2004

Summary

Productive development in open economies

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PRODUCTIVE DEVELOPMENT IN OPEN ECONOMIES

Summary

The countries of the Latin American and Caribbean region have shown a keen and lasting interest in mechanisms of economic development and public policies for its promotion. This is a process in which ECLAC has been involved ever since its founding over half a century ago. Today, the debate on these issues continues against the backdrop of a globalization process in which the remarkable dynamism of some dimensions –especially its economic, financial and cultural aspects– contrasts with the slow formation of an institutional network capable of coping with the increased interdependence of nations on various levels and of gradually rectifying the striking asymmetries of the global order.

Over the past two decades, the Latin American and Caribbean region has wagered heavily on its integration into the global economy. In fact, of all the developing regions of the world, it has been the most resolute in its pursuit of economic liberalization. A review of this period brings to light a number of extremely important achievements, but it also reveals areas in which the region is lagging behind and others in which unfinished business remains. ECLAC contends that the region must build upon the progress it has already made, but it also has to close existing gaps and address unresolved issues. The inroads made in these areas may play a vital role in consolidating the region's fuller integration into the world economy and in ensuring that the social, economic and political costs of the economic reform process have not been incurred in vain.

I. Basic features of the current global environment

The 1990s saw the consolidation of economic and financial traits which are firmly rooted in the past. During that period, the conditions were created that ultimately allowed the world economy to evolve from an aggregate of national economies linked by trade, investment and financing flows into a set of global market and production networks that span national borders. While this process is undoubtedly an increasingly powerful one, it has not been accompanied by an equivalent development of global institutions, whose agenda is incomplete and asymmetrical (Ocampo, Bajraj and Martin, 2001).

1. Major economic events

Against a backdrop of slower global growth, international trade expanded at rates of close to 6% per year between 1990 and 2003; foreign direct investment (FDI) verged on US$ 1.4 trillion in 2000 (a sevenfold increase over the early 1990s), and transactions on currency markets have totalled over US$ 1.5 trillion per day in the early years of this century. Meanwhile, innovation and technological change have become even more concentrated in the developed countries.

(a) Slackening global economic growth

Between 1990 and 2003, world economic growth averaged just 2.6% per year, the lowest level for any equivalent period since the Second World War. This result reflected the lacklustre performance of the developed countries, the crisis in Eastern Europe and sluggish growth in Africa and in Latin America and the Caribbean. By contrast, Asia grew swiftly and growth rates picked up in the Middle East, as shown in table 1.

Table 1
Annual growth rates, selected periods
(Average annual rates)

	World	Developed countries	Devel-oping coun-tries	Latin America	Africa	Asia	Middle East	Eastern Europe
1950-1960	4.4	4.1	5.1	4.9	4.5	5.7	5.7	9.2
1960-1973	5.1	5.0	5.5	5.5	5.0	5.2	7.7	6.7
1973-1980	3.4	3.1	5.1	5.1	3.5	6.2	4.4	4.6
1980-1990	3.2	3.2	3.7	1.6	2.6	7.0	1.6	2.4
1990-2003	2.6	2.3	4.4	2.7	2.8	6.0	3.3	-0.3
Per capita								
1950-1960	2.8	2.8	2.8	2.2	2.0	3.6	2.9	8.2
1960-1973	3.1	4.1	3.0	3.3	2.5	2.9	4.8	5.5
1973-1980	1.6	2.3	2.9	2.4	0.3	4.3	1.4	3.7
1980-1990	1.5	2.4	1.7	-0.4	0.1	5.1	-1.6	1.7
1990-2003	1.2	1.7	2.7	1.0	0.4	4.5	1.1	-0.4

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from various official international sources.

Within the group of developed countries, the performance of the United States in 1990-2003 (annual average growth of 3%, with the rate picking up to over 4% in 1997-1999) contrasted sharply with the results posted by the European Union (2% per year) and Japan (an average annual growth of 1%, with negative rates being recorded in 1991 and 1998). These trends in the developed countries were accompanied by major macroeconomic imbalances. In the United States, rising expenditure and the downturn in fiscal revenues triggered by tax cuts and an economic recession turned the fiscal surplus of the 1990s into a hefty deficit, thereby raising the problem of the "twin deficit" once again. Meanwhile, in the European Union, other events were overshadowed by the historic entry of 10 new members into the European Union on 1 May 2004.

The developing countries, including the transition economies of Eastern Europe, entered the 1990s with sharply differing growth rates. The most dynamic countries in 1990-2003 were those of South-East Asia, China and India. With the exception of Indonesia, the countries of South-East Asia recovered rapidly from the 1997 crisis, while China more than tripled its output over this period (226%) and India virtually doubled its GDP (98.1%). China's remarkable growth has made it the world's third-largest importer, behind the European Union and the United States. Meanwhile, from 1996 onward, the transition economies have returned to a growth path which has tended to stabilize at around 4% in the early years of the present decade. After its poor performance of the early 1990s, Africa has been growing fairly steadily at about 3% per year since 1994. Like the

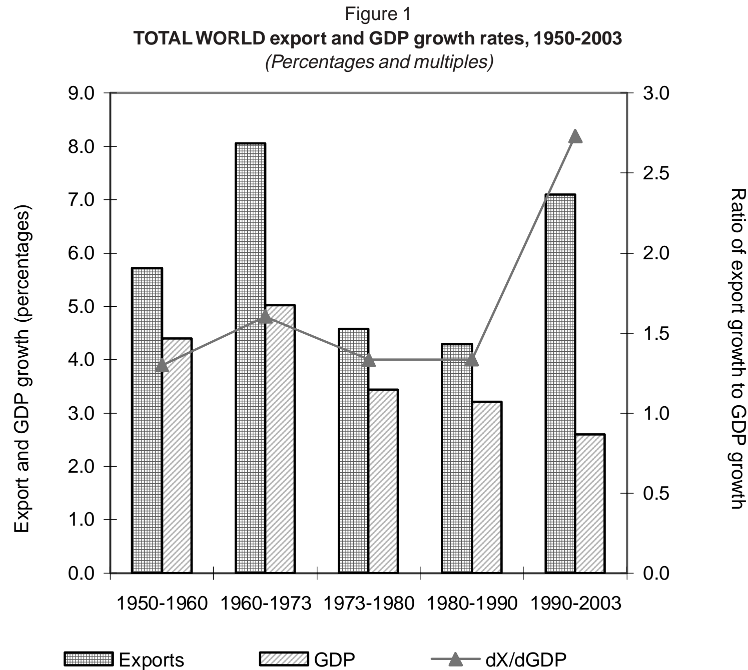
Middle East, Latin America and the Caribbean performed better in the first half of the 1990s than in the second and particularly since 1997; in fact, in 1999 and 2001, output declined sharply.

(b) Exports and economic growth: a changeable relationship

In 1990-2003, world trade once again attained annual growth rates similar to those of the first two decades of the post-war period, following a sharp slowdown between 1973 and 1990. Since world output growth rates fell at the same time, the ratio between the two variables in 1990-2003 was the highest since the Second World War, with exports growing almost three times as fast as output (see figure 1). In fact, exports grew faster than output every year from 1985 to 2000. Increasing trade liberalization in manufacturing and services, together with the rising volume of intra-firm trade being fueled by the dynamics of international systems of integrated production, are one of the reasons for this gap between the growth rates for world trade and GDP (UNCTAD, 2002a).[1]

1 Something similar, although less marked, had already happened between 1960 and 1973, when, as a result of a steep rise in intra-industry trade in Western Europe, international trade consistently grew faster than world output.

Figure 1
TOTAL WORLD export and GDP growth rates, 1950-2003
(Percentages and multiples)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from various official international sources.

This tendency was more pronounced in developed economies than developing ones and, among the latter, much stronger in Latin America and the Caribbean than in the Asian economies. In fact, Latin American and Caribbean exports expanded, on average, around 3.5 times as fast as GDP between 1990 and 2003, while the ratio was 1.4 in Taiwan Province of China, 1.6 in China and 1.8 in the Republic of Korea and India. Trade liberalization was particularly vigorous in Latin America and the Caribbean in the 1990s, while a number of Asian economies had already opened up to international trade in previous decades.

Rapid economic growth has been more and more closely associated with export success, but strong export performances have been seen within a wide range of different trade policy frameworks. In point of fact, no robust relationship has been observed between export growth and trade liberalization. By the same token, rapid growth in developing countries has taken place in the presence of different combinations of economic orthodoxy and "local heresies" (Rodrik, 1999 and 2001).

The composition of world trade in terms of different categories of goods has changed substantially in recent years (UNCTAD, 2002). Table 2 divides goods into dynamic and non-dynamic, or stagnant, products (i.e., those growing faster and slower than average, respectively) and indicates their relative importance based on a world trade classification developed by ECLAC, which highlights the intensity of natural resource and technology use.[2]

Table 2
DYNAMIC AND STAGNANT PRODUCTS IN WORLD IMPORTS, BY TECHNOLOGICAL CATEGORY, 1985 AND 2000
(Percentages of total imports)

	Dynamic products				Stagnant products				Net increase or decrease (A-B)
	Number of items	1985 (1)	2000 (2)	Increase A=(2)-(1)	Number of items	1985 (3)	2000 (4)	Decrease B=(4)-(3)	
Commodities	15	0.7	0.8	0.1	132	22.5	11.6	-10.9	-10.8
Natural-resource-based manufactures	65	5.3	6.8	1.6	134	14.3	8.9	-5.4	-3.8
Low-technology manufactures	71	7.3	10.8	3.5	90	7.1	4.9	-2.2	1.3
Mid-level technology manufactures	91	16.7	21.1	4.4	111	11.8	8.6	-3.3	1.1
High-technology manufactures	45	9.5	21.6	12.2	21	2.2	1.3	-0.9	11.3
Unclassified products	4	1.4	2.8	1.4	7	1.4	0.9	-0.5	0.8
Total	291	40.8	63.9	23.1	495	59.2	36.1	-23.1	0.0

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of the Competitive Analysis of Nations (CAN) program, 2001, and the International Commodity Trade Data Base (COMTRADE).

Commodities are strikingly non-dynamic, as are natural-resource-based manufactures, largely as a result of protectionist practices in the developed world. What is more, these practices, together with growing competition in the market, have helped drive down commodity prices (Ocampo and Parra, 2003). Manufactures based on the use of high technology have been far more dynamic than the rest, increasing their share by more than 11 percentage points.

2 This ECLAC (1992) classification groups items at the four-digit level of the Standard International Trade Classification (SITC).

(c) The global leadership of transnational corporations

The appearance of new technologies and the rapid advancement of existing ones have significantly altered the way production is organized within companies, production sectors and, ultimately, the world economy. Although global conglomerates and oligopolies are not new to the world economy, what *is* new is the increase in the number of sectors where they have become the standard way of organizing production; this is particularly the case in industries involving a great deal of technological research and development (R&D) and in manufacturing enterprises that make use of large economies of scale. In this context, coordination of the entire production chain is a key source of competitive advantages, and for this reason the network is used as a strategic asset.

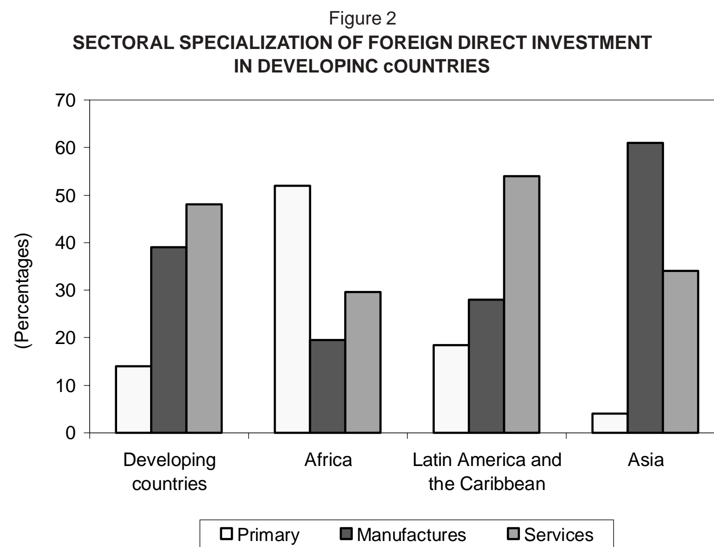
Transnational corporations have been the most dynamic economic agents in this move towards the creation of global oligopolies in more and more sectors and activities, as these types of companies have been able to react the fastest to changes in the way production is organized and have succeeded in capitalizing on their competitive advantages to organize international systems of integrated production. The expansion of transnational corporations has fueled a rapid increase in foreign direct investment (FDI) flows which has been accompanied, to differing degrees depending on the sector and the region of the world, by intense merger and acquisition activity. This global integration of production is being driven by some 64,000 transnational corporations that control over 870,000 foreign subsidiaries. Operating at a supranational level, with capital flows and a capital formation capacity that are worldwide in scope, transnational corporations are both the main architects and the chief beneficiaries of globalization.

From the vantage point of developing countries, transnational corporations are viewed in two ways: quantitatively, with the emphasis on FDI and on external financing as seen from a balance-of-payments perspective; and qualitatively, with the focus being on the contribution they may make to productive development in host countries.[3] A useful way of reconciling these sometimes conflicting outlooks is to analyse the corporate strategies that lead transnational corporations to invest in developing countries (ECLAC, 2004).

3 This contribution may include the establishment of new activities to improve the quality of linkages with the world economy; access to new technologies, their transfer and assimilation; the development and deepening of production linkages; human resources training; and development of local entrepreneurial capabilities.

There are four main motivations underlying the production of goods and the provision of services. The empirical evidence appears to suggest that the various regions of the developing world have taken different (passive or active) approaches to the use of these corporate strategies based on their comparative advantages. This, in turn, has led to significant differences in the sectoral composition of FDI in the various regions, with FDI stocks being concentrated in the primary sector in Africa, in manufacturing in Asia and in services in Latin America and the Caribbean (see figure 2).

Figure 2
SECTORAL SPECIALIZATION OF FOREIGN DIRECT INVESTMENT IN DEVELOPINC cOUNTRIES



Source: World Bank, *Global Development Finance 2004: Harnessing Cyclical Gains for Development*, Washington, D.C., 2004.

Striking similarities are also beginning to emerge in trade and investment links. Regional and bilateral trade agreements are gradually being converted into investment agreements and, in a number of cases, agreements on double taxation (UNCTAD, 2003). These arrangements place greater restrictions on the treatment of transnational corporations than those agreed to in multilateral negotiations.

