

Honoring the Past, Building the Future

Fifty Years of Development
in Latin America and the Caribbean



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Latin America and the Caribbean

Inter-American Development Bank

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PREFACE

A Half-Century of Growth and Challenges

“It is necessary to look at the map of America, to place oneself before its splendid multiplicity, before the cosmic generosity of the wide places which surround us.” These words, spoken in 1971 by the Chilean poet Pablo Neruda, are an excellent prelude to this book commemorating the first 50 years of existence of the Inter-American Development Bank (IDB). The following pages are more than just an exercise in the history of this institution. They are a celebration of the achievements of a very disparate and complex region that has succeeded in setting itself on the path to progress, despite some tremendous obstacles.

There is no doubt that despite these setbacks, Latin America and the Caribbean have achieved progress on multiple fronts. Over the past five decades, as the region’s population has increased from 218 million to 579 million, life expectancy has risen from 56 to almost 74 years. Other social indicators, such as literacy or the Unsatisfied Basic Needs Index (UBN), show that the improvements, which sometimes seem rhetorical given the magnitude of the problems, are real. Apart from the positive results of recent years, per capita income during the same period reached a record US\$4,722 (in constant 2000 dollars) in 2007.

All this has occurred amid some profound changes in the way growth has been encouraged and alongside changing notions about the role of government. Thus, most of the hemisphere's nations have abandoned the import substitution model and closed regional agreements in favor of trade liberalization and redefining the role of the public sector in the economy. Thanks to this situation, ties among the region's countries are closer now than they ever were before, as demonstrated by intra-regional trade, investment, and tourism figures. However, because no regional agreement exists, many different bilateral treaties or treaties among groups of nations have been signed with governments on other continents.

Such changes have occurred because the schemes of the last 25 years have been unable to solve the problems arising from the endemic balance of payments deficit and, in some cases, from hyperinflation. One must also make mention of the horrifying debt crisis that earned the 1980s the label of "the lost decade." Although some five-year reform attempts succeeded in resolving some of the issues that emerged and made more room for private initiative and foreign investment, certain phenomena such as the volatility of capital flows and exchange rate appreciation have proven to authorities across the continent that the challenges may be different, but they never end.

Moreover, as the region's governments tested development formulas of greater or lesser scope, new phenomena were emerging that appeared to be irreversible. One of them is the population shift to

the region's urban centers, where almost 80 percent of Latin Americans now reside. Another is the overall decrease in the birth rate, accompanied by a change in the age pyramid. The growing participation of women in the labor force and higher levels of schooling are equally significant trends.

Yet another notable development is the preponderance of democracies in the region, in stark contrast to a half-century ago, when the region was characterized by the pervasiveness of dictatorships, many of which were military governments. While it is clear that the freedom to elect and to be elected is only the beginning and not the end of the democracy-building process, there are many examples of progress on this front, including the trend toward greater decentralization and the strengthening of government powers. These events have been accompanied by a growing respect for the rights of indigenous peoples and those of African descent, whose voices are being heard in a part of the world that is deeply multi-ethnic and multi-cultural.

The establishment of new channels of expression and participation has likely provided the spark for an unprecedented display of creativity that has manifested itself in literature, art, cinema and music. This creativity is also reflected in the business community's ability to develop world-class companies and in the endeavors of a larger and more diverse scientific community that is searching for solutions to the problems we all face.

However, as positive as these developments are, one cannot ignore the difficulties of a region in transition, one that is becoming increasingly modernized but is still tied to the past. While the gross domestic product (GDP) of the region keeps growing and exports are reaching levels that were unthinkable only a few years ago, inequality continues to be the main stigma of a region that is still seen as the least equitable geographic area of the world. As a result of this situation, poverty affects one out of every three Latin Americans and indigence affects one out of every 12, despite the improvements seen in this century.

As 2009 begins, the world now faces a difficult situation with a profound international financial crisis that has spread to the real sector, posing enormous costs in terms of loss of employment and well-being and representing a new challenge for the region. Despite the improvements seen in various indicators confirming that the region has learned from the painful experiences of the past, a slowdown is inevitable. Thus, the region's biggest challenges will be not to lose ground with respect to gains made in the social area, and not to go backwards by rejecting policies that have proven to be successful.

The region must be prepared to take advantage of the cycle of expansion once recovery begins. It must not only redouble its efforts to defeat age-old problems such as poverty, the poor quality of education and backwardness in infrastructure, but it must also

successfully meet new challenges such as climate change, which can do so much damage to an area that is so rich in resources yet so very vulnerable.

The above facts demonstrate that the region's work is far from done. Still, there are reasons to celebrate the progress that the region has made over the past five decades, and these congratulations are meant to affirm that there are solutions to unresolved problems, although these solutions may require effort across more than one generation. In the final analysis, that is the purpose of this book, which combines historical reviews with quantitative comparisons and adds the voices of experts and case histories involving ordinary people.

The crucial role that the IDB has played in all of these areas is clear. It has acted not only as the region's main funding agency, approving loans and guarantees worth US\$169.266 billion between 1961 and 2008, but also as a leader in developing the most diverse industries and in the transfer of know-how and best practices. Although some may be surprised to find that these pages do not describe the IDB's programs in exhaustive detail but rather focus on reality from another point of view, it is all, in fact, one and the same story. As Felipe Herrera, the first President of the IDB, so aptly expressed it, "we will be more than a Bank if we remember that our final objective is to accelerate the development of the entire Latin American region."



credit *El Tiempo*

In a political rally, in the workplace, and in the home, the people of Latin America and the Caribbean are striving to create better lives for their families and future generations. The IDB's mission is to finance programs that give these people new opportunities to use their ingenuity and hard work to address pressing social and economic challenges. In 2008, on the eve of celebrating its 50th anniversary, the IDB approved financing totaling a record \$11.2 billion.

