

# The crisis opportunity for LAC

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**LUIS ALBERTO MORENO** was elected president of the Inter-American Development Bank on 27th July 2005 and took office on 1st October the same year. Before joining the IDB, Mr Moreno served as Colombia's Ambassador to the United States for seven years, prior to which he had a distinguished career in both the public and private sectors in Colombia. Throughout his career, Mr Moreno has received some of the highest decorations and distinctions awarded by the Colombian state and the country's private sector.

**T**he Summit of the Americas in Trinidad and Tobago comes at a time when the world economy is suffering its worst downturn in decades. But crises also breed opportunities: if our countries act boldly and in concert, we have a chance to lay the groundwork for a strong recovery and a more broadly shared prosperity.

Latin America and the Caribbean did well in recent years. Nearly 48 million people – more than the sum of the population of Ecuador and Peru – emerged from poverty since 2003, when the region began a period of robust growth.

Right now, the top priority is to protect those gains. More than 190 million people in Latin America and the Caribbean live in poverty, including 65 million who are extremely poor. Due to the current crisis, these numbers are likely to rise.

Our countries face many other persistent challenges that cannot wait for better times. 1 in 12 children below the age of five is underweight. More than half of the region's workers toil in the informal sector, with precarious access to social safety nets. One-third of the rural population lacks access to safe water. And we need to generate vast amounts of additional energy to fuel growth.

## The lean years

Until a few months ago, most Latin American and Caribbean economies were enjoying a bonanza underpinned by sound economic policies at home and strong international demand for our traditional exports. International reserves had risen to a US\$400 billion. Public debt, measured as a proportion of GDP in the region, dropped to 35 per cent in 2007 from 51 per cent in 2003.

This year the global economy is likely to shrink. Commodity prices have plummeted. And private capital inflows have largely dried up. Our countries will not be able to export their way out of this crisis, as they did in the late 1990s. Growth rates will be the lowest since 2002. Tax revenue will decline and many investment projects will be either cancelled or postponed. We can expect higher unemployment. Even remittances, a vital source of income for millions of families in our region, are likely to decline for the first time since we started tracking these flows in 2000.

Despite these grim conditions, the outlook is not catastrophic. We are not facing a generalised

breakdown like in the early 1980s, when Latin America stumbled into a 'lost decade'. Fiscal and monetary management has improved in many countries. Some financial institutions may come under stress but the region's banking systems are relatively healthy, thanks to the hard lessons learned from 31 banking crises in the past quarter century.

Countries that were more cautious with their public money during the good times, such as Chile, are in a better position. Others will have a harder time obtaining resources to soften the impact of the downturn.

With budgets tightening, governments must use money wisely. The IDB considers conditional cash transfer programmes – in which poor families get subsidies if they keep their children in school and take them to regular medical checkups – an effective way to ensure that transfers go to the right households. So far, 15 countries in our region have such programmes, many of which receive IDB support.

Governments will also have to find new ways to attract investments to strategic sectors such as transportation, water and sanitation. Such spending will not only prop up employment but also improve the quality of life of millions and prepare our economies for a stronger recovery. A recent IDB study of nine Latin American nations showed that a 10 per cent reduction in transportation costs can help boost exports by 39 per cent.

To achieve the UN Millennium Development Goal on clean water, by 2015 Latin America needs to provide water access to 40 million individuals and sanitation to 60 million. This will require US\$30 billion, while providing universal coverage of both services would push the bill to US\$50 billion.

The IDB is already lending close to US\$1 billion per year to help close this service gap in Latin America and the Caribbean. Last year, our efforts in this sector received a major vote of confidence when the government of Spain asked us to manage US\$400 million in grants to help improve water and sanitation services in poor communities. Over the next four years, the IDB and Spain could direct as much as US\$5 billion to projects in this crucial sector.

Above all, during these trying times we must resist the temptation of closing our economies. More integration and trade with our neighbours and with the rest of the world will help increase our economic efficiency, boost growth and, ultimately, reduce poverty.

### Beyond the crisis

Over the next decade Latin America and the Caribbean will have to deal forcefully with structural shortcomings that hamper productivity and perpetuate inequality. At the same time, we need to foster the kind of growth that will protect the environment.

Improving the quality of education remains one of the biggest challenges. Our countries have succeeded in expanding school enrolment and closing the gender gap that long characterised our region's education. But graduating students still underperform in reading, writing and maths. This will only deny them opportunities to get ahead.

The world's most dynamic economies are the ones that foster scientific and technological breakthroughs or are quick to adopt their benefits. As a region, Latin America and the Caribbean apportion less than one per cent of GDP to science and technology research and development. South Korea alone invests more than all Latin American nations combined. China has twice as many investigators as Latin America in per capita terms. These gaps will make it hard for us to keep up in a competitive world.

Our region's energy needs – a key issue on the agenda for the Summit in Port of Spain – are expected to grow 75 per cent through 2030. Such an expansion would require investments of more than US\$1.6 trillion. Mexico alone will have to spend US\$5.5 billion a year to keep up with demand over the next five years.

We need more energy, but we have to produce it in sustainable ways. Today, Latin America produces about a quarter of its energy using renewable sources. Given the region's comparative advantage, this could increase to nearly 47 per cent by 2030. Much of the work to be done now is technical in nature. In Panama, the IDB is helping draw up wind maps. In Chile, we are underwriting feasibility studies on harnessing the power of sea currents to generate electricity.

Biofuels fell somewhat out of favour following last year's spike in food prices. But Latin America and the Caribbean already are big producers of ethanol. They also are in a unique position to expand output without affecting food supplies or contributing to global warming or deforestation. The IDB is helping 10 countries in the region draft national biofuels action plans.

The cleanest energy is not generated but saved. A 10 per cent reduction in energy consumption would save our 26 borrowing member countries a whopping US\$36 billion in investments by 2018.

To help understand how countries can transition to low-carbon economies, we are funding studies on the impact of climate change in Mexico, Colombia and Peru at a national level, and in the Caribbean, Central America and South America at a regional level. Over the next decade, governments will have to show leadership

by drafting regulatory frameworks that promote renewable energy, reduce fossil fuel consumption and provide incentives for the private sector to invest in and adopt cleaner technologies. Multilateral institutions can help fund the costly switch from a business-as-usual model to a low-carbon one.

### Pragmatism required

The best approach to tackle these challenges is to deepen cooperation among our countries. It is not a matter of either public or private concern; joint, concerted action is the best response. These are also times for multilateral actions, in which institutions like the IDB need to fill the funding gap caused by the crisis.

As the leading source of development financing in the region, the IDB can act as an honest broker between players that have often had an uneasy relationship. Sometimes the IDB's participation in a project serves as a catalyst to attract more resources. On other occasions, we step in when there is a need to make an indispensable investment that does not provide an adequate return for a private actor.

Given the magnitude of the task ahead, there is only so much the IDB can do. That is why we are in discussions with our shareholders to find ways to increase our lending capacity. Improving Latin America and the Caribbean's access to international capital markets or expanding its domestic financial systems is not incompatible with boosting the wherewithal of multilateral banks. By definition, our lending should increase in difficult times, ensuring that key investments are made when the social return is high.

The current crisis is an opportunity for our governments to make tough but correct decisions – choices that may help put an end to inequality and exclusion in our region within our lifetimes. **E**

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An aid worker hands out nutrition packages under Mexico's *Oportunidades* conditional cash transfer programme