(d) The predominance of financial capital and the volatility of capital flows

The growth of international trade and FDI has been accompanied by an expansion of international financial flows, which have come to play a dominant role in the world economy. International economic transactions grew far more rapidly than GDP in 1990-2003. Trade grew faster than

GDP but more slowly than bank credit and much more slowly than international bond placements. The increase in the stock of outstanding financial derivatives, meanwhile, has been much sharper, although not all of these instruments correspond to international transactions (see table 3). Globalized financial capital seems to have become increasingly detached from the real economy, even though, theoretically, its function is to finance that sector of the economy. The provision of financing to non-financial agents creates the base for an inverted pyramid of derivatives that swell the assets and liabilities of intermediaries and offer financial investors a multitude of investment options that are entirely divorced from real investment and commercial transactions.

Table 3

ECONOMIC, TRADE AND FINANCIAL INDICATORS, 1990-2003

(Average annual growth rates)

	Growth rate
World output	2.6
World trade	5.9
Developed-country bank assets in the rest of the world [a]	8.3
International bond issues [a]	15.0
Financial derivatives (options and futures) [a]	22.6

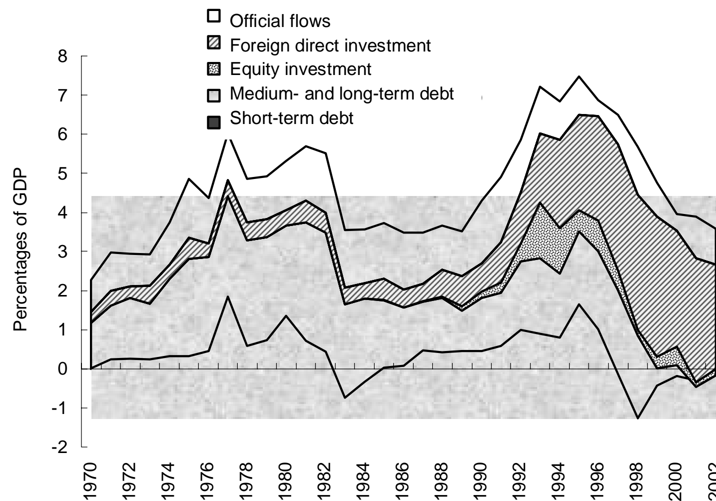
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures from the countries and from the United Nations Conference on Trade and Development (UNCTAD), International Monetary Fund (IMF) and Bank for International Settlements (BIS).

[a] Figures refer to year-end stocks.

Volatility and contagion have been two of the inherent characteristics of this rapid financial development process. Volatility is not a new phenomenon, but certain features of today's markets have tended to heighten it. These include, firstly, insufficient regulation of the agents operating in financial markets and the procyclical nature of existing regulatory systems. Secondly, problems of contagion have been associated with an inadequate supply of information on emerging markets, a situation which appears to be at least partially attributable to geographic proximity, the level of trade and the similarity of economic policies. Thirdly, the fact that different agents use the same risk assessment system and employ a short time horizon in its application tends to intensify the bandwagon effect, which is further compounded by the procyclical behaviour of risk rating agencies (ECLAC, 2001).

In the 1990s, unlike previous decades, FDI and short- and medium- or long-term private sources provided most of the financing for developing countries, chiefly through bond issues. Broadly speaking, FDI followed an upward trend up to 2000 and behaved less procyclically (see figure 3).

Figure 3
NET FINANCIAL FLOWS TO DEVELOPING COUNTRIES



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Bank, *Global Development Finance 2003: Striving for Stability in Development Finance*, Washington, D.C., April 2003

In marked contrast to FDI, sources of short- and medium- or long-term private financing have been subject to fluctuations, and financing conditions have been highly sensitive to the ups and downs of international markets. Portfolio equity flows and placements of American Depository Receipts (ADRs) exhibited the greatest instability. Unlike FDI, these other sources of finance, as a group, were strikingly procyclical in 1990-2003 (Ffrench-Davis and Ocampo, 2001).

(e) The concentration of innovation and technical progress

The intensification of product and process R&D and the development of worldwide brands have also increased companies' fixed costs. Thus, economies of scale in R&D and in marketing have combined with economies of scale in production, and global producers are now struggling to win sufficiently large market shares to cover their fixed costs. Furthermore, economies of agglomeration tend to lead to a geographic polarization of the most dynamic activities. These phenomena must be understood in order to comprehend how the world economy of today works. They also play a substantial role in the accentuation of the productive and technological asymmetries existing between developed countries and the developing world.

First of all, the developed countries account for 84.4% of gross R&D expenditure and a somewhat smaller percentage of scientific researchers and engineers (see table 4). Other indicators provide an even more glaring picture of the asymmetries existing between developed and developing countries: the ratio of gross R&D expenditure per capita is 19:1; the ratio of scientific researchers and engineers per capita is 7:1; and gross R&D expenditure per researcher is more than double. It should be noted, nonetheless, that there are also striking disparities within the developing world itself, with the new industrial economies of Asia standing out from the rest. Be this as it may, not only are R&D as such concentrated in the developed countries, but so are the sectors and production activities that are most closely linked to technological change. These activities are highly dynamic elements within the production structure and world trade and are a source of large innovation rents.

Table 4

WORLDWIDE DISTRIBUTION OF RESEARCH AND DEVELOPMENT (R&D) ACTIVITIES, 1996-1997

Groupings and countries	Gross expenditure on R&D (GERD)				Researchers			GERD per researcher (thousands of PPP dollars)
	Amount (billions of PPP dollars)[a]	% world GERD	% of GDP	Per capita (PPP dollars)	Number (thou-sands)	% of world total	Per million inhab-itants	
World	547	100.0	1.8	100	5 189	100.0	946	105
-Developed countries	461	84.4	2.2	377	3 713	71.6	3 033	124
-Developing countries	86	15.6	0.6	20	1 476	28.4	347	58
-United States	199	36.4	2.6	750	981	18.9	3 697	203
-European Union	138	25.2	1.9	370	825	15.9	2 211	167
-Japan	83	15.2	2.8	661	817	15.8	6 498	102
-Russian Federation	6	1.0	0.9	39	562	10.8	3 802	10
-Central and Eastern Europe	6	1.0	0.8	49	168	3.2	1 451	33
-Latin America	17	3.1	0.5	34	348	6.7	715	48
-New industrial economies of Asia	27	4.9	1.1	66	241	4.6	595	111
-China	21	3.9	0.6	17	552	10.6	454	38
-India	11	2.0	0.7	11	143	2.8	151	76
-Africa	4	0.7	0.3	6	132	2.5	211	29

Source: United Nations Educational, Scientific and Cultural Organization (UNESCO), *The State of Science and Technology in the World, 1996-1997*, Montreal, UNESCO Institute for Statistics (UIS), 2001.

[a] Purchasing power parity dollars.

Secondly, technological change in the developed world affects developing countries in many ways, such as the transfer to developing countries of production sectors that are considered to be technologically

mature in developed countries; the transfer of technology as such, including technologies that are embedded in production equipment; and the possible participation of developing countries in the more dynamic production activities and sectors. All these mechanisms are subject to constraints or costs, however, including the low profit margins and protectionism existing in mature industrial sectors; the fact that technology transfers may be subject to the payment of innovation rents, which are increasingly protected by the universalization of strict rules on the protection of intellectual property; and the possibility that developing countries' opportunities to participate in highly dynamic sectors may be largely confined to low-skill activities.

The combined effect of all these factors explains why major asymmetries continue to exist at the world level: the marked concentration of technical progress in the developed countries, these countries' continuing dominance in the registration of intellectual property in the most dynamic sectors of international trade and their hegemonic influence over the creation of large transnational corporations. Thus, the economic opportunities of developing countries continue to be largely determined by the position they occupy in the international hierarchy.

2. International regimes

Globalization has given rise not only to growing interdependence, but also to sharp inequalities across countries. This is attributable to the fact that economic processes have been allowed to follow their course without consideration for the various countries' differing resources and possibilities. What is more, in addition to the failure to pay due attention to the inequalities existing at the outset of the process with a view to creating a more equitable world, in many cases developing countries have found themselves on what amounts to an essentially uneven playing field. Today's globalization process thus calls for new institutions to reconcile a more efficient management of global interdependence with the adoption of clearly defined principles of international solidarity. Only thus will it be possible to ensure that globalization "becomes a positive force for all the world's people", as stated in the Millennium Declaration (United Nations, 2000).

Major obstacles stand in the way of the creation of a new institutional structure, however: the lack of shared principles among the main stakeholders, the unequal influence exerted by those participating in the process and the difficulty of creating stable coalitions as a basis for addressing the various issues. This situation is compounded by the central paradox of the current globalization process, i.e., the contrast between problems of global scope and the lack of any genuine internationalization of political affairs (Ocampo and Martin, 2003). The current status of the

multilateral debate on a number of issues of particular importance for the definition of productive development strategies in open economies will be discussed in the following sections.

(a) Macroeconomic and financial regimes

The uncertainty stemming from the South-East Asian crisis of 1997, together with the perception that the international financial architecture was not fully equipped to deal with it, set the stage for a political debate concerning the macroeconomic dimensions of the crisis and its implications for the promotion of development and the eradication of poverty (United Nations, 1999 and 2001). This prompted ECLAC to highlight the value of macroeconomic and financial stability as a global public good and to underscore the need to correct the asymmetries of the world economy in this respect (ECLAC, 2002).

International macroeconomic and financial stability is a global public good that generates positive externalities for all international market participants and averts the negative externalities associated with contagion, both during booms and at times of financial panic or when recessionary forces come to the fore. This explains the importance of certain global processes that are taking place on various fronts.

Firstly, the lack of mechanisms for dealing with the effects that the major economies' macroeconomic policies have on the rest of the world is a basic failing of the current international order.

The second front on which action is called for is the preventive macroeconomic surveillance of all economies and the drafting of codes of good practice. Major strides have been made in recent years in the areas of crisis prevention and the creation of early-warning vulnerability indicators, in addition to the adoption of codes of good macroeconomic management practices. Many developing countries are finding some of these standards to be very complex and difficult to implement, however. Consequently, they are asking for the gradual and differentiated implementation of such standards and are emphasizing the need for international support and technical assistance.

The third front in the effort to secure global macroeconomic stability is the formulation of international standards for the prudential regulation and supervision of financial markets and the provision of better market information. With this aim in mind, it is hoped that improvements along a number of these lines can be made in the proposals formulated by the Basel Committee on Banking Supervision concerning the drafting of a new agreement (Basel II) for entry into force by late 2006.

Apart from the systemic issues related to global macroeconomic and

financial stability, international efforts should focus on the gradual correction of macroeconomic and financial asymmetries in the world economic system. The primary objectives here are to make access to international financial resources less segmented and volatile for developing countries and to give these countries greater scope for the adoption of countercyclical macroeconomic policies.

In order to upgrade existing mechanisms for the provision of liquidity in crisis situations, the International Monetary Fund should gradually broaden its role as an international lender of last resort. The provision of liquidity should be supplemented by a system for resolving debt overhangs, for which no international arrangements have yet been established. In recent years progress has been achieved in some related areas, but apart from the specific inroads made in the bond market (collective action clauses) and the Paris Club (government creditors), the IMF effort to develop a comprehensive statutory approach to solvency problems has not garnered the necessary support. The proposed sovereign debt restructuring mechanism was strongly opposed by private financial institutions on the grounds that it would have constrained their negotiating capacity and made it easier for borrower countries to default.

Another important sphere of action is the strengthening of multilateral banking and development cooperation. Multilateral development banking often complements the role played by IMF in supplying liquidity, as well as performing other critical functions, such as stimulating innovative activities (particularly in the area of social development) and private-sector participation in infrastructure projects, supporting the expansion of financial systems and especially of national development banks in developing countries and providing technical assistance in general.

At the International Conference on Financing for Development held by the United Nations in Monterrey, Mexico, in March 2002, the international community made a commitment to strengthen international financial cooperation for the relatively less developed countries. Although the efforts made after that conference in respect of official development assistance (ODA) and the Heavily Indebted Poor Countries (HIPC) debt reduction initiative were noteworthy, the increase in ODA made by donor countries still falls far short of the US$ 100 billion per year that would be needed to meet the United Nations Millennium Goals (United Nations, 2004).

The HIPC Initiative has also proved difficult to implement. Late in 2003 a group of 27 countries reached the HIPC decision point and became eligible for debt relief measures that reduced their debt by about two thirds of its net present value. Only eight countries in the group, among them Bolivia, also reached the completion point and thus left the programme.

Nonetheless, there is no certainty that countries that reach the completion point have actually reduced their debt to a sustainable level.

The last piece in this overall picture is the negotiation of a new international agreement on the scope of conditionality with a view to making a firm sense of ownership of macroeconomic and development policies an integral part of international practice. The progress made in this area includes the analysis and discussion of the issue in the International Monetary Fund in 2001. Nevertheless, in some cases, advocacy of a sense of policy ownership actually conceals new forms of conditionality; this underlines the need for an explicit international agreement on the subject.[4]

(b) Trade negotiations

The Fourth Ministerial Conference of WTO, held in Doha in November 2001, ushered in a new round of negotiations, which should be completed by January 2005. Developing countries played a key role in defining the programme of work, which places priority on reducing the asymmetries between the rights and obligations of member countries (currently 148 in number). This position is based on the orientation of the multilateral trading system, in evidence ever since the Uruguay Round, towards establishing a homogeneous regulatory framework that disregards the asymmetries existing in the world economy (Ocampo and Martin, 2003).

As the globalization process has proceeded, the scope of international trade negotiations has been extending far beyond conventional provisions governing cross-border transactions of merchandise to encompass more and more issues that were formerly addressed soley within a national policy setting. As a result, negotiations now have to be approached in a far more comprehensive and consistent way than before while covering a wide variety of issues

To succeed with this systemic approach, developing countries will have to build the necessary institutional capabilities to design and implement appropriate, coherent policies on various fronts and will need to allocate large amounts of public funds that are needed for other purposes. The Doha Round covers 21 issues. These issues are divided into eight groups, six of which form part of the "single undertaking" established in the Uruguay Round. In accordance with this principle, uncontroversial subjects are tied to the success or failure of negotiations on issues about which the member countries hold sharply differing positions.

4 For some recent suggestions regarding this subject, see Rodrik and Subramanian (2003).

The texts that came out of Doha have given rise to a development programme that reaffirms the principle of special and differentiated treatment and includes commitments regarding cooperation and training in developing countries, particularly the least developed ones.

