The economic infrastructure gap and investment in Latin America

Introduction

Economic infrastructure is a fundamental capital input for the creation of wealth and a necessary element at all stages of economies’ development. Its impact may be transformative, boosting productivity and competitiveness in international markets and thus driving growth and economic and social development. Investments in infrastructure projects help improve the coverage and quality of public services (for example, in health, education and leisure), reduce the costs associated with mobility and logistics and open up access to different markets (goods and services, labour and financial markets). As a result, these investments create a positive environment for increased general well-being.

The networks of services that rely on energy, transport, telecommunications and drinking water and sanitation infrastructure together form the core element underpinning the economic structure of territories and markets. These networks are also concrete mechanisms for linking national economies to the rest of the world, enabling the transport of goods and passengers, and making transactions possible within a particular economic and geographical space, and outside it (Rozas and Sánchez, 2004).

To what extent does economic infrastructure contribute to the creation of wealth, and to economic growth and development? How much investment is needed, and in which sectors? Is the current pattern of investment in infrastructure conducive to sustainable development? To answer these and other questions, and to design and recommend public policies, analysts, planners and policymakers require coherent and consistent data. For example, they need data to measure the impact of infrastructure on the economy and on well-being, and to estimate sectoral financing requirements and thereby implement strategic infrastructure development plans.

For infrastructure to have the desired impact, policymakers must have a clear idea of the amount of investment on infrastructure in their country or region. What is more, the positive effects of infrastructure (where provided with adequate...
quantity and quality) on growth and on individuals’ living standards, are maximized when accompanied by the proper regulatory, organizational and institutional arrangements.

A major obstacle to effective policymaking in Latin America and the Caribbean has been the lack of data on how much is invested in infrastructure, how much is invested by the public and private sectors, respectively, and how this expenditure is shared between the different tiers of government. Similarly, the absence of clear definitions and common measurement practices in different countries makes it difficult to obtain good-quality data and, therefore, a valid analysis of the figures (including international comparisons).

Papers published in the early 2000s by the World Bank economists Marianne Fay, Mary Morrison, César Calderón and Luis Servén paved the way in the study of infrastructure investment trends in Latin America.

In this connection, the paper by César Calderón and Luis Servén, Infrastructure in Latin America (World Bank policy research working paper No. 5317) (2010) has been of great use. It provided the first database on infrastructure investment in Latin America, covering six countries in the region from 1980 to 2006, and is currently the series whose data reaches the furthest back in time.

This line of research was taken up in the middle of the decade by the Infrastructure Services Unit (ISU) of the Natural Resources and Infrastructure Division of ECLAC, first as an initiative to build a database on economic infrastructure investment in some countries, then in the context of a theoretical examination of development problems (Patricio Rozas and Ricardo Sánchez, 2004), and later in an analysis of obstacles to development posed by infrastructure deficits in the largest countries of the region (Patricio Rozas, 2008; Patricio Rozas, 2009; Patricio Rozas, José Luis Bonifaz and Gustavo Guerra-García, 2010; Daniel Perrotti and Ricardo Sánchez, 2011). Also on this subject, Rozas, Bonifaz and Guerra-García examined the main aspects related to the funding of investment in infrastructure (institutions, instruments and mechanisms), with reference to an economically and financially sustainable sectoral policy. Meanwhile, Perrotti and Sánchez calculated the infrastructure gap that Latin American and the Caribbean countries must close if they are to sustain their growth and respond to emerging needs in the period to 2020.

As far as the task of further developing a database on economic infrastructure investment is concerned, since 2012 ECLAC has received support from the Development Bank of Latin America (CAF) in collecting and systematizing investment information with the commonly agreed goal and programme of work to develop a database on public and private investment made in the countries of the region since 2009. The first stage of the initiative included ten countries (Argentina, Brazil, Chile, Colombia, Ecuador, Guatemala, Mexico, Peru, the Plurinational State of Bolivia and Uruguay) and was supported by Jorge Lupano and Mauro Gutiérrez; a further five countries (Costa Rica, El Salvador, Nicaragua, Panama and Paraguay) were subsequently included, thanks to the participation of researchers from the University of Chile (Jorge Rivera, Gonzalo Aguilar, Roberto Jalón, Miguel Vargas, George Vega and Alejandra Sepulveda). The Inter-American Development Bank (IDB) joined the initiative in 2014.

