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# WHY SOME LATIN AMERICAN ECONOMIES GROW AND SOME DON'T

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## **Executive Summary**

Economic growth and development in Latin America has been a far cry from the inflated expectations of explosive growth anticipated in the early 1990s. Despite concerted efforts and profound policy reforms, the region has been unable to generate sustained growth in an open economy.

This lacklustre performance across the region has stimulated widespread debate spanning the policy spectrum. Politics and ideology certainly have played a significant role in the economic development of Latin America over the years and continues to taint the debate even today. While countries across the region have experimented with contrasting approaches from state-led growth and economic nationalism to high-paced economic liberalism, the all-important issue of development continue to elude the region – regardless of the paradigm of choice.

But there have been exceptions. Those high growth performers scattered across the region share some common characteristics. These include a basic set of fundamentals that forms the foundation for feasible growth and development. The implementation and timing of these policies and initiatives result in an arguably more heterodox than orthodox approach to economic development. Given the general shortage of savings, investment – and particularly foreign direct investment (FDI) – is key to growth and development. And, in a world where politics and policy count, the growth performers have had leaders that display a visionary approach to economic management and strategy mixed with strong virtues of accountability and responsibility. Political stability (or perceived stability) is an essential prerequisite for FDI and sustainable growth.

Chile is the best example of the gradual, consistent though somewhat heterodox reformer, where economic liberalisation was implemented at its own pace and where privatisation of a key strategic industry, mining, is still incomplete. Yet the country attracts some of the largest inflows of investment in Latin America (relative to economy size), and growth and development are well ahead of the regional average.

The debate around growth and development has shifted from one seeking a common set of policies and reforms formatted as a consensus or extended list of requirements to one focused on country attributes and specific growth diagnostics. While key attributes of ability and capacity are at the core of economic growth in developing countries, country-specific diagnostics is a more useful way of assessing economic performance and developing policy advice.

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## **Introduction: Reform and Growth in Latin America**

What drives economic growth? This question has baffled economists and practitioners for literally hundreds of years and continues to generate endless debate and investigation today.

The question of economic growth and its link to development is most controversial in Latin America. Nowhere else in the last 15 years has this issue been more politicised or polarised. After undergoing a rigorous process of liberal economic reform in the early 1990s, economies across the region have experienced erratic growth surges that have been followed by dramatic declines and, in some cases, total economic collapse. This has had serious social and political repercussions, which are manifested in a shift away from neo-liberal orthodox policy sentiment and the resurrection of a leftist and populist-style political leadership reminiscent of Latin America in the 1960s.

Despite varying degrees of growth across the region since 1990, development has generally been slow and real economic growth in per capita terms has been disappointing. But there are exceptions. Some countries have managed to achieve sustainable economic growth with more profound results, which is based less on the commodity boom or initial phases of market liberalisation and more on diversity, innovation and sound institutional support.

This paper explores some of the reasons and experiences behind growth in selected Latin American economies. While the debate around the feasibility of the much-vaunted Washington Consensus — the so-called 'neo-liberal' set of reforms designed to bring market-led growth to underperforming countries — is ongoing, literature and studies both in favour of and opposed to the current economic orthodoxy seem to agree on one important point: reforms are dependent on circumstances. In other words, there is no standard template for growth and development, or no 'strait-jacket' of 10, 15 or 20 'consensus points' that will guarantee growth and development for all.

Rather than adding to the mounting literature that either strives to justify the market-friendly policies associated with the Washington Consensus or seeks an alternative orthodoxy that better suits the Latin American social and political climate, this paper highlights a few simple and relatively straightforward characteristics and trends common among the growth performers in Latin America. These, in essence, comprise a set of circumstances and responses over and above the required set of macro-economic reforms implemented across the region. Some reference is made to the new trend in analysis that suggests an agenda that 'reforms the reforms' through an 'augmented Washington Consensus', one that advocates a more developmental reform agenda inclusive of softer issues like education and welfare, while placing greater emphasis on institutions.<sup>2</sup> But while these are important arguments still unfolding in policy debates and academic discussion, the real focus of this paper identifies basic principles and factors that appear to have contributed to ongoing growth in some countries, while their absence seems to have been detrimental in others.

## **An Economic History – From Dependency and Nationalism to Hyper-Capitalism?**

In the late twentieth century, Latin America underwent a massive set of changes that started (for the most part) in the mid-1980s. These changes, described by Peruvian economist Alvaro Vargas Llosa as 'epoch-making', launched the region into an era of free markets and free

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<sup>2</sup> John Williamson, the father of the original Washington Consensus, along with Dani Rodrik, William Easterly and others have dedicated much of their effort to understanding what an augmented Washington Consensus might add to growth. Recent studies by Rodrik consider the role of particular circumstances in country-specific growth patterns. From a 'political-economy' perspective, the importance of political stability and the related impact on FDI flows has stimulated focus on this aspect.

societies. Years of state oppression and dictatorships gave way to political democracy. A broad set of reforms characterised by stabilisation, liberalisation and privatisation replaced nationalist tendencies in economic policy-making, bringing with it a significant shift from the development paradigm that had dominated the region for so long.

After emerging from a situation of near collapse in the early 1980s, countries across the region were desperate for change. This economic disaster and resulting sentiment paved the way for the radical reforms of the 1990s, while, concurrently, relentless pressure for social and political change finally paid off with democratic transition.

But the *transition* to a vision of an open society in a free market system has proved to be notoriously different from the actual *creation* of an open society. This is especially the case in Latin America, where a rich political history and firmly embedded economic norms and traditions have moulded the landscape and culture that defined the political economy in the region in the past and still does so today.<sup>3</sup>

### The Rise of Dependency

In the post-World War II period a tendency toward structuralism emerged in economic thinking across Latin America. This gave rise to the dominant force of dependency, which advocated various protectionist policies and staunchly politicised the policy debate in the region. Dependency theory provided a philosophical justification for economic nationalism and, at the same time, the rise of populism. It was a direct response to the export model that had shaped production and the economic climate in Latin America for the preceding decades. Latin America had been the most important supplier of primary products to the world until World War I,<sup>4</sup> but, following the depression in the 1930s, the model collapsed and it was clear that under such a paradigm individual countries in the region had very little control over their economic destinies.<sup>5</sup>

Import substitution became the new instrument of industrial development as economic nationalism was embraced in varying degrees of intensity and by using various methods in countries across the region. The Hugo Chavez of that era was the Argentine president Juan Peron, who became a symbol of such policies and, like Chavez today, used them to build his own political stronghold at the cost of democracy and, ultimately, economic progress.