The development programme's agenda gives a prominent place to analysis of the countries' scope for adopting development policies, particularly as regards export diversification. The Uruguay Round significantly reduced the opportunities for middle-income countries to use national policies to promote exports and strengthen their links with national productive development. As in other fields, the agreements authorize types of subsidies that are used more in developed countries (for technology, subnational development, the environment) while restricting those used more often in developing nations (export processing zones, direct subsidies for export activities and performance agreements).

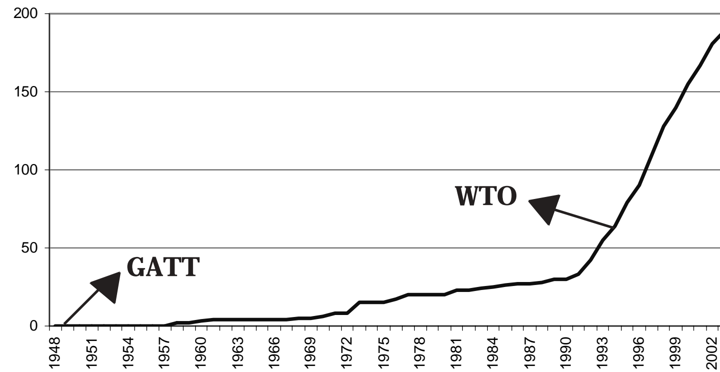
For the most part, the work undertaken as a result of the Doha Round has not proceeded as originally intended. Overall, asymmetries in the progress of the negotiations can be seen on two different levels. Firstly, few advances have been made in relation to subjects of interest to developing countries, such as agriculture and rules on antidumping and subsidies. This stands in contrast to the more rapid progress seen in discussions on investment, services and further liberalization of trade in industrial products. Secondly, there is an almost complete absence of progress in the specific tasks defined as part of the "development dimension".

At the Fifth Ministerial Conference of WTO, held in Cancún in 2003, the greatest difficulties arose in the areas of agriculture, market access for non-agricultural goods and the four "Singapore issues". The situation was compounded by the consideration of a number of other issues relating to the development agenda, including special and differentiated treatment for developing countries and problems with implementation, on which no significant consensus was reached.

In addition to the obvious difficulties encountered in reaching significant multilateral agreements, there have been a number of other disturbing developments. One such development is the expiration of the deadlines for various transitory regimes, which threatens to leave a series of important issues in an indeterminate status for an indefinite period of time.[5] Another is the proliferation of regional and bilateral treaties, some of which involve both developed and developing countries (see figure 4).

5 One case in point is the non-actionable subsidies that expired in 1999 and the "peace clause" of the Agreement on Agriculture, which expired in 2003.

Figure 4
PREFERENTIAL FREE TRADE AGREEMENTS, 1948-2003
(Number of agreements notified to WTO)



Source: United Nations Educational, Scientific and Cultural Organization (UNESCO), *The State of Science and Technology in the World, 1996-1997*, Montreal, Institute of Statistics, 2001.

[a] Includes the free trade agreements on goods (GATT Art. XXIV), services (GATS Art. V) and the Enabling Clause (regional integration among developing countries) notified and in force as of December 2003.

Given the current state of affairs, developing countries are faced with some difficult choices. On the one hand, it is usually better to continue negotiating than to sign a disadvantageous agreement and, in fact, the firmness shown by the G20+ countries in Cancún is a step forward, since it is the first time that developing countries have wielded some measure of power in multilateral negotiations. On the other hand, the paralyzation of these multilateral negotiations fits in with the strategy of the developed countries, particularly the United States and the European Union, which continue to sign free trade agreements with countries or regions in the developing world covering many issues about which there is no multilateral consensus. For many developing countries, signing a free trade agreement in order to increase and stabilize their access to developed-country markets is a high-priority objective, and this also falls into line with this trend. There is a risk that these agreements could undermine the negotiating parties' determination to move the international negotiations forward on significant issues while at the same time siphoning off the already scarce supply of technical resources from these negotiations.

(b) Environmental sustainability

The United Nations Conference on Environment and Development (the "Earth Summit" held in Rio de Janeiro, Brazil, in 1992) was a landmark event in the formulation of a global agenda for sustainable development.

This meeting marked a turning point in the negotiation of multilateral agreements on sustainable development, since it was there that a broad view of development was adopted which recognized the importance of reconciling economic production and international trade with sustainable natural resources use and environmental protection.

At the World Summit on Sustainable Development (Johannesburg, South Africa, 2002), the political commitments of the Rio Declaration were reaffirmed, particularly the principle of common but differentiated responsibilities and the precautionary principle. Furthermore, the 34 targets agreed to at the Summit complement the commitments previously established in respect of the development goals set forth in the United Nations Millennium Declaration. This was also the first time that recognition was given to the importance of specific regional initiatives and of cooperation among public-sector, private-sector and civil society actors through voluntary partnerships.

The global agenda being shaped by current international debates covers a number of important issues (ECLAC, 2003; United Nations, 2002; ECLAC/UNEP, 2001). First, it stresses the need to alter certain unsustainable patterns of consumption and production in both developed and developing countries. In this area, energy efficiency is unquestionably one of the most important items on the agenda. The Kyoto Protocol is the multilateral instrument *par excellence* for pursuing this strategy, while the regional mechanism set up by the European Union (the "Eurokyoto") is the first concrete example of a global environmental services market.

A second important issue is the sustainable management of ecosystems and biological diversity. What is needed in this case is an alliance to uphold a world commitment to conserve biodiversity *in situ*, preserve important ecosystems and prevent their degradation. This global alliance should be formed within a framework that combines the principles of global management for the protection of land and marine environments. In order for these initiatives to be implemented effectively, a global compensation fund should be set up to finance the conservation and restoration of ecosystems; recognition of the environmental services provided by natural ecosystems should be part of this framework.

It is also important to encourage countries to ratify the Cartagena Protocol on Biosafety so that it can enter into force. The importance of biotechnology in building competitiveness should not blind the countries to the need to use the approved mechanisms for analysing the risk that genetically modified organisms could pose to biodiversity. To develop these multilateral mechanisms, it will be necessary to consolidate operational approaches for mobilizing the global resources needed to tackle global problems in accordance

with the principle of common but differentiated responsibilities. Steps should be taken to explore opportunities for taxing activities of international scope that are potentially damaging to the world environment. These tax revenues could then be used to set up specific funds for solving these problems at a multilateral level based on the “polluter pays” principle.

There is also a need for greater coherence and compatibility between the world trading system, including intellectual property protection, and sustainable development. The Doha Declaration clearly specifies that countries may take steps to protect human and animal health, plant life and the environment, providing that the measures they use to do so are not disguised forms of trade discrimination or protectionism. In addition, analysis of the effects of environmental measures on market access, particularly in the case of developing countries, is identified as a priority issue for the Trade and Environment Committee, as is the analysis of the main provisions of the agreement on intellectual property protection and environmental labelling.

(c) International migration

International migration has become one of the most delicate issues in the international arena in recent years owing to growing concern about references to its consequences in developed countries. Nevertheless, the inclusion of migration on the international agenda is an important component of an international system designed to overcome the asymmetries of the world order. Asymmetrical market liberalization has regressive effects at the world level, since it benefits the more mobile factors of production (capital and skilled labour) and is detrimental to the less mobile ones (low-skilled labour).

As ECLAC has emphasized in recent years, there is still a crucial need for global agreements on migration if a democratic, shared and sustainable contemporary agenda concerning this phenomenon is to be achieved. These agreements need to replace approaches aimed at controlling migration with provisions that are more closely attuned to the dynamics of labour markets and the protection of individual rights (ECLAC, 2002).

The lack of an international framework for the governance of migration increases the risk of exclusion, discrimination and abuse of human rights, particularly in the case of undocumented migration, which continues to increase as methods for evading controls on the entry and residence of foreigners proliferate. One extreme situation is the traffic in persons, with the most serious manifestation of this phenomenon being the exploitation of minors. This phenomenon underscores the ethical imperative of protecting human rights and the need for the relevant

international instruments to be ratified or, where they have already been adopted, fully implemented.

The governance of international migration needs to include improvements in the remittances market (one of the most visible manifestations of contemporary migration), the creation of innovative mechanisms that take advantage of the continued development of communications media to link countries of origin with their emigrants, and gender mainstreaming, especially in view of the fact that a majority of migrants are women. Remittances to developing and transition countries are estimated to have totalled about US$ 93 billion in 2003, with a third of this sum going to countries in Latin America and the Caribbean, particularly Mexico (see table 5).

Table 5
REGIONAL DISTRIBUTION OF REMITTANCES, 2001-2003
(Billions of dollars)

Region	2001	2002	2003	Increase 2001-2003 (percentages)
East Africa and the Pacific	13.7	17.0	17.6	28.9
Europe and Central Asia	10.2	10.3	10.4	1.9
Latin America and the Caribbean	22.9	26.8	29.6	29.3
Middle East and North Africa	13.2	13.0	13.0	-1.2
South Africa	13.1	16.9	18.2	38.7
Sub-Saharan Africa	3.9	4.1	4.1	3.5
Total	**77.1**	**88.1**	**93.0**	**20.7**

Source:World Bank, *Global Development Finance 2004: Harnessing Cyclical Gains for Development*, Washington, D.C., April 2004.

Despite its size, the family remittances market is very imperfect, with high and variable transfer costs and asymmetrical participation by agents. The lack of policies for stimulating or orienting the productive utilization of family remittances minimizes their effect on the recipient communities. Although less significant in quantitative terms, collective remittances are potentially a very important pool of resources, depending on the relevant communities' capacity for their generation and utilization and on the role they play as a transnational link.

One disturbing aspect of international migration is the part it plays in selectively draining off skilled human resources, thereby heightening the already deep asymmetries between developed and developing countries in terms of their research and development capabilities. Two factors combine to increase migration flows of skilled personnel. One is the rising returns and substantial externalities of knowledge creation, which give rise to a

concentration of scientific communities. The other factor is the migration policies implemented by developed countries in response to the growing demand for highly skilled personnel.[6] The policy inaction of developing countries in the face of this long-standing problem, which is perceived to be of growing importance, stands in striking contrast to these policies.

II. Stylized facts related to the region's recent development

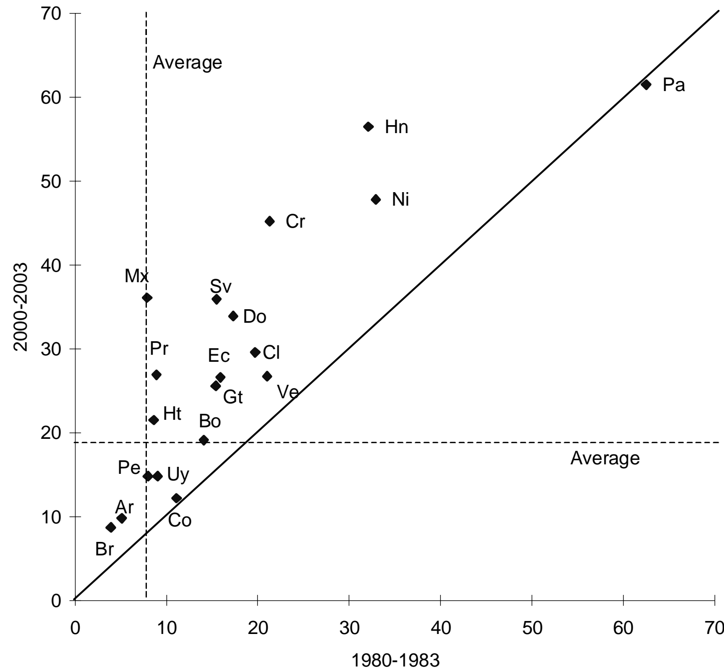
Although the reform effort is usually associated with the 1990s, experiments in economic liberalization began in the 1970s in the Southern Cone (Argentina, Chile and Uruguay) and, to a lesser extent, in other countries as well. Between 1982 and 1985, following the debt crisis, many of the reforms included in liberalization programmes were halted and, in some cases, were even reversed. From 1985 onward, a wave of economic reform began to sweep across virtually the entire region. The liberalization of trade and of national financial markets were the first reforms to become widespread in the region. Liberalization of international capital flows followed, beginning in 1991. Thus, a significant convergence was seen among these three areas of reform starting in the second half of the 1990s. In contrast, there has been less convergence in the areas of privatization and tax reform (Ocampo, Bajraj and Martin, 2001).

1. More open trade

One of the most salient events of the reform period was the dramatic and widespread liberalization of trade in the region's economies. Openness coefficients increased considerably between 1980-1983 and 2000-2003, as shown in figure 5. All of the region's economies are significantly more open today than they were at the beginning of the 1980s, with the regional average for this indicator more than doubling. The two economies that were least open in the 1980s (Argentina and Brazil) have not changed in that respect, however, while Colombia, Peru and Uruguay, which were above the regional average, are now below that average. The remaining countries –especially the smaller ones– were, and are, more open than the regional average. Mexico is particularly noteworthy for having quintupled its openness coefficient during the period in question.

6 The main pole of attraction is the United States, which in the 1990s received almost a million developing-country specialists in the area of information technology alone under the special H1-B visa programme. A number of other OECD countries (Australia, Germany, New Zealand and the United Kingdom) have also implemented selective programmes along the lines of Germany's "green card" scheme (Solimano, 2002).

Figure 5
latin america and the caribbean: changes in trade LIBERALIZATION, 1980-1983 and 2000-2003



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

Notes:
- The openness coefficients have been calculated as ½(X+M)/GDP, at constant 1995 prices.
- Ar: Argentina; Bo: Bolivia; Br: Brazil; Cl: Chile; Co: Colombia; Cr: Costa Rica; Ec: Ecuador; Sv: El Salvador; Gt: Guatemala; Ht: Haiti; Hn: Honduras; Mx: Mexico; Ni: Nicaragua; Pa: Panama; Py: Paraguay; Pe: Peru; Do: Dominican Republic; Uy: Uruguay; Ve: Venezuela.