I The Challenging Path of Economic Growth

José María Moratalla still remembers how difficult the environment was in the community of Iberia, a marginalized neighborhood of San Salvador, where he arrived as a priest 20 years ago. Crime, unemployment and the lack of opportunities seemed like insurmountable obstacles. Even so, Moratalla was convinced that the neighborhood's youths could create and manage their own businesses. In fact, they were the ones, he emphasized, who proposed the creation of workshops where they could perform a trade within their own community. Two decades later, this shared vision has become an entire system covering 11 industrial cooperatives that generate an annual income of \$900,000, on land that used to be a garbage dump.

Examples such as these are increasingly common in Latin America and the Caribbean. "Insofar as national economies have grown and require better products in a competitive environment, it is possible to find cases where small businesses and previously mar-

ginalized areas are making qualitative and quantitative leaps forward," says Moisés Naím, editor of *Foreign Policy* magazine and an expert on issues concerning the region. "Much remains to be done, but it's a good start. It all depends on the circumstances."

CHANGE

Indeed, the prevailing conditions and models of growth have changed drastically over the past half-century, as any glance at the history books will prove. The import substitution approach is a telling example. It began to gain prevalence due to the Great Depression and the restrictions imposed by the Second World War and by the post-war reconstruction period in Europe. During these years the nations of the Western Hemisphere raised their tariffs in a sustained manner for the purpose of protecting their industries, while governments took on a clear role in promoting specific industries, often by committing public funds.



Steel pipes stretching from the Amazon to the Pacific transport natural gas to consumers in Peru and markets abroad in an IDB project that set new environmental standards.

In general terms, there was skepticism as to the possibility of improved terms of trade among regions that exported basic goods and imported manufactured products. In addition, there were doubts as to the entrepreneurial capabilities of the private sector and faith in the effectiveness of government planning, along with an increasing mistrust of foreign capital channeled not towards the building of factories, but towards activities of extraction (IDB, 2002).

So began the era of inward growth, the results of which were impressive. Between 1945 and 1973, the gross domestic product (GDP) grew at an average annual rate of 5.3%, while yearly per capita income growth was nearly 3%. The industrial sector became an engine of this growth, with annual rates of growth in excess of 6% and a share of GDP that reached 26% by 1973, an 8 percent increase over 1950 (Thorp, 1998).

During this time, the world at large was also experiencing a boom period, despite serious political tensions. The rivalry between Washington and Moscow, the arms race and the division of the world into two opposing camps

led to the creation of regional blocs, and Latin America and the Caribbean were no exception to the rule. It was in this context that the Inter-American Development Bank (IDB) was founded, despite differences of opinion as to the need for a regional entity with a role that bore similarities to that of the World Bank (IDB, 1999).

The relative success of the import substitution model was accompanied by a significant change in the geographical distribution of the region's population, which increasingly moved from rural areas to the cities. This factor exerted pressure upon public finances in terms of higher outlays for infrastructure, health and education. The cost to governments of providing industrial subsidies and welfare benefits was not accompanied by an increase in tax revenue. Although government expenses in the region increased from 20.7% to 25.7% of GDP from 1960 to 1970, tax revenues only increased from 14.4% to 17.2% during the same period (Thorp, 1998). This imbalance resulted in chronic deficits in the balance of payments, in currency crises, and in an increase in domestic inflationary pressures.



Many of the region's small and medium-sized industries have gained new access to financing and technology through IDB-financed programs for the private sector.

THE BIG CRISIS

It was, however, an external shock that caused the first major problems: the decision by the Organization of Petroleum Exporting Companies (OPEC) to raise the price of oil in the early 1970s. This not only was a blow to the developed world but also generated considerable surpluses in fuel exporting countries, the revenues of which were placed with the major banks. Such liquidity ultimately stimulated a significant increase in foreign lending to Latin America and the Caribbean, a move that was welcomed by the region's governments, who preferred this option to making a major adjustment. As a result of this, the debt of the region as a whole increased by 109% between 1978 and 1982, reaching US\$315 billion by 1982 (ECLAC, 1985).

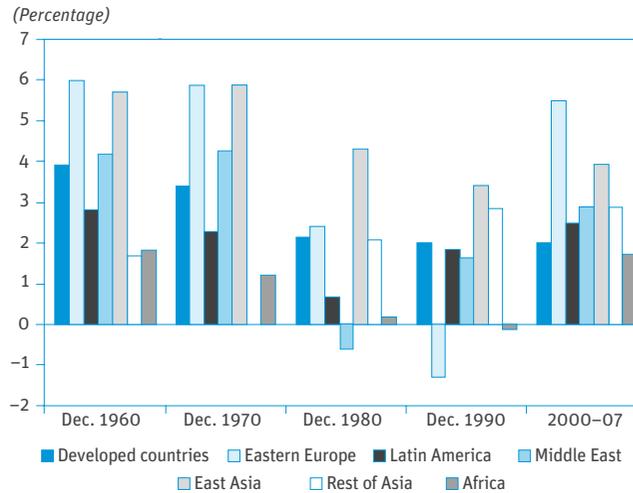
The announcement by Mexico in August 1982 that it would suspend payments on its foreign debt caused panic in the markets and a sharp drop in offers of credit to the region. Consequently, many of the region's countries were forced to adopt emergency measures over the course of several years, including exchange-rate adjustments, budget cuts, and aid requests to multilateral or-

ganizations. Also, governments began the process of selling off public assets, which led to private control of formerly state-owned businesses.

Among the many consequences of the debt crisis, perhaps the most significant one was the squelching of Latin America's growth while other areas of the world continued to enjoy economic growth (Figure 1.1). According to the Economic Commission for Latin America and the Caribbean (ECLAC, 2008c), as global per capita GDP grew from US\$4,521 to US\$5,155 between 1980 and 1990, Latin America's GDP fell from US\$5,183 to US\$5,072 during the same period.¹ Also, while mean regional income expressed as a percentage of that of the most developed countries was around 28% between 1870 and 1980, it had fallen to 22.7% by 1990 and to 21.5% in 2006 (ECLAC, 2008c) (Table 1.1).