Supporters of this era of economic nationalism (loosely referred to as the development paradigm) or those opposed to economic liberalism insist that Latin America generally benefited from such protectionist policies. And according to basic statistics, it appears (on the surface) that they may be right. Annual economic growth rates between 1950 and 1980 were generally higher in most large Latin American countries than in the developed world. Brazil grew on average by 7% per annum, Mexico by 6.5%, Peru by 4.9% and Argentina by 3.8% — above the regional average in the 1990s. But growth before this period matched these figures.

More significant is the role these policies played in shaping the political and economic trajectory of the region. While this era of protectionism did assist in developing certain industries, which helped to diversify some economies, it tended to leave economies more vulnerable to external shocks than they were before. In the late 1970s and early 1980s, Latin American economies became synonymous with debt crises and seemed to lack the basic

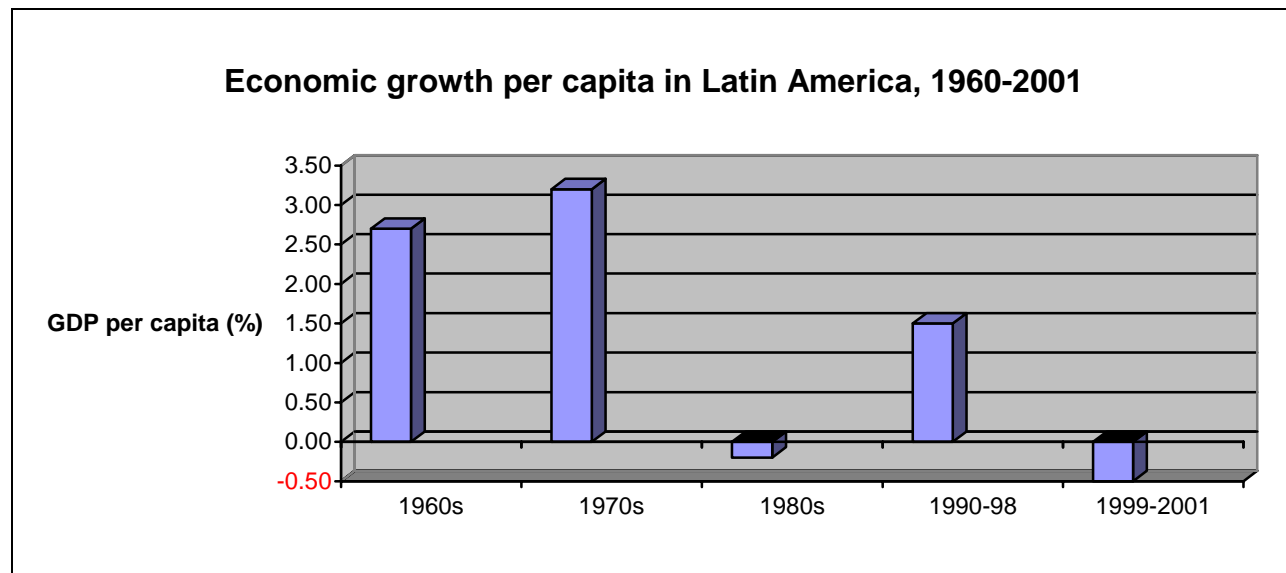
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<sup>3</sup> This point is raised and discussed in some detail by Alvaro Vargas Llosa, *Liberty for Latin America: How to Undo Five Hundred Years of State Oppression*. New York: Farrer, Strauss and Giroux, 2005.

<sup>4</sup> Latin America's contribution to world markets during this time included: 84% of coffee, 64% of meat, 97% of nitrates, 50% of bananas, 30% of sugar, 43% of corn and a large proportion of the world's base and precious metal supplies. It was clearly the breadbasket of the world.

<sup>5</sup> See Vargas Llosa, op. cit., pp. 45–48.

fundamentals and temperament to handle economic decline and collapse. But most significant of all, import substitution failed to achieve its single most important goal (which was the reason it emerged in the first place): development was still an anomaly in Latin America.



Source: Vargas Llosa (2005) and ECLAC ([www.eclac.cl](http://www.eclac.cl))

Latin American countries had based an entire economic model — which applied for most of the region — on an ideology. The essence of the development paradigm was based on the fallacy of economic nationalism: that underdevelopment was a result of the state of dependency of the developing world on markets in developed countries.

Unfortunately, the fallacy that links dependency to underdevelopment was identified too late. In fact, some of the central tenets that place this paradigm firmly in the context of Latin America have proved to be far from accurate or grossly misinterpreted. For example, there has never really been a shortage of finance in Latin America, particularly in the 1970s, when aid and loans reached record levels, but foreign direct investment (FDI) was still low compared to other underdeveloped regions like Asia. Rather, the region seems to lack the ability and capacity to accumulate and build capital. The debt crisis and region-wide collapse of economic and political institutions that ushered in the infamous 'lost decade' in Latin America was the ultimate result and legacy of economic nationalism and the *raison d'être* for the rigorous reforms that followed.