This FAL Bulletin aims to present and encourage the use of the economic infrastructure investment database for Latin America and the Caribbean (EII-LAC-DB), developed by the Infrastructure Services Unit of ECLAC. Users have access to information broken down by country, infrastructure sector and private or public source.

This document has a further six sections, besides the introduction. Section 2 describes the experience of quantifying economic infrastructure investment and briefly outlines some of the procedures used to this end. Section 3 presents the approaches used. The fourth section describes some outcomes of this activity and briefly summarizes the findings of the Perrotti and Sánchez study, while Section 5 makes some important observations regarding the quality of data. The sixth and final section presents conclusions and general recommendations. The annex acknowledges those who worked on building the database since 2013.

The compilation, recording and processing of information on economic infrastructure investments is a gradual process, and one that will require continuous updating and improvement in the short, medium and long term. Thus far, only the initial steps have been taken. Procedures still need to be improved and it is hoped that gradually greater precision will be reached in cross-sector and sector-specific data and coverage will be expanded to all the countries of Latin America and the Caribbean.

Challenges involved in estimating economic infrastructure investments

Building an infrastructure investment database entails plenty of conceptual and methodological challenges, some of which are mentioned below. The first of these challenges is to define the concepts of investment and infrastructure.

From a macroeconomic standpoint, in the System of National Accounts, gross investment1 is termed “gross capital formation” (GCF), which is one of the components of gross domestic product (GDP). The concept of “investment” is seen as a flow: gross capital formation (GCF) in turn

1 It is called “gross” because it is not adjusted for the depreciation of capital.
The database constructed by ISU, four economic infrastructure sectors were selected for each country (excluding health, education and housing infrastructure). These are:

- **Energy**: electricity generation, transmission and distribution; and the transportation and distribution of natural gas. This category does not include economic infrastructure investments by State-owned enterprises in oil and gas production, or investments in refining or petrochemicals.
- **Drinking water and sewerage**: the provision of mains drinking water and sanitation services.
- **Telecommunications**: fixed, mobile and satellite telephony, Internet and multimedia services.
- **Transport**: roads, public transport systems and railways (infrastructure and rolling stock), ports and airports.

A **third challenge** arises from the need to reconcile the criteria for recording expenditure and investment by the various national sources. This requires a detailed review of governments’ financial reporting and budgetary classification systems, in order to ensure that the compiled data achieve a minimum level of homogeneity.

Recording private investment in infrastructure, which has risen in recent decades, presents a **fourth challenge**, mainly because of the limited availability of information.

A **fifth challenge** is that of recording investment in infrastructure by subnational (State, provincial, and municipal) governments using their own resources. This investment is significant in various countries and is driven by the progress that many of them have made in decentralizing their administrative structures. Many cases involve programmes that are part-funded by national governments, meaning that data compilation should at least include capital transfers by central governments.

### Data compilation procedures

The four infrastructure sectors (transport, energy, telecommunications and drinking water and sewerage) have been classified in turn as public and private investment, depending on the entity responsible for the investment. Public investment is broken down by central and subnational levels of government.

Websites were consulted and personal interviews conducted in respect of the following sources of information:

#### 1. Public sector investments

Public financial statistics are recorded using one of four accounting bases: accrual, due-for-payment, commitment and cash. As recommended by the International Monetary Fund (IMF) in the *Government Finance Statistics Manual 2001*, the accrual basis was adopted for this project. Under
this method, “flows are recorded at the time economic value is created, transformed, exchanged, transferred or extinguished. In other words, the effects of economic events are recorded in the period in which they occur, irrespective of whether cash was received or paid, or was due to be received or paid” (International Monetary Fund, 2001).