This process coincided with the strong growth of the Asian countries, starting with Japan after the Second World War, continuing with South Korea, and followed by some of the smaller economies of the region. All these changes paled in comparison, however, with the economic reforms undertaken in China, triggering a trend of acceler-

Figure 1.1 Per Capita GDP Growth, by Region and Decade



Sources: IDB (2000), for the decades of 1960 and 1970, and World Development Indicators, World Bank, from the 1980s onward.
 Note: Per capita GDP at constant 2000 prices.

ated economic growth 25 years ago that continues to this day, despite the pressures the world economy has been experiencing since the middle of 2008. A decisive element in the rise of this third economic axis in Asia, alongside North America and Europe, was the nature of the technological changes leading to the fragmentation of production

and its reorganization into global value chains, spurring a robust increase in productive integration and, therefore, trade integration (ECLAC, 2008c).

Aside from its economic and social effects, the debt crisis represented a crucial turning point for the region. This is because, until the 1980s, predominating theories were based on a model of accumulation of the factors of production (essentially capital and labor). Accordingly, the primary role of politicians was considered to be that of facilitating the accumulation of capital. This resulted in an emphasis on saving, from the domestic standpoint, and the importance of foreign financing, from the external standpoint, in closing financial gaps and enabling a rate of capital accumulation compatible with targeted growth, hence the important role initially given to multilateral organizations in providing financing and defining the best investment projects deserving of financing to enable growth. The accumulation of human capital also became a key factor in ensuring growth, although it played a lesser role, with a longer-term horizon.

(Continued on page 8)

Table 1.1 Changes in Disparities among the Regions of the World, 1820–2006

	1820	1870	1913	1950	1973	1980	1990	2006
A. Product per capita, region								
<i>(In USD according to 1990 PPP)</i>								
Western Europe	1,204	1,960	3,457	4,578	11,417	13,197	15,965	21,098
Australia, Canada, United States and New Zealand	1,202	2,419	5,233	9,268	16,179	17,935	22,345	30,143
Japan	669	737	1,387	1,921	11,434	13,428	18,789	22,853
Asia (except Japan)	577	548	658	635	1,225	1,511	2,109	4,606
Latin America	692	676	1,494	2,503	4,513	5,183	5,072	6,495
Eastern Europe and the former Soviet Union	686	941	1,558	2,602	5,731	6,231	6,460	7,000
Africa	420	500	637	890	1,410	1,538	1,449	1,697
World	667	873	1,526	2,111	4,091	4,521	5,155	7,282
B. Inter-regional disparities								
<i>(Percentages)</i>								
Less developed region/more developed region	34.9	20.7	12.2	6.9	7.6	8.4	6.5	5.6
Latin America/more developed region	57.5	27.9	28.6	27.0	27.9	28.9	22.7	21.5
Latin America/world	103.8	77.4	97.9	118.6	110.3	114.6	98.4	89.2
Latin America/less developed region	164.9	135.2	234.4	394.0	368.5	343.0	350.0	382.7
C. Share of global production								
<i>(Percentages)</i>								
Western Europe	23.0	33.1	33.0	26.2	25.6	24.2	22.3	17.7
Australia, Canada, United States and New Zealand	1.9	10.0	21.3	30.7	25.3	24.3	24.6	22.7
Japan	3.0	2.3	2.6	3.0	7.8	7.8	8.6	6.2
Asia (except Japan)	56.4	36.0	22.3	15.5	16.4	18.3	23.2	36.4
Latin America	2.2	2.5	4.4	7.8	8.7	9.8	8.3	7.7
Eastern Europe and the former Soviet Union	9.0	12.0	13.4	13.0	12.9	11.9	9.8	6.0
Africa	4.5	4.1	2.9	3.8	3.4	3.6	3.3	3.3
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Sources: ECLAC, based on J. A. Ocampo and J. Martín, *Globalización y desarrollo, una reflexión desde América Latina y el Caribe*, ECLAC/Alfaomega (2003); and A. Maddison, *Contours of the World Economy 1–2030 AD—Essays in Macro-Economic History*, Oxford University Press (2007).

Interview with Eduardo Lora



Eduardo Lora is the Manager and Chief Economist, a.i., of the Research Department at the Inter-American Development Bank.

He holds a master's degree in economics from the London School of Economics. He has been an associate member of St. Antony's College at Oxford University, the editor of *Coyuntura económica*, and Executive Director of Fedesarrollo, the main center for economic studies in Colombia. Since joining the IDB in 1996, Lora has coordinated the Report on Economic and Social Progress in Latin America (IPES in Spanish), the IDB's flagship report, which changed its name to Development in the Americas (DIA) in 2008.

What is your view of economic development in the hemisphere over the past 50 years?

The economic performance of Latin America and the Caribbean has been unexceptional. The region has lost ground in relative terms with regard to developing countries and has been outpaced by other regions of the developing world. Over the past 50 years there were frequent spells of high inflation, problems with fiscal indebtedness and cases of financial crises. Macroeconomic instability has been an albatross around the region's neck in its fight against poverty. The five-year period between 2003 and 2008 was a noteworthy exception to these low growth and instability patterns. Even though the region has weathered the global financial crisis that broke out in mid-2008 quite well, it is still too soon to claim victory. Although the more specific causes differ case by case, the most common reasons for Latin America's mediocre performance have to do with the quality of macroeconomic policy and the region's institutions. The integration patterns, deep inequalities, and the limitations of its democratic systems are possibly the deepest reasons why it has been so difficult for

the region to develop better policies and institutions.

What do you believe the IDB's role has been in what has happened?

The IDB has never pretended to have a magic formula to solve those problems. Its role has consisted of standing side-by-side with Latin American governments and corporations in seeking out more appropriate policies and institutions for their stage of development and for their social, economic and political circumstances.

How do you view this issue looking to the short- and long-term future, and what should the Bank's role be?

The IDB's principal tool is its financing. The power of this leverage depends not only on the amount of resources or their cost, but on there being an open channel for development problems. And that crucially hinges on the understanding one has of the countries, sectors or regions and businesses at which the financing is aimed. For that reason the IDB is seen more and more not only as a financial entity, but as a center for the generation, diffusion and mobilization of knowledge in terms of institutional, social and economic development.

