A preliminary assessment of the policies implemented by the governments of Latin America and the Caribbean in response to the crisis

Third meeting of Ministers of Finance of the Americas and the Caribbean

Lima, 27 and 28 May 2010

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This document was prepared by the Economic Development Division at the request of the Ministry of Economic and Financial Affairs of Peru.

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Foreword

This document was prepared by the Economic Commission for Latin America and the Caribbean (ECLAC) at the request of the Ministry of Economic and Financial Affairs of Peru, to be presented at the third meeting of Ministers of Finance of the Americas and the Caribbean, with a view to assessing the policies implemented by the governments of the region in response to the international crisis.

The macroeconomic stability shown by most Latin American and Caribbean countries during the years preceding the international crisis marked a significant change compared with the customary financial problems experienced in the course of similar episodes in the region during its recent history. The exceptional period of buoyancy in the world economy and in international finance enabled these countries to strengthen public accounts, reduce and improve their debt profile and build up their international reserves, something they had not previously been able to do. This gave governments leeway to implement unprecedentedly active government policies, designed to counteract the negative impact of the deterioration in international conditions. Broadly speaking, these measures can be divided into those intended to restore confidence and make financial markets operational and those intended to bolster aggregate demand and the capacity to create jobs.

At first, the central banks tried to restore liquidity to allow the normal functioning of domestic credit markets. The low level of monetization, however, and the shallowness of the region's financial markets, together with the uncertainty that reigned in the financial sphere from the end of 2008 onwards and for a good part of 2009, limited the impact of these measures on the level of economic activity. In some cases, efforts were made to offset the slack credit supply through a more active rote for public banks, a tool whose effectiveness depends on the importance of credit in the economy and the public banks' share of total lending, which means that it is restricted to only a few countries

More generally, and as of the first quarter of 2009 in particular, countries announced and gradually implemented a strategy based on increasing the fiscal stimulus, sometimes through a temporary and selective tax reduction and sometimes by raising government spending. In particular, there was an increase in current expenditure, usually associated with an increase in direct transfers, even though in some cases there was also an increase in capital expenditure, which will extend beyond the 2009 fiscal year.

This brief document aims to provide an evaluation of the impact of the measures taken by the countries in the region to offset the impact of the crisis. It is not intended to compare the effectiveness of the various strategies adopted, but to give a synthesis of the information available so as to gain an idea of the scope of the efforts made by countries and the similarities and differences in approaches in the various instruments used. As such, it is a prelude to a more complex exercise, bearing in mind the problems involved in evaluating the impact of measures that are different in terms of features and scope, that are applied in combination with other measures, and whose effects, moreover, depend on the very different situations in which they were applied.

Tables 1 to 4 in the next section give an overview of the measures taken by groups of Latin American and Caribbean countries in the following five categories:[1]

- Monetary policy
    - Monetary policy rates
    - Expansion of primary liquidity
- Financing from public banks
- Fiscal policy
    - Tax cuts
    - Variation in spending
- Exchange-rate and foreign trade policy
- Labour policies

Regarding the impact of the measures, section C includes and comments on tables and charges showing the quarterly trend in the GDP and employment and annual inflation rates. This section mentions the special features of the rapid recovery which, in general, is being shown by the region's economies, underlining the importance of government policies both in sustaining demand and in creating jobs.

The document ends with a section that analyses the challenges which, going beyond the short term, show the need to transform this recovery into renewed sustained growth as a necessary condition for remedying the region's endemic ills of poverty and inequality.

ECLAC offers this document as a contribution to the public policy debate geared towards assisting the governments of the region in rising to the constant challenge of achieving inclusive and sustainable development.

Alicia Bárcena
Executive Secretary of the Economic Commission for
Latin America and the Caribbean (ECLAC)

[1] It should be noted that, although the measures announced are clearly aimed at a particular sector or market or are intended to deal with social issues, they had a fiscal impact so they have been considered as a whole within government spending variations, because of the difficulty of obtaining a quantitative breakdown.