### Free Markets and Free Societies

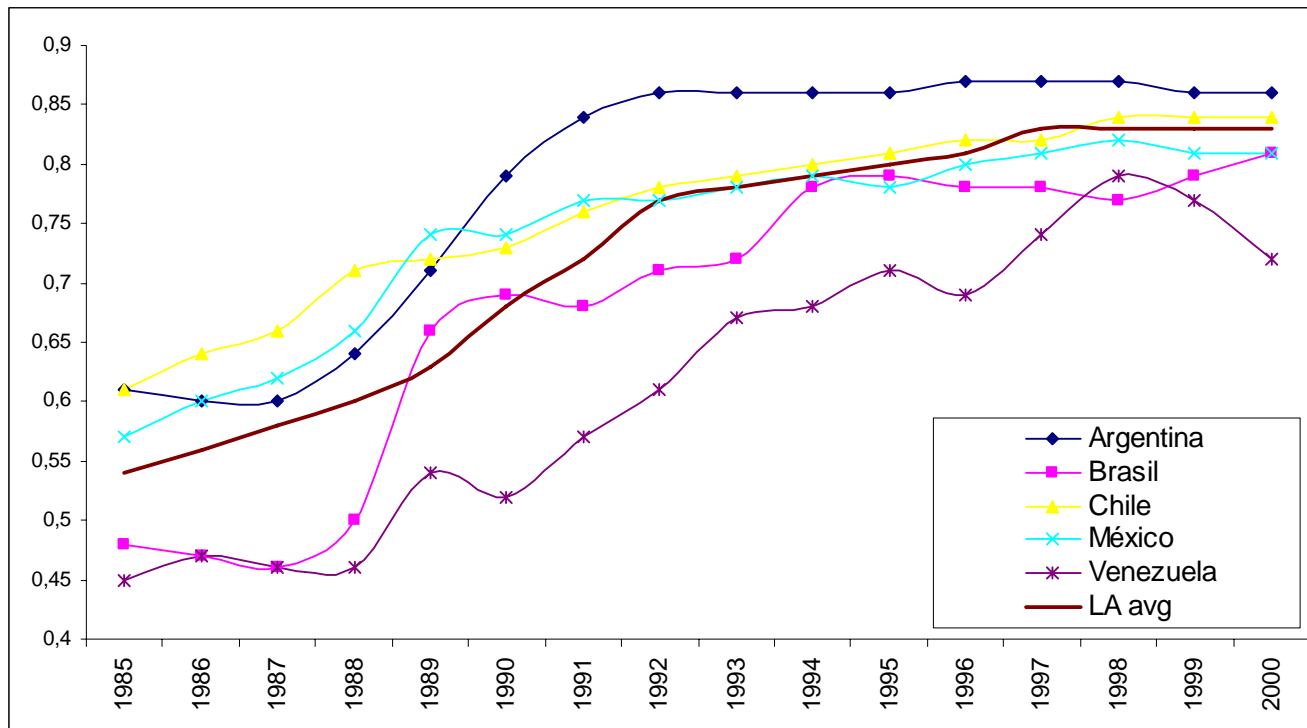
While economic nationalism brought large amounts of public investment, following the debt crisis of the early 1980s, governments and banks were unable to sustain those flows and the key element of growth and development lacking in the development paradigm in Latin America became blatantly obvious: the region had failed to attract foreign investment. Regardless of the country or previous experience, popular consensus (in Latin America and elsewhere) suggests that economic growth is generally preceded by investment. This is especially the case when domestic savings are low, as is the case in all Latin American countries.

The reforms in the 1990s transformed the Latin American political economy into a globally integrated, export-driven liberal economy that welcomed the support of foreign investors and international financial institutions (IFIs). Policies were designed to reverse the effects of

import substitution, and the key components of trade liberalisation and privatisation were geared for local industry development (and international exposure) and foreign investment.

The hype around free market reforms that opened huge industries and markets to international players made Latin America the flavour of the month among investors. Through the privatisation of key strategic industries from mining, oil and hydrocarbons to telecommunications, Latin America became the second largest recipient of FDI in the developing world (after Asia). In the 1990s the region attracted nearly \$400 billion of capital. At its peak, Latin America accounted for over 40% of FDI in the developing world: in 2000 alone it attracted close to \$100 billion. Between 1993 and 1998, seven of the top 15 developing country recipients of FDI were from Latin America.<sup>6</sup>

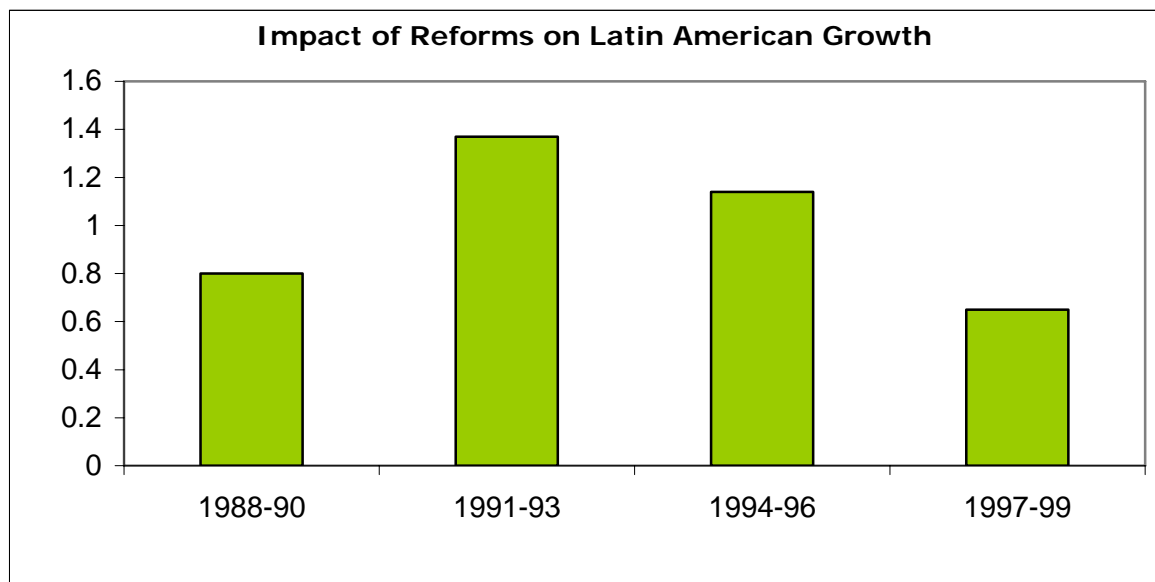
**Structural Economic Reform Index**



Source: Data based on Lora, Eduardo A., Panizza, Ugo G. and Quispe-Agnoli, Myriam, 'Reform Fatigue: Symptoms, Reasons, Implications,' Inter-American Development Bank, October 2003. Available at SSRN: <http://ssrn.com/abstract=472421>