Box 1.1 The Role of the IDB in Economic Development

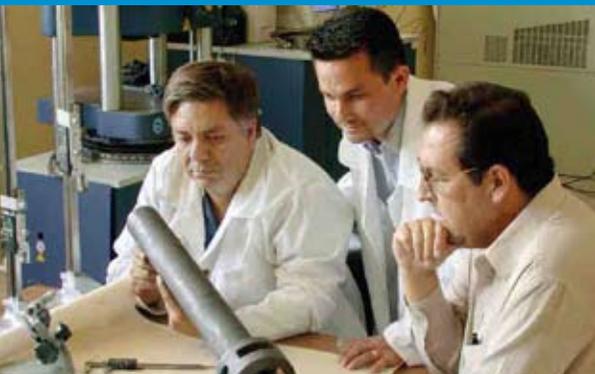
Throughout the last half-century, the Inter-American Development Bank has promoted the establishment of healthy macroeconomic fundamentals and stability in the economic environment, including the fiscal, financial and foreign sustainability of the region's economies. In recent years, and given the comparative advantages of each one of the international organizations involved in the area, it was determined that the IDB's activities in the area will be focused on consolidating institutions for macroeconomic stability through strengthening tax systems and their management, improving budgetary and tax management institutions, and strengthening tax institutions at the sub-national level (IDB, 2003).

In addition, it was decided that the IDB will act in collaboration with other international organizations to lend resources in times of transitional scarcity of foreign financial resources, such as what happened toward the end of 2008, and develop financial mechanisms and international architecture that allow for a reduction in the volatility of international financial flows. The objective of emergency loans is to provide financial backing to ease the social and economic effects of international financial crises. New financial mechanisms include the establishment of a credit system for exports for the purpose of support, especially to those countries where financial and currency problems have affected the normal finance mechanisms of foreign trade.

Having said that, the Bank clearly places a preferential emphasis on social progress as a condition for economic development by means of consolidating sectoral reforms in education, health and housing. Therefore, the IDB will constantly seek to increase the quality of these services in a way that is compatible with resources available for the short, medium and long term. Better conditions in education, health and housing will increase the productivity of the workforce and will lead to an increase of income for Latin American people, with an impact on the increase in production and consumption.

Along the same lines, the IDB has actively participated in research projects promoting development and economic growth in Latin America and the Caribbean. The IDB's work has been aimed at solving general problems in the region (such as how to establish credit limits or sources of growth), as well as solving the specific problems of the various countries that make up the region. Some of the IDB's most significant contributions can be found at: http://www.iadb.org/res/ipes/past_reports.cfm?language=en and <http://www.iadb.org/res/index.cfm?language=En>.

A small metal-working firm in Guadalajara, Mexico, used credits extended through an IDB program to boost its competitiveness by improving the quality of its products.



Stock markets make up part of an increasingly sophisticated financial system in the region that is finding innovative ways to serve businesses and individuals.

(Continued from page 4)

A NEW FOCUS

In addition to the consequences that the debt crisis brought to the internal structures of the countries affected, there was a clearly increased emphasis on seeking external markets in order to overcome one of the region's endemic weaknesses. This change of direction followed an initial phase of higher tariffs and import restrictions in order to accumulate foreign currency holdings, and coincided with a favorable environment for international trade. According to the United Nations, world exports of goods grew at an average annual rate of 14.9% between 1985 and 1990, falling to 8.5% over the next five years, and then to 5.2% by 2000 (United Nations, 2008), before the rate began rising again this decade. In the case of Latin America, trade as a percentage of GDP went from 28.4% to 35.6% between 1990 and 1999, much higher than in 1970 (22.3%), and even higher than in 1980 (30.2%). However, in the case of Asia the increase was from 38.3% to 53.5% during the same period (IDB, 2002).

During the 1990s, this trend was bolstered by the development of regional integration agreements and by

the signing of bilateral pacts for the purpose of dismantling trade barriers. The year 1991 saw the creation of the Southern Common Market (MERCOSUR), followed by the signing in 1992 of the North American Free Trade Agreement (NAFTA) by Canada, the United States and Mexico. These agreements were the first to be signed in the Western Hemisphere since the creation of the Caribbean Common Market (CARICOM) in 1973, and were to be followed by many others. Consequently, intra-regional trade grew at much higher rates than extra-regional trade.

Although this was not the first time Latin American countries were endeavoring to forge closer ties, this resurgence of regionalism was drastically different from the previous model in that it maintained low tariffs on trade with the rest of the world. Guaranteed access to these markets led to a diversification of the productive base and made it necessary to adopt institutional reforms through which the various governments concentrated on their regulatory function, thus widening the playing field for the private sector.

One of the consequences of this new approach was a significant and

sustained increase in foreign direct investment (FDI) due to the sale of public assets and to the greater opportunities resulting from trade and integration. Thus, while FDI represented less than 10% of the region's GDP in 1990, by 1999 it had jumped to 23%. Although this trend was worldwide, according to IDB calculations the amount of FDI that Latin America was receiving as of 1999 was 60% greater than its share of the gross world product (IDB, 2002).

Moreover, the debt crisis led to the questioning of the role previously assigned to external financing, and to a broader understanding of the problems of growth. At the beginning of the 1990s, the Washington Consensus² outlined a series of prescriptions that had come to be considered necessary conditions for the recovery and sustained growth of the region's economies. The list included fiscal and monetary policies to ensure macroeconomic stability and policies of openness to foreign trade, privatization, the liberalization of financial markets and the simplification of tax systems in order to enhance the flexibility of markets and promote economic efficiency.

However, despite the profound transformations that occurred in most of the region's countries, the reforms following the crisis of the 1980s did not necessarily result in a significant overall improvement. Although there was clear progress in terms of controlling inflation, which went down from double to single digits, with an average of 9% as of 1997, the outcome in terms of growth was unsatisfactory. Indeed, between 1998 and 2002 the region's performance and lack of progress on such indicators as per capita income were so disappointing that this period was dubbed "the lost five years."

