Development Finance,* Washington, D.C., various issues.

Table 11.5
NET INFLOWS OF FOREIGN DIRECT INVESTMENT, 1990–1999

Country	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
Antigua and Barbuda	61	55	20	15	25	31	19	28	26	12
Bahamas	-17	-1	40	11	22	10	11	17	147	145
Barbados	11	7	14	9	13	12	22	18	16	15
Belize	17	14	16	9	15	21	17	12	18	-7
Dominica	13	15	21	13	23	54	18	20	11	13
Grenada	13	15	23	20	19	20	18	22	51	43
Guyana	8	13	147	70	107	74	81	90	47	48
Haiti		-2	-2	-2	-3	7	4	5	11	30
Jamaica	138	133	142	78	170	245	273	137	369	524
Saint Kitts and Nevis	49	21	13	14	15	20	17	25	34	77
Saint Lucia	45	58	41	34	32	30	23	45	84	87
Saint Vincent and the Grenadines	8	9	15	31	47	31	18	42	28	25
Suriname	-77	19	-54	-47	-30	-21	7	-9	9	5
Trinidad and Tobago	109	169	178	379	516	299	320	1,000	730	633
Total	378	525	614	634	971	833	848	1,452	1,581	1,650

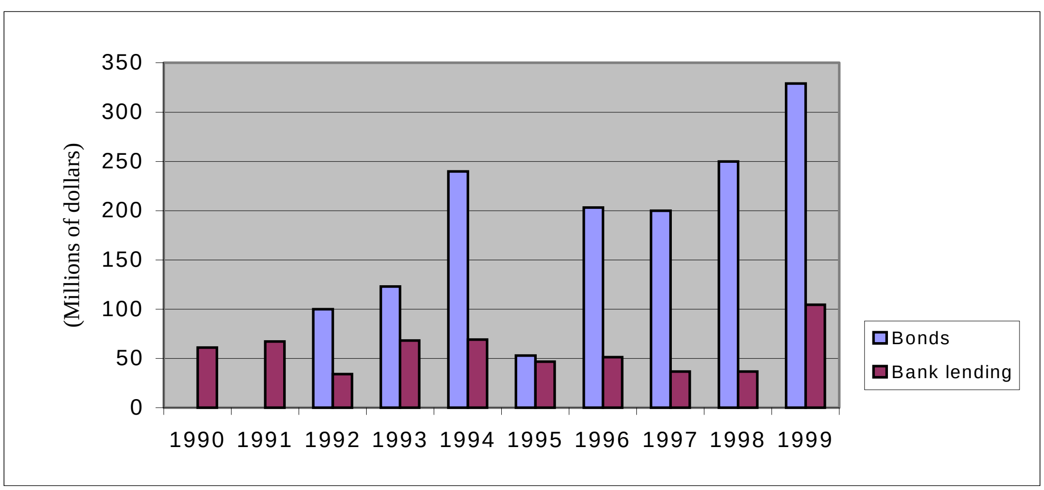
Source: ECLAC, *Foreign Investment in Latin America and the Caribbean*, Santiago, Chile, various years.

During the 1990s, net FDI in the subregion grew significantly, from U$ 378 million in 1990 to US$ 1.65 billion in 1999. However, these aggregate figures mask significant variations among countries. The bulk of FDI went to Trinidad and Tobago and to Jamaica, with these two countries accounting for nearly 69% of total FDI flows. The lion's share of FDI received by Trinidad and Tobago has been channelled into the petroleum industry (exploration, production and refining facilities and petrochemical firms) (ECLAC, 1998d and 1999a). Transnational corporations such as BP Amoco, British Gas, Enron and the Spanish firm Repsol have become more active in the natural gas industry in Trinidad and Tobago (ECLAC, 2001h). FDI flows to Jamaica have been channelled into light manufacturing activities such as textiles and apparel and, more recently, into the tourism industry. FDI flows to Guyana have also picked up considerably since 1992. The smaller, service-oriented OECS economies have also attracted significant amounts of FDI relative to their size. Between them, they accounted for an average of 18% of FDI flows to the subregion during the 1990s.

Other components of private flows (equity portfolios, bonds and commercial bank lending) have been of less significance to the Caribbean countries. However, in recent years there has been a greater reliance on bonds to finance development projects. Since 1992, a number of Caribbean countries, notably Trinidad and Tobago, Jamaica and Barbados, have issued international bonds either for the first time or after having returned to the bond market after many years' absence. One of the factors that helped make this possible was the improved credit ratings of these countries issued by international agencies such as Standard & Poor and Moody's Investor Services.

Commercial bank lending has not been a significant component of capital flows to the Caribbean since the debt crisis of the 1980s. These flows have exhibited erratic patterns, rising from US$ 61.2 million in 1990 to US$ 69.3 million in 1994, falling to US$ 51.5 million in 1995 and rising again to US$ 104.5 million in 1999 (see figure 11.3). The trend in bank lending has also been concentrated in a very few markets, most notably Jamaica, Belize and, to a lesser extent, Barbados and Trinidad and Tobago.