Between 1985 and 2000, a period characterised by the most drastic market reforms, countries across the region underwent varying degrees of economic structural adjustments, which resulted in different outcomes for each. The graph above illustrates – in particular - the general trend of rapid economic reform between 1989 and 1993. Argentina displays the most extreme changes while Chile maintains the most moderate position of the group. Brazil and Venezuela also reflect some drastic economic modifications starting in 1988, and which were retracted somewhat toward the end of the 1990s again. These reforms and the way they were implemented correspond with the varying rates and nature of economic growth across the region.

<sup>6</sup> See Lyal White, 'Why do investors invest? The rationale of South African firms in Latin America', *Brenthurst Discussion Papers*, 1/2007.



Source: Data based on Lora, Eduardo A., Panizza, Ugo G. and Quispe-Agnoli, Myriam, 'Reform Fatigue: Symptoms, Reasons, Implications,' Inter-American Development Bank, October 2003. Available at SSRN: <http://ssrn.com/abstract=472421>

Economically, the region grew moderately through the 1990s, with some countries displaying impressive rates of growth after years of stagnation and decline. Argentina grew by an average of about 5% per year between 1991 and 1996, and Chile averaged 7% for the decade. But growth in some of the larger economies — notably Brazil — was disappointing, and the region failed to realise real economic growth in per capita terms. Despite the 'fever of privatisation' that attracted a huge influx of FDI and granted multinational corporations a large stake in Latin American output, development still evaded the large majority of the countries of the region. With the exception of Chile and, to a lesser degree, Mexico, Colombia and a couple of Central American countries, neo-liberal reforms failed to deliver on the all-important development dimension. Growth, for most parts, was achieved. But this was largely unsustainable and reminiscent of previous growth spurts in Latin America's history, which was exclusionary and intricately intertwined in a political network that contradicted all the virtues of a free market system.

The result was the cyclical behaviour that has come to characterise recent economic history in Latin America. The boom was followed by economic decline (or collapse) coupled with a social backlash bringing down political institutions and demanding a paradigm shift to the other extreme — hence the rise of Hugo Chavez in Venezuela, Evo Morales in Bolivia and, most recently, Rafael Correa in Ecuador, all promising a world of growth and delivery through renewed nationalisation of key industries.

Toward the end of the 1990s and start of the new millennium economies across the region began to stagnate and some slipped into a state of crisis. However, following a crisis in Argentina and Venezuela in 2001–02, the Brazilian 'slow-down' around the same time and Mexico's somewhat disappointing and severely skewed growth over an extended period of time, Latin America seems to be regaining momentum. With renewed international demand growth has bounced back. The economic performance in Latin America is reflecting a positive trajectory. Average growth in the region has exceeded 4% for the past four years and per capita gains have been higher than in previous growth cycles. FDI figures are up and exports are booming. But this growth is based almost entirely on the boom in commodity prices, with countries like Argentina and Venezuela recording double digit growth on the back of high oil and soya bean prices. History has shown that such growth is unsustainable.

FDI is still concentrated in the traditional mining, oil and hydrocarbon sectors. But evidence shows that the historically less risky and more transparent destinations, like Chile, continue to attract a larger proportion of investment relative to the size of their economies. What is more, Chile — and increasingly Colombia — attracts reinvestments, which are drawn to new projects in diversified industries, through targeted guarantees and policy continuity. Colombia, for example, is by far the largest recipient of FDI in the Andean region, where in 2005 it accounted for 65% of the FDI flows in that region.<sup>7</sup>

The cyclical nature of growth and development (or underdevelopment) in Latin America illustrates two important points irrespective of the ideological bent underscoring the nature of reforms. Firstly, a country cannot rely on commodity booms and natural resource endowments for long-term growth. This is shortsighted and clearly unsustainable. It is also inevitably tied to a political agenda where the economic cycles and the political lifespan of individuals simply do not correspond. Secondly, politics and policy matter. Uncertainty around political leadership and policy reform (best illustrated by recent events in Venezuela, Ecuador and Bolivia) does not attract FDI and will dampen economic growth and development. Those countries that demonstrate policy continuity and appoint sensible political leadership seem to be more successful in attracting FDI and achieving regular growth patterns. It is an ongoing process that — as Colombia has shown — does not necessarily require the immediate solving of large and complicated problems, but rather the careful management of difficult issues by a competent and committed leadership willing to engage with local and international economic role players.

### **The Reform Debate and Sources of Disillusion**

*'When things look right but are in fact wrong, the result can be worse than when they are obviously wrong.'*

Alvaro Vargas Llosa, 2005

*'Meant well, tried little, failed much.'*

Anne Krueger, 2004

The debate around economic reform in Latin America has tended to focus on two questions:

- How have the set of reforms implemented in the 1990s contributed toward growth?
- Would state-led growth and the development paradigm have delivered better results?

Unfortunately, the debate has been tainted by ideology and politics, which is no surprise, given the Latin American context and the cyclical nature of economic performance determined throughout history by a political network — be it the state or the economic elite. This has, to some degree, hampered recent studies and research on this issue, which generally seek a more feasible reform agenda that might be better suited and applicable to Latin America by attempting to explain the disappointing post-reform results.

Most experts would agree that Latin America has underperformed. Some even argue that the underlying principles of the Washington Consensus, notably fiscal discipline, privatisation and trade openness, have delivered a poorer set of results than the period of import substitution. For most — regardless of their ideological inclination — the fact that macro-economic stability and openness has not dissipated volatility or contributed in any significant way to development is extremely puzzling.