Much of the blame for what occurred was placed on external shocks that revealed the region's vulnerability to rapid changes in international conditions (Figure 1.2). As explained by Nancy Birdsall and Carlos Lozada, "problems in one emerging economy in particular might trigger a temporary withdrawal from several or all economies considered to be in the same asset class" (Birdsall and Lozada, 1998). Consequently, the various crises that originated in Mexico, Thailand, Russia and Turkey ultimately hit all the other countries in their area quite hard beginning in the mid-nineties, in some

cases forcing the adoption of special measures to maintain exchange rates, balances of trade and macroeconomic stability.

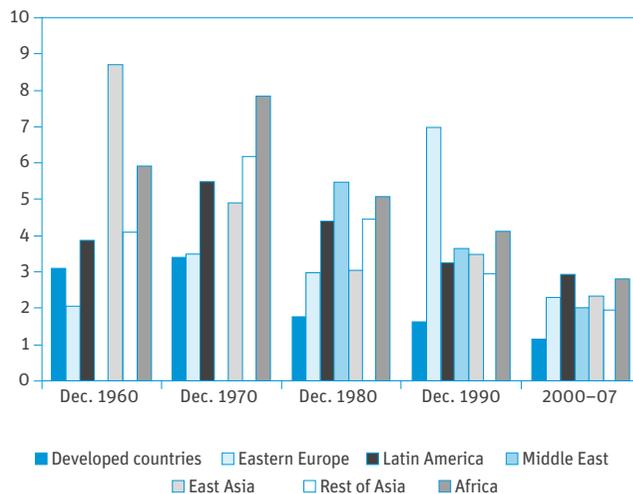
THE RECENT BOOM

However, the economic picture changed radically starting in 2003 due to the confluence of three favorable factors: high prices for raw materials,

favorable conditions for financing, and substantial remittances from Latin Americans who emigrated to other locations. As José Antonio Ocampo puts it, “the economic history of Latin America shows that the combination of the first two of these elements invariably leads to rapid economic growth. The last time this occurred was in the 1970s. The combination of all three was unprecedented” (Ocampo, 2008) (Table 1.2).

In the case of the first element, the strong increase in the global GDP and the increasing importance of China as an importer of primary commodities were decisive in causing a rapid increase in international prices. Minerals were the most extreme case, particularly energy products, which rose in cost dramatically, reaching prices that, in inflation-adjusted terms, had not been seen since 1973 and 1979. The cost of food also increased substantially, although in inflation-adjusted terms prices were similar to what they were in the early 1980s (Figure 1.3). A new development in this cost spiral, which ended in the second half of 2008, was that there was a clear connection between agricultural and energy commodities due to the surge

Figure 1.2 Per Capita GDP Volatility, by Region and Decade (Percentage)



Sources: IDB (2000), for the decades of 1960 and 1970, and World Development Indicators, World Bank, from the 1980s onward.
Note: Per capita GDP at constant 2000 prices.

Table 1.2 Annual Change in GDP, Latin American Countries, 2000–07

Country	2000	2001	2002	2003	2004	2005	2006	2007
Argentina	-0.8	-4.4	-10.9	8.8	9.0	9.2	8.5	8.7
Bolivia	2.5	1.7	2.5	2.7	4.2	4.4	4.8	4.6
Brazil	4.3	1.3	2.7	1.1	5.7	2.9	3.7	5.4
Chile	4.5	3.4	2.2	3.9	6.0	5.6	4.3	5.1
Colombia	2.9	2.2	2.5	4.6	4.7	5.7	7.0	8.2
Costa Rica	1.8	1.1	2.9	6.4	4.3	5.9	8.8	7.3
Dominican Republic	5.7	1.8	5.8	-0.3	1.3	9.3	10.7	8.5
Ecuador	2.8	5.3	4.2	3.6	8.0	6.0	3.9	2.7
El Salvador	2.2	1.7	2.3	2.3	1.9	3.1	4.2	4.7
Guatemala	3.6	2.3	3.9	2.5	3.2	3.3	5.3	5.7
Honduras	5.7	2.7	3.8	4.5	6.2	6.1	6.3	6.3
Mexico	6.6	0.0	0.8	1.4	4.0	3.2	4.8	3.2
Nicaragua	4.1	3.0	0.8	2.5	5.3	4.3	3.9	3.8
Panama	2.7	0.6	2.2	4.2	7.5	7.2	8.7	1.2
Paraguay	-3.3	2.1	0.0	3.8	4.1	2.9	4.3	6.8
Peru	3.0	0.2	5.0	4.0	5.1	6.7	7.6	8.9
Uruguay	-1.4	-3.4	-11.0	2.2	11.8	6.6	7.0	7.4
Venezuela	3.7	3.4	-8.9	-7.8	18.3	10.3	10.3	8.4
Average	4.0	0.3	-0.4	2.1	6.1	4.8	5.6	5.7

Source: ECLAC (2007).

Note: Constant 2000 prices.

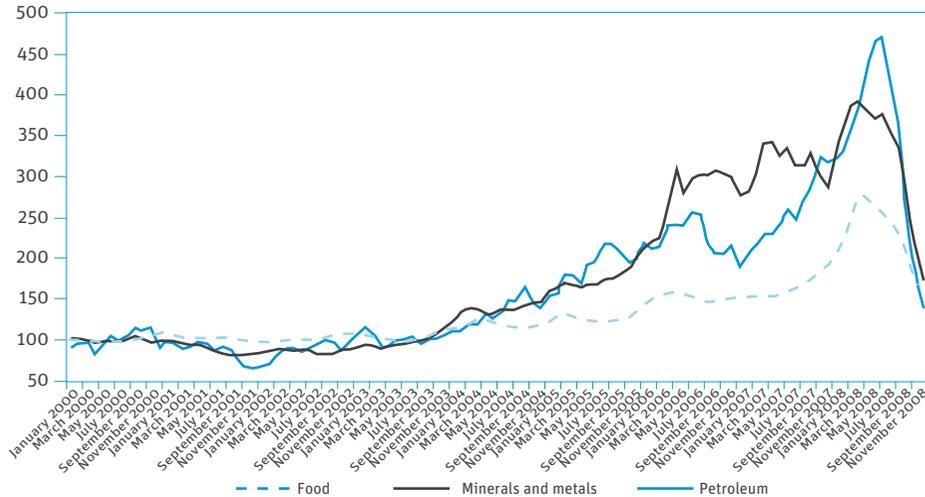
in biofuels as a partial substitute for petroleum derivatives.

