
DELTA AIRLINES SPEAKER SERIES – SOUTH AMERICA ECONOMIC OUTLOOK FEBRUARY 19, 2004

The South America Project organized an off-the-record discussion on the economic prospects for South America in 2004. The featured speakers were Eduardo Lora, principal advisor at the Inter-American Development Bank; Rafael de la Fuente, Chief Economist for Latin American Research at BNP Paribas in New York; and Inés Bustillo, the Washington office Director of the Economic Commission for Latin America and the Caribbean (ECLAC). In addition to offering their own prognosis for the region, the panelists sought to pinpoint the drivers of the expected economic rebound as well as the risks that lie ahead.

All of the speakers agreed that Latin America is in the process of a strong recovery fed by external factors in the global economy, and further supported by domestic policies and realities. According to Eduardo Lora, who forecast 4% growth in 2004, the external reasons behind last year's success include a recent increase in world-wide growth, a rise in commodity prices (especially oil) to levels only previously seen before the East Asian Crisis, improving spreads, an increase of capital inflows through investment, and more competitive and powerful currencies as real exchange rates continue to rise. These external factors responsible for recent levels of growth are buttressed domestically by moderate levels of inflation and falling interest rates.

Lora warned that the current success may be temporary due to risks posed by high public-debt levels, low productive installed capacity due to a previous lack of investment, political instability, discredited reforms such as the Washington Consensus resulting in decreased support for the liberal model and international trade integration, and the social debts of the region due to high levels of unemployment and increasing numbers of poor. In order to sustain the new growth of the South American economies, Lora recommended greater fiscal discipline to combat deficits, a renewed focus on export-driven growth, and a reinforcing of current reforms to enhance their effectiveness in the region.

Inés Bustillo, who predicted a more conservative 3.5% growth for 2004, acknowledged that indicators are present for a South American recovery, however, she warned that the improvement will not be dramatic enough to reverse the previous 6 years of stagnation. While she noted that remittances are high (\$33 B), and exports have grown by 7.4% in the past year (soybean, copper, gold), Bustillo claimed that investment levels are still low (investment as a % of GDP is at a historical low point), credit hasn't recovered yet, and unemployment has yet to improve (700,000 people joined the unemployed last year).

Her recommendations for South America stressed the importance of sustaining growth through the export sector, exploring innovative methods of evolving South American exports from base commodities to value-added products to increase competitiveness. Secondly, she recommended reconciling the great disparity in income distribution across the segments of society through increased social spending.

Rafael de la Fuente concurred with Lora and Bustillo in their analysis of the factors contributing to South

America's projected recovery, pointing to high global growth (especially in the US which experienced 5% growth last year), high commodity prices, competitive real exchange rates due to low inflation, tight monetary and fiscal policies, weak labor markets creating advantages for employers, ample liquidity in the market, and low levels of account debts. De la Fuente was optimistic in his projection for growth in 2004 (4%), but he cautioned that structural risks and complacency with moderate growth could threaten the sustainability of this recovery period. To illustrate these risks, de la Fuente discussed country-specific examples calling for structural reforms in Argentina, Mexico, and Venezuela. According to de la Fuente, Argentina, with 8% growth in 2003, has become complacent with growth levels and is not undertaking necessary banking reforms. Likewise, Mexico is passively waiting for the US manufacturing sector to rebound instead of working to change internal structural deficiencies in its economy. De la Fuente assured that Venezuela would eventually face a fiscal crisis given current political instability and irresponsible spending by the Chavez administration. On a more positive note, he lauded Brazil as a bright spot in South America for lowering interest rates and continuing to address key issues.