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<sup>7</sup> Economic Commission for Latin America and the Caribbean (ECLAC), *Investment Report, 2005*.

Studies of economic growth in Latin America have proved that inflated claims of exponential growth as a result of reforms were simply wrong. According to Rodrik, '[t]he take-home message with regard to economic reform is this: the vast majority of growth take-offs are not produced by significant economic reforms, and the vast majority of significant economic reforms do not produce growth take-offs.'<sup>8</sup>

Those countries that have grown substantially and in a sustainable fashion are characterised by deeper underlying factors beyond neo-liberal reforms that have ignited and ensured long-term growth. For one thing, the timing and process of implementation or the way it was enforced has proved to be more significant than the reform itself. Political stability and policy continuity through changing regimes – not to mention a general consensus around the vision and appropriate policies for the country – is all-important.

The success cases of Chile and, to a lesser degree, Colombia and Mexico began their processes of privatisation and global integration far earlier than the rest. Unlike their neighbours around the region, they were not swept away by the euphoria of shedding nationalist and protectionist policies in a powerful symbolic gesture of 'true capitalism'. Instead, their gradual piecemeal methods ensured a more thorough and lasting effect. Reforms in these countries were building blocks that were put in place in tandem with social and political developments in the countries that ensured greater acceptance and even a sense of ownership across society.

By contrast, others in Latin America, particularly Argentina, Bolivia and Venezuela opted for a *Tsunami* set of reforms that were geared for immediate and dramatic market-driven adjustments but were largely unsustainable in their volatile socio-political climates, which have subsequently delivered a backlash that has threatened to take these countries back to where they started: to economic nationalism, the failures of which seem to have been washed away from recent memory.

In general, reforms were most profound in countries that had performed poorly from 1950 to 1980, and less profound in those countries where previous performance did not seem to warrant an urgent need for radical change. This tends to support a point made by Rodrik with reference to growth performers and policies in the global context. Top performers in Asia, from the Asian tigers to the more recent success stories of China and Vietnam, may have become more market-oriented over time, but did not adopt a fixed set of orthodox policies. The successful performers in Latin America followed a similar course and can be distinguished from the others by what appears to be heterodox policies.

Such heterodoxy actually represents clear differences in the timing and nature of implementation of policies. As already mentioned, Chile is the best example of this. The country began a process of market-driven reforms (especially privatisation) under the authoritarian leadership of the Pinochet government in the 1970s, well before the rest of the region. Mexico was the next country to undertake a similar liberalisation process, which, during the 1980s was responsible for 20% of worldwide privatisation. Colombia, which also seems to fall outside of the typical orthodox mould, was never deeply nationalist in its economic policies in the first place and managed to retain moderate growth in the 1980s and 1990s. It opted for a more gradual process of reform.

Apart from this, these countries have also implemented some unique heterodox policies over the years — including capital controls — and in Chile, despite widespread privatisation, the state has retained a 40% stake in the all-important mining industry through Corporacion Nacional del Cobre (Codelco). Against the tide of privatisation that swept across Argentina,

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<sup>8</sup> See Dani Rodrik, 'Rethinking growth policies in the developing world', *Luca d'Agliano Lecture in Development Economics*, Turin, Italy, October 2004.

Peru, Bolivia and Brazil, where large and strategic industries were all privatised and enormous amounts of capital brought in, these heterodox economies — led by Chile — are today the real growth performers in the region.

### **New Consensus, Neo-Liberalism or No Consensus?**

There is no consensus on how to achieve growth and development in Latin America. The old set of reforms, based on the Washington Consensus, provided an important foundation on which to build a successful liberal economy. While regional growth was disappointing, studies show that those countries that liberalised trade and reformed the role of the state grew more than those that did not. Basic principles of macro-economic stability, global integration, property rights and contract enforcement — which were either part of the original Washington Consensus or have been included in the template in recent years — generally make up the foundation of any successful economy.

While the original Washington Consensus has proved to be too rigid for the economies in Latin America, most observers would agree that the only logical alternative to the present economic orthodoxy is one developed from and underpinned by the original list that dates back to a conference in 1989. Rodrik has referred to an 'augmented Washington Consensus' that tops up the original set of reforms with a targeted policy structure that is both dynamic and firmly institutionalised to ensure effective implementation and continuity.<sup>9</sup> It also includes a range of 'soft' issues such as education, health and welfare. But the fact that the list of reforms can extend beyond 10 to 20 or even 30 points to accommodate economic diversity and incorporate the broad range of socio-economic needs makes it both limitless and amorphous, thus detracting from the original motive behind the creation of a list of policy recommendations and reforms in the first place.

Rodrik himself is the most critical of his augmented consensus. The augmented version of the old consensus actually reflects what a developed country already looks like. A country still grappling with development issues and associated social challenges cannot simply create the institutions and targeted policies that the new consensus advocates: such a country simply cannot create what it does not have;<sup>10</sup> it needs the capacity and ability to do so. These attributes, and how certain countries in Latin America have created and developed the basic fundamentals of capacity and ability, is discussed in the following section.

Given the clear lack of consensus as to whether the reforms were correct or incorrect or whether they went too far or were not deep enough — and worked with varying degrees of success across the region — it seems logical to place greater emphasis on country-specific issues.

While Latin American countries have suffered from a number of common problems, and the region has generally underperformed in terms of growth and development, many issues and criteria — particularly the politics of reform — differ substantially from one country to the next. The drawback of such a cross-country approach, which identifies binding constraints that hamper economic growth in specific individual cases, is that it diagnoses the problem and identifies the faults, but does not always provide an appropriate and applicable solution, which is the real challenge. The experience of those success stories in Latin America can provide lessons for others, so long as the reforms and strategies are explained and contextualised in detail, with constant reference to local dynamics, before they can be generalised and connected to broader reforms that were pursued at the same time across the region. After all,

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<sup>9</sup> See Dani Rodrik, 'Goodbye Washington Consensus, Hello Washington confusion?' *Journal of Economic Literature*, Vol. 44, Issue 4, January 2006.

