Half a Century of Deep Economic Transformations in Latin America

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The half century that has passed since the creation of LASA has been one of deep economic transformations in Latin America. In 1966, the region was in the midst of a rapid industrialization process and about to experience its fastest rate of growth in history in 1967–1974 (6.7 percent per year). The industrialization model was already undergoing significant changes since the early 1960s, particularly the decision of most countries to mix import substitution with export diversification and regional economic integration. The combination of these strategies, which was behind the 1967–1974 boom, is why the term “state-led industrialization” captures much better the nature of the development process under way at the time than the usual term “import-substitution industrialization.” Growth continued until the end of the 1970s, supported by high commodity prices and access to external financing on a scale that the region had not known since the 1920s, thanks to the recycling of petrodollars from the oil price rises of 1973 and 1979. This was, however, the prelude to Latin America’s worst economic crisis of the twentieth century: the debt crisis of the 1980s that led to Latin America’s “lost decade,” when in most countries of the region foreign capital flows ceased, growth stagnated, and unemployment soared, and five of them experienced hyperinflation.

There have been intense debates about why the debt crisis was so strong. One hypothesis is that this was the result of the distortions generated by high levels of state intervention and the macroeconomic instability that characterized the industrialization process. However, this interpretation is not convincing. The levels of state intervention in Latin America were actually weaker on average than those of other developing countries. Moreover, the countries undergoing market reforms—trade liberalization, privatization of state enterprises, and deregulation of the financial sector—in the second half of the 1970s, those of the Southern Cone, were actually more affected by the debt crisis, notably in the scale of their domestic financial crises. Chile, the market-reform poster child, suffered a 16 percent decline in its GDP between 1981 and 1983. Lack of macroeconomic discipline, particularly large public sector budget deficits, did spread prior to the debt crisis, but this had not been a general trend in the region during state-led industrialization, except in the Southern Cone and Brazil. A more persuasive interpretation is that Latin America once again became a victim of boom-bust cycles of finance, an experience that had been familiar in the past (the last time in the 1920s–1930s) and has continued to be frequent in recent decades. The unfortunate management of the crisis by international financial institutions—the International Monetary Fund and the World Bank—was also a major reason for the depth of the crisis, particularly because of their initial diagnosis that the crisis was only a temporary phenomenon and their stubborn decision later on to exclude any write-off of the debt as part of the recovery package. This was only done seven years after the outbreak of the crisis, with the 1989 Brady Plan, which provided a moderate reduction in debts and played an important role in putting an end to the “lost decade.”

Market reforms that reduced the state role in the economy have spread throughout the region since the mid-1980s, under strong pressure by international financial institutions, but also as a result of changes in the balance of the economic debate and the power relations generated by the crisis. Most countries, therefore, followed the path set by the Southern Cone, notably Chile, in the 1970s. There were, however,
differences associated with national politics in the midst of the democratic wave that Latin America experienced during the 1980s and 1990s. The major expectation of market reformers was that less government intervention and stronger participation in the global economy would lead not only to a short-term economic revival but actually to faster long-term economic growth.

That expectation was entirely frustrated. This was so despite the fact that reforms did lead to an increase of Latin America’s share in world trade and attracted significant levels of foreign direct investment. Economic growth settled on an average rate of 3.1 percent in 1990–2015, just above half of that achieved in 1950–1980, when Latin America grew at 5.5 percent a year. The slowdown was particularly strong in the two largest economies: Brazil slowed from 7.0 percent in 1950–1980 to 2.6 percent in 1950–2015, and Mexico from 6.6 percent to 2.7 percent. The only exception to slow growth since 1990 has been the 2003–2008 quinquennium, when GDP grew at 5.1 percent per year thanks to massive positive external shocks: rapid growth of international trade, booming commodity prices, the best access to external financing since the 1970s, and rising migrants’ remittances. In contrast to what some have argued, this is not true for the 2003–2013 decade as a whole, as growth came down again in 2008–2013 to rates that were close to the mediocre average of the last quarter century. As a result of its slow growth, Latin America’s share in the global GDP, which had increased from 5.2 percent in 1929 and 7.2 percent in 1950 to 9.5 percent in 1980, fell to 8.0 percent in 1990 and has remained around that level since then.³