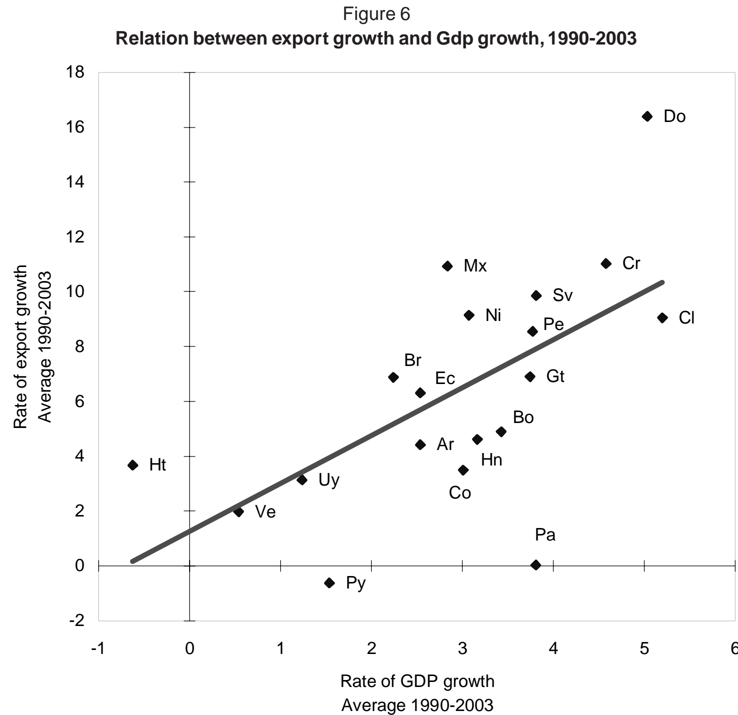
Both exports and imports showed robust growth. The physical volume of exports grew at an unprecedented rate between 1991 and 2000 (9.3% annually), which was above the world average and was exceeded only by the rates posted by China and India. The problems in the international economy in 2001-2002 interrupted this growth, which began to recover, however, in 2003. While Mexico's exports, which represented almost half the regional total, helped to boost the regional average, Brazil's modest export performance up to 2000 had the opposite effect. Most of the remaining countries experienced strong export growth, in the neighbourhood of 8% per year.

Meanwhile, imports increased even more than exports (ECLAC, 2004). The main reason for this was the swift, broad-based reduction of tariffs against a fairly generalized background of local currency appreciation, which made imports less expensive. In addition, there was a rising trend in the purchase of foreign inputs and services by export firms and service providers. This was especially notable among transnational firms that have international supplier networks. At the same time, the restructuring of businesses oriented to the domestic market, when successful, required growing imports of capital and intermediate goods, as well as technological services. Finally –since openness operates in both directions– a process occurred in which locally produced consumer goods were replaced by imported items.

Performance by country shows a strong relation between rates of increase in exports and GDP growth, in that the countries with the fastest growth are the ones that most increased their exports (see figure 6).[7] It should be emphasized that all the current patterns of export specialization in the region included both success stories and cases of more mediocre performance. This contradicts the "curse of natural resources" postulate and runs counter to the well-known secular trend towards the worsening of terms of trade for commodities. Chile is the most conspicuous example of such a case. Despite its specialization in natural-resource-based exports, it maintained high GDP and export growth. This contrasts with the poor performance of Ecuador and Venezuela, whose exports are also heavily dependent on natural resources. Mexico has benefited little, in terms of economic growth, from its notable success in expanding and diversifying its exports. Costa Rica, El Salvador and, especially, the Dominican Republic have achieved greater synchronicity between export performance and economic growth (Ocampo, 2004).

7 The exceptions are Panama and Paraguay, in which service exports predominate.

Figure 6
Relation between export growth and Gdp growth, 1990-2003

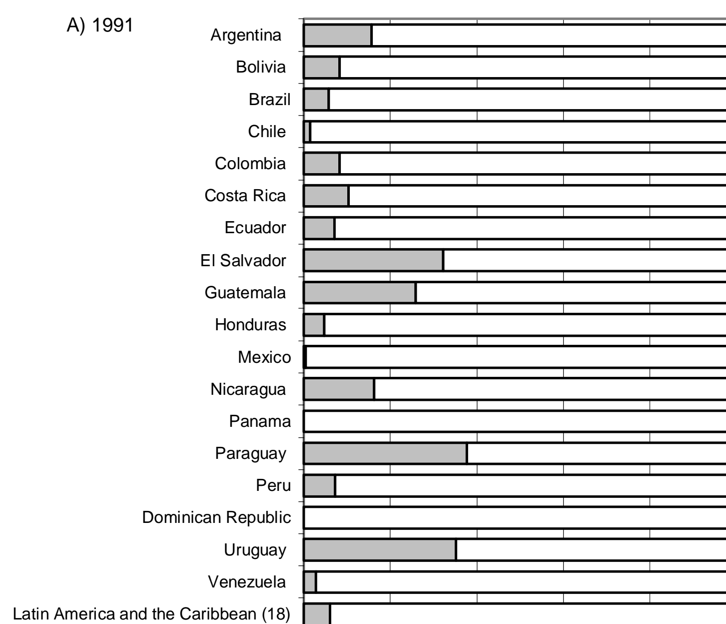


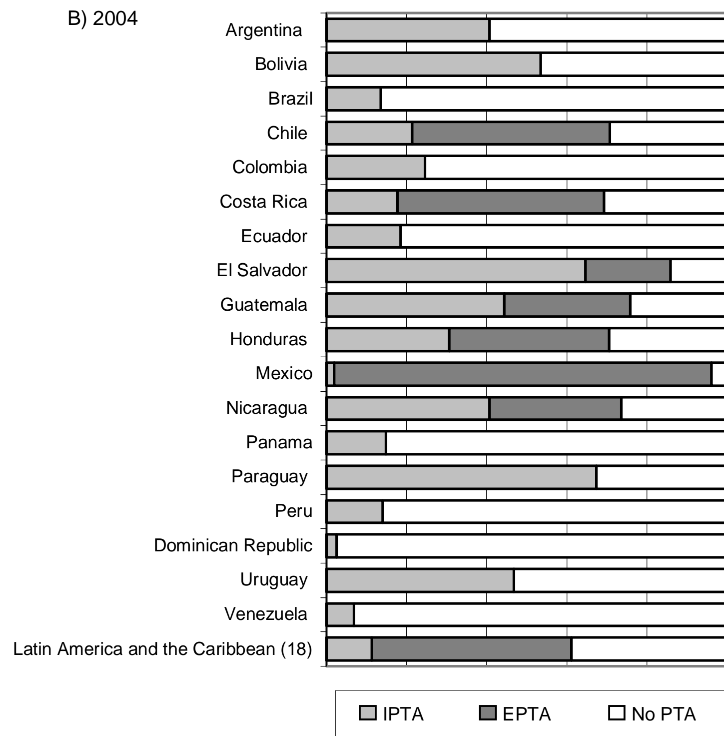
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures from the countries.
Note: Ar: Argentina; Bo: Bolivia; Br: Brazil; Cl: Chile; Co: Colombia; Cr: Costa Rica; Ec: Ecuador; Sv: El Salvador; Gt: Guatemala; Ht: Haiti; Hn: Honduras; Mx: Mexico; Ni: Nicaragua; Pa: Panama; Py: Paraguay; Pe: Peru; Do: Dominican Republic; Uy: Uruguay; Ve: Venezuela.

In macroeconomic terms, these changes, in the aggregate, led to a structural worsening of the relation between growth and the trade balance. Trade deficits in 1990-2000 rose to levels comparable to those of the 1970s, but with rates of GDP growth nearly three percentage points lower. Contributing to the structural deterioration was the weakness of the linkages between exports and the rest of the production system, as well as the short-term bias of macroeconomic policy, which tended to generate exchange-rate lags as a result of the abundance of foreign capital for much of the 1990s.

The export orientation of the region's countries and the protectionist practices of the developed countries have made the issue of market access more important. Hence, the Latin American and Caribbean governments have been particularly active in reaching bilateral and plurilateral preferential agreements that are both intraregional and extraregional in scope (see figure 7). The rationale for this strategy is that unilateral liberalization does not guarantee the openness of target markets. Thus, in an economy that is undergoing globalization and regionalization simultaneously, countries seek strategies for positioning themselves in import markets in ways that will give their products greater and more reliable access to those markets.

Figure 7
Exports in the framework of preferential agreements
(As percentages of exports)





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

Notes: - IPTA: Intraregional preferential trade agreements.
- EPTA: Extraregional preferential trade agreements.
- PTA: Preferential trade agreements.

In 1991 multilateral preferential agreements were practically the only ones in force. They were associated with the region's four imperfect customs unions, which represented roughly 6% of total exports. This situation changed dramatically in the 1990s. Considering export destinations in 2003 and current preferential agreements, 61.2% of the region's exports may be expected to occur within the framework of these agreements in 2004. The most notable cases are Mexico (95%), the Central American countries (75%) and Chile (70%).

2. Meagre and volatile economic growth

Another significant economic phenomenon of the period 1991-2003 was increased domestic and, particularly, external confidence in the authorities responsible for macroeconomic management, as a result of their success in reducing price instability and controlling fiscal imbalances, two of the region's endemic ills. Central government fiscal deficits have fallen significantly as a percentage of GDP since the late 1980s. Starting in 1999, however, significant differences could be observed from one country to another, with fiscal crises affecting a number of economies in the last few years and high debt-to-GDP ratios still prevailing in some countries (ILPES, 2004). The progress made in terms of price stability has been more uniform and has had more lasting effects. Average inflation in the region fell steadily, reaching single-digit levels in 2003 (ECLAC, 2003).

Expectations that controlling fiscal imbalances and inflation would lead to faster economic growth and a steady increase in investment did not materialize, however. In fact, the macroeconomic management model that produced such significant progress on these fronts has also been partially responsible for the increased sensitivity of economic growth to foreign capital flows and for some undesirable features of the productive restructuring process, as well as the propensity for national banking crises in a number of countries (Ocampo, 2001).

Although a few Latin American and Caribbean economies started growing again towards the end of the 1980s, the recovery did not spread to the region as a whole until the early 1990s, when capital inflows rebounded after a long period of negative external transfers. These flows facilitated structural reform, as well as price-stabilization programmes based on exchange-rate anchors. Meanwhile, the ability to attract foreign capital increased as a result of economic reforms, particularly the liberalization of capital-account regulations and privatizations, which spurred large-scale foreign direct investment.

GDP growth, however, was low in comparison to the rates posted in earlier decades, except in the lost decade of the 1980s. In the period 1991-2003, the annual average increase in GDP was only 2.5%, or less than half the 5.5% recorded between 1950 and 1980 (see table 6). Moreover, the region's performance in the 1990s was clearly poorer than that of other developing regions, especially South-East Asia, which expanded at an average rate of 6%.

Table 6
GDP GROWTH AND VOLATILITY IN SELECTED PERIODS
(Average annual rates)

	World		Latin America	
	Average rate	Standard deviation	Average rate	Standard deviation
1950-1980	4.6	1.49	5.5	1.70
1981-2003	2.8	1.05	2.1	2.17
1991-2003	2.5	0.87	2.5	1.93

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

The region's economic growth has been not only slow, but also highly volatile. While the standard deviation of annual growth rates in Latin America and the Caribbean with respect to the average rate (1.70) was very close to the corresponding value at the world level (1.49) between 1950 and 1980, it was more than double that value between 1981 and 2003 (2.17 and 1.05, respectively). Both in the region and worldwide, growth was less volatile between 1991 and 2003 than it had been in the previous decade. However, the relation between the two groups' standard deviations stayed the same (1.93 and 0.87, respectively). While a number of elements (trade factors and domestic policy) had an impact on the volatility of the region's growth, changes in the capital account are the single most important element in this respect.

One lesson that emerges clearly from the region's recent experience is that instability in real variables is also very costly. In recessionary phases of the business cycle, resources that may be unrecoverable are dissipated. This is the case when firms lose tangible and intangible capital and when the economy loses human capital as a result of unemployment and underemployment. Furthermore, the uncertainty associated with volatile growth rates can be very harmful for new investment, as it triggers defensive microeconomic strategies designed only to protect firms' assets in a hostile environment, as opposed to offensive strategies, which require high rates of investment and incorporation of technical advances.

Meanwhile, in expansionary phases, economic agents, both public and private, tend to underestimate the long-term effects of their spending and financing decisions. When a crisis breaks out, the resulting costs tend to be very high. In addition to the loss of assets laboriously accumulated over the years, pressure is generated to socialize these losses, as the only alternative to a systemic crisis. The magnitude of the consequences of this breaking of contracts depends on how widespread the phenomenon is. In any case, it compromises present and future levels of fiscal (or quasi-fiscal) expenditure and hurts the financial system's credibility. Restoring confidence

takes time, and the financial system becomes more risk-averse, to the detriment of its ability to fulfil its primary economic function.

The region's poor investment and productivity performance helps explain its disappointing economic growth. Gross investment as a percentage of GDP increased slightly until 1997, then fell to a level lower than the one posted at the beginning of the decade. Its counterpart, saving, was also disappointing in this period. Public saving fell and private saving failed to rise, essentially because domestic credit was channelled into consumption and external saving replaced domestic saving to a large extent, as more capital flowed into the region (Uthoff and Titelman, 1998).

In a sample consisting of 10 countries of the region, total factor productivity rose at an average annual rate of only 0.6% if measured in terms of the simple average for these countries, or 0.2% if measured in terms of the weighted average.[8] The difference between the two averages is explained by the poor performance of the two largest economies (Brazil and Mexico), which had negative rates. Moreover, 1997 marked a turning point in productivity trends. Between 1990 and 1997, the simple average of the annual rates of productivity growth (1.9%) was not far from the figure for the period 1950-1980. On the other hand, the trend was decidedly poor from 1997 to 2003, with annual rates of -1.1% owing to the backslide observed in all the countries, especially those whose productivity had increased the most in 1990-1997 (Argentina, Chile, Peru and Venezuela).

3. Increased structural disparity among the region's economies

The fact that export growth far outpaced economic growth in 1991-2003 is related to a stage of structural transition marked by abrupt and indiscriminate trade liberalization in a context of rather widespread exchange-rate lags. Productive enterprises consequently faced profound changes in the rules of the game. Although new activities emerged, the dominant phenomenon was not the creation of a new production structure, but rather the initial destruction of the most fragile segment of the existing production base.

