Protecting the gains of recent years

By PAMELA COX
Regional Vice President, Latin America and the Caribbean, The World Bank

PAMELA COX has been the Vice President for Latin America and the Caribbean since 2005. During the early years of her career in the Bank, Ms Cox was an economist working on agricultural and environmental issues in Africa, South Asia and Latin America. She holds a PhD in Development Economics and Policy from the Fletcher School at Tufts University, an MA in Law and Diplomacy, Development Economics, and a BA in International Studies/ International Economics from Reed College.

In the midst of the most severe global economic and financial crisis in decades, new opportunities are emerging to reshape relations between countries in the Americas towards common interests, and new partnerships (clean energy, trade, science and technology), that could contribute to a more inclusive and sustainable path to economic recovery. To put this process in motion we must at the outset recognise that there will be no solution to this global economic crisis if the point of view and concerns of developing countries, including Latin American and Caribbean nations, are not taken into account.

The problems we are confronting now are very different from those of the past. The global economy is likely to shrink this year for the first time since World War II. World Bank forecasts show that global industrial production by the middle of 2009 could be as much as 15 per cent lower than levels in 2008. World trade is on track in 2009 to record its largest decline in 80 years.

The financial crisis will have long-term implications for developing countries. Debt issuance by high-income countries is projected to increase dramatically, crowding out many developing country borrowers, both private and public. Many institutions that have provided financial intermediation for developing countries have virtually disappeared. Developing countries that can still access financial markets face higher borrowing costs and lower capital flows, leading to weaker investment and slower growth in the future. It is not clear when and how we will emerge from the current crisis. And it is not entirely clear how this will reshape the global economy. But one emerging trend is an increased reliance on the state in ways unthinkable only a few years ago.

Global Crisis, Global Response

The time when global agreements could be negotiated among a few rich countries is over. The G20 leaders have agreed that emerging and developing country economies need to have a seat at the table together with developed countries, as all countries must work together to meet this unprecedented crisis. As World Bank President Robert Zoellick recently said: "A more flexible and broadly representative multilateral group is needed to coordinate the crisis response. Sustainable and inclusive globalisation is key – without it, our world will remain unstable, despite financial rescue packages."

Regional powerhouses such as Brazil and Mexico are prepared to respond as responsible global stakeholders in the design of a new global financial architecture. The global community will also benefit from the knowledge of financial regulators who have made large strides in improving supervision and regulation in these countries and have learned the lessons from past crises.

Clearly, opportunities to advance a common hemispheric agenda will be affected by the current economic circumstances. That is the main concern of the regional leadership and as Brazilian President, Luis Inácio Lula da Silva, has indicated the best thing the US could do for Latin America today is to put its own economic house in order. Success in the fiscal stimulus in the US may help the region recover from the current downturn. Unfortunately for Latin America and the Caribbean, this crisis has brought to a screeching halt more than five years of sustained economic growth – averaging 5.3 per cent per year – fuelled in part by the adoption of responsible macro and fiscal policies and also by a favourable global context characterised by a boom in commodity prices.

Unlike past crises, today the effects are being mostly transmitted through the real not the financial sector. Latin America is not the epicentre of the crisis; on the contrary, the Region is a victim of the global shock. And although the situation is changing rapidly, the financial sectors in most countries in the Region met this crisis on solid ground thanks to the tightening of financial regulation and supervision during the last decade.

However, we are already seeing economies stalling and unemployment increasing. In September 2008 the consensus forecast for Latin America and the Caribbean was 3.7 per cent growth for 2009. Projections are now a moving target. By January 2009 the expectation was 1 per cent growth for 2009. More recently, the consensus forecast dropped to an anemic 0.3 per cent, aligned with downward revisions of global growth. While in the period 2002-07, Latin America managed to lift 52 million people out of poverty, this trend is now in danger of being reversed. World Bank projections indicate that 4 million people in the Region could fall into poverty by the end of 2009 as a result of the impact of the global crisis.

New Opportunities to Protect Social Gains

The challenge for the Region is how to manage the short-term difficulties of the crisis while also maintaining conditions for long-term growth.

The current global financial crisis must not become a human and social crisis, and therefore, timely and decisive actions are imperative to protect the social gains made in recent years.

But this crisis can also be an opportunity to lay the groundwork for a sustainable recovery and growth through increased competitiveness. The structural challenges Latin America faced before the crisis, including the critical need for increased investments in education and infrastructure, can start to be addressed through the fiscal stimulus packages being put in place in several countries. What can governments with the support of multilateral organisations do under these extraordinary circumstances?

There are at least five key areas for action:

• Support for the most vulnerable

The region is already moving ahead with well targeted support to the most vulnerable through social protection packages to ensure broad access to health insurance services, protect public spending on key areas such as nutrition and vaccines, and provide additional targeted cash support.