A. The measures implemented[2]

1. Monetary policy

- The region's central banks implemented a series of measures of different types designed to guarantee a sufficient level of liquidity in domestic financial markets. The generalized fall in the inflation rate, helped by the drop in the price of food and energy, enabled monetary policy to be more flexible, not only in countries with specific inflation goals but also in those which follow trends in a particular monetary aggregate or any other operational criteria and was particularly noticeable in Brazil, Chile, Colombia, Honduras, the Plurinational State of Bolivia, Peru and the Dominican Republic.[3] In some case, the maintenance of relatively high levels of inflation limited the monetary authorities' capacity to bring about a fall in interest rates.

- As indicated, the fall in monetary policy reference interest rates was accompanied by increased monetary expansion. As can be seen in table 1, at the end of 2008 the central banks greatly expanded domestic credit, while reducing reserve assets, a situation that was gradually reversed throughout 2009.

- Given that the effort made by the central banks to increase liquidity in the financial system did not result in an increase in private bank lending, the public banks' activities in many cases formed part of the countercyclical strategy of the region's governments. In this connection, it should be pointed out that the impact of this tool depends on the extent of the official bank's participation in the financial system, a fact that underlines the importance of Brazil's strategy, where the public bank lending represents some 35% of total credit.

[2] In many cases, the problem of obtaining a breakdown governed the choice of the variables used, and also of the period of time chosen for the analysis.

[3] It should be noted, however, that in many cases even though interest rates fell sharply the rate of inflation fell even more rapidly, which led to higher interest rates in real terms, thereby negating the objective pursued.

Table 1

Latin America: monetary and financial policy

	Monetary policy reference rate (%)			Variation in primary liquidity (% of GDP)				Variation in public bank lending (% of GDP)
	Average July-September 2008	Average October-December 2009	Difference	Q4 2008 / Q3 2008		Q4 2009 /Q4 2008		
				Reserves	Domestic credit	Reserves	Domestic credit	
Argentina	11.3	11.6	0.3	-0.27	1.05	1.86	-1.05	-0.9
Bahamas	5.3	5.3	0.0	-0.74	0.03	2.33	-1.66	n.d
Bolivia (Plurinational State of)	9.7	3.0	-6.7	-0.53	1.96	2.62	3.36	n.d
Brazil	12.9	8.7	-4.2	-0.91	1.27	2.32	0.38	4.2
Chile	7.8	0.5	-7.3	-0.69	1.07	1.51	-1.02	1.1
Colombia	10.0	3.8	-6.2	-0.03	1.22	0.44	0.07	0.3
Costa Rica	9.5	9.0	-0.5	-0.05	0.82	1.60	-1.25	0.0
Guatemala	7.1	4.5	-2.6	-0.22	0.84	1.35	-0.47	0.1
Haiti	8.0	5.0	-3.0	n.d	n.d	n.d	n.d	n.d
Honduras	9.0	4.5	-4.5	0.67	0.56	-2.86	2.22	n.d
Jamaica	14.0	12.5	-1.5	-3.62	4.99	1.24	-0.36	n.d
Mexico	8.0	4.5	-3.5	-0.32	1.30	1.33	-0.87	1.1
Nicaragua	n.d.	n.d.	n.d.	0.30	0.46	1.09	-0.86	n.d
Paraguay	6.0	2.4	-3.6	-0.82	2.09	5.83	-2.41	0.4
Peru	6.3	1.3	-5.0	-2.83	3.41	1.05	-0.74	0.1
Dominican Republic	9.3	4.0	-5.3	0.03	2.08	3.37	-2.78	n.d
Trinidad and Tobago	8.4	6.1	-2.3	2.08	-0.56	-1.38	2.89	n.d
Uruguay	7.3	6.8	-0.4	0.06	1.18	4.19	-3.76	0.3
Venezuela (Bolivarian Republic of)	12.7	n.d.	n.d.	1.62	1.39	-2.07	4.23	3.1

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

2. Fiscal policy

- The positive fiscal stimulus was one of the distinctive aspects of economic trends in 2009. The average primary balance in the region went from a surplus corresponding to 1.4% of GDP in 2008 to a deficit of around 1% of GDP in 2009. This difference of over two points in the GDP was caused both by the drop in government income and the increase in expenditure and, in this connection, there was an increase in both current expenditure and capital expenditure.