Figure 11.3
INTERNATIONAL BOND ISSUES AND BANK LENDING



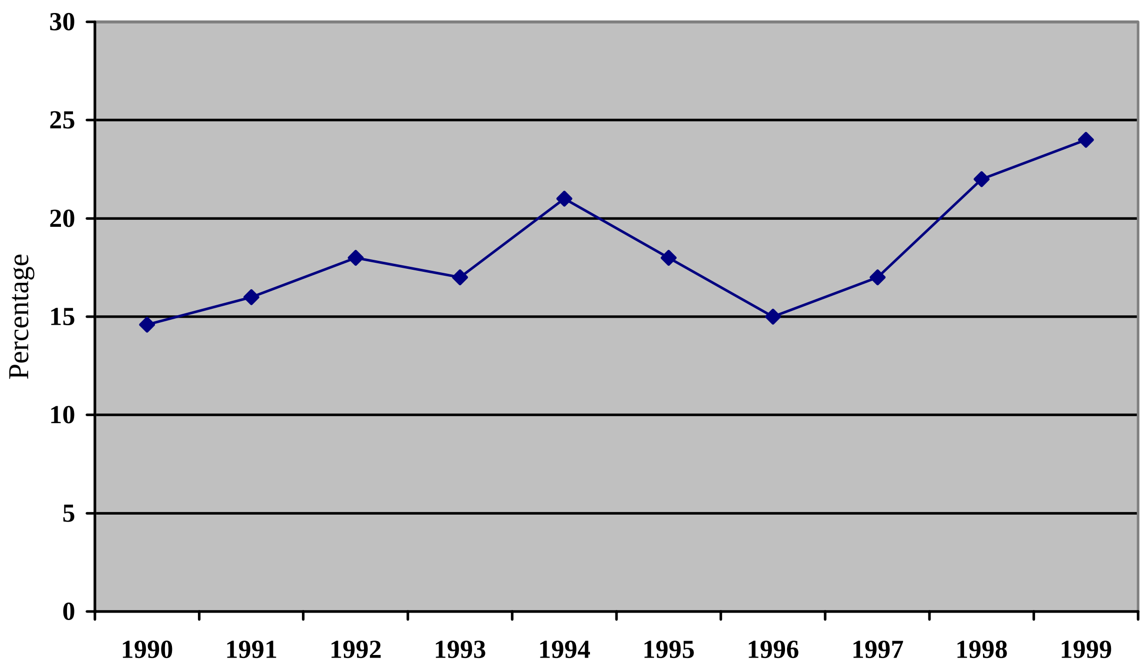
Source: World Bank, *Global Development Finance*, Washington, D.C., various issues.

The shallowness of capital and equity markets in the smaller countries, which have few functioning stock exchanges, may have precluded the use of bonds and equity flows to finance private investment. To address this problem, Caribbean countries have undertaken a number of initiatives aimed at developing and deepening capital markets. One such initiative was the introduction of cross-listing and trading of securities, especially among the stock exchanges of Barbados, Jamaica, and Trinidad and Tobago. However, this is still at an early stage of development.

The effect of capital flows, especially of FDI, on the Caribbean economies has varied, depending on the mode of investment (mergers and acquisitions or greenfield projects) and, more importantly, on the differences in how countries have managed their integration into international financial markets. Greenfield investment has been the dominant mode of FDI in the Caribbean. However, acquisitions have become significant since the early 1990s owing to the privatization of State-owned entities in areas such as banking and finance, public utilities, transportation, and manufacturing industries such as sugar and cement.

One of the most important contributions made by capital flows, particularly FDI, has been in the financing of domestic investment. Caribbean economies have traditionally relied on foreign capital flows to close both foreign-exchange and savings-investment gaps. The importance of FDI in domestic investment, as measured by the ratio of FDI to gross fixed capital formation, increased significantly during the 1990s (see figure 11.4).

Figure 11.4
FDI AS A PERCENTAGE OF GROSS DOMESTIC FIXED CAPITAL FORMATION FOR THE CARIBBEAN, 1990-1999
(Averages)