<sup>10</sup> See Rodrik (2004), *ibid.* Also, Murat Iyigun and Dani Rodrik, 'On the Efficacy of Reforms: Policy Tinkering, Institutional Change and Entrepreneurship,' *National Bureau of Economic Research Working Paper 10455*, April 2004.

certain reforms were much more successful in some countries than in others, and these successes have, in recent years, been overshadowed by the policy failures and dramatic crises that have gripped the region.<sup>11</sup>

### **Necessary Attributes and 'Growth Diagnostics'**

Beyond the standard set of orthodox policies and reforms that institute fiscal austerity and drive economic liberalisation, or the new augmented version, which ultimately attracts FDI and stimulates economic growth, there are general attributes and a range of factors or circumstances that have impacted positively on economic growth in certain countries.

The debate around reform has tended to be very broad and even superficial at times, revolving around 'should' or 'could' statements, which are at best academic and lack real-world relevance in the context of country-specific cases. The experience and particular attributes of some countries tend to reveal important explanations and lessons for growth in Latin America.

Larry Summers, former US Treasury Secretary and president of Harvard University, insists that economic growth is determined by a country's ability to integrate with the global economy (and attract trade and investment), the capacity to manage its financial and monetary environment, and the ability to create and maintain institutions that will facilitate and enforce transactions, contracts and other basic commercial rights (like property rights).<sup>12</sup> Rodrik rightly points out that these basic criteria are far from specific policies along the lines of the Washington Consensus, but rather key attributes of *ability* and *capacity* that are embedded or developed in a particular country.

Chile, by far the most successful economy in Latin America, possesses both these attributes.

Apart from the attributes identified by Summers, the case of Colombia, which has enjoyed 5% economic growth from 2002-06 and a relatively stable economy before that — despite an endless conflict fuelled by drugs and a diversity of insurgencies — reflects some interesting lessons for countries in the region and abroad.<sup>13</sup>

Firstly, geography matters. Colombia is blessed with some of the most dramatic terrain and topography on Earth. This has, in the past, hampered the influence and reach of a relatively weak state. Topography is a natural divider. It tends to perpetuate existing divisions in a country like Colombia, which is culturally diverse and in a state of conflict. It needs to be managed effectively to ensure that broad-based society is on board for national priorities, which include anything from security to economic strategy and policy reform. Obviously, smaller and more navigable countries, where the influence of the central government is well rooted, are far easier to manage and direct in terms of national issues and policies.

Secondly, politics and policy are all-important. Experience shows that while a rich endowment of natural resources and favourable commodity prices do attract capital and boost exports, growth based on uncontrollable exogenous factors like commodity prices is unsustainable. Unlike the rest of the region, where economies are booming as a result of price surges in oil or agricultural commodities, growth in Chile and Colombia is based more on a range of different factors, which include favourable policies that combine investment security and incentives for

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<sup>11</sup> See Jeromin Zettlemeyer, 'Growth and reforms in Latin America: A survey of facts and arguments', *IMF Working Paper 06/210*, September 2006.

<sup>12</sup> See Larry Summers, 'Globalisation and American Interests.' *Godkin Lectures*, John F. Kennedy School of Government, Harvard University, 7 April 2003.

<sup>13</sup> See Greg Mills & Lyal White, 'Killing Pablo's Image: Security and State-Building in Colombia,' *RUSI Journal*, Vol. 152, No. 1, February 2007.

new projects in 'non-traditional' sectors. Beyond politics and policy, both Chile and Colombia have recognised the need to build legitimate state institutions that instil confidence in the country (especially given the adverse situation in Colombia). These institutions encourage investment and commercial exchanges in the country by securing property and contractual rights and through general macro- and micro-economic management capabilities. Simply, they provide the necessary guarantees that foreign investors require.

Thirdly, the influence of drugs and other contraband items (arms, etc.) corrodes government and hampers real economic progress in a country. These elements tend to hamstring legitimate economic growth and prosperity by crowding out business and tainting the image of the country abroad. Despite the progress made in Colombia, the joint stigma of drugs and criminal activity is still the common perception of the country around the world. This is out of kilter with the real situation in Colombia, which is today one of the most vibrant and sophisticated economies in the region. But it will take years of national marketing abroad and unwavering progress in the country to alter this perception and rectify the psychological drawback of the current image of Colombia.

Fourthly, leadership matters. This is a factor that resonates in Latin America, where the best performers seem to have been blessed with solid and sensible leadership. In the case of Chile, President Ricardo Lagos' vision has ensured sustainable growth and progress in the country despite a divergent social agenda and challenging regional dynamics during his time in office. President Alvaro Uribe of Colombia is probably the best recent example of the difference that good leadership can make to the progress of a country. His style of leading from the front has set a precedent in Colombia, where he has prioritised security through a process of nation building. Even his staunchest critics agree that he has managed to bring the country together and created a sense of social cohesion that has been essential for the progress and economic continuity of Colombia. By effectively managing a traditionally adverse environment — addressing perceived key issues and seeking immediate results — Uribe and his government have created an economy conducive to foreign investment and growth.

Fifthly, security counts. Underdevelopment breeds insecurity; and insecurity tends to perpetuate underdevelopment. Most Latin American countries are plagued with varying degrees of insecurity. This, in most cases, is a problem that is very difficult to solve, especially in the short to medium term. Colombia (under Uribe) has demonstrated that so long as the problematic situation is effectively managed, and not necessarily resolved, economic interest in the country can still be generated.

Finally, relations with Washington are important. This tends to contradict the current trend in Latin America, where most countries have subscribed to one-time Mexican president Porfirio Diaz's famous statement: 'Poor Mexico, so far from God and so close to the United States.' Yet in Latin America, anti-Americanism and strained relations with the United States have generally been to the detriment of economic growth in the region.