- The behaviour of public income was a reflection, on the one hand, of the evolution of economic activity levels, which had an effect on tax collection, and, on the other, the fall in the price of the region's export commodities, which are a very important source of public revenues in some countries. In many cases, to these must be added the impact of political decisions which led to reduced tax revenue. Other factors were the reductions and other benefits relating to income and corporation tax, as well as the temporary tax incentives intended to boost demand in certain sectors of the economy.

- On the spending side, the measures taken have been fairly ambitious and in many instances involved a marked increase in current expenditure (generally more flexible) and, to a lesser extent, in capital expenditure, which is usually slower to implement. In some countries highly specialized in commodities, the reduction in the fiscal space resulting from the sharp fall in commodity prices made it difficult to implement countercyclical measures.

■ **Table 2** ■

Latin America: variation in tax revenues and spending, 2008-2009

(Percentages of GDP)

	Variation in tax revenues			Variation in spending		
	Total	By evolution of level of activity and other factors	Anti-crisis measures[d]	Total spending	Current spending	Capital spending
Argentina	-1.0	-0.5	-0.5	4.1	3.5	0.6
Bolivia (Plurinational State of)[a]	-0.4	-0.4	0.0	…	…	…
Brazil	-0.8	0.0	-0.8	1.9	2.0	-0.1
Chile	-3.9	-3.1	-0.8	3.4	2.5	0.9
Colombia	-0.4	-0.4	0.0	1.7	1.6	0.1
Costa Rica	-1.9	-1.9	0.0	1.8	2.2	-0.4
Ecuador	0.7	0.7	0.0	-1.5	0.1	-1.6
El Salvador	-1.1	-1.1	0.0	1.4	1.3	0.0
Guatemala	-0.6	-0.6	0.0	1.0	1.3	-0.3
Haiti[a]	…	…	…	1.6	…	…
Honduras	-1.6	-1.6	0.0	-0.8	1.0	-0.9
Mexico[b]	-0.4	-0.4	0.0	0.6	1.5	-0.8
Nicaragua	-0.2	-0.2	0.0	0.3	0.2	0.1
Panama	0.3	-0.2	0.5	0.4	-0.3	0.7
Paraguay	1.0	1.0	0.0	4.3	2.5	1.8
Peru	-2.0	-2.0	-0.1	1.4	0.0	1.4
Dominican Republic	-1.9	-1.9	0.0	-2.7	-1.1	-1.6
Uruguay	0.3	0.3	0.0	0.8	1.0	-0.2
Venezuela (Bolivarian Republic of)[c]	-0.2	-0.2	0.0	0.6	1.2	-0.5

Source: Economic Commission for Latin America and the Caribbean, on the basis of official figures; *Preliminary Overview of the Economies of Latin America and the Caribbean, 2009* (LC/G-2424-P), Santiago, Chile, December. United Nations publication, Sales No.E.09.II.G.149.

[a] No official closing data for 2009.
[b] Includes only non-oil tax revenues.
[c] Preliminary figures estimated by the Central Bank of Venezuela.
[d] In Costa Rica, does not include the impact on revenues of the accelerated depreciation system. In Mexico, does not include the impact of tariff cuts.

3. Trade policy

- In some cases, there has been an increase in import tariffs and other trade-restricting measures, particularly during the first moments after the crisis became acute, when the virtual disappearance of trade financing deeply affected foreign exchange liquidity and contributed to rapid currency depreciation in some countries in the region at the end of 2008. Ecuador is a case in point, where this type of restriction extended to almost 40% of imports and to a certain extent offset its economy's problem in raising the real exchange rate, via currency depreciation.