In turn, substantial international liquidity was accompanied by improved conditions with regard to payment

terms and interest rates, together with low margins of risk, in keeping with historical patterns. However, the greater availability of funds did not result in a substantial increase

Figure 1.3 Price Indexes for Basic Products

(2000 = 100)



Source: ECLAC, based on data from the United Nations Conference on Trade and Development (UNCTAD).

in external public debt (Figure 1.4), because during the period in question many of the countries in the region preferred to change the makeup of their debt portfolio, relying more on financing in their national currency. In addition, FDI was particularly robust, not only in extraction industries, but also in the development of various national markets. According to ECLAC, the total received in Latin America and the Caribbean in 2007

reached a record-breaking US\$105.9 billion, an increase of 46%, making it one of the most dynamic regions in the world (ECLAC, 2008b). In 2008, tourism-related FDI represented a significant portion (between 15% and 25%) of the GDP of several Caribbean countries. In other Central American and South American countries, FDI represented, on average, 4% of GDP (ECLAC, 2008a) (Figure 1.5). Given such high proportions, the effect of the global crisis that began in 2008 has become a key concern for the region.

Perhaps the most striking element of all has been the increase in remittances from abroad, which rose from US\$20 billion to US\$66.5 billion between 2000 and 2007, according to estimates from the Multilateral Investment Fund (MIF) of the IDB. Not only did these remittances double during that period, exceeding 2% of regional GDP, but they became the principal source of foreign revenue in the case of a handful of small and medium-sized economies, representing more than 20% of local GDP.

As a result of this mix of favorable factors, Latin America and the Caribbean experienced an average

Figure 1.4 Short-Term Foreign Debt and International Reserves, Latin America

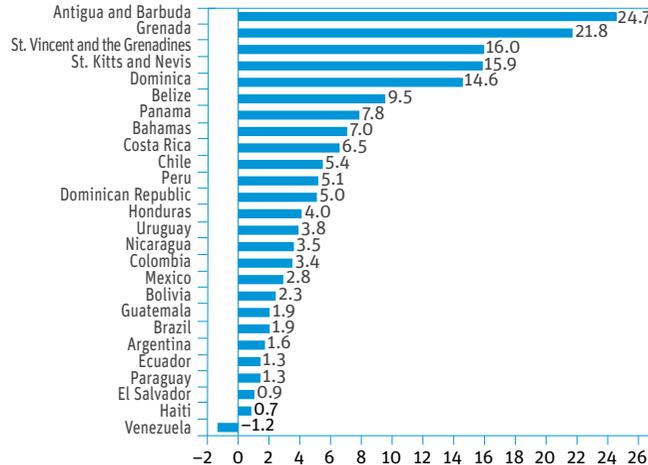


Source: ECLAC, from the Global Development Finance online database of the World Bank.

annual rate of growth of 5.6% between 2003 and 2007, the second highest rate in history after the figure reported between 1967 and 1974, which was one percentage point higher. Although this surge lasted well into 2008, because regional growth was 4.6% according to ECLAC, the change was dramatic. The international crisis that began with the problems in the U.S. real estate market that subsequently contaminated the North American and European financial systems called into question once again the region's ability to confront what is undoubtedly the greatest challenge facing the global economy since the days of the Great Depression.

Figure 1.5 Net Foreign Direct Investment, Latin American and Caribbean Countries

(Percentage of GDP)



Source: ECLAC, based on official figures from the listed countries and the IMF.



Throughout the years, improving the quality of education has always been a priority for the IDB.

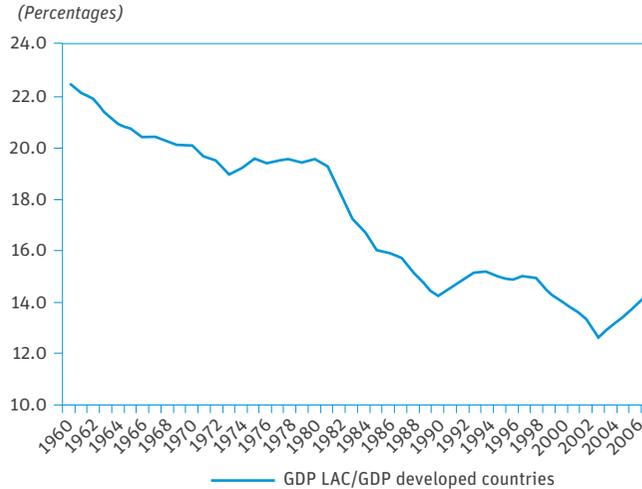
LASTING CHALLENGES

The answer to this riddle will determine whether the region will be able to catch up after falling behind on the global stage. Although the results of the past 50 years have ultimately been positive, the region never experienced exceptional growth rates during any of these decades, and consequently, its relative position in terms of income, compared to other regions, has declined. The relative income gap in comparison with developed countries has increased over the last few decades—in 1960, average per capita income in Latin America was equivalent to 22% of the per capita income of the wealthiest nations, but currently it represents only about 15% (Figure 1.6).³

It is now possible that growth during the final years of this decade will turn out to be below that of the preceding five years, due to the worsening of international conditions. Indeed, a disturbing characteristic of economic growth in Latin America has been a high degree of instability, which on average is higher than in the other regions of the world.

