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Post-pandemic pick up; Latin American economies.

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The region has a chance to grow, if protectionists do not get in the way

RUA 25 DE MARÇO in São Paulo is the biggest shopping area in Latin America. Before the pandemic, an average of 400,000 people a day went there looking for makeup, electronics, household items and more. Most of the goods were imported from Asia. Despite an easing of pandemic restrictions and increasing vaccination rates, the crowds have not returned. Around a fifth of shops have closed permanently. Edmilson Lucas, who runs a shop there, says it is hard to obtain supplies, with the value of the Brazilian real down by a fifth since the start of the pandemic, to \$0.18. It is even harder to sell his goods, considering that 14% of the population is unemployed. "I don't know how much longer I can keep the doors open," he says.

Laments like these can be heard across Latin America. No region has suffered more as a result of the pandemic. More than 2.1m people in Latin America and the Caribbean have died of covid-19; the death rate in the region is easily the highest in the world, according to The Economist's excess-mortality tracker. The economic toll has also been crushing. Output dropped by 7% in 2020, the steepest decline of any region. And although a surge in commodity prices early in 2021 is likely to have boosted growth this year to a respectable rate of more than 6%, GDP will remain below its pre-pandemic level at the end of 2021. The IMF forecasts that growth in 2022 will be lower in Latin America than in any other part of the world.

The economic pain of the recent past stings the more because of the disappointing years which preceded it. The opening decades of the new millennium were good ones for emerging markets. In the 2000s more than 80% of them enjoyed faster growth in output per person than the United States, up from 34% in the 1980s. Hopes swelled for Latin America. By 2005 Mexico's trade with Canada and the United States was up by 118% compared with 1993, as a consequence of joining the North American Free Trade Agreement (NAFTA), which took effect in 1994. Optimists reckoned still better times lay ahead. But as the long commodity boom drew to a close in the 2010s, economic fortunes turned.

A sense that a moment has been missed now hangs over the Americas. GDP per person in East Asia, at purchasing-power parity (PPP), stood at just 12% of the level in Latin America in 1980, but has since risen to 71%. High levels of inequality persist across the region. Democracies look almost uniformly less healthy than they did a decade ago.

Debt loads have risen above 100% of GDP in Argentina, Belize and Jamaica. In Brazil, rising interest rates are adding to the government's cost of borrowing, pushing it uncomfortably close to a crisis like the one that caused a deep recession between 2014 and 2016. Exacerbating the region's difficulties are the growing costs of climate change. Latin America and the Caribbean have taken a battering from extreme weather of late, including hurricanes and long droughts.

Take a chance

These risks create the impression of a region running short of time. And yet, as the world emerges from the worst of the pandemic, a moment of opportunity has arrived. The period of rapid growth across emerging markets which unfolded from the late 1990s to the mid-2010s was associated with a surge in world trade, which rose as a share of GDP from below 40% in the 1980s to 61% in 2008. This was helped by the spread of global supply chains, whose share of world trade leapt by ten percentage points between the 1980s and 2008, to just over 50%. This boosted average productivity and increased incomes. Employment growth is also higher in places where a larger share of people work at firms which both import and export.

Latin America largely sat out the surge in supply-chain trade, which rose by 0.1% from 1995 to 2015, compared with 19% across the rest of the world. Parts of the region in which firms were more linked into global supply chains, such as Mexico, suffered from intense competition from China, thanks to the close overlap in export competencies between the two countries. Had Chinese export capacity remained constant from 1995 to 2005, global demand for Mexican exports would have been 2% to 4% higher, according to Gordon Hanson of Harvard University and Raymond Robertson of Texas A&M University.

As long as we're together

The region may now get another chance. Increased political uncertainty in China has many firms in the United States rethinking their dependence on Chinese factories, while global shipping bottlenecks demonstrate the virtues of more evenly distributed trade. Geographic proximity generally translates into economic integration; indeed, it is surprising that interwoven supply chains across the Americas are not already in place. Both the quantity of trade and diffusion of technology decline with distance, economists reckon. Regional development may thus have a compounding effect, in which faster growth among neighbours leads to still more trade and higher incomes.

But to unlock these potential benefits, Latin America will need to confront problems which have impeded deeper integration in the past. The failure fully to exploit supply-chain opportunities has several causes. Problems are partly logistical. In Colombia and Brazil, the costs of shipping a standard container from the factory door to its destination are among the highest in the world (though other parts of the region, such as Panama and Chile, do better). Shoddy transport links raise costs and travel times.

Within the region, trade with countries which share a land border primarily takes place over land, rather than via sea or air, yet road infrastructure is often of low quality. About 70% of roads in Latin America and the Caribbean are unpaved, compared with less than 50% in South Asia and under 30% in East Asia. Rail is no better; of the 20 countries in the world with the worst rail infrastructure, ten are in Latin America--including Brazil, Colombia and Peru. With the exception of Panama, which has prospered as a logistics hub, Latin American economies are weakly linked into major sea shipping routes, and often have substandard ports.