Table 3

Latin America: trade-restricting measures applied, November 2008-February 2010

	Number of measures	Percentage coverage of imports for 2009	Number of tariff lines	Number of sectors
Argentina	49	14.5	92	20
Bolivia (Plurinational State of)	1	1.2	44	5
Brazil	24	6.1	15	11
Chile	2	0.0	1	1
Colombia	3	0.0	1	1
Costa Rica	...	...	...	...
Ecuador	4	39.6	316	30
El Salvador	...	...	...	...
Honduras	...	...	...	...
Mexico	11	5.8	64	24
Nicaragua	...	...	...	...
Panama	...	...	...	...
Paraguay	4	1.6	60	6
Peru	5	0.0	...	...
Dominican Republic	1	0.0	...	...
Uruguay	...	...	...	...
Venezuela (Bolivarian Republic of)	2	52.0	...	...

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

4. Labour policies

- The countries have reacted to the current crisis by implementing a range of policies directed at the labour market. Particular mention is warranted by unemployment insurance, which has been adapted in response to the crisis, by extending the duration of benefits, broadening coverage to new beneficiaries or using it in combination with training and job protection policies.
- The countries have also continued to implement active labour market policies of a more traditional nature, such as labour intermediation and training. As far as training is concerned, greater emphasis has been placed on meeting real skills requirements, in combination with intermediation and direct job creation policies. Several countries have introduced training mechanisms as instruments to avoid job loss at the same time as enhancing workers' employability, as well as retraining programmes for those who have lost their jobs as a result of the crisis.
- An important role has also been played by public-sector policies of direct and indirect job creation, aimed especially at raising the income of the most vulnerable families.
- Hiring subsidies have been used as an active policy of indirect private-sector job creation, combined with intermediation through public employment bureaus and training opportunities, with a view to increasing beneficiaries' chances of quickly re-entering the labour market.

Table 4

Latin America (selected countries): labour programmes, 2009

Country	Main areas	Beneficiaries	Beneficiaries in relative terms
Argentina	- Youth employment integration	- As of July 2009: 46 000 direct beneficiaries	- 0.3% of EAP[a]
	- Retention of employment	- As of November 2009: 139 000	- 0.8% of urban EAP
Brasil	Extension of unemployment insurance	216 500	- 0.2% of EAP; 3% of unemployed (at 2008)
Chile	- Emergency employment	- 186 000 as of December. 2009 (increase of 155 000 December 2008-December 2009)	- 2.5% of EAP
	- Subsidies for youth hiring	- 55 000	- 0.8% of EAP
	- Modification of unemployment insurance	- average for the year 146 700 beneficiaries (+33% compared with 2008)	- 20.7% of unemployed
Colombia	Youth training	152 000 training places	- 0.7% of EAP; 2.8% of young EAP
Costa Rica	Youth entrepreneurs		- 0.2% of EAP
El Salvador	Temporary employment plan	5 000 in 2009	
México	- Temporary employment	- 722 000 in 2009	- 1.6% of EAP
	- Job preservation	- 196 000 as of September 2009	- 0.4% of EAP
Paraguay	Temporary employment		
Perú	- Temporary employment	- 164 000 in 2009	- 1.1% of EAP
	- Training and technical assistance for firms	- 18 700 in 2009	- 0.1% of EAP
Uruguay	Employment retention through training		

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

[a] Economically active population.

B. Impact of the measures implemented

1. Activity levels

Table 5

Latin America: quarterly GDP variation, seasonally adjusted, 2008 and 2009
(Percentages)