This method of recording data reconciles the time at which public-sector transactions are recorded with the guidelines on methodological recommendations adopted in other synthetic statistical instruments, such as national accounts, the balance of payments, monetary and financial statistics, etc. The accrual basis consequently provides the best estimation of the macroeconomic impact of government fiscal policy.

The national budgets processed by finance ministries provide the main source of information, although data is also taken from reporting on budget execution by the ministries responsible for public works, energy, transport, telecommunications, water and sanitation, and other sectors.

To date, the database has focused exclusively on public-sector activities carried out by central and subnational governments, and therefore does not include investments made by autonomous bodies or State-owned enterprises. This exclusion may be significant in relation to some countries and sectors.

2. Private sector investments

As stated above, the information on private sector investment is limited. The main source used is the Private Participation in Infrastructure (PPI) Project Database, published by the World Bank.

For certain years and countries, data have been drawn from the financial statements of dominant enterprises in sectors of interest.

III. Findings: the economic infrastructure gap and main trends

The aim of this section is to highlight some of the findings of the EII-LAC-DB and to show the type of analysis that it may be used for, without going into great detail. The figures presented below have been grouped by sector for all of the countries on which data has been compiled, without illustrating specific cases. However, it should not be forgotten that aggregate behaviours may conceal heterogeneous outcomes in specific countries, regions or sectors.

The database cannot be reproduced in this FAL Bulletin owing to space restrictions; however, full annual series are available at the website of the Infrastructure Services Unit of ECLAC: http://www.cepal.org/transporte/.

A parameter of investment needs is essential for finding out whether a specific country is investing enough. This was the subject addressed by Perrotti and Sánchez in their research on calculating the infrastructure gap in Latin America and the Caribbean, in which they analysed investment trends in the four major sectors that constitute economic infrastructure (energy, transport, telecommunications and water and sanitation) and, ultimately, estimated and quantified investment needs using alternative measurements.

It is worth noting that the infrastructure gap is defined in relation to factors that are internal to the country or region analysed. This means identifying differences between supply and demand trends, as a result of economic activity.

By calculating this gap, the authors determined the level of annual investment required to respond to the emerging needs of enterprises and final consumers in the region between 2006 and 2020. After updating their calculation for the period 2012-2020, the authors obtained the annual value of 6.2% of GDP (US$ 320 billion in 2012). This calculation rests on the assumption that the pattern of investment will remain unchanged from the study period, in other words, that investment decisions are repeated in relation to alternative transport and energy technologies, among others. The value would probably therefore change if, as ECLAC proposes, infrastructure investment decisions were to adopt a more sustainable and inclusive pattern.

One of the methodologies used by the authors to measure the gap analyses the evolution of the infrastructure stock in relation to the demand trend. Figure 1 shows both variables: the evolution of the infrastructure supply in the selected countries is represented by an infrastructure capital stock index, which was compared with a volume of trade index as a proxy for demand. Taking 1990 as the base year, it was concluded that the growing disparity between the variables (greater than 200% in 2005) reflected a widening of the relative gap.

Figure 2 includes various aspects of the history of investment in infrastructure in Latin America since 1980, and gives an idea of the potential of the EII-LAC-DB and the type of analysis that it may be used for.

When the external debt crisis struck in the 1980s, most of the region’s governments stopped using external credit to fund investment in infrastructure, and instead used their own resources. After a considerable fiscal effort over a number of years, this became unsustainable, leading to a steep drop in public investment levels. Despite the obstacles, investment in infrastructure on average accounted for 3.5% of GDP during the 1980s.
In the 1990s, investment by the public sector fell as a share of total investment, since many countries were bound by fiscal constraints and debt servicing requirements. Public investment thus took on a more passive role than had hitherto been the norm. Plans were set in motion under the Washington Consensus, which was presented as the best viable alternative for overcoming the economic stagnation of the 1980s, and which aimed to give the markets a bigger influence over the economy, at the expense of the role of State.