The effects of poor infrastructure are multiplied, however, by bad trade policy. The growth miracles of East Asia were supported by policies which prioritise the development of export industries. Latin American governments, in contrast, have tended to prioritise the displacement of imports with domestic production, using trade barriers to shield producers at home.

Latin American governments are enthusiastic negotiators of trade agreements: nearly 450 bilateral deals have been signed since 1973. But more than 370 are intra-regional, and do not involve deep integration with richer countries which supply technology and high-value inputs, and which are avid consumers of advanced manufactures. In terms of overall trade restrictiveness, with respect to both tariff and non-tariff trade barriers, Latin America is the second most inaccessible region of the world, pipped only by sub-Saharan Africa, according to the World Bank.

Thus although the region has a big manufacturing industry, its growth has been disappointing. Nearly half a million Brazilians worked in the country's automotive sector in 2014. But the trade restrictions which protect the industry shut it off from foreign suppliers--denying Brazilian producers access to their know-how and technology--and coddling inefficient firms. Brazil exports its cars to members of Mercosur, a free-trade agreement which also includes Argentina, Paraguay and Uruguay, but does not source parts from outside the region, nor has it had much success selling cars on global markets.

The Americas are not monolithically protectionist. Mexico, in addition to its participation in NAFTA (and its successor agreement from 2020, known as the United States-Mexico-Canada Agreement), is a member of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Peru is as well; Chile has agreed to but not yet ratified the deal, partly because of protests against it in 2019.

The difference in trade orientation shows. Over the two decades prior to the pandemic, Chile and Peru persistently outgrew the United States' economy, and fared substantially better than more closed economies like Brazil's. Costa Rica and the Dominican Republic have benefited from their membership in a free-trade agreement with the United States. Yet for some sceptics of the export-oriented model, Mexico looms as a cautionary tale. From 1999 to 2019, income per person on a PPP basis grew more slowly than in the United States and Brazil. Manufacturing labour costs in Mexico have now been overtaken by those in China.

Get to know you better

Yet even as Mexico lost market share to China, its manufacturers have transformed: relying less on low-value industries, such as textiles, and participating more in electronics, automotive and aerospace manufacture. CPTPP membership might have generated more tangible benefits--though it is still early days--had it not been for the interruption of the pandemic. Even in the more reflexively protectionist milieu of South America's Atlantic-facing economies, there were hints of a willingness to open up before covid-19 struck. Mercosur, for instance, concluded a deal with the European Union in 2019, though ratification was subsequently delayed over EU worries about Jair Bolsonaro, Brazil's populist president, and rampant deforestation in the Amazon. Uruguay is pursuing a deal within Mercosur with South Korea (and one outside it, with China).

Whether this momentum can be sustained in the more trying post-pandemic atmosphere is unclear. Mercosur's cohesiveness is being tested: Argentina has withdrawn from further negotiations between the bloc and other economies. The election of leftist politicians around the Americas, such as Pedro Castillo in Peru, may give investors pause.

Some multinational firms are curtailing investments in Chile ahead of presidential elections in November. Gabriel Boric, who favours higher taxes on top incomes, is currently leading the polls (within the margin of error). In Mexico President Andrés Manuel López Obrador, who is tightening state control over the energy sector, recently said that lawmakers must decide whether "they are in favour of the people or private businesses".

But the benefits of greater openness could be high in coming years. President Joe Biden seems ready to make deals. He is keen to address the "root causes" of migration across the United States' southern border, and has promised to spend \$4bn in Central America tackling such issues. His administration has touted its "Build Back Better World" partnership (B3W) as a counterweight to

China's Belt and Road Initiative, through which the latter invests in infrastructure in its developing-world trading partners. Daleep Singh, Mr Biden's deputy national security adviser and point man for B3W, chose three Latin American economies--Colombia, Ecuador and Panama--as the first stops on a "listening tour" intended to drum up interest.

Funding mobilised by the United States could be deployed to help tie the Americas together, through roads, rails, ports and broadband. And the intensifying strategic rivalry between the United States and China may well change the normally fraught politics of trade. A deepening of trade ties, which might otherwise be seen as a threat to domestic firms, may instead come to seem like insurance against the further deterioration of Sino-American relations.

That does not mean it will be easy for the governments of countries which have suffered terribly through the pandemic to take a gamble on liberalisation. Neither will it be easy to persuade Latin Americans who have repeatedly been let down by their leaders that this time is different. In Buenos Aires, Gabriel Pablo Imperiale, a driver, sighs, "People don't believe in the government--how are you going to invest and bring the country forward if one day you've got legislators saying they're going to change tax rules, [and] just like that, change the rules?" But if ever there were a moment to take a leap of faith, it is now. Another opportunity like this one could be a long time coming.

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