	2008				2009			
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Argentina	1.2	2.1	1.5	0.1	-0.4	0.2	0.2	1.9
Bolivia (Plurinational State of)	0.9	1.8	1.9	-0.5	-1.0	3.7	0.9	0.9
Brazil	1.8	1.2	1.4	-3.5	-0.9	1.4	1.7	2.0
Chile	1.9	2.1	-0.8	-2.5	-0.8	-0.3	1.5	1.7
Colombia	-0.4	0.5	0.4	-1.5	0.1	0.8	0.4	1.1
Costa Rica	1.2	-0.4	-0.3	-2.2	-1.6	1.7	1.9	1.0
Ecuador	0.5	2.1	1.9	-0.5	-0.7	-0.2	0.1	0.3
El Salvador	-0.6	1.4	-0.1	0.6	-3.5	-0.6	-0.7	-0.2
Mexico	1.2	-0.4	-0.1	-1.9	-6.9	0.3	2.5	2.0
Panama	3.9	3.0	0.9	0.2	-0.7	1.7	-0.4	2.9
Paraguay	3.0	1.8	-3.3	3.0	-6.9	0.8	2.0	3.6
Peru	3.6	2.3	1.6	-1.0	-1.1	-0.5	2.4	2.5
Dominican Republic	2.8	1.6	-2.2	3.5	-1.3	1.3	0.6	6.1
Uruguay	2.5	3.3	1.2	0.3	-1.8	1.4	2.8	2.1
Venezuela (Bolivarian Republic of)	-0.5	3.4	0.1	0.2	-2.9	0.0	-1.9	-1.2
Latin America (weighted average)	1.3	1.1	0.7	-1.9	-2.6	0.6	1.4	1.8

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

- In late 2008 and early 2009 consumer and business expectations took a turn for the worse across the region, which was reflected in a decline in both private consumption and investment. In fact, as shown in figure 1, only public consumption showed positive variation in the first part of the year, thanks to the capacity available in many of the region's countries to implement countercyclical policies which partially offset the negative performance of the other components of domestic demand and helped to speed the recovery process in the second half of the year.

Figure 1

Latin America (simple average): breakdown of total supply and demand, 2008 and 2009

(Percentages)

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

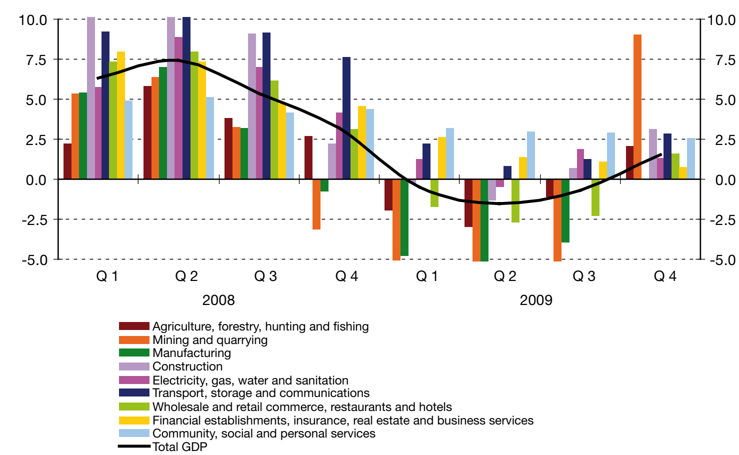
- Aggregate supply and demand trends were reflected in the evolution of the different sectors of activity. Goods-producing sectors, especially mining and industry, were the worst affected by the crisis. Construction also registered a downturn, as did commerce and hotels and restaurants, as a result of declining tourism activity.

- The performance of government and personal services reflected the increase in public spending and remained buoyant over the year.

Figure 2

Latin America (simple average): activity levels by sector, 2008 and 2009

(Percentages)



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

2. Inflation rates

■ Table 6 ■

Latin America and the Caribbean: year-on-year variation in the consumer price index, December 2009

(Percentages)

	2008	2009
Latin America and the Caribbean	8.3	4.6
Argentina	7.2	7.7
Bolivia (Plurinational State of)	11.9	0.3
Brazil	5.9	4.3
Chile	7.1	-1.4
Colombia	7.7	2.0
Costa Rica	13.9	4.0
Cuba	7.5	-0.1
Ecuador	8.8	4.3
El Salvador	5.5	-2.3
Guatemala	9.4	-0.3
Haiti	10.1	2.0
Honduras	10.8	3.0
Mexico	6.5	3.6
Nicaragua	12.7	0.9
Panama	6.8	1.9
Paraguay	7.5	1.9
Peru	6.7	0.3
Dominican Republic	4.5	5.8
Uruguay	9.2	5.9
Venezuela (Bolivarian Republic of)	31.9	26.9