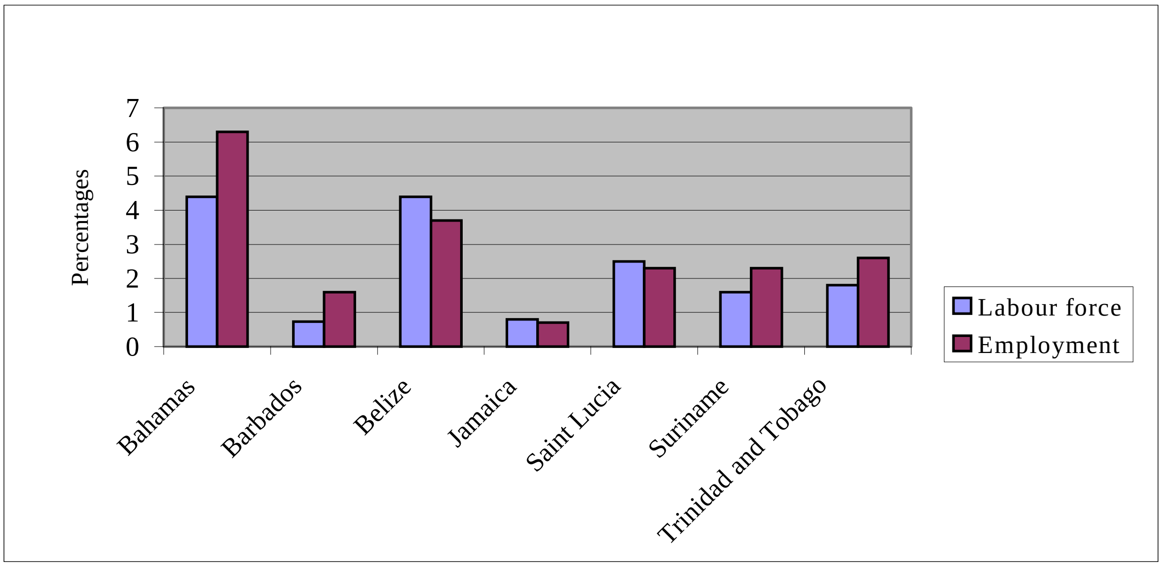


Source: ECLAC on the basis of national data.

IV. Labour issues and migration

In general terms, during the 1990s unemployment rates remained high, although they did fall slightly, from an average of 15% to 12% (see figure 11.5). At a sectoral level, the effects of globalization on employment have stemmed from changes in the composition of output and trends in intra- and extraregional investment flows.

Figure 11.5
EMPLOYMENT AND LABOUR FORCE GROWTH
(Averages, 1991-1997)



Source: ILO Caribbean Office, *Caribbean Statistical Digest,* various issues.

Employment in agriculture has decreased. The uncertainties surrounding the European Union banana regime have also been felt in the banana-producing countries of the Organization of Eastern Caribbean States (OECS). The statistics point to significant job losses. For example, in the Windward Islands, employment in the banana industry declined from 56,428 workers in 1990 to 35,796 workers in 1998 (Sandiford, 2000). The anticipated erosion of trade preferences as a result of the implementation of the Cotonou Agreement and the opening up of the European Union banana market to other countries on a first-come, first-served basis could adversely affect growth and employment in the banana-exporting countries.

The absolute share of the manufacturing sector in employment has declined in virtually all the countries except Belize and Grenada (see table 11.6). In Barbados, Jamaica, and Trinidad and Tobago, this sector bore the brunt of import competition, since these countries' industries developed on the basis of import-substituting industrialization and were unable to compete with cheaper imported manufactured products. The sector experienced negative growth, contraction of employment and a decline in its contribution to overall employment and national output. Of the three countries, the impact seems to have been more pronounced in Jamaica, where average annual growth in employment contracted by 2.4%. The impact of globalization on the manufacturing sector was aggravated by NAFTA, which has eroded the competitive position of the Caribbean countries vis-à-vis Mexico.

Table 11.6
GROWTH OF MANUFACTURING EMPLOYMENT, 1992-1997

Country	Percentage change in share of sector, 1992-1997	Average annual growth, 1992-1997	Shift in percentage of total employment, 1997
Antigua and Barbuda	….	….	….
Barbados	-8.6	0.2	-0.1
Belize	1.7	4.4	1.5
Dominica	….	….	….
Grenada	7.8	0.0	3.1
Guyana	….	….	….
Jamaica	-16.5	-2.4	-1.4
Saint Kitts and Nevis	….	….	….
Saint Lucia	-3.1	0.0	-0.4
Saint Vincent and the Grenadines	….	….	….
Suriname	-21.4	-4.0	-1.6
Trinidad and Tobago	-2.1	2.2	1.0

Source: ILO Caribbean Office, *Globalisation and Employment in the Caribbean: A Review of Labour Market Policies and Development in the 1990s in Light of the Commitments of the World Summit for Social Development*, August 1999.

Note: "…" means no *data* are available. Data for Trinidad and Tobago exclude sugar and oil refining.

FDI in the services sectors in Barbados, Jamaica and the OECS countries has contributed to job creation. The tourism industry has emerged as one of the largest employers in many Caribbean countries. However, the positive contribution of FDI to job creation may have been offset by job losses in the manufacturing sector, especially in Jamaica, owing to trade liberalization. As noted earlier, manufactured exports, particularly garments, have been declining since the entry into force of NAFTA. The impact of NAFTA on manufactured exports from Jamaica is clearly illustrated by the fact that employment in EPZs in Jamaica rose from a mere 960 workers in 1983, when the free zones were established, to 14,220 in 1992.

However, total employment has been declining since then, and it is estimated that the total had fallen to around 6,000 workers by 1998 (UNCTAD, 1999a; Willmore, 1993). The garment industry has been hit the hardest by NAFTA. The number of workers employed in the industry grew from 6,191 in 1982 to 28,700 in 1992 but fell sharply, to less than 6,000, in 1997-1998.