The United States is the largest and most active economic partner to Latin America. It is the largest contributor of aid and investment to the region and the number one trading partner with most individual countries in Latin America. Despite widespread criticism of the various bilateral trade agreements the United States has signed with countries around the region, evidence shows that each agreement has delivered favourable growth in trade and economic benefits for those countries that have entered into such agreements with the United States. Officials in Colombia, for example, expect the recently signed free trade agreement (FTA) to increase the annual GDP growth of the country by two percentage points. The associated sentiment and confidence around an FTA with the United States also adds a positive impression for investors and IFIs.

Countries that have shared a long, healthy relationship with the United States have generally enjoyed longer, more sustainable periods of growth. This is evident, once again, in the cases of Chile, Colombia and Mexico, which have a close economic engagement with the United States, but still retain independent and sometimes opposing views in multilateral forums. Meanwhile, countries like Argentina, Bolivia, Ecuador and Venezuela have bounced from one extreme to the other in their ties with the United States over the last 15 years, which matches the economic volatility that has prevailed in these countries during that time. It seems that an engaging relationship of open dialogue with a healthy and balanced economic exchange is far better than one that is confrontational and divisive.

The core attributes highlighted by Summers seem to resonate through all six points above. President Lagos of Chile, who was in office from 2000 to 2006 and is widely regarded as one of the most successful Latin American presidents of all time, emphasises two important prerequisites for growth: FDI and capacity. From Lagos' perspective, economies (like Chile and other Latin American countries) must grow for the sake of democracy. Growth and development help galvanise democracy. Capacity building is essential and should be directed toward core problems in Latin American countries: public goods and service delivery.

These are points of discussion that are often, at best, academic. But leaders like Lagos and Uribe have proved that, apart from reforms, if basic principles are followed and the abilities and capacities of individual countries are developed and used effectively, economic growth and development are not only possible, but also sustainable.

### **Conclusion: Making it happen, letting it happen, or wondering what happened?**

With the exception of two or three outlying economies, Latin America has underperformed for the last 30 years. Growth and development have been disappointing. The only general consensus around appropriate reforms in Latin America is that there is no consensus. This paper does, however, reveal some important points and issues that individual economies should take cognisance of in their particular growth strategies.

Firstly, while broad-brush reforms have failed to deliver adequately in Latin America, there is a standard set of fundamentals, like macro-economic stabilisation and market liberalisation, that all successful economies have adhered to.

Secondly, the politics of policy and reform should never be underestimated. This also applies to the ideology and rationale behind general policy trends witnessed in Latin America. Despite the lacklustre performance across the region after reforms were implemented, economic nationalism is no better alternative. Nowhere in the world has the nationalisation of strategic industries generated a higher output that has benefited the economy. To ensure these industries operate efficiently, ongoing investment and innovation are essential. This is only available through FDI.

Thirdly, leadership has proved to be a key ingredient for growth in Latin America. This, for most parts, is a highly subjective 'black-box' issue. But generally, a sensible and committed leadership with a clear vision that extends beyond the political lifespan of the office bearer does contribute toward a positive trajectory.

Fourthly, country-specific strategies that appear to be more heterodox — due to timing and style of implementation — seem to have been more successful than perceived orthodoxy. Early reformers that initiated and sustained a gradual and multi-phased process have achieved higher long-term growth.

Fifthly, the attributes of ability and capacity are important prerequisites for growth and development. This relates to a country's institutions and how they facilitate and enforce broader policy reforms and commercial activities.

Finally, social cohesion and effective management of key issues or problems that may hamper economic activity and growth have proved to be far more relevant than initially anticipated in Latin America. Problems do not necessarily have to be solved. If they are managed appropriately and there is a clear perception of government control and stability, investors will come and the economy will continue to thrive even in the face of adversity. Successful economies in Latin America have all addressed pressing issues through social cohesion and a broader agenda of nation building. This sense of common purpose and ownership greatly assists the state in the management of core problems and allows for the easy implementation of new policies.

The words of Ronald Reagan resonate in the context of growth, reform and development in Latin America: 'There are those who make it happen, those who let it happen and those who wonder what happened!' In Latin America, growth and development have come to those who have internalised the various exogenous factors. In other words, the real performers have not waited around for outside forces — whether they be markets or lending agencies — to offer a helping hand. These countries leave little to chance and avoid blaming external trends and players for poor results. The high growth performers have taken hold of their own destinies.

## APPENDIX: ECONOMIC GROWTH AND PERFORMANCE IN LATIN AMERICA

### LATIN AMERICAN AND THE CARIBBEAN: GROSS DOMESTIC PRODUCT, AT CONSTANT MARKET PRICES

(Millions of dollars at constant 2000 prices)