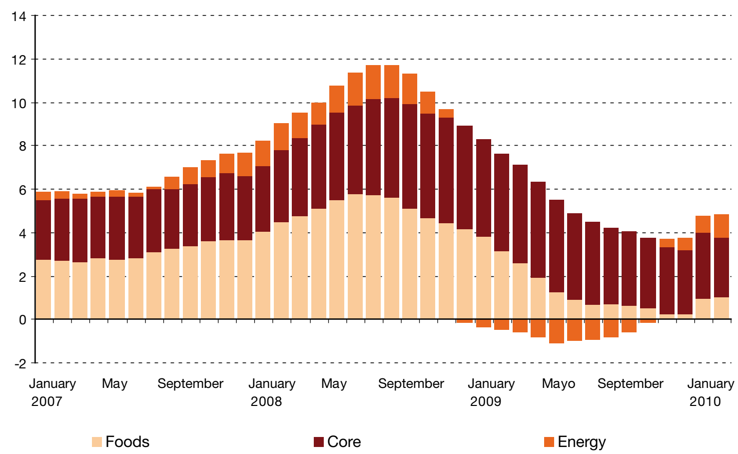
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Inflation came down from 8.3% in 2008 to around 4.5% in 2009. Starting in late 2008, inflation began to drop in the countries of the region as a result of falling international prices for foods (cereals, oilseeds and oils) and fuels (natural gas, gasoline and other petroleum products). This was in addition to the significant contraction in domestic demand as the international crisis took its toll on national economies.

■ Figure 3 ■

Latin America (simple average): breakdown of inflation rate

(Percentages)



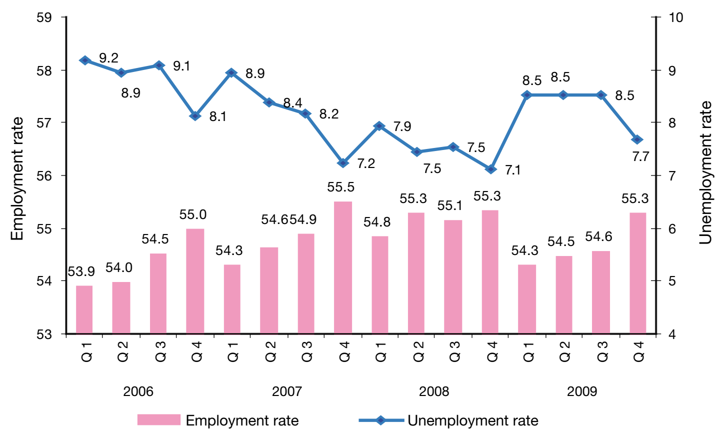
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

3. Labour indicators

- The crisis began to affect labour markets in the region in the second semester of 2008, as the year-on-year rise in employment rates slowed in the third quarter then came to a halt, with employment rates falling outright in the fourth quarter. The downturn continued into the following quarters, with the largest falls in year-on-year employment rates occurring in the second quarter of 2009 (0.8 percentage points). The unemployment rate mirrored this trend, with the year-on-year rise peaking in the second quarter of 2009 at 1.1 percentage points. In the third quarter the labour market began to stabilize and by the fourth the employment rate was back up to the level of the same quarter of 2008. In the fourth quarter of 2009, the unemployment rate was up by 0.6 percentage points on the year-earlier period, reflecting an increase in labour supply towards the end of the year, which was a response to the perception of better employment opportunities in the context of improving economic activity levels.

Figure 4

Latin America (9 countries): employment and unemployment rates, first quarter 2006 to fourth quarter 2009
(Percentages)



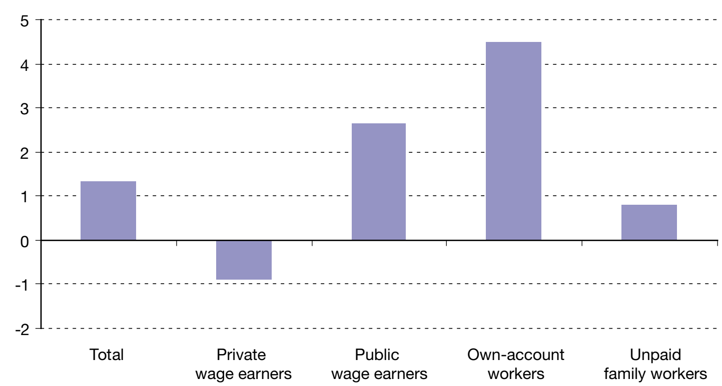
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- At the regional level, for the year overall, the employment rate fell by 0.5 percentage points with respect to 2008. The weakness of economic growth was expressed above all in private wage employment, since labour demand contracted amid lower levels of production.