Many countries in the Region already have well targeted social protection networks, such as in Brazil (Bolsa Familia), in Mexico (Oportunidades) as well as similar programmes in El Salvador, Panama, Jamaica, and Colombia, among others. These programmes are now being expanded to mitigate some of the worst effects of the economic slowdown that are yet to come. The World Bank has actively supported targeted social programmes in the past. This calendar year we will provide over US$2 billion (bn) to implement conditional cash transfers programmes in the region. But these programmes alone will not be enough; a broader social safety net may be needed as the crisis deepens, focusing on additional measures.

• Targeted stimulus spending

Where savings or borrowing from multilaterals permit, well-designed increases in expenditure (fiscal stimulus packages) may be appropriate, investing in human and physical capital while boosting domestic demand. Multi-billion stimulus packages have been set in motion in Argentina, Brazil, Peru, Mexico and Chile among others, with the objective of investing in infrastructure, protecting jobs, facilitating credit and promoting consumer spending.

These programmes can link short-term gains such as employment opportunities and increased consumption, with long-term perspectives such as positioning countries for a larger presence in world markets through sustained investments in infrastructure, trade facilitation, quality of education, and logistics. The World Bank is supporting these programmes either through development policy lending or through direct investments.

• Job creation and public works programmes

We are also moving ahead in supporting initiatives to create jobs through public works programmes, programmes boosting microcredit and self-employment and small enterprise development among others. Together with retraining and training programmes for the unemployed and wage and employment subsidies, these measures will have not only a direct human effect but will contribute to the economic recovery.

• Better resource allocation, reforming universal subsidies

Crises often present opportunities to deal with ‘sacred

The challenge for the Region is how to manage the short-term difficulties of the crisis while also maintaining conditions for long-term growth

Photograph: Tomas Sennett/ World Bank

Tough times for the transportation sector: world trade is on track in 2009 to record its largest decline in 80 years

The best thing the US could do for Latin America today is to put its own economic house in order

cows'. Countries in the region could take advantage of the present crisis to review policies on 'universal subsidies,' which are subsidies that are going not only to the poor but to the middle class, and to a large degree, to the well-off. An overhaul of subsidies in many countries could result in substantial savings that could then be used for targeted safety net programmes and economic stimulus. The region annually spends between five and 10 per cent of GDP on subsidies. Approximately one third of this is captured by the top income earning 20 per cent of the population. This would be enough to triple (or more) direct transfer programmes for the poor.

• Restoring global trade

Countries in the Americas are still committed to open trade and the April Summit of the Americas is an excellent opportunity to reconcile global and regional interests with the common goal of expanding economic relations that are mutually beneficial for all countries. Positive movements on the Doha trade negotiations by major stakeholders are key to restore confidence in global free trade. A revival of protectionism would not only jeopardise global recovery but result in an unbearable burden for developing countries. Through our private sector arm, the International Finance Corporation (IFC), we are putting in place trade finance lines to help keep trade moving.

A Multilateral Response

We are using all of our resources – financing, hedging products and guarantees, knowledge services, and partnerships – to mobilise rapid assistance. In this crisis, all the multilaterals – the World Bank and regional banks – must play a coordinated counter-cyclical role to provide funding as other sources of financing dry up.

Consistent with such counter-cyclical approach, we are increasing financial support throughout the developing world, including lending for middle income countries through IBRD (US$100 bn total from 2009-11), grants and concessional lending for low income nations (through the US$42 bn of IDA Fund) and loans for the private sector through the International Finance Corporation (IFC).

One of the new financial products developed to better serve the needs of middle income countries is a committed credit line – the so-called Deferred Drawdown Option (DDO) – which provided an immediate source of liquidity to several Latin American countries – Colombia, Mexico, El Salvador and Uruguay, among others – to respond to shocks. The DDO reflects the commitment of the World Bank to assist governments in providing positive markets signals by creating a preventive source of financing. In Latin America, the Bank is responding rapidly to the region's demands. We expect to make a total of US$13 bn for the fiscal year ending June 2009. These additional resources are critical to sustain jobs and social gains, boost ongoing public sector programmes and inject liquidity into countries where needed. As the crisis evolves, we will continue to provide timely and rapid support tailored to country needs.

This is a time to act and responsible leadership is crucial. With the same strong leadership that made possible the robust growth and the social progress achieved in recent years, Latin America will be part of the global solution, aimed at creating a global fair environment that provides opportunities for all. A stronger partnership in the Western Hemisphere will facilitate that process. F

Photograph: Alejandro Lipszyc/ World Bank

Support for the most vulnerable: the region is taking steps to protect public spending on key areas such as nutrition and vaccines