Growth also became more unstable, more than twice as unstable as was typical during the industrialization period, as measured by the coefficient of variation of the annual growth rate. This largely reflects the periodic crises generated by the boom-bust cycles in external financing: the Mexican shock of 1994–1995, the series of crises in the emerging markets that started in East Asia in 1997 and worsened with the Russian default of 1998 and then spread to Latin America, the effects of the 2007–2009 North Atlantic financial crisis, and now the collapse of commodity prices, in large part due to China’s slowing growth and lessened demand for raw materials.

The reasons for this weak performance during the market reform period have been subject to equally heated debates. For reformers, the incomplete character of reforms was the major problem. In their view, the orthodox package was not fully implemented (e.g., privatizations), and there was also a lack of important ingredients, particularly deep labor market reforms that would make it easier to fire workers, restrict labor unions, and allow managers full flexibility to reshuffle workers as needed. In contrast, for Latin American structuralists, the explanation was the premature and powerful deindustrialization process that was unleashed by both the debt crisis and market reforms, as well as the massive lag in technological development that has characterized the region vis-à-vis both the developed countries and the most dynamic developing countries of East Asia. This reflects, in the structuralists’ view, the lack of a central role for production and technological strategies under the market reform model.

There is a consensus that productivity growth has been weak over the last quarter century, and indeed negative if measured by the evolution of total factor productivity. The modernization of leading firms has certainly taken place. But there has been a lack of capacity to absorb in high-productivity sectors the labor that has lost jobs due to market restructuring. This has been reflected, in turn, in high levels of labor market informality, with large numbers of workers self-employed or laboring in unregulated enterprises without contracts or social protection.

One issue that was entirely absent from the orthodox criticism of state-led industrialization, which in contrast was at the center of structuralist critiques, was the high level of domestic inequalities associated with that model. Industrialization was accompanied by rapidly increasing levels of human development, as measured by the United Nations Development Program, and particularly a reduction in the gaps with developed countries in health and, to a lesser extent, education. Also, about two-thirds of the poverty reduction achieved in Latin America from 1913 to 1990 took place between 1950 and 1980.³ However, trends in income distribution were not as positive. There was an early improvement in this area in the Southern Cone countries, but also a deterioration during the military dictatorships of the 1970s and part of the 1980s. Brazil also experienced increased inequality in the later stages of state-industrialization, but there were improvements since the mid-1960s or in the 1970s in other countries, such as Colombia, Costa Rica, Mexico, and Venezuela.⁴ Overall, income distribution probably worsened in several countries and in the region as a whole during the industrialization period, and inequality certainly remained excessively high.

With much better information for recent decades, we know that income distribution worsened in most countries during the 1980s and 1990s. This means that both
I prefer this term to that of "neoliberal" reforms or "neoliberalism" for two basic reasons. The first is that the concept "liberal" is used in very diverse senses in different parts of the world, and notably in the United States (and even the United Kingdom) vs. continental Europe. In fact, it would be more appropriate to call the market reforms "neoconservative" rather than "neoliberal." The second reason is that reforms were much more diverse than usually recognized and, in this sense, they did not follow a uniform "neoliberal" recipe.

As we close the half century examined in this dossier, the economic challenges facing Latin America are immense. South America is facing an economic crisis, which is particularly strong in Venezuela and Brazil. Renewal of growth requires more active production sector strategies focused on major technological catching up—the traditional strategy of the East Asian countries. But this requires a major shift in development policies. It is also critical to generate quality employment to match rising educational levels, the "scaling up" that is taking place in East Asia. Continuation of the positive social trends of the past decade is key, but poverty is rising again and improvements in income distribution have stalled. To paraphrase the title of this dossier, the time is ripe for renewed, strong, and speedy transformations.

Notes
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