While private investment responded with faster growth, this was unable to counterbalance the drop-off in public investment, which meant that total investment in infrastructure plummeted. A wave of privatizations in the region’s countries in the late 1980s gave substantial impetus to the inclusion of private capital in the infrastructure sector. Public works concessions offered a second mechanism whereby private actors were able to participate in the financing, construction and management of infrastructure services, especially from the mid-1990s onwards (Rozas, 2010; Rozas Balbontín, Bonifaz and Guerra-García, 2012).

Since 2002, the region has experienced a commodity price supercycle and an improvement in the terms of trade, leading to ten years of sustained economic growth (with the exception of 2009). Investment in infrastructure staged a partial recovery during this period. Substantial windfall revenues as a result of the price boom permitted an increase in national savings and a significant improvement in governments’ fiscal positions. This proved essential in reducing the region’s external vulnerability and enabled a countercyclical response, in the form of vigorous public investment programmes, when the global financial crisis broke in 2008-2009. 2009 also saw investment in infrastructure return to the average levels of the 1980s.

Investment in infrastructure over the past decade has averaged 2.7% of GDP, which according to the Perrotti and Sánchez study, indicates that the region is not investing sufficiently. These authors propose that the region should invest 6.2% of GDP annually between 2012 and 2020 in order to meet the needs of domestic firms and consumers. An appropriate response to these requirements will be a key factor in the region’s linkages with the world economy in the twenty-first century, and in the quality of life of its inhabitants.

Total investment in the four infrastructure sectors covered by the EII-LAC-DB shows an overall uptrend over the period 2003-2012. With few exceptions, most investment since 2005 has been in the transport sector, followed by investment in energy, telecommunications, and water and sanitation. The sharp increase in investment in 2009 occurred mainly in the energy and transport sectors. In 2012, the latest year for which records are available, investment again increased, led by the energy sector (mainly in Uruguay, Peru, Brazil, Guatemala and Chile) and the transport sector (in Brazil, Panama and Costa Rica). Investment in water and sanitation, as a percentage of GDP, also edged up especially in Costa Rica, Brazil and Panama (see figure 3).
better accessibility to distant locations, where it is probable that new settlements will be established, increasing the demand for water, electricity and telecommunications services; environmental concerns may be the result of changes to the transport mix, reducing the propose of fossil-fuel powered vehicles and replacing them with electric cars and bicycles.

Figure 3
LATIN AMERICA: INVESTMENT IN INFRASTRUCTURE BY SECTOR, 2003-2012 (Percentages of GDP)

Source: Infrastructure Services Unit of the Natural Resources and Infrastructure Division of ECLAC, with data from Calderón and Servén (2010), Rozas (2008) and the unit itself.
Note: data from the unit are preliminary.

IV. Observations on data quality

This section offers a brief summary of some of the problems and challenges identified by the Infrastructure Services Unit of ECLAC, in the course of its work compiling information on economic infrastructure investment in the different countries of Latin America.

1. Public sector investments

As noted above, the main source of information on central government public investment is public sector budgets. Given the gradual trend towards decentralization in the countries of the region, it is becoming more difficult to draw together information on all subnational projects under way in each country. Subnational governments are often simultaneously funded by more than one level of government, meaning that in some cases information on investments must be drawn from different government units in order to arrive at a total amount. It is therefore possible that the data for subnational investment is underestimated.

On the other hand, the accounting records of many ministries are conducted on a cash basis, whereas others use an accrual basis, in line with the Government Finance Statistics Handbook 2001. Where the source of information consists in the budget implementation of sectoral ministries (transport, public works, energy, telecommunications or water and sanitation), the problems are similar to the previous instance (cash basis and not accrual basis), although they may be aggravated by the difficulty of consolidating information from various sources, which may contain differing definitions and classifications.

It is likewise possible that some data are not necessarily comparable, since each country uses its own definitions and classifications of investment in infrastructure. In some cases, information on projects is not distinguished from current and capital expenditure, and includes categories such as project management, installation expenditure, fees paid, trade and transport expenditures, taxes, VAT, profits, administration and supervision, and feasibility studies. These items should be addressed systematically according to the international statistical recommendations, and included in summary statistical systems.