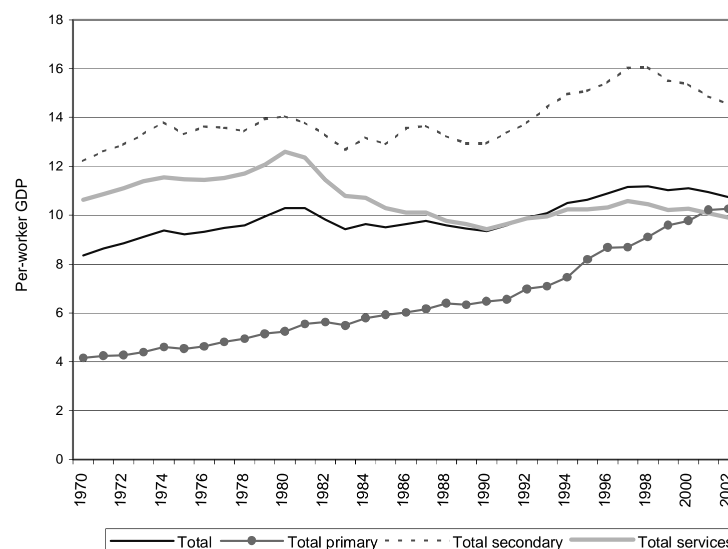
The keener competition that characterizes open economies has made the business environment more uncertain. This is because liberalization transmits to the domestic environment the factors that create insecurity in the international environment: the effects of technological change, variations in relative prices at the international level, and activity levels and

8 The countries considered are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, Peru and Venezuela.

exchange rates in export markets and in countries that produce competing goods. Local uncertainty about macroeconomic conditions, rules of the game and the learning process imposed by the presence of new domestic and foreign competitors is also a factor. This proliferation of uncertainty helps to explain the current concentration of new investment in just a few sectors and agents. Without question, the conditions in which these changes took place did not provide a level playing field for all the various agents of production in the region's economies. The process of adaptation has been marked by flaws in the market and, in particular, sharp information asymmetries between different producers. These phenomena have created significant differences in terms of principles and practices for connecting with foreign markets, access to financing (especially long-term) and the technological knowledge needed to compete in the new environment. This, in turn, gave rise to very different responses in the production system as a whole, which have accentuated the structural heterogeneity of the region's economies and, most importantly, have led to the exclusion of many economic agents from the transition to a more modern production sector.

Thus, beyond the poor performance of aggregate productivity, trends in each economic sector were different, as figure 8 indicates. Average labour productivity in the primary sector showed strong, sustained annual growth beginning in 1970, in both agriculture (4.1%) and mining (6.8%). Between 1991 and 1997 this increase in productivity accelerated moderately in agriculture (4.4%) and intensively in mining (12.6%). The increase in mining productivity is linked to the sector's notable expansion, and both phenomena are the direct result of economic reform. Indeed, mining potential in a number of countries was developed to an unusual extent in this period.

Figure 8
latin america (10 countries): change in labour productivity, by sector
(Simple average for the countries)



Source: André Hofman, *Crecimiento y productividad en América Latina: una visión a largo plazo* (LC/R.1947), Santiago, Chile, Economic Commission for Latin America and the Caribbean (ECLAC), 1999.

For the agricultural sector, economic liberalization and market deregulation changed the output and export baskets and affected the adoption and the repercussions of new technology, including increased yield, greater activity in livestock and forestry and a general decline in employment. In several cases, these factors accelerated changes in agriculture that had begun one or more decades earlier. Increased agricultural productivity reduced the disparity between sectors, since average labour productivity is lower in agriculture than in other sectors. On the other hand, opportunities for raising agricultural productivity varied enormously within each country, depending on the size of farms and producers' access to inputs and resources.

Labour productivity in the secondary sector (manufacturing and construction), after a long period of stagnation with minor fluctuations, increased between 1990 and 1997 (by an average annual rate of 2.6% in manufacturing and 4.4% in construction) and then fell between 1998 and 2002 (-1.9% and -2.8% per year, respectively). Thus, increases and decreases have been more marked in construction than in manufacturing. The performance of the manufacturing sector varies from one subsector to

another and, above all, between production units of different sizes. There are major differences in productivity between large firms, on the one hand, and small and medium-sized enterprises (SMEs), on the other (as the latter firms, on average, have less than half the productivity levels of large firms), and also between SMEs and informal-sector microenterprises (whose productivity is not even a third of the levels seen in large firms, and went down in the course of the 1990s).

Lastly, labour productivity in the tertiary sector fell steadily in the 1980s (-2.6% annually), then recovered between 1990 and 2002 (2.7% annually). This is the result of two contradictory trends. On the one hand, there was a great deal of restructuring, both in public services and in the financial sector, as privatization and foreign investment boomed. This restructuring was associated with processes of expansion and personnel cuts in privatized firms. On the other hand, business services expanded considerably as a consequence of outsourcing (ECLAC, 2004). The increase in labour productivity after 1990 is largely attributable to these factors. Meanwhile, the productivity of other services continued to follow the downward trend that had begun in 1980. Seven out of every ten jobs created in the 1990s were in the urban informal sector (ILO, 2000).

Trends in small businesses, both urban and rural, vary widely. In a number of countries and sectors, many such firms have disappeared or moved into the informal sector. While many of these changes occurred in the 1980s as a result of a pronounced slump in per capita income, the process was not reversed in the 1990s. On the contrary, renewed growth was insufficient to prevent an increase in informal employment, which grew from somewhat over 30% of total employment in 1980 to 43% in 1990 and 48.4% by the end of the 1990s. Perhaps one of the most distinctive features of recent years has been the increase in informal employment in urban areas, where its share of total employment rose by five percentage points, representing 20 million individuals (ECLAC, 2001).

III. Productive development in open economies

Economic development follows a general logic that consists of accumulating resources, mobilizing them productively and using them ever more effectively. The ways in which this can be done, however, vary widely. Both old and new studies on growth theory have put forward a range of possible analytical approaches that is far from being exhausted by existing models. Concrete analysis, however, is not concerned with multiplying the number of possible approaches, but with identifying one or more that are demonstrably plausible and relevant. Proposals based on arguments that are presumed to be universally valid are thus of little use. Almost by

definition, economic development is a non-repeating process that occurs at a specific time and place and creates irreversible changes in the configuration of activities and the behaviour of agents (Furtado, 1956). The raw material of development analysis consists of episodes that are in some sense unique; that is, episodes that share elements of the general logic cited above, but cannot be used as a basis for mechanical extrapolations.

One long-standing and useful distinction is the one between an economy's development and the mere expansion of its scale. The hallmark of economic development is structural change –i.e., a change in the sectoral composition of production– that results in greater diversification of economic activities (with more division of labour), of the economy itself and, probably, of its relations with the rest of the world. Accordingly, it is to be expected that the production apparatus and individual skills will become more complex as behaviour, institutions and modes of social interaction change. Although development entails changes in the configuration of the economy, the ability to continually generate new activities that are dynamic and innovative, in a broad sense, is an essential determinant of rapid economic growth (Ocampo, 2002).[9]

These changes can hardly be expected to conform strictly to a pre-set course. The success of an economy is more likely to depend on how agents identify and take advantage of opportunities and deal with the constraints imposed by the immediate and global economic environments. Opportunity is a dynamic phenomenon, and the economic system must adapt to changing circumstances. While it is important for countries to have a development strategy so that economic agents can take it into account when allocating resources and taking other decisions, productive development is most probably the outcome of a series of responses to problems that emerge over time.

In any case, it is essential to have a common vision that is based on collective thinking about specific issues and therefore transcends mere doctrinaire definitions and the disagreements that customarily accompany them. For the vision to have political legitimacy, the different social groups must recognize that the chosen course can benefit their interests and must trust that the issue of distributive balance will be addressed. As Prebisch (1963) stated, the proof of a development process's dynamic validity is its

9 Schumpeter's (1961) definition of types of innovation, or "new combinations", as he called them, includes the introduction of new goods and services or major changes in quality; the development of new production or marketing processes; the opening of new markets; the discovery of new sources of natural resources or new ways of exploiting known resources; and the establishment of new structures in production sectors.

ability to speed up growth and to progressively improve income distribution. From this point of view, it is clear that economic development goes far beyond purely economic or narrowly technical issues (Sen, 1999).

Since development is generated through the introduction of new activities and forms of production, it is unlikely to progress continuously, with the different strata of the economy advancing in parallel. Alternation between upswings and downswings, as well as tension and ruptures in the system, are unavoidable features of the process. The outcome depends on how these vicissitudes are dealt with, and, ultimately, on the solidity of the coalition for development.

It is useful to regard innovation as a process that generates productivity gains through localized learning and that has knock-on effects that operate through complementarities and linkages (Bardhan, 1998). The existence of these effects, which has been reasonably well documented in a number of cases, shows that growth generates externalities, whose intensity depends on the economy's configuration. Growth has a systemic component that arises from the interaction between the expansion of the activity in question and productivity gains in other activities, and also from the provision of more and better collective services, such as traditional public goods, infrastructure and social services (health, education, etc.).

Sustained growth is hard to achieve without the use of localized stimuli, which entail, at least initially, more uneven economic growth. At the same time, development requires that increased productivity and income spread to the rest of the economy in one way or another. This means that, beyond the lags and delays that are to be expected, the stimuli must be spread and propagated. The need to facilitate progress in those segments of the economy that have growth potential, while ensuring a certain homogeneity so that progress in these segments can spread and produce systemic effects, may give rise to dilemmas that are difficult to solve in the abstract, without examining specific problems and conditions in the economy (ECLAC, 1990).[10] Thus, a structural perspective that is concrete and non-dogmatic seems to be the best approach.

10 A dilemma arises, for instance, when it is advantageous for a given activity with growth potential to have access to high-quality, low-cost inputs that could be imported, and yet, at the same time, it is felt that the activity's backward linkages could be an important means of transmitting growth to the rest of the economy.

2. Principal components of productive development

Development is associated with changes in the social system as a whole, as indicated by the simple observation of economies that have made the transition. Although phenomena must be somehow isolated before they can be studied with any degree of precision, it is a mistake to assume that certain elements of the system, such as institutions, for example, remain constant. All this suggests that the analysis of development is necessarily an intricate conceptual construct.

As a general analytical approach, the potential growth curve of an economy's output can be represented by an expanded production function whose arguments include the accumulation of physical capital (natural and constructed), human capital, the knowledge capital embedded in technology and business practices, and institutional capital. Trends in these growth factors, in turn, will be influenced by current and expected future resource levels. This perspective is useful because it focuses on the interaction between these factors, their complementarities and their substitution possibilities as general determinants of growth. The marginal effect of each factor, and hence the forms of resource accumulation that seem most urgent or promising, vary according to the state of the economy, the actual availability of resources and conditions beyond the country's borders. It is not enough to say that development requires increases in all the factors of production. At any given time, dilemmas will arise as a result of budgetary constraints, which affect public policy.

Furthermore, these factors, like the very indicator used to measure development levels quantitatively, such as GDP, are not simple variables. On the contrary, they reflect aggregates of very diverse components. When these black boxes are opened up –to echo Fajnzylber's (1990) manner of referring to technology– the analysis becomes more complex, but only then does it begin to deal with concrete things; i.e., with matters on which specific decisions are taken. Hence, it is unlikely that investment in technology or education will have the same meaning in a large, diversified economy as it does in a small, low-income economy concentrated in the primary sector.

The frame of reference for this analysis consists of the lessons incorporated into economic theory and good practices. These, as heuristic indications, have been inferred from previous cases, while respecting the principle of the "originality of the copy" (Cardoso, 1977). In looking at the specific problems encountered in a given economy's development, it is necessary to make a considerable analytical effort to consider the idiosyncratic features of the case. At the same time, it is possible to impart a certain perspective to issues that have been the subject of intense debate.

(a) *The macroeconomy, investment and sustainable development*

At the outset, it should be stressed that no clear distinction can be made between long-term growth trends and short-term fluctuations (Heymann, 2000). On the one hand, the evidence suggests that macroeconomic volatility affects growth. The willingness to invest certainly depends on the maintenance of predictable macroeconomic conditions and on a level of activity that makes ample use of the available factors of production. Thus, decisions regarding the expansion of supply capacity are influenced by the level and variability of demand (Kaldor, 1978; Barro, 1991). On the other hand, changes in public and private agents' perceptions of growth trends may have macroeconomic consequences of the first order. Budget constraints mean that agents' spending capacity depends on the generation of present and future income. Accordingly, economic growth and productivity gains are essential elements of macroeconomic sustainability.

Considering that the region's recent history was characterized by low growth combined with high volatility, it is essential to implement macroeconomic policies that not only control inflation but also help to smooth out business cycles. These policies should be based on a broader definition of macroeconomic stability that also includes real targets for variables such as the pace and stability of economic growth (Ffrench-Davis, 2004). During the growth phase of the business cycle, macroeconomic policies should be geared towards preventing excessive increases in borrowing by public and private stakeholders, significant imbalances in key relative prices and price bubbles in domestic assets that will require overadjustments when the cycle enters a downswing. Fiscal policy should include fiscal deficit and public spending criteria based on structural variables such as potential GDP, and should provide for the creation of public revenue stabilization funds pertaining to income from taxes, raw materials exports and windfall profits from the sale of public assets. Monetary policies should be aimed at preventing cyclical upturns in external financing from triggering excessively rapid increases in external and domestic credit to the private sector and at keeping interest rates compatible with internal and external balances. Exchange-rate policy is now subject to demands that are contradictory and hard to reconcile, since the exchange rate reflects the logic of both trade and finance. Accordingly, managed floats, which fall between the exchange-rate regimes at either end of the spectrum, are the most attractive policy alternative for preventing the real exchange rate from straying too far from long-term equilibrium and for combining flexibility with stability. Thus, the difficulties inherent in monetary management are heightened in open economies, although it is possible to

enhance the effectiveness of such management and the degree of freedom to manage the interest rate by incorporating certain elements into monetary policy. These include controls on capital inflows, increased liquidity requirements during upswings in the business cycle, an active approach to the prudential regulation and supervision of financial systems (incorporating countercyclical considerations into the determination of provisioning requirements for loan portfolios) and an explicit "liability policy" aimed at improving the maturity profile of public and private debt, both domestic and external (ECLAC, 2002).

In the region, the financial system has tended to amplify the macroeconomic effects of economic shocks and, accordingly, to increase the frequency and sharpness of the business cycle. As mentioned above, mitigating these effects through appropriate policies, proper countercyclical regulation and financial deepening is essential for the developing economies. It is also necessary to develop a local-currency financial market to avoid the instability associated with the dollarization of financial assets and liabilities. Dollarization is related to the level and volatility of inflation and to economic stakeholders' expectations as to future inflation trends. Considering the region's history, the consolidation of a local-currency financial market will require a long period of stability. During the transition, countries should seek to develop mechanisms for medium- and long-term saving in local currency. A key instrument for achieving this is an inflation-indexed unit of account. In view of the risks entailed by the use of foreign currency in financial transactions, it is important to impose higher reserve requirements for foreign-exchange deposits and higher provisioning requirements for foreign-exchange loans to the non-tradables sector. Moreover, international institutions could accelerate the creation of local-currency financial markets by providing guarantees to support the issuance of debt in those currencies (Eichengreen, Hausmann and Panizza, 2003).