- This contraction was offset by the increase in public sector employment and self-employment, as well as unpaid family work.

Figure 5

Latin America (median for 12 countries): variation in employment by category of occupation, 2009
(Percentages)



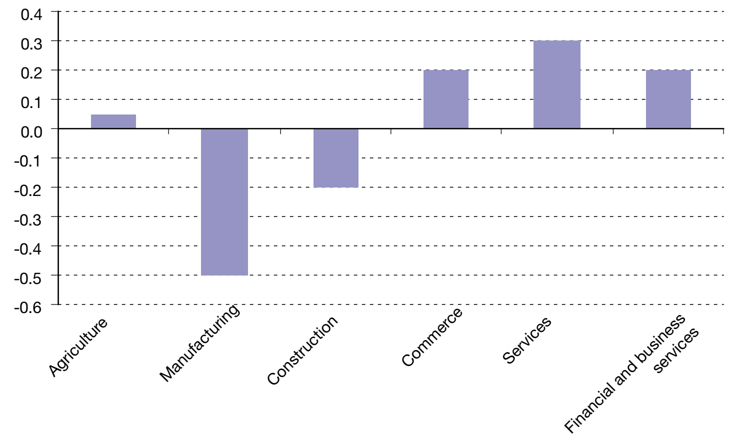
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Output performance by sector axis reflected in employment patterns. Whereas employment decreased in manufacturing and construction, it actually rose slightly in the main branches of the tertiary sector, commerce and community, social and personal services, owing to the expansion of public employment and of the informal sector.

Figure 6

Latin America (median for 15 countries): changes in the composition of employment, 2009

(Percentage points)



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

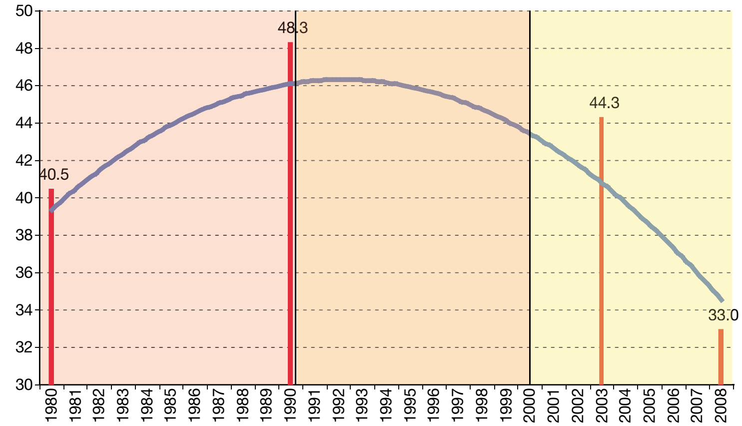
4. The outlook beyond the short term

- The crisis interrupted an extraordinary period of growth in which the countries of the region had begun to show a path of improvement in social indicators. This made it possible to bring rates of poverty and indigence well below the levels of 1990, when practically half the Latin American population had insufficient income to cover their basic needs. There was also a substantial reduction in poverty in comparison with 1980. The road ahead is still a long one, however.