In some cases, uncertainty prevails regarding institutional coverage, because in some ministries those responsible for submitting information may not have the tools at their disposal to deliver all the details required in each of the figures.

Similarly, the database contains some years and sectors with gaps because the figures could not be accessed, even though the infrastructure projects were implemented.

Lastly, it is noted that in the short term, and more strongly in the medium and long term, the procedures currently in use may give rise to the problem of “statistical fatigue”, which consists in a gradual deterioration in the interview responses of the focal points. This might affect the quality and truthfulness of the findings, while it is also possible that no response is obtained.
2. Private sector investments

Private-sector investments in economic infrastructure are in most cases excluded from the public-sector records. This is why the PPI database of the World Bank was generally used by ISU to compile information on the private sector, in many cases correcting for pre-established criteria, such as the treatment of privatizations, mergers and acquisitions, which are not considered under the category of gross capital formation spending on infrastructure. Some projects are a mix of public and private participation, which was taken into account by making the appropriate corrections.

Divergences in the manner in which information is recorded meant that, in most cases, PPI data are not comparable with those submitted by public finances, so that the joint use of public- and private-sector data can cause problems of statistical consistency.

Conclusions and main challenges

As estimated by Perrotti and Sánchez, the investments required to close the infrastructure gap are enormous, amounting to 6.2% of annual GDP for the period 2012-2020. However, this calculation assumes that the historical pattern of investment repeats itself. This means that the 6.2% value is an approximation of investment needs, and not a specific recommendation. As ECLAC has maintained, it is necessary to revise the pattern of investment decisions so that it can be guided towards new infrastructures that support efforts in favour of equality, sustainability and inclusion. For these purposes, notable in the case of transport, priority should be given to sustainability and inclusion. For these purposes, notable in the case of transport, priority should be given to sustainability and inclusion. For these purposes, notable in the case of transport, priority should be given to sustainability and inclusion. For these purposes, notable in the case of transport, priority should be given to sustainability and inclusion.

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With strengths and weaknesses, this type of exercise has allow for the construction of a series of preliminary data, which may be considered “good” in the sense that they respond to the best solution found to a challenge that must be met with limited resources. Given the countless obstacles faced in this task, constant monitoring is required, both to update and review the figures, and to improve the definitions and procedures that have been used until now.

In order to overcome some limitations, the ECLAC Infrastructure Services Unit has produced a document, “Glossary for the collection of data on publicly funded economic infrastructure investments in Latin America and the Caribbean”. This document is composed of two complementary instruments: a “glossary” and a “form”. Both are intended to serve as a guidance tool for the appropriate compilation, recording, validation and processing of information on publicly funded economic infrastructure investments, following a mechanism that facilitates the standardization of the data obtained, and their comparison over time and across countries.

The “glossary” and the “form” contain metadata and procedures in an attempt to ensure greater accuracy.

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4 Co-modality is the use of one transport mode, or a combination of modes, for a journey or set of journeys, which maximizes the efficiency of travel through the optimum use of each for of transport, and its possible combination with other modes, so that the journey is efficient and sustainable in accordance with the particular transport needs, and the distance that has to be travelled. (Lardé and Marconi (2014), “Glossary for the collection of data on economic infrastructure investments on the basis of public finances in Latin America and the Caribbean”, draft.)

5 The full document was produced in 2014 by Jeannette Lardé of the Natural Resources and Infrastructure Division of ECLAC and Salvador Marconi of the Statistics Division of ECLAC, in the context of the memorandum of understanding between IDB, CAF and ECLAC. It will be published in due course, once the results of the pilot test have been included.
so that the users of this information understand and support that data that they are compiling and, if they so require, are able to reproduce and reconstruct their search processes. Both documents will be used to compile and record information from the public sector from the 2013 financial year, and in order to validate current series, following a consistent procedure.

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