Aside from the fact that income levels in Latin America are modest, and

Figure 1.6 Per Capita GDP of Latin America and the Caribbean in Relation to Developed Countries



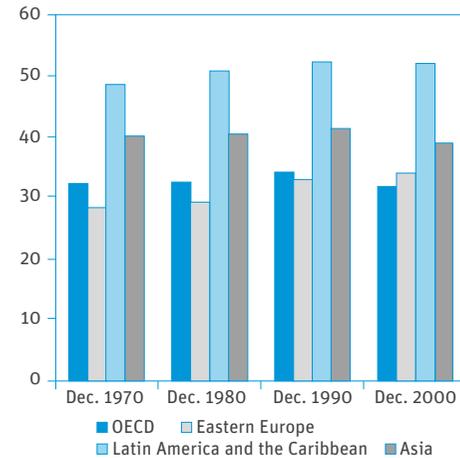
Sources: World Development Indicators, World Bank, and Heston, Summers and Aten (2006).
 Note: Per capita GDP at constant 2000 prices.

that they have grown in a relatively slow and unstable manner, they are also very unequally distributed. In terms of the distributive dimension of economic development, the region's performance is poor, with consistently high rates of income concentration that are higher than those found anywhere else in the world. In Latin America, 5% of the population receives 25% of national income,

while the wealthiest 10% receives 40% of it. By contrast, in the countries of Southeast Asia, the wealthiest 5% of the population receives 16% of national income on average, while in the developed countries it receives 13% (Figure 1.7). In recent decades, the concentration of income has increased in nearly every Latin American country, with very

(Continued on page 18)

Figure 1.7 Gini Index of Income Concentration, Selected Regions, by Decade



Source: De Ferranti et al. (2004), for the decades of 1970, 1980 and 1990; World Development Indicators, World Bank, for the decade of 2000.

Note: For the year 2000 calculation, the last year available for each country was used and a simple average was computed.

Interview with Ricardo Lagos



Ricardo Lagos, the former president of Chile, has been an exceptional witness to the changes that have taken place in Latin

America throughout the last 50 years. In addition to his political career, he has been involved with the academic world at several universities in South America as a professor and researcher. In this interview Lagos analyzes recent developments in the region as well as its challenges.

How would you describe the economic performance of Latin America and the Caribbean over the last 50 years?

I believe that for 50 years now, we've been influenced by a major event: to be precise, the creation of the IDB, which was almost immediately followed by the inauguration of President John F. Kennedy in the United States. President Kennedy was the driving force behind the Alliance for Progress. Both events reflect a certain way of understanding the economic growth and development of that time in history. There were high expectations concerning integration processes, but we're also talking about a world still heavily influenced by the ideas of Keynes. That way of looking at growth was prevalent until the eighties, when questions began to surface about the ability to maintain that model, and the substitution of imports, an issue that remained from the 1930s, was called into question. At that point a movement began where it was believed that the government's role should be a minor one and there should be more liberalization, and we entered a stage of having to make structural adjustments.

Then what happened?

Well, this made the eighties a difficult decade from the point of view of economic growth, and some came to speak of "the lost decade." But the most important thing is the vision, which later culminated with the Washington Consensus at the beginning of the nineties. This argued for the need to make extensive structural reforms, a higher level of international opening up, a need to drop tariffs, to loosen regulations, to establish that certain businesses should not continue as either government-owned or government-run, but rather that task belongs to the private sector, and thus we entered into a different stage here.

Now, I am under the impression this stage is coming to an end, not only because of the current financial crisis, or because the issue of regulations tends to be viewed differently. I believe the Washington Consensus missed an additional component (as its author Williamson himself has said). And we have to have social policies so we can make sure that when there is growth, it trickles down to all sectors and not just to some. I believe the IDB report *The Politics of Policies* marks the beginning of this stage where it is said the market

is crucial for determining levels of growth, but sometimes the market by itself does not meet the social demands our countries face. I think there were elements of that with the Latin American success from 2003 to 2008 and its 5% annual growth rate that came to be interrupted by the current crisis.

What else would you emphasize?

There has been a second factor that is quite important. Today, when we are making economic policies that do not make sense, everybody knows about it. There is no mystery to the fact that there have to be independent monetary authorities, balanced budgets, an opening up of the markets, that you have to let the markets work, and it's no secret there must be social policies. When there is growth, we can create it in such a way that everyone benefits.

Why has Latin America been unable to break the cycle of inequality?

I believe there are two reasons. One is historically based and has to do with the ownership of assets in the region when certain types of privatizations were carried out with little transparency. The other one, equally important, is from the disparity in access to educa-

tion. There is a concentration of income there that has a great deal to do as well with educational opportunities that are highly segmented. Some people belong to an income bracket where they have received only basic or primary education, others are in a bracket where they have only completed high school, and completely separate from these two groups are those who are in a bracket where they have attained a university-level education. So, I think this is more of a long-term issue that has to do with how to guarantee universal access to higher education.

What would you like to see happen?

First, that we would get through this international crisis that we had nothing to do with. Second, when we get out of this, I believe we are going to need a financial architecture that's slightly different from the one we have now. But I also believe that at that time the world should pick up a proper pace of growth again and Latin America should regain the momentum that was cut short by this crisis. Looking at history, one sees that a 20- or 25-year expansion is feasible and we have to be capable of taking advantage of it. I believe we have also seen that in good

times we have to learn to save for the bad times, but not every country in the region is doing that.

What type of role do you envision the IDB playing in that scenario?

Well, the role it has always played. I had the privilege of being a student of the first President of the IDB, Felipe Herrera, who was a professor at the University of Chile at that time. Then I had the chance to follow closely the creation of the IDB from its inception. I would say the Bank is defining itself as the bank that ensures, along with essential economic policies for sustaining growth, that there are social policies as well, so that growth reaches every sector, especially the most impoverished ones.

What have we learned?

We have learned over the past 50 years that economic growth is essential, but also that political democracy is necessary for ensuring economic growth through public policies, the policies citizens define by means of voting. This crucially important trifecta—society, the government, and the market—can only come together when you have a democratic system.