To mitigate the impact of liberalization on labour, Caribbean countries have introduced educational and skills-training programmes to enable workers to meet the demands of the constantly changing economic environment. In addition, technical and vocational institutions have been restructured to make them more relevant to the needs of labour markets. Some countries, notably Barbados, have expanded the curricula at the secondary level to offer a wide range of courses in business studies, information technology, clothing and textiles, and industrial arts.

In recognition of the important role that small and medium-sized enterprises play in creating jobs, many countries have, in partnership with international and multilateral institutions, introduced a myriad of programmes and mechanisms, including tax breaks and subsidized credit, aimed at promoting the development of these enterprises. Some countries have also introduced measures to increase labour-market flexibility.

At the CARICOM level, many countries have also signed Protocol II to the Treaty of Chaguaramas, which seeks to establish free movement of labour, capital and businesses. Some CARICOM businesses have been establishing a presence in other CARICOM countries as well. For example, the Jamaican hotel chain, Sandals Resorts, has opened hotels in a several other

CARICOM countries. However, labour movements are still limited because many countries still have trepidations about allowing the free movement of people within the subregion.[10]

Intraregional labour flows have, nonetheless, been growing within the last decade, although there is limited information on their volume. Migrant labour tends to flow from lower-income to higher-income countries (for example, from Haiti to the Bahamas and the Dominican Republic and from Guyana to Trinidad and Tobago). Migrant workers are mainly unskilled agricultural workers or workers in construction and service industries. Although they can have a positive impact on countries experiencing economic booms, such as Trinidad and Tobago, they pose economic as well as political problems for small and fragile economies such as Antigua and Barbuda, where about 30% of the labour force is made up of citizens of other Caribbean countries.

Extraregional migration flows have been motivated by other considerations and comprise a larger share of skilled workers. These flows are determined by push factors in individual Caribbean countries, such as economic decline, political instability and increasing crime levels, and by pull factors in developed countries, particularly increased demand for skilled labour. The pull factors in developed countries are largely generated by the ageing of the workforce and shortages of skilled workers, such as teachers and nurses, and by the rapid growth of information technology (IT) industries, as well as by the use of new technologies in the so-called “old-economy industries”. Developed countries, such as Canada, the United Kingdom and the United States, have embarked on recruitment drives in response to the shortage of skilled workers in those countries. For example, it is estimated that the United States will need about 2 million teachers by the end of the present decade. The United Kingdom is currently in need of about 26,000 teachers; hence the active recruitment of teachers abroad. Teachers in the Caribbean, especially in Jamaica and in Trinidad and Tobago, have been taking advantage of this opening for prospective migrants, giving rise to fears of adverse impacts on the education system. Similar concerns have been raised in relation to the recruitment of nurses from the region. Jamaica, however, has responded to the situation by undertaking its own recruitment of nurses and teachers from developing countries such as Cuba.

The corollary to intraregional and extraregional flows is return migration, which has been fostered by the information and communications revolution. So far, however, there is only anecdotal evidence of such flows. Professionals, in particular IT specialists who studied abroad and joined the labour force in their host countries, have been returning to the Caribbean either to take up jobs with transnational corporations or to establish their own businesses. Returning migrants have also established consultancies, in some cases in partnership with residents, to cater to the growing needs of business as well as government for high-value services. This is perhaps truer of the service-based economies, such as those in the OECS and the Bahamas, as well as Jamaica, where the services industry, especially telecommunications, has been growing significantly since the early 1990s. Other Caribbean nationals who have completed their working life abroad are also returning to set up businesses or retire in the region.

Return migration is not peculiar to this phase of globalization. It was encouraged in the 1970s by the Governments of Jamaica and Guyana, which provided incentives to entice qualified nationals to return to their home countries to fill vacancies in the public sector. The difference now is that the market is providing the incentives, and the return migrants are pursuing job opportunities in the private sector. Be that as it may, governments are facilitating return migration, through legislation, as in Saint Kitts and Nevis, and through community projects, as in Jamaica.

[10] Few countries have enforced the provision allowing for exemption of work-permit requirements for graduates of tertiary institutions in the region. The Bahamas, which is not a member of the Caribbean Common Market, is reluctant to join the CARICOM Single Market and Economy because of the implications that free movement of labour would have for its economy. A similar concern would also be applicable to the small countries in the Eastern Caribbean.

A major effect of labour migration has been the growing role of remittances. These flows have been significant in Haiti, Jamaica and the OECS countries, with the exception of Antigua and Barbuda. This has been facilitated by the development of better and more efficient intermediation channels, such as electronic funds transfers. Remittances have grown in both absolute and relative terms. By 1999, such flows represented 17% of Haiti's GDP and 11.7% of Jamaica's. Remittances have also been significant in Grenada and in Saint Kitts and Nevis (ECLAC, 1998f). Although remittances tend to be used largely for consumption purposes, there is evidence that they are also being used to finance housing and small businesses (ECLAC, 2000i).