Since the financial sector plays a key role in enabling agents of production to reconcile their intertemporal income and expenditure needs, it is essential to reduce intermediation costs by developing financial instruments for hedging risk. This will make it possible to meet the needs of a diverse production system and to finance long-term investment projects. Such initiatives are particularly important for small and medium-sized enterprises (SMEs), which have always had trouble obtaining financing at rates compatible with the profitability of their investments. Because the banking sector plays such an important role in the region's financial systems, any strategy for channelling more resources to the production sector must include measures to strengthen private and public banks' financial intermediation capacity, while not neglecting the development of capital

markets. Guarantee funds, credit scoring systems, factoring, leasing and leaseback arrangements are some of the instruments that have been developed in countries of the region and that should be promoted. In addition, public development banks, with new operating and corporate governance modalities that correct the mistakes of the past, should contribute to the development of production either by providing financing to stakeholders that have heretofore been excluded or by acting as a catalyst and developer of new forms of financial intermediation.

The correlation between macroeconomic stability and growth hinges on the dynamics of saving and investment. In cases of successful development there have been significant increases in the physical capital stock and in productivity, made possible by a rise in the investment ratio. The physical capital stock is also a complex variable, however. In recent debates on this subject, it has been suggested that there is a profound complementarity, in terms of the real economy, between productive investment by private enterprise and a country's infrastructure stock. Owing to the strong influence of infrastructure on business productivity and on the economy's systemic competitiveness, and ultimately on growth, governments have sought to ensure that adequate infrastructure is available. In order to grow at a rate of 3% annually between 2000 and 2010, Latin America will have to invest about 3% of GDP in infrastructure each year, or US$ 70 billion. This figure reflects new investment of US$ 57 billion (about 2.2% of GDP) and investment in replacement and maintenance of US$ 13 billion. New investment needs are not the same in all sectors. As table 7 shows, for the period 2000-2010, the estimates of investment needs are highest for the electric power and roads sectors (Fay, 2001; Fay and Yepes, 2003).

Table 7
ESTIMATES OF NEW INFRASTRUCTURE INVESTMENT REQUIREMENTS IN LATIN AMERICA, 1995-2010
(Percentages of GDP)

	1995-2000	2000-2010
Fixed telecommunications	0.22	0.27
Electricity	0.76	0.99
Paved roads	0.15	0.48
Railways	0.60	0.23
Water	0.12	0.10
Sanitation	0.38	0.18
Total	**2.23**	**2.25**

Source: Marianne Fay, *Financing the Future: Infrastructure Needs in Latin America, 2000-2005*, Washington, D.C., World Bank, 2001; Marianne Fay and Tito Yepes, "Investing in infrastructure: what is needed from 2000 to 2010", *World Bank Policy Research Paper*, No. 3102, 2003.

In the current circumstances, this level of investment can only be reached through combined public and private efforts. However, the future of private investment in infrastructure in the region is uncertain at best. In addition to the risks perceived by private firms and the difficulties stemming from frequent processes of contract renegotiation, there is growing dissatisfaction among users with the quality and cost of public services that have been privatized or franchised to the private sector. According to recent surveys, in Argentina the percentage of satisfied users of privatized and franchised services fell from 50% in 1998 to slightly over 10% in 2002. In Mexico, the percentage decreased from 60% to 25% and in Brazil, from 55% to 35%. In Chile and Bolivia, user satisfaction dropped by almost 20 points, from 60% in 1998 to 40% in 2000 (Foster, 2004).

The foregoing underscores the need to improve and strengthen the regulatory mechanisms of the public sector in relation to the various modalities of public-private partnership. The need for active government regulation depends on the degree of competition in the infrastructure sectors in which the private sector becomes involved. Where opportunities and incentives for competition are absent, greater regulation is required (Cavalcanti and Santos de Franca, 2003). There is thus a need to improve regulation so that private investment in infrastructure will transmit productivity gains to families and production sectors. Only then will it become a significant engine of productive development.

In several countries of the region there has been an obvious dearth of public investment in infrastructure over the past decade. Such investment is essential for improving the economy's competitiveness and, in particular, for incorporating certain sectors and geographical areas into the productive development process. Increasing the infrastructure stock involves not only improving its quality, but also increasing the availability of adequate resources. Accordingly, in a context of fiscal discipline, the applicable regulations should provide that certain infrastructure outlays should not be treated as deficits in the programmes agreed upon with international lending institutions. These programmes serve as an essential source of financing, either directly or by affording access to private credit markets. A proposal in this regard was presented by Mexico, on behalf of a group of countries of the region, at the Evian Summit held in 2003, and by the Presidents of Brazil and Argentina to the International Monetary Fund. These initiatives seek to bring about greater flexibility in the management of fiscal accounts by refining fiscal and budgetary control instruments so that capital expenditures are treated differently from current expenditures and investments are thus accounted for in a way that does not inhibit rational economic decision-making. This same line of thought is evident in the

Carta de Lima, a joint declaration signed by the representatives of the governments of the South American countries at the most recent annual meeting of the Inter-American Development Bank.

One way of introducing greater flexibility and promoting a growth-oriented fiscal policy is to recognize that investment and current expenditure are different economic phenomena and that, as such, they should be treated differently, in particular by avoiding the imposition of limits or cutbacks on public investment in the case of projects whose rates of return will exceed the investment costs.[11] The conventional rule of fiscal control, which imposes deficit goals in relation to total spending, does not take account of the assets generated by public investment, but only of the cost of acquiring them, thus creating an anti-investment bias. Fiscal control should revolve around the concept of intertemporal solvency rather than deficit, as the former concept is more important for fiscal sustainability. It incorporates the notion that public investment generates financial returns that will enable governments to fulfil their obligations in the medium and long terms.

A second means of introducing greater fiscal flexibility is by strengthening mechanisms that will stimulate various forms of public-private partnership, which, among the possible forms of collaboration, have become an important alternative. These partnerships enable governments to create new infrastructure without immediately adding capital outlays to the budget, since the investments are financed by the private sector, which is remunerated by the government through charges, fees, rents or another form of current expenditure once service delivery is operational. This mechanism not only makes it possible to utilize private capital and administration, but also helps to spread investment costs over time, as the investment is amortized with the outlays that the government pays periodically to the operators of the service.[12]

11 Similar arguments have been put forward by various countries of the European Union. Faced with the need to increase investment in infrastructure, those countries have suggested that some flexibility should be allowed in the rules of the Union's Stability and Growth Pact so that infrastructure investments are exempted from the targets and ceilings imposed by those rules (International Monetary Fund, 2004).

12 Public-private partnerships enable the private sector to supply infrastructure and services in areas traditionally deemed to be the province of government, such as hospitals, schools, jails, roads, water and sanitation. Under this arrangement, the government establishes what service is to be provided by the private sector, which then designs, builds, finances and operates the service.

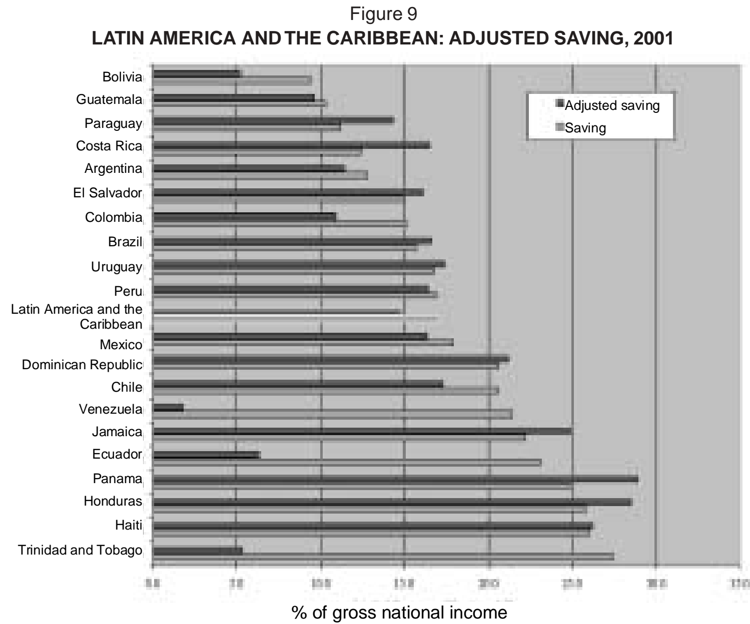
At present, numerous countries of the Organisation for Economic Co-operation and Development (OECD) have adopted arrangements of this type. Possibly the best public-private partnership programme developed to date is the Private Finance Initiative, created by the United Kingdom in 1992, which accounts for 14% of public investment in the country and is applied in key areas of infrastructure services. Other countries where public-private partnerships contribute significantly to investment are Australia and Ireland.

A third way of increasing fiscal flexibility in the management of public investments has to do with the role played by multilateral development banks. Today, the capacity of these institutions to disburse approved loans is being diminished by the budgetary practices of the public sector. This type of financing is recorded as an expenditure, and is therefore subject to the quotas and ceilings imposed by public expenditure containment policies, which delay the execution of loans and thus hinder the progress of works. For this reason, IDB, for example, disbursed only 60% of its approved budget for investment projects in 2000; in 2003 the percentage fell to 30%. The projects financed by multilateral development banks are generally high-quality projects that ensure the microeconomic consistency and transparency of the investments. It is therefore reasonable to expect that they will yield positive social returns. Accordingly, as with public-private partnerships, the expenditure that these projects generate should be accounted for in national budgets at the time when governments make payments on the loans, not when they receive the loans. This would make it possible to spread the financial burden over time, thereby exerting less pressure on fiscal goals and opening up greater fiscal leeway for obtaining financing from multilateral development banks.

In short, it is necessary to use a variety of mechanisms to give the region's governments more flexibility to invest in infrastructure, without, of course, neglecting the need to keep the public debt at levels compatible with the country's medium-term fiscal capacity.

Lastly, the expansion and sustainability of the economy's production capacity requires not only the conservation and expansion of the capital stock, but also the exploitation, valuation and conservation of natural resources. Indeed, the poor saving performance of the region's countries looks even worse when losses in terms of natural capital are taken into account.

Figure 9
LATIN AMERICA AND THE CARIBBEAN: ADJUSTED SAVING, 2001



Source:Based on World Bank, *World Development Indicators, 2003*, Washington, D.C.

Thus, sustained growth requires a framework of policies and institutions to protect the production base that relies on natural resources. The complementarity between economic growth, increased productivity and preservation of the integrity and environmental sustainability of natural capital is linked to the capacity of public policy to correct market flaws caused by the absence of effective pricing and ownership regimes, coupled with the existence of incomplete markets for numerous natural resources and environmental services.

Based on the evidence accumulated in recent years, the environmental agenda should focus on three lines of action that will allow better linkage between productive development policies and the sustainable management of natural resources and the environment. The first consists of strengthening the capacity of the Latin American and Caribbean countries to play an active role in various international negotiations. At present there are two issues of vital importance on the agenda of international agreements. One is the debate on intellectual property rights, which tends to generate conflicts, given that the countries of the region are the owners

of a significant proportion of biodiversity, while the developed countries have a high level of technological development and in many cases hold industrial patents. The World Trade Organization (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) implies a "privatization" of the rights to these resources, a matter which the countries of the region need to examine carefully in order to identify strategies for negotiation. The other major issue concerns the proposal of the developing world to work towards the elimination (or reduction) of tariffs and non-tariff barriers to environmental goods and services. This is also a source of controversy, although the WTO member countries have agreed to carry it out, in accordance with the Doha Ministerial Declaration.

The second line of action consists of developing an institutional platform for explicitly integrating the objectives and instruments of environmental policy into economic and sectoral policies. This is particularly important in relation to technological innovations designed to improve the sustainable management of forest, energy, mining, fishing and agricultural resources.

The use of renewable energies is another element that should figure prominently on the public agenda. The development of these types of energy could benefit from the gradual emergence of an international market for projects to reduce greenhouse gas emissions. The region has the opportunity to participate in this market by opting for more efficient and, preferably, alternative sources of energy (wind, solar or hydraulic energy) and by maintaining and strengthening ecosystems with high carbon absorption capacity.

The third line of action consists of recouping the cost of negative environmental externalities arising from the activities of various production sectors. Tax rebates, subsidies and tax exemptions aimed at attracting investments and projects in natural resource sectors and activities with known environmental impact have had a negative effect on the environment and run counter to efforts to develop instruments for quantifying and internalizing the social costs of environmental degradation. Fiscal instruments for dealing with the environmental externalities of production processes may be guided by one of two basic premises: the polluter pays principle or the consumer pays principle, meaning that the cost is assumed by either investors or consumers.

(b) Structure and productive development

The idea that development is associated with an ongoing process of increasing productivity says nothing, in principle, about an economy's international linkages. However, the most productive economies show an ability to increase exports and, in particular, exports entailing a higher degree of processing and technological content. Though international economic relations are asymmetrical, it is difficult for economies such as those of Latin America and the Caribbean to aspire to development without close and growing interaction with the world economy. Economic growth involves a deepening of the division of labour and ongoing improvements in production techniques and processes. This requires a diversified set of inputs, many of which are complex. Some are physical, but others include knowledge and abilities that are not incorporated into objects and that may even be tacit.[13] Obtaining them requires broad and fluid access to the rest of the world's production.

The diversification of demand may be expected to be accompanied by an increase in import coefficients in relation to GDP. Hence, exports may be expected to increase more rapidly than GDP. An expansion of exports involves various elements. Quantitatively, it involves generating resources to maintain the demand for imports relative to a given level of aggregate spending. This requirement is linked with the need to work within the bounds of intertemporal budgetary constraints, that is, being able to finance accumulation without excessive borrowing, which can lead to the need for recessionary adjustments. Thus, it is not the composition of exports, but rather their total value that is important in this respect.

However, exports also have a qualitative dimension, insofar as the quality of exports contributes to an improvement in production capacity. Thus, the economy's participation in international markets for relatively complex goods, along with the consequent need to meet quality standards and requirements in terms of the stability of supply, can translate into a learning process.