■ Figure 7 ■

Latin America : population below the poverty line

(Percentages)



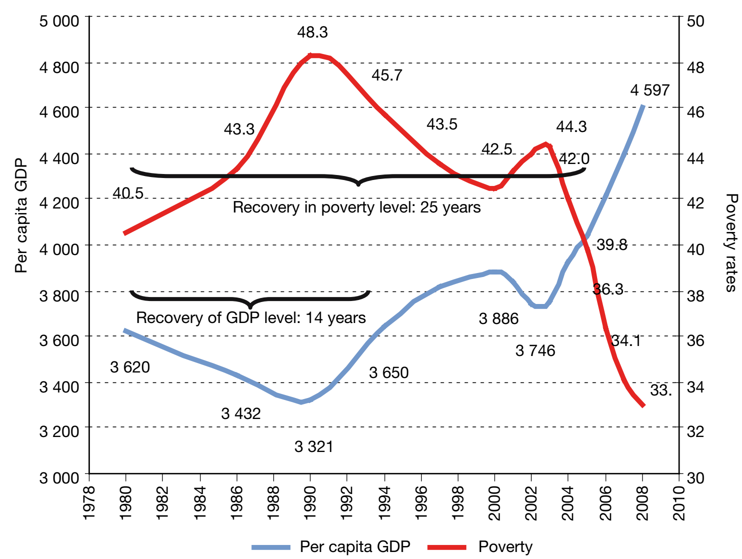
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- Latin America learned from other crises how hard it can be to make up social gaps. It took the region 14 years to regain the levels of per capita GDP from before the debt crisis, but 25 years to reduce its poverty rates back to the level recorded before that episode.

■ Figure 8 ■

Latin America: per capita GDP and poverty rates

(Dollars and percentage of the population)



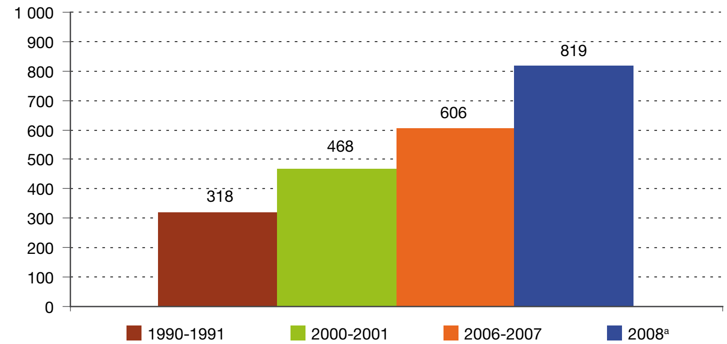
Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

- The scant progress in poverty reduction and limited mechanisms for growth spillover into income for the poor have prompted a reformulation of social policy, with a significant increase in spending. Preliminary information indicates that this growing effort in social expenditure has been maintained as part of the response to the crisis by governments in the region.

■ **Figure 9** ■

Latin America (simple average): social public spending per capita, 1990-1991 to 2008

(Dollars at constant 2000 prices)



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

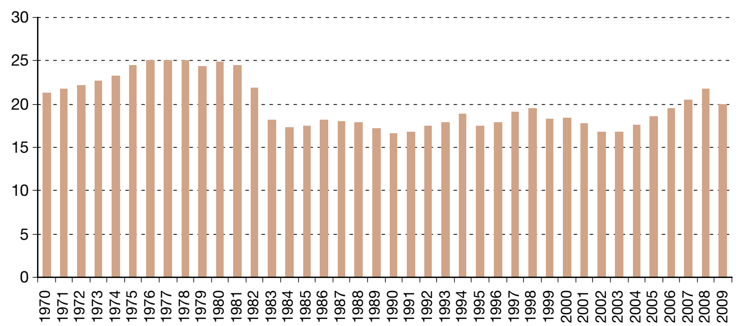
[a] Simple average for 12 countries.

- Although this is good news, it is not enough. In order to make significant strides with the reduction of poverty and inequity, the region must regain a path of growth combined with job creation, which poses the challenge of increasing investment rates. This gap has yet to be closed, because the Latin American countries have still not regained the levels of investment recorded prior to the crisis of the 1980s.

■ **Figure 10** ■

Latin America: investment rate

(Percentages of GDP)



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

- Faced with the need to offset the effects of the crisis, the States of the region produced an unprecedented response, to the best of their capacities, thus enabling a rapid recovery of activity and employment levels. However, the objective of regaining a path of sustained growth raises new and more complex challenges, making the creation of public policy space an essential task for the countries of the region from now on.

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