V. Globalization and macroeconomic policy and performance

Sharp macroeconomic imbalances and, in particular, balance-of-payments difficulties and declining output growth rates led the larger Caribbean countries (Barbados, Guyana, Jamaica and Trinidad and Tobago)[11] to undertake market-oriented reforms in the 1990s. These included fiscal and monetary policy measures aimed at scaling back the role of government in economic activity and giving greater recognition to the role of prices in a freer market.

Reform-oriented Caribbean countries implemented fiscal policy reforms designed to reduce expenditures and increase revenues. At first, the decline in expenditure was mainly achieved through a decrease in capital investment, but it later took the form of a freeze on the wages of public employees, job cuts in the public sector and a reduction in government transfers to public enterprises, including public utilities. Economic reforms also included a tightening of monetary policies, mainly through decreases in public-sector credit, the abolition of controls on interest rates and the phasing out of interest-rate subsidies. Exchange-rate policies were also part of the announced reform programmes; they were generally liberalized *de jure*, and exchange controls were phased out. Other aspects of these economic reform programmes included policies designed to facilitate FDI. Trade reforms included tariff reductions and the elimination of quantitative restrictions.

Smaller Caribbean countries (Antigua and Barbuda, Dominica, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Anguilla and Montserrat) continued to apply the policies agreed upon at the time of the formation of the Eastern Caribbean Currency Union and the parallel creation of the Eastern Caribbean Central Bank (1983).

Growth rates were lower in the 1990s than in the previous two decades, with average growth in real per capita GDP declining from 1.6% in the 1980s to 1.4% in the 1990s. Average growth fell in eight of the 13 countries for which comparative data were available (table 11.7).

The Bahamas and Barbados were able to maintain their lead in growth performance within the region. In contrast, the decline was particularly evident in the OECS countries (a relative success story of the 1980s),[12] with only Dominica managing to achieve a higher growth rate in the 1990s. Among the other OECS countries, growth was down sharply in Antigua and Barbuda, Saint Lucia, and Saint Kitts and Nevis.

The growth performance of the larger economies was mixed. Guyana and Trinidad and Tobago and, to a lesser extent, Barbados recorded an important upturn in growth. On the other hand, growth slowed in Jamaica and, more slightly, in Belize. The reduction in GDP growth was accompanied by an increase in its volatility and divergences among Caribbean countries. As measured by the standard deviation, volatility increased from 3.1 in the 1980s to 3.3 in the 1990s.

[11] See Hilaire (2000).

[12] OECS countries had posted significant income growth in the 1980s as a result of sound macroeconomic management, favourable commodity export flows and prices, and foreign capital inflows.

Table 11.7
CARIBBEAN COUNTRIES: GROWTH IN REAL GDP, 1991-2000

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	1981-1990	1991-2000
Anguilla	-3.6	7.1	7.5	7.1	-4.2	3.5	9.2	5.2	8.7	-0.7	…	4.0
Antigua and Barbuda	2.7	0.8	5.1	6.2	-5.0	6.1	5.6	3.9	4.6	3.1	6.1	3.3
Aruba	5.0	4.0	5.0	5.9	5.7	3.9	4.2	2.8			…	4.6
Bahamas	-4.0	-2.0	1.7	0.9	0.3	4.2	3.3	3.0	6.0	4.9	…	1.8
Barbados	-4.1	-5.7	1.0	3.8	2.9	4.1	2.6	4.8	2.4	3.7	1.1	1.6
Belize	3.1	9.5	4.3	1.5	3.9	1.5	4.0	1.3	6.4	8.2	4.5	4.4
Dominica	2.2	2.7	1.8	2.2	1.6	3.0	2.2	2.3	0.9	0.2	4.4	1.9
Grenada	3.6	1.1	-1.3	3.3	3.2	2.9	4.2	7.3	7.5	6.4	3.5	3.8
Guyana	6.0	7.8	8.2	8.5	5.0	7.9	6.2	-1.7	3.0	3.0	-2.9	5.4
Haiti	0.3	-13.2	-2.4	-8.3	4.4	2.7	1.4	3.1	2.3	1.0	-0.5	-0.9
Jamaica	0.7	1.5	1.5	1.0	0.7	-1.4	-2.1	-0.7	-0.4	0.8	2.2	0.2
Montserrat	-20.9	2.7	2.5	0.9	-7.6	-21.5	-20.0	-8.6	-12.8	-1.9	…	-8.7
Saint Kitts and Nevis	2.3	3.1	5.4	5.4	3.5	5.9	7.3	1.0	3.7	7.5	5.8	4.5
Saint Lucia	0.0	7.4	-1.6	4.6	1.7	1.4	0.6	2.7	3.5	0.7	6.8	2.1
Saint Vincent and the Grenadines	1.4	6.9	1.8	-2.9	8.3	1.2	3.1	5.7	4.2	2.1	6.5	3.2
Suriname	3.2	-1.8	-11.6	-0.7	0.7	13.0	5.7	10.7	-4.1	-5.5	0.5	1.0
Trinidad and Tobago	2.7	-1.6	-1.5	3.6	4.0	3.8	3.1	4.4	5.1	4.0	-2.6	2.8

Source: ECLAC, based on national data.