Taking advantage of the opportunities that –despite the presence of asymmetries– exist in international trade, without creating types of segmentation in the economic system that would be difficult to reverse later on, poses significant problems. These problems cannot be tackled, however, by rejecting integration with the larger world or by opening up

13 That is, the combination between Romer's "idea gap" and "object gap" (Romer, 1994), which distinguishes between the externalities inherent in physical investment and the accumulation of material inputs.

the economy indiscriminately. The basic objective must be to improve the quality of the country's international position by diversifying its exports in terms of destination markets and products and by incorporating greater value added and knowledge. The following measures may be useful in this regard:

(i) Eliminating the anti-export bias in the prices of inputs and services, either through drawbacks of indirect taxes or through temporary clearance regimes;
(ii) Supporting pioneering export firms by providing incentives for exports of new products or for penetrating new markets that help defray the high initial costs of these activities and that compensate firms for the positive externalities they generate for other firms that imitate them.;[14]
(iii) Establishing an active form of commercial diplomacy aimed at lifting existing barriers to the region's products, particularly in developed countries. This strategy must take into account the negative impact that tariff escalation in the developed world has in terms of the need for greater value added;
(iv) Providing institutional support for export activity in such areas as information, export financing and insurance, management training and the promotion of exportable supply abroad;
(v) Disseminating information on the requirements of export markets in terms of quality, environmental regulations, standardization, time frames and volumes;
(vi) Providing access to export financing and insurance, particularly for SMEs;
(vii) Vesting responsibility for export promotion policy in a single institution with stable financing and qualified professional staff, or coordinating initiatives in the different areas involved.

In general, the design of incentives should take into account the fact that their primary aim is to promote new export products or new export markets; that the support they provide must be moderate so that it will attract firms that are really willing to share the cost of the programme; that the assistance must be temporary so as to avoid the use of permanent subsidies; that the programme's results should be subject to periodic external

14 The simplified drawback applied in Chile could be an appropriate instrument, although its implementation is now subject to the restrictions imposed by the World Trade Organization since the Uruguay Round. Another instrument for supporting these activities could be the facilitation of access to credit at international rates, which is not considered a subsidy under the WTO rules, but is a valuable incentive for the firms in the region, bearing in mind the difficulties faced by their capital markets.

evaluations so that it can be modified or suspended if it does not help to increase and diversify exports; and that the programme must be designed and administered jointly by public and private agencies. Lastly, it is essential that export promotion policies be approached as medium- and long-term strategies so that their continuity will be assured, regardless of changes in the government teams that implement them.

The countries of the region recognize that local incentives are not sufficient unless access to larger international markets is achieved. In view of the lacklustre results attained at the multilateral level, regional and bilateral agreements are seen as an alternative means of obtaining market access, since they tend to reduce discriminatory practices on the part of developed countries. As a matter of fact, the number of agreements registered with WTO has more than doubled in recent years In addition to North-South agreements, developing countries have undertaken negotiations designed to step up South-South trade. While these agreements may be advantageous in the short run, their rules of origin are beginning to generate high administrative costs. The region will undoubtedly benefit from advances in multilateral negotiations on agricultural products and from increased access to developed-country markets. It should be stressed that it is not the exports' degree of processing that determines their impact on growth, but rather their effect on the accumulation of resources and capacities within the economic system. Thus, expansion depends on the existence of productive and technological linkages, as well as on the development of entrepreneurial capacity and ties among firms (partnerships, public-private synergies at the local level, production clusters and value chains).

In a developing economy, the export mix will probably shift towards more complex and processed products. This shift is usually gradual and is essentially a sign of development rather than a force driving development. Thus, part of the learning process that is an inherent component of development encompasses the ability to produce goods on a competitive basis that were previously purchased abroad. Since this can take the form of a learning-by-doing process based on practical experience, public policy mechanisms for fostering infant industries and for encouraging the prospective identification, transfer, adaptation, and creation and diffusion of technology are relevant in specific situations, provided that problems arising with regard to such incentives are handled properly.[15]

15 As pointed out by Acemoglu, Aghion and Zilibotti (2002), there are two types of learning that are relevant to economic growth, namely the adaptation of existing technologies and innovation in creating new ones. Ramos (2000) analyses the importance of this distinction for the countries in the region.

This form of import substitution seems to be an inherent part of the growth process and requires sustained saving and investment. Opportunities in this connection may be generated by domestic demand, supported by public policies that bolster private accumulation by promoting the development of national innovation systems.

To improve the Latin American and Caribbean economies' linkages with the global economy in both quantitative and qualitative terms, simultaneous and coordinated efforts in a number of policy areas, above and beyond trade policy per se, are therefore needed within the framework of a systemic approach. If countries rely exclusively on trade policies and neglect both their productive development and macroeconomic environment, they may, at best, boost their exports, but without invigorating the rest of the economy. On the other hand, limiting export promotion to trade reforms and the preservation of macroeconomic equilibrium may lead to stability but not growth, and still less to the generation of endogenous processes of increasing productivity and competitiveness.

In other words, the sectoral composition of a country's exports reflects its resource endowment, average productivity and stage of technological development. The structure of comparative advantages and the removal of imperfections and distortions in the domestic market define what products a country can export in the immediate future, while its policies on technology, investment and education determine what it will be able to export in the medium and long terms.

Moreover, when countries fail to invest in technology training, human resources development and infrastructure, their policies for the promotion and development of exports will probably not be viable, since the high systemic costs of producing each unit of the good or service to be exported will have to be defrayed. In the long run, there is a real risk that these exports will not be sustainable once subsidies are reduced or eliminated.

Although there is no universally valid paradigm that indicates what paths lead to improved international competitiveness and increased presence in foreign markets, general guidelines can be set out with respect to the elements that may contribute to the design of an effective strategy for enhancing the region's integration with the international economy.

National strategies for technological development should take into account each country's existing technological capacities, its national innovation system and its available resources, since these factors limit the complexity and scope of the science and technology programmes that may be undertaken. Thus, no single technological development strategy can be designed to suit the need for innovation of all the countries in the region.

In any event, the countries of the region are faced with the challenge of moving towards a conception of technology policy which is more pragmatic than those applied in the past, which incorporates the interaction between supply and demand in the innovation process and makes use, in support of these objectives, of more effective instruments for each case and the coordination of different instruments according to the level of development of technological capacity.

In general terms, what is envisaged is an array of horizontal policies –to which in principle any firm can have access– which are designed to spread public goods and remedy static market failures, such as those affecting training, R&D incentives, and technological services for enterprises.

As far as possible, the new horizontal policies should be proactive and should be designed to attain a critical mass of resources for their beneficiaries, in order not to scatter the scarce available resources over a large number of small projects, with the aim of achieving effective results more quickly. The combination of these two conditions calls for some degree of targeting, which should be in keeping with the national technological development strategy.

Nevertheless, it may be necessary to include some selective policies in keeping with the conception of technology policy or the projection of existing technological capabilities. This would be so, for example, in the case of the need to enhance the international standing of some enterprises in the network by improving supplier-client relations or, more generally, to turn the generation and circulation of knowledge into dynamic competitive advantages within the network.

Likewise, in some sectors where there are already specific regulations or instruments and in some knowledge-intensive activities, horizontal policies should be supplemented with selective or targeted sectoral innovation policies. Similarly, in some regions where there is potential for innovation or the development of clusters, regional innovation policies need to be formulated which combine horizontal (and possible sectoral) policies within a particular territorial area.

The combination and coordination of horizontal, vertical and selective policies and measures to improve their position in global production networks is a typical practice of the most successful economies (European Commission, 2002 and 2003).

Policy execution requires a model adapted to the institutional capacity and level of production complexity of each country. As countries improve their institutional capacity and develop more complex structures of production they can extend the scope of their policies and develop vertical and selective policies in conjunction with horizontal ones.

The deployment of an innovation promotion strategy in the various dimensions in question calls for considerable coordination both in the design of the strategy and in policy formulation and execution. Strengthening the national innovation system demands careful coordination of actions and interventions as diverse as those aimed at promoting interactions between enterprises, their suppliers and clients, universities, public and private scientific and technological institutes and financial institutions.

These interactions must be promoted at all levels, but it is at the local level and in the development of clusters that they have the greatest possibilities of generating positive synergies through these coordinated actions.

On the other hand, not all the components of the national innovation system respond favourably to direct intervention. It is therefore crucial for the State and the public sector to show their leadership qualities in carrying through the innovation strategy. Furthermore, the State can produce a public good with considerable impact in terms of the directions and magnitude of innovations and the creation of technological capabilities: productive and technological scenarios which serve as a means to coordinate the innovation processes of enterprises and whose interactive discussion leads to the identification of attainable complementarities, as well as serving as a frame of reference for the design of public policies to promote innovation.

In defining the areas to be promoted and in designing instruments, it should be borne in mind that economic liberalization and increasing competition for scarce fiscal funding, aggravated by the need to address urgent social issues, have reduced the potential for implementing sectoral policies of the type that were characteristic of ISI, not only because they involved intensive use of public funds, but especially because it became increasingly difficult to use import tariffs on a widespread basis.

In view of this situation, it becomes essential to establish clear priorities for the areas to be addressed and the instruments to be used when designing a productive development strategy. Horizontal lines of action (strengthening of clusters, promotion of SMEs, improved international participation, and others) can and must be complemented by more selective policies.

In this regard, there is a clear regional trend in terms of initiatives to encourage the integration of productive chains, increase local value-added content and incorporate knowledge into activities with proven capacity to compete successfully on international markets. Policy-target sectors vary according to the countries considered, forming a wide spectrum ranging from primary products (crops and livestock, forestry, aquaculture and mining) to services (such as tourism), also including manufactures –generally natural-resource-intensive or linked to maquila export activity, but also a number of sectors that export goods of high technological content.

This is a practice that needs to be deepened, strengthening productive linkages (both upstream and downstream) in order to increase locally-sourced value-added and diversify the productive structure, creating new sectors, as shown by the successful experiences of a number of countries that have generated a complex and sophisticated productive structure based on a relatively abundant endowment of natural resources.[16]

Emphasis on these sectors, however, does not rule out the possibility of selectively promoting initiatives aimed at creating new sectors that are not necessarily closely associated with the region's comparative advantages, at least from the static point of view. The aim of generating dynamic comparative advantages based on new productive activities should form part of any comprehensive productive development strategy.

It is impossible to define a single policy agenda for the region, as this will depend on the constraints imposed by the size of national markets and accumulated capacities in each country. Institutional capacity can also be a major constraint, especially in the short run; this does not mean it is impossible to implement productive development policies, rather that their scope should be in accordance with those capacities. In other words, the alternative is to reduce the scale of activities rather than to attempt to exceed one's limit. In any event, improving the institutional capacity of the State is a prerequisite both for implementing policies to strengthen productive structures aimed at speeding up growth in the region's economies, and for implementing social policies aimed at achieving a fairer distribution of the benefits of that growth.

In addition, in a setting where competition for available fiscal resources is increasingly fierce, it is essential to work on issues relating to the legitimacy of productive development policies.[17] Implementation capacity needs to be improved, to narrow the gap between policy design and institutional capacity for effective implementation, the persistence of which undermines policy credibility. The strengthening of public-private dialogue and the establishment of participation channels for bodies that represent productive sectors will contribute towards this objective. Progress also needs to be made in evaluating the impact of initiatives implemented in terms of their ultimate objectives: economic growth, technological progress, increased

16 A case in point is Finland, which has used its forestry wealth to generate productive linkages that enabled it, over time and at different stages, to become highly competitive in the production of furniture, chemicals and capital goods, and even to enter the cellular telephony market. See Ramos (1998) and World Bank (2002).

17 This point is emphasized in Peres (1997), Stallings and Peres (2000), and Peres and Stumpo (2002).

productivity, among others. Some progress has been made on this issue, but much remains to be done.[18]

In short, the challenge of productive development is to find the combination of policy instruments, action and opportunity for public intervention that is best adapted to the specific development problems an economy faces, and to its capacities and available resources. One can only work with what one has, recognizing that problems, opportunities and constraints will change as the process unfolds. The important point is not to decide whether to intervene much or little, but to ensure that whatever interventions are undertaken address specific constraints on expansion. Thus, policy action is justified, in a particular case, when concrete benefits can be anticipated, and when the intervention is compatible with the resources available and with maintaining the appropriate incentives. Within this framework, it is possible to identify examples of densification of the productive, technological and business apparatus whereby production activities that are more complex and have a higher content of innovations can be tackled with a view to generating dynamic comparative advantages.

(c) Labour market, social protection and education: towards a covenant for social cohesion

Third, the liberalization process has brought new social risks, because of the relation between competitiveness and jobs. Job stability is no longer a dominant feature of how work is organized, and wage uncertainty has increased (Rodrik, 2001). "Lifetime employment" has been replaced by frequent changes of job and company, accompanied by changing skill requirements.

This global trend was heightened in the region by the low and unstable growth rate, rapid economic liberalization and the wave of privatizations of public enterprises. In the absence of comprehensive social protection mechanisms, labour supply moved countercyclically in line with families' need to overcome income insecurity via the employment of their working-age members. This accentuated the trend for women to enter the labour market. Production processes favoured mechanization because exposure to competition in a context of increasing market opening and currency appreciations raised the cost of labour compared with the cost of capital

18 An interesting example is the Business Development Programme of Mexico 2001-2006, which explicitly mentions quantitative targets. The programme proposes to create a public evaluation system including strategic indicators, control and coordination mechanisms, and participatory evaluation, periodic accountability and a monitoring unit for micro, small and medium-sized enterprises, as an information source.

goods and accelerated the adoption of advanced technologies in frontier sectors. New production technologies, involving an intensive use of skilled labour, undermined income distribution to the detriment of workers without tertiary education.

The outcome has been a rise in the rate of unemployment from 6.9% at the beginning of the decade to 10.6% in 2003. The increase in unemployment has occurred against the background of an expansion in the informal sector and a widening gap in the income of formal and informal workers. The result is a growing diversity in the labour market and a deterioration in income distribution. In this context, the reduction in poverty during the period 1990-2003 –from 48.3% of the population to 44.4%– is due to a 60% increase in per capita social spending during the period.[19]

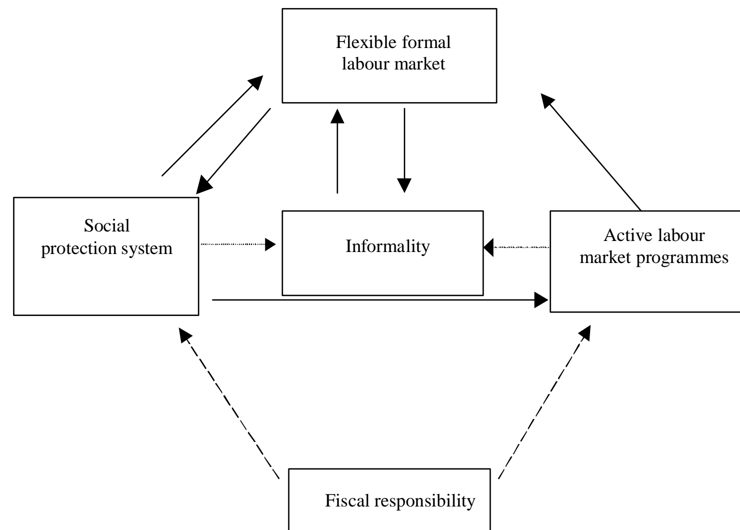
The emergence of jobs with fixed-term contracts and temporary jobs with no contract or no social protection, together with a drop in the wages of unskilled workers to the income levels of the informal sector, aggravated traditional employment problems. The active population faced an unstable job situation, which eroded their development prospects, training incentives and productivity gains. Social protection systems failed to cover these new risks and, in addition, were affected by a shortage of public funding and new institutional mechanisms that linked social benefits to the job stability of each individual worker.