Country	1995	2000	2001	2002	2003	2004
Antigua and Barbuda	538.7	665.3	680.5	700.9	733.9	772
Argentina	250382.8	284345.9	271809.2	242197.4	263599.6	287401.7
Bahamas	4040.1	5003.7	5044	5148.7	5233.3	5328.3
Barbados	1492.8	1758.9	1713.2	1712.2	1755.9	1839.7
Belize	621.8	832.4	870.8	911.9	995.5	1041.3
Bolivia	7091.1	8379.9	8539.3	8747.5	8990.6	9312.7
Brazil	539057.6	601732.7	609615.4	621381	624736.4	655348.5
Chile	61347.7	75197	77736.4	79434.3	82545.6	87633.3
Colombia	80029.5	83766.6	84999.2	86642.8	89985.3	94283
Costa Rica	12536.4	15946.5	16118.5	16584.8	17646.5	18377.5
Cuba	22537.8	28206	29042.7	29488.5	30357.6	31729.5
Dominica	207	230.2	220.6	209.4	209.6	216.2
Ecuador	15202.7	15933.7	16784.1	17496.7	18131.9	19518.4
El Salvador	11298.8	13134.1	13358.6	13671.3	13985.7	14242.2
Grenada	299.1	409.6	398.4	391.1	420.5	407.9
Guatemala	15890.9	19288.9	19738.7	20182.7	20613.1	21162.1
Guyana	517.6	592.5	606	612.8	608.9	618.5
Haiti	3236.3	3664.5	3626.2	3617.1	3630.2	3502.4
Honduras	5189.1	6024.7	6181.6	6349.6	6570.5	6900.7
Jamaica	7402.2	7374.1	7486.4	7569.1	7740	7812.7
Mexico	445336	580791.4	580600.8	585082.7	593216.9	617901.7
Nicaragua	3082.2	3938.1	4054.7	4085.2	4188.2	4403.6
Panama	9266.4	11620.6	11687.3	11947.8	12450.3	13391.6
Paraguay	7164.3	7095.3	7241.7	7238.2	7516.1	7826.9
Peru	47170.5	53335.5	53448.7	56204.8	58397.2	61445.1
Dominican Republic	16270.3	23416.5	23954	25159.6	25058.5	25728.2
Saint Kitts and Nevis	263.2	329.2	337.8	351.1	365.6	385.2
Saint Vincent and the Grenadines	287.4	335	337.8	351.1	365.6	385.2
Saint Lucia	594.4	684.7	619.2	631.3	658.6	682.5
Suriname	716.3	774.6	820.3	836.1	887	955.2
Trinidad and Tobago	5665.9	8154.3	8494.2	9167.1	10394.9	11071.1
Uruguay	18092.3	20085.5	19405.6	17264.8	17640.3	19725.4
Venezuela(Bolivarian Republic of)	112851.4	117147.6	121123.9	110397.6	101878.3	120068.3
Latin America and the Caribbean*	1683142.7	1972007.6	1977642.3	1962285.3	2001131.2	2119672.7
Latin America**	1660496.1	1944863	1950024	1933685.9	1970781.3	2088173.4
Caribbean***	22646.6	27144.6	27618.3	28599.4	30350	31499.3

\* The calculation does not include Cuba, but does include the GDP of Guatemala

\*\* The calculation does not include Cuba

\*\*\* Includes the sum of GDP at basic prices for Barbados, Dominica, Guyana & Jamaica

Source: The Economic Commission for Latin America and the Caribbean  
(www.eclac.cl)

**LATIN AMERICAN AND THE CARIBBEAN:  
GROWTH RATES OF GROSS DOMESTIC PRODUCT**

<b>Country</b>	<b>1995</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
Antigua and Barbuda	-5.0	1.5	2.3	3.0	4.7	5.2	5.6
Argentina	-2.8	-0.8	-4.4	-10.9	8.8	9.0	9.2
Bahamas	4.4	1.9	0.8	2.3	1.4	1.8	2.7
Barbados	2.4	2.3	-2.6	0.5	2.0	4.8	3.9
Belize	0.7	13.0	4.6	4.7	9.2	4.6	3.1
Bolivia	4.7	2.5	1.7	2.4	2.8	3.6	4.1
Brazil	4.2	4.4	1.3	1.9	0.5	4.9	2.4
Chile	10.6	4.5	3.4	2.2	3.9	6.2	6.3
Colombia	5.2	2.9	1.5	1.9	3.9	4.8	5.1
Costa Rica	3.9	1.8	1.1	2.9	6.4	4.1	5.9
Cuba	2.5	6.1	3.0	1.5	2.9	4.5	
Dominica	1.6	1.3	-4.2	-5.1	0.1	3.1	3.6
Ecuador	1.7	2.8	5.3	4.2	3.6	7.6	3.9
El Salvador	6.4	2.2	1.7	2.3	2.3	1.8	2.8
Grenada	3.2	7.0	-4.9	0.4	7.5	-3.0	5.2
Guatemala	4.9	3.6	2.3	2.3	2.1	2.7	3.2
Guyana	5.1	-1.4	2.3	1.1	-0.7	1.6	-3.0
Haiti	9.9	0.9	-1.0	-0.3	0.4	-3.5	1.8
Honduras	4.1	5.7	2.6	2.7	3.5	5.0	4.1
Jamaica	2.6	0.7	1.5	1.1	2.3	0.9	1.4
Mexico	-6.2	6.6		0.8	1.4	4.2	3.0
Nicaragua	5.9	4.1	3.0	0.8	2.5	5.1	4.0
Panama	1.8	2.7	0.6	2.2	4.2	7.6	6.4
Paraguay	5.5	-3.3	2.1		3.8	4.1	2.9
Peru	8.6	3.0	0.2	5.2	3.9	5.2	6.5
Dominican Republic	5.9	7.9	2.3	5.0	-0.4	2.7	9.2
Saint Kitts and Nevis	3.6	4.3	2.0	1.0	2.2	6.5	7.0
Saint Vincent and the Grenadines	8.3	1.8	0.8	3.9	4.1	5.4	2.8
Saint Lucia	2.3	3.6	-9.6	1.9	4.4	3.6	7.3
Suriname	2.8	4.0	5.9	1.9	6.1	7.7	5.7
Trinidad and Tobago	4.0	6.9	4.2	7.9	13.4	6.5	7.0
Uruguay	-1.4	-1.4	-3.4	-11.0	2.2	11.8	6.6
Venezuela (Bolivarian Republic of)	4.0	3.7	3.4	-8.9	-7.7	17.9	9.3
<b>Latin America and the Caribbean*</b>	<b>0.5</b>	<b>3.9</b>	<b>0.3</b>	<b>-0.8</b>	<b>2.0</b>	<b>5.9</b>	<b>4.5</b>
<b>Latin America**</b>	<b>0.4</b>	<b>4.0</b>	<b>0.3</b>	<b>-0.8</b>	<b>1.9</b>	<b>6.0</b>	<b>4.5</b>
<b>Caribbean***</b>	<b>3.1</b>	<b>3.5</b>	<b>1.7</b>	<b>3.6</b>	<b>6.1</b>	<b>3.8</b>	<b>4.2</b>

\* Preliminary figures

\*\*The calculation does not include Cuba, but does include the sum of GDP at basic prices for Barbados, Dominican, Guyana & Jamaica

\*\*\*Includes the sum of GDP at basic prices for Barbados, Dominican, Guyana and Jamaica

Source: The Economic Commission for Latin America and the Caribbean (www.eclac.cl)