Macroeconomic stabilization and structural adjustment were not associated with any significant improvement in saving on investment in the region. Between 1990 and 1999, the region's persistent external current-account deficit was reflected in a saving-investment gap of about 10% of GDP. Saving averaged 19% of GDP, while investment averaged 29%. The savings ratio declined in Jamaica in the late 1990s, partly as a result of the crisis in the financial sector, but it remained relatively stable in most of the other countries. Investment rebounded strongly in Trinidad and Tobago in the late 1990s thanks to major projects in the petrochemicals sector. In spite of the financial difficulties experienced in the latter part of the decade, investment remained vibrant in Jamaica, reflecting outlays mainly in tourism and enclave manufacturing. Investment ratios remained relatively strong in Barbados, Guyana and the OECS countries. The recovery of investment in Guyana, in particular, was linked to adjustment and reform efforts and the renewed confidence of foreign investors. Gross domestic investment in Guyana increased from 22% of GDP in 1989 to 28.7% in 1998.

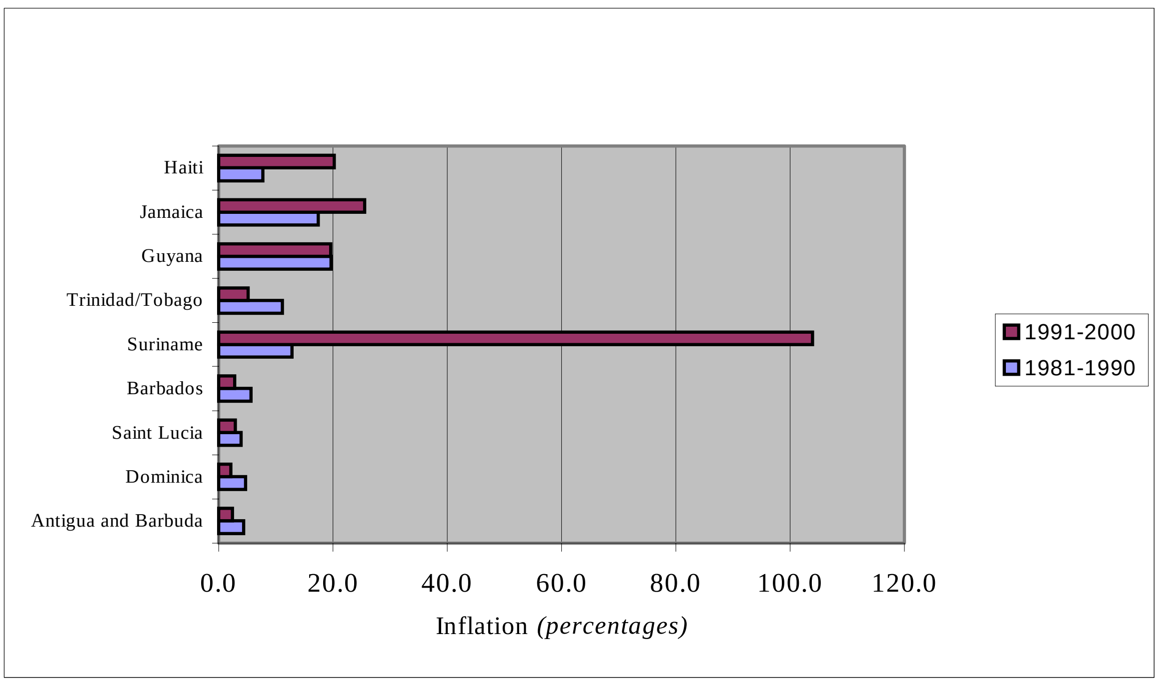
Financial liberalization and deregulation in the presence of weak financial regulation and supervision proved dangerous in many developing countries. In the case of the Caribbean, Jamaica's financial crisis during the second half of the 1990s illustrates this danger. As a result of the raped liberalization and deregulation of the domestic economy, financial institutions proliferated. Taking advantage of lax supervisory and regulatory standards, financial institutions started to offer high interest rates to attract deposits, using the proceeds to expand lending and engage in risk activities. Poor planning, improper risk assessment, mismatching of assets and liabilities, and non-transparent lending to interconnected entities contributed to weak loan portfolios. This, coupled with high interest rates, meant that many financial institutions faced a high percentage of non-performing loans and ultimately a liquidity crisis. This prompted the Jamaican Government to set up a financial adjustment company (FINSAC) to examine and address solvency and liquidity problems in the financial sector. The economic and social cost of the financial crisis has been significant. However, the lessons learned should go a long way towards helping to guard against a recurrence of such crises.