The current situation calls for more complex solutions, which go to the very root of employment problems and the ability of social protection mechanisms to cope with the new risk structure facing workers. The wide variety of proposed solutions call for active social and economic policies, hinging on a social cohesion covenant resting on four pillars: consistency with the foundations of macroeconomic policy; job creation; social protection; and education and training.[20] A social protection system should be developed so that budgetary resources permitting, people can find a new place in the job market after a short period of unemployment or, failing this, through the assistance provided by active labour-market-oriented programmes. If, on the contrary, they remain in informal jobs, active job-market-oriented programmes should seek to improve the productivity of informal enterprises, adapt social protection systems to their characteristics and promote their formalization through institutions that promote their development.

19 The poverty level continues to be higher than it was in 1980 (40.5%) and 1997 (43.5%).
20 On this point, see Weller (2001), IDB (2003b), Titelman and Uthoff (2003) and ECLAC (2003).

In order to achieve these objectives, authorities should introduce a social cohesion covenant whose components match those illustrated in figure 10 below. The continuous lines indicate workers' mobility, the short dotted lines indicate allocations of resources, which must be strengthened towards the informal sector, both in terms of active programmes oriented towards this segment of the labour market and in terms of adapting social protection to its characteristics. The long dotted lines indicate solidarity-based financing for protection systems under a fiscally responsible system. The interactions should revolve around three components, in addition to sheer labour flexibility.

Figure 10
SOCIAL COHESION COVENANT



Firstly, these measures must be consistent with the macroeconomic context so as to avoid generating wage and price inflation. Additionally, it would also be appropriate to open up a debate on the tax burden and the tax yield. This should be reviewed in terms of the capacity to generate solidarity-based financing for socially acceptable protection targets.

Secondly, every effort should be made to ensure that the measures are consistent with the new designs for social protection, which should offer unemployment, disability, old age and life insurance, and with the health

service system, which should provide coverage in keeping with the new risk profiles associated with changes in the production structure.

Thirdly, there should be consistency with active support programmes for the generation of employment, information systems, informal productivity and training and skills development.

The covenant should be based on the recognition that labour policies do not, on their own, generate employment. They imply a recovery in the demand for employment and active labour policies to make sure that there is a supply of appropriate skills and to avoid other possible bottle necks. Based on these criteria, labour flexibility without a rapid growth in demand must go hand in hand with a good unemployment insurance coverage, active public employment policies and support policies for the informal sector. The covenant therefore combines the labour flexibility necessary for workers to adapt to the new conditions for competitiveness in the global market with a fiscally and socially responsible level of economic protection for workers. In order to formulate an agreement that takes into account the current state of development of the social protection system and the gradual development of active policies directed towards the formal and informal labour market, the proposal must be adjusted with variations that match the context in which it is applied.

New technologies and work processes require increasing creativity, initiative and versatility, and less specialization. Therefore, basic skills are more important to develop than specific skills, if workers are to have a knowledge base that enables them to adapt better to new jobs, and if the cost of greater flexibility in the labour market is not to fall entirely on them.

In situations that feature increasing levels of innovation and knowledge, education prefigures the fate of individuals and societies. Today's patterns of production and the changes associated with globalization require human resources trained for new modes of interaction, work, production and competition. Education is, thus, a requisite both for individuals to gain access to the benefits of progress, and for economies to ensure sustained development through more highly knowledge-intensive competitiveness. This means improving secondary school graduation rates, adapting the educational system to the needs of the labour market, and reducing international and social gaps in the use of information. Education has considerable potential long-term effects on equity, but the condition for them to materialize is that sufficient high-quality jobs be created. Education and jobs are the key to economic growth with social equity (ECLAC, 2000a).

(d) Institutional development and governance

Fourth, the relation between institutional design and functioning and economic development is a two-way phenomenon. Some basic institutions of the economic system allow agents to be reasonably confident about taking advantage of the productive opportunities in the economy.[21] At the same time, the type and quality of institutions are also a function of economic development, both because of the increasing complexity of the economy and because more resources are available. More important, yet, the perception of opportunities for economic growth leads to building and redesigning institutions. In various circumstances, it has been observed that institutional change does not emerge from a diffuse notion that reform is necessary, but from precise incentives and from the will to follow a specific economic trajectory that seems promising. Having a perspective on development makes it possible to identify priorities and define interests in such a way that the motivating factors behind certain institutional actions or changes become clear, and their implementation is facilitated. Hence, it is not only that economic development requires institutional changes, but that the crucial institutions function on the basis of the expected course of the growth. The current process of globalization is a good example of the exigencies of development and the adaptation of institutions, as shown at the beginning of this summary.

Beyond the greater or lesser depth of reforms, institutional functioning depends on experience and lessons that require a medium-term perspective.[22] One requirement is obviously macroeconomic stability –that is, achieving some degree of consistency between expectations and the actual performance of the economy. When agents have a realistic and reasonably specific view of the direction of the economy, crises are less likely to develop. At the same time, investment is more likely to be well placed –and this includes investment to develop capacities and reputation, which tend to strengthen institutions.

21 Rodrik and Subramanian (2003) draw an interesting distinction between types of institutions. Basic institutions are those that are created by the market. Without them, the market would not exist, or would not function well. However, long-term economic development requires other groups of institutions—those that regulate certain markets (where externalities, economies of scale and imperfect information are present), guarantee macroeconomic stability (foreign exchange, monetary and fiscal institutions), and confer social legitimacy (social protection systems, unemployment insurance and social funds).

22 Dixit (2004) maintains that the best strategy is not to attempt to reproduce the institutions of developed countries, but rather to modify those that already exist in each country.

Open regionalism, in the terms proposed by ECLAC (1994) is an option that can moderate some of the dilemmas mentioned above in relation to competition in the global economy. Indeed, in the 1990s, the four imperfect customs unions in the region generated intra-regional trade, as well as the potential for cooperation on various fronts. Toward the end of the decade, however, the process stagnated, while some countries (first Mexico, then Chile) began to favour free trade agreements to ensure access to certain markets in developed and developing countries. Because of changes in the Free Trade Area of the Americas negotiations, other countries (Central American and some Andean Community countries) are adopting similar strategies. In this context, subregional blocks face the choice of either strengthening their economic unions or moving, collectively or individually, into multiple free trade agreements with the rest of the world. In the latter case, the significance of existing blocks would be seriously affected.

IV. Some strategic guidelines for public intervention

Any thinking regarding Latin America and the Caribbean must begin by recognizing the great differences among the countries that make up the region, and the need to respect their unique characteristics. Nevertheless, there are common features that make it worthwhile to think about the countries as a whole, while bearing in mind that these are general principles and require significant complementary adjustment before being applied to specific circumstances in individual countries. In essence, the task is to define a “roadmap” that articulates public policy in different areas, while taking into consideration the specific present situation.

First, dissatisfaction with the results of the 1990s reforms, in terms of economic growth and social equity, is leading to an alternative vision. The change can be summarized conceptually as a transition, from an approach that advocated more market and less State to one that, without denying achievement in developing market economies, places renewed emphasis on better government –that is, on interventions of higher quality.

Second, a new balance must be reached between private initiative and public interest, paying special attention to equal opportunity and social cohesion. In a number of the region’s countries, many citizens and social groups have been losing their sense of belonging, along with ability to see common objectives as their own. Overcoming these centrifugal tendencies requires “society creation”, as well as more active participation in democratic political institutions, more tolerance for differences and greater willingness to compromise. With this object in mind, public policy must regain its original sense, addressing all types of decision-making in

pursuit of the common interest, not restricting itself to today's most common meaning of State action, that is, making "others" responsible.

Third, the foregoing is made easier when there is a shared vision of how to create an inclusive future. In all of the region's countries, there have always been marked differences regarding the well-being of their inhabitants. However, in a number of cases, during more or less prolonged periods, there was a perception that there existed the possibility of a better future, based on people's own efforts and within the framework of the opportunities that society offered. Today, the situation is different and requires a mobilization of social energies around a common endeavour, in order to establish long-term agreements (explicit or implicit) between the State and political and social actors regarding objectives, and the set of policies and innovations needed to achieve them. These agreements must be based on mutual commitments, particularly in the case of the business sector, and not merely on a unilateral attempt to gain rent-seeking concessions from the State.

Fourth, the countries of the region have a more diverse productive structure than they did in the past and than other developing economies such as those of East Asia. This situation can be represented, in diagrammatic form, through a "three-speed" economic model, based on the size and legal constitution of enterprises that make up the economy. One group is composed of informal enterprises that, because of their structure and capacity, are of lower productivity and operate in an environment that offers them little opportunity for development and learning. The second group is made up of formal small and medium-sized enterprises which, in turn, have problems accessing resources (particularly financial) and gaining access to certain markets for factors of production that would allow them to develop their ability to compete. The final group consists of large national and foreign enterprises, whose productivity often rivals that of businesses operating on the global scale, but with few links to the rest of the domestic economy and, in some cases, with poor capacity for innovation.

Fifth, as is true in the international arena, asymmetries —macroeconomic and financial, productive and technological, and of different degrees of mobility of productive factors— that characterize the relation between developed and developing countries, tend to reproduce and amplify inequalities. Moreover, at the national level there is a lack of genuine equality of opportunity that would allow ventures of the different productive entities mentioned to prosper on an equal basis. Proactive public policy is therefore needed to level the playing field, through specific measures designed to eliminate the obstacles that unevenly affect different productive units.

A differentiated structure of support and incentives could bring together three major public strategies: inclusion, modernization and densification. The strategy of inclusion is designed to move as many small productive units as possible from the informal to the formal sector of the economy. The policies that make up this strategy have broad coverage, but are also selective in terms of their beneficiaries, based on a definition, adjusted for each country, of the productive units to which they are directed. Notable among these policies are the simplification of rules and administrative procedures, lower tax liabilities, with simpler declaration procedures, expanded access to credit for small investments (and, above all, for working capital), and basic training programmes in management and technology skills. By moving businesses into the formal sector of the economy, they will be able to access other public policies and instruments, making it possible to advance their businesses, while providing a degree of social protection to their workers.

The modernization strategy is based on horizontal policies, combined with selective measures directed at productive clusters or specific productive chains. Support for modernizing production includes horizontal policies designed to improve access to information, credit, technology and marketing systems. Exporting can be enhanced through services offering guidance on foreign markets and available support, provided by specialized public agencies in association with private-sector business associations. Added to these are other policies involving training activities, incorporation of improvements in production, technology and procurement of new machinery and equipment. The selective policies are aimed at promoting the development of links with small and medium-sized enterprises ("associativity"), fostering links with larger businesses and strengthening local production structures or specific production chains. In several countries there are policies of both these types in place, but there is a need for major improvements in their design, for participation on the part of the potential beneficiaries, for establishing follow-up and assessment mechanisms and, above all, for increasing their coverage.

This last strategy can be summarized by the concept of "densification," since it aims to incorporate more knowledge in the national productive landscape, as well as to establish a more articulated web of productive, technological, entrepreneurial and labour relations. In principle, the overall policy and proper functioning of the institutions within a market economy would allow large businesses, which are more closely linked to international markets, to operate under reasonable conditions. Ideally, however, this framework should be supplemented by specific measures designed to produce changes in the public interest. In this case, it involves strategic

–and, therefore, highly selective– measures that require public officials to exercise a high degree of skill in negotiating and persuasion, in order to mobilize private efforts. This strategy can: provide implementation, through a variety of programmes, including programmes aimed at strengthening links within the export base; foster public-private cooperation in specific areas of innovation in order to realize potential competitive advantages; attract higher-quality foreign investment for productive links and technological capacities; support the expansion and internationalization of domestic enterprises; and strengthen the services infrastructure, in order to eliminate bottlenecks in productive development.

Sixth, the adoption of differentiated strategies, such as those referred to earlier, requires a considerable increase in the transparency of public policy. This will strengthen its legitimacy and provide for major improvements in design, based on a fruitful interaction with the potential beneficiaries. It is also necessary, in the interest of greater transparency and effectiveness, to implement follow-up and assessment mechanisms that make it possible to learn from successes and failures and, as a result, re-plot the course or make adjustments in order to achieve the objectives that have been outlined. Together these requirements point to the importance of improving the functioning of democratic institutions, as well as the quality of government officials overseeing strategic areas. This task can be met successfully, as demonstrated by the progress that various countries have achieved with technical teams dealing with monetary and fiscal issues.

Seventh, the policy instruments in an open economy are fewer and of more limited scope than those used in semi-closed economies. International regulations, free trade agreements and a number of regional agreements restrict the use of many such measures that were commonly used in the past. At the same time, budgetary and financial constraints make it necessary to be more selective in their application. Thus, the incentives will certainly be more moderate than those of past eras, particularly the strong incentives that characterized the period of industrialization overseen by the State, including quantitative or tariff restrictions on the importation of specific goods and the channelling of vast amounts of fiscal resources to public enterprises operating in sectors considered strategic for national development. All of this requires a targeting of efforts, increased efficiency and, above all, identifying new ways of making public policy.

As a final thought, it is worth noting that economic growth is simultaneously a condition and a consequence of the foregoing. However, it seems impossible to imagine not undertaking major efforts to increase domestic savings and channel them more effectively to productive

investment. Although developing economies should be the recipients of foreign savings, one of the most disruptive factors to economic decisions in recent years has been the variability in the supply of international financing. Thus, it would be wise to rely more on countries' own strengths, rather than depending exclusively on those of countries outside the region. Similarly, it is vital to establish a new fiscal covenant for social cohesion that financially supports the public functions required by productive transformation accompanied by social equity, in the framework of market economies that are open to the world, as is currently the case of the region's economies.

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