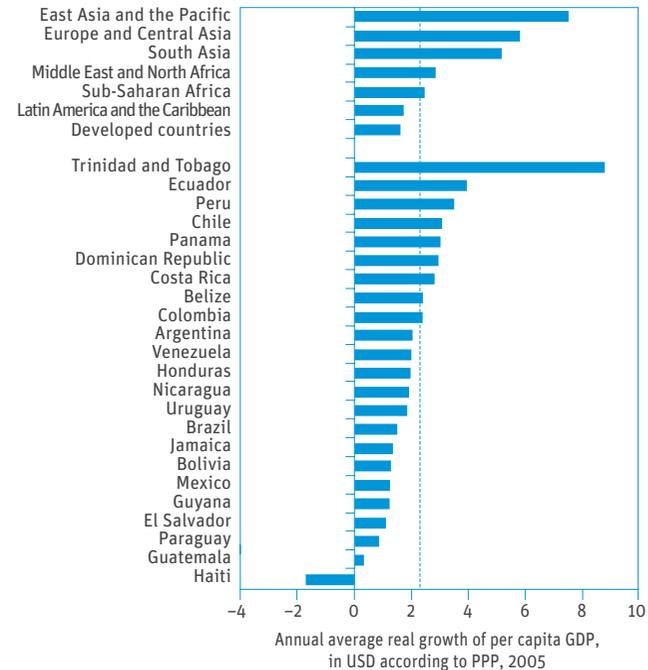
(Continued from page 15)

few notable exceptions, such as Brazil. However, this trend is not exclusive to this region. Increased concentration of wealth has been observed worldwide, and appears to be linked to features of the technological changes that have taken place in recent decades, and perhaps also to the inroads that China and other countries with cheap labor have made in international trade.

It is also important to keep in mind that, in terms of economic growth and per capita income, the countries of Latin America and the Caribbean form a very heterogeneous region. In this decade, Trinidad and Tobago, the region's wealthiest country, has also enjoyed the highest growth, with rates that can only be compared to those

of China or India (Figure 1.8). In terms of income level, it is followed by Chile, where development in recent years has been less exceptional than in previous decades, although it continues to be respectable by regional standards (Figure

Figure 1.8 Real Per Capita GDP Growth, Selected Regions and Countries, 2001–06



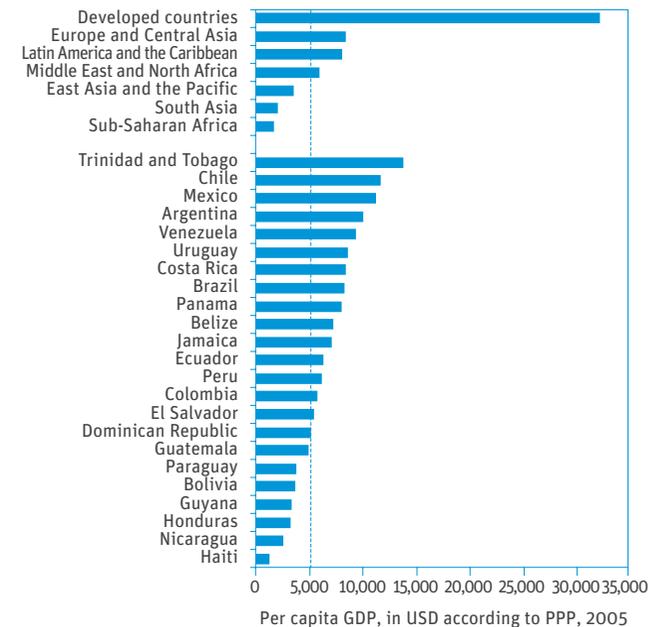
Source: Authors' calculations for IDB (2008b) based on World Bank figures (2007).
Note: The dotted line represents median worldwide economic growth between 2001 and 2005 (2.65% annual real average).

1.9). Mexico, which is next on the list of highest income levels, has had much more modest growth. The fact that the countries with the worst growth rates in the region are also some of the poorest is a cause for concern. These include Guatemala, Haiti and Paraguay, where per capita incomes are on a par with the averages for the poorest regions of the world.

If one were to divide the world's countries into two groups based on their per capita income level, most Latin American countries would belong to the half with higher incomes. The only exceptions would be (in descending order of income) Guatemala, Paraguay, Bolivia, Guyana, Honduras, Nicaragua and Haiti. However, if one were to divide the world into two groups based on each coun-

try's per capita growth rates (from 2001 to 2006), most Latin American countries would be in the half with slower growth. The only countries that would be in the group with faster growth would be (in descending order) Trinidad and Tobago, Ecuador, Peru, Chile, Panama, the Dominican Republic, and

Figure 1.9 Average Per Capita GDP, Selected Regions and Countries, 2001–06



Source: Authors' calculations for IDB (2008b) based on World Bank figures (2007).
 Note: The dotted line represents average median per capita GDP between 2001 and 2006 for 122 countries (US\$5,089, in constant 2005 dollars according to PPP).

Costa Rica. Even so, some of these countries would belong to the high-growth club for only a portion of the period in question.

LESSONS LEARNED

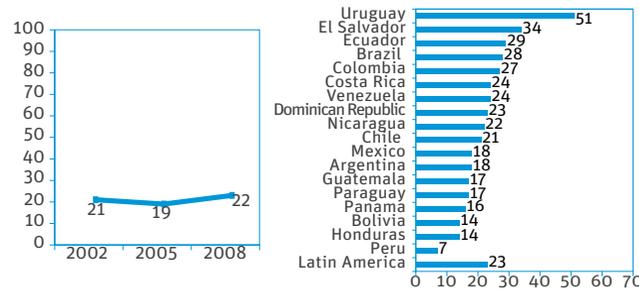
From a broader perspective, an analysis of the countries of Latin America and the Caribbean has underscored the importance that various factors have in determining growth. These include (i) the poor quality of public institutions, (ii) the unsuitability of macroeconomic policies, (iii) the weakness of the financial system, (iv) the poor quality of the physical infrastructure, (v) the low level of human capital, and (vi) the adverse international environment. In addition, a series of studies have demonstrated that growth and poverty reduction measures are mutually reinforcing. On the one hand, average growth is one of the most important determinants in reducing poverty, while on the other hand, actions aimed at reducing poverty may contribute significantly to economic growth. The importance of these