In contrast to their weak growth performance, the economies of the region have exhibited, for the most part, a stable price environment. To a large extent, in most economies price stability is the outcome of a commitment to fixed exchange rates[13] which, in conjunction with a favourable external environment, have allowed the Caribbean economies to reduce inflation rates to single-digit levels.

Average inflation fell in most countries during the 1990s. The main exceptions were Suriname, which had high inflation rates in the mid-1990s, and Jamaica, where inflation was relatively high until 1997. Many countries, having had painful experiences with fiscal deficits and the monetization of those deficits, strengthened their fiscal and monetary management in an effort to squeeze inflation out of the system. Average inflation declined by almost half in the OECS countries, to 2.6%, while for the other countries, with the exception of Suriname (see figure 11.6), average inflation had contracted from 11.1% during the 1980s to 9.5% in 1999.

Figure 11.6

AVERAGE INFLATION RATES FOR SELECTED CARIBBEAN COUNTRIES, 1981-2000



Source: ECLAC on the basis of national data.

[13] There are four exchange-rate regimes in the Caribbean. The first consists of a monetary union with a fixed exchange rate against the dollar. This exchange-rate regime was adopted by the small economies in the Caribbean (Antigua and Barbuda, Dominica, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Anguilla and Montserrat), following the formation of the Eastern Caribbean Currency Union and the parallel creation of the Eastern Caribbean Central Bank (1983). The second exchange-rate regime, applied by Bahamas, Barbados and Belize, consists of a nationally determined exchange rate peg to the United States dollar. The third type of exchange-rate regime is a floating exchange rate, which is in force in Guyana, Jamaica, and Trinidad and Tobago. The fourth type is a dual exchange-rate regime, which is applied, for example, by Suriname. However, in practice, most countries peg their exchange rates, given the negligible variability of their nominal exchange rates.

While the commitment to fixed or pegged exchange rates has resulted in price stability, it has also led to real currency appreciation. Combined with poor export growth and a strong import performance, this has resulted in persistent balance-of-payments problems, underscoring the need for high interest rates and foreign capital inflows.

In addition, the small size of these economies and the nature of their exchange-rate regimes do not provide any scope for price variations, thus placing the weight of adjustment on income effects. This has important implications for fiscal policy, employment and growth. In particular, a macroeconomic framework such as this precludes a countercyclical use of fiscal policy.

In the long run, it also curbs the growth potential of these economies. Simply put, this is because this fiscal stance, combined with high interest rates and consumption-driven imports, limits the extent to which Caribbean economies can develop human and physical infrastructure.

Import liberalization has strong fiscal effects for those countries that are highly dependent on import revenues. In some of the OECS countries, taxes on international trade account for up to 60% of government revenue. Tax reform would pose a major challenge in countries such as Antigua and Barbuda and Saint Kitts and Nevis, where personal income tax was abolished several years ago. Undoubtedly, countries that are heavily dependent on trade taxes will have to adopt alternative measures, at least in the medium term. A value added tax (VAT) or some combination of alternative taxes would have to be considered, although such measures might be politically difficult to implement. In Antigua and Barbuda, recent attempts to introduce a relatively low sales tax met with major public opposition.

The larger countries have also resorted to the introduction of alternative tax structures to compensate for the loss of revenues from international trade taxes. Jamaica and Trinidad and Tobago are cases in point.

VI. Sustainable development issues

Globalization has affected the use of natural resources, the expansion of human settlements and development policies aimed at addressing poverty and income inequality, which are among the most serious sustainable development issues confronted by the Caribbean countries.

The region is vulnerable on several counts. High population density is a major problem in the islands, with the exception of Bahamas. Barbados, for example, has a density of 625 persons per square kilometre. Population pressure on the land, as well as on agricultural practices and the pattern of specialization, has had an adverse impact on the environment.

Shifting patterns of specialization have also had an effect on sustainable development. Specialization in natural-resource-based activities in countries such as Guyana, Jamaica, Suriname, and Trinidad and Tobago —which enjoy comparative advantages in aluminium ores and oxides, timber, gold, diamonds and petroleum— poses an important challenge in managing the rate of depletion of non-renewable resources. This is especially true in the case of bauxite in Jamaica and gold in Guyana. For example, Guyana has one of the largest open-pit gold mines in South America, and its reserves have been declining as a result of increased production by foreign investors. The value added associated with specialization in this field of production is limited and can only contribute to increased foreign-exchange earnings through intensification of exploitation, which would lead to a rapid depletion of this natural resource. Moreover, the production process has to be managed so as to minimize any negative impact on the environment but, as is well known, transnational corporations will weigh the costs and benefits of environmentally positive approaches to natural resource development. Governments may then have to trade off positive environmental practices to attract and maintain foreign investment in these sectors.

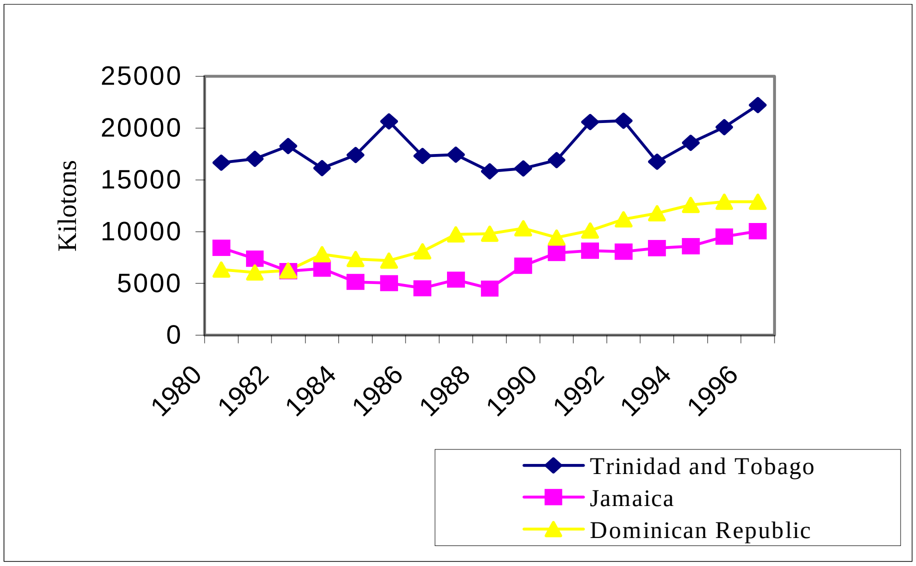
Diversification into highly polluting capital- and energy-intensive industries has adversely affected the environment in countries such as Jamaica, Trinidad and Tobago and Suriname. This has resulted in significant levels of pollution, measured as CO_2 emissions (see figure 11.7). The natural land ecosystems that normally absorb CO_2 have been under threat from the type of activities pursued in countries such as Jamaica and Trinidad and Tobago (cutting of firewood, establishment of squatter settlements, hillside farming, intensive farming and poor agricultural management). Intensive farming aimed at increasing yield from existing hectarage has been affecting soil and water quality through reliance on significant amounts of chemical fertilizers, fungicides, pesticides and herbicides that contribute to excess nitrogen emissions (ECLAC, 2001g).

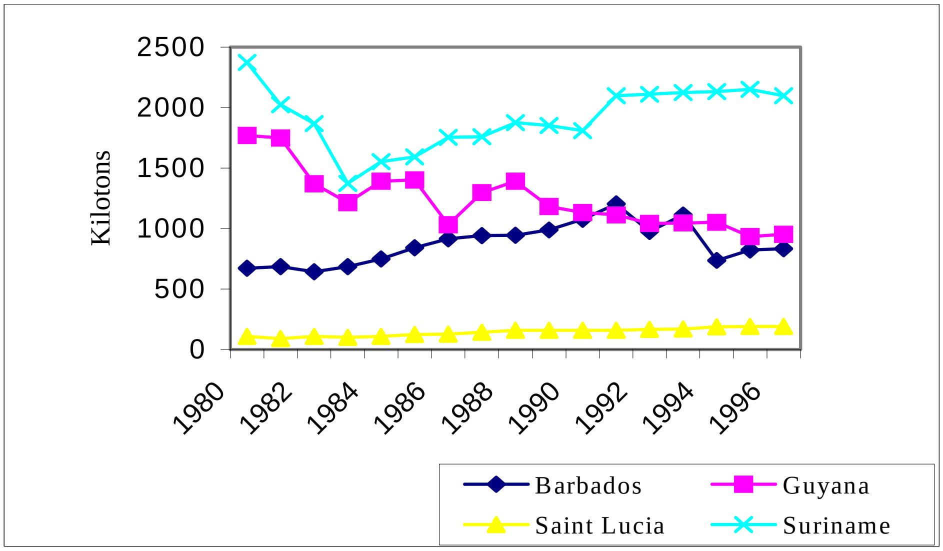
The increasing development of tourism has also adversely affected the environment owing to the erosion of beaches and coastline and the destruction of coral reefs. Illegal sand mining has also contributed to erosion. The significant increase in tourism and, in particular, cruise-ship arrivals over the years has put pressure on the natural (and built) environment because of the increase in demand for water and in waste production.

Although cruise and yacht tourism has contributed to value added and foreign-exchange earnings, the potential for growth is constrained by the carrying capacity of the islands. The fact is that small countries in the region have quite limited space and infrastructure facilities to cater to fairly large-scale cruise tourism.

Population pressure and high poverty rates have resulted in practices, such as those mentioned above, which have contributed significantly to deforestation in the Caribbean, especially in Haiti, Jamaica and Saint Lucia. Jamaica has the highest rate of deforestation (7%) in the region and the second highest in the world (after Lebanon) (ECLAC/UNEP, 2001). Deforestation has resulted in flooding, degradation of watershed areas and pollution of groundwater. Jamaica experienced significant flooding and agricultural sector-losses of about US$ 12 million during the latter half of 2001.

Figure 11.7
CARBON DIOXIDE EMISSIONS (CO_2) FOR SELECTED CARIBBEAN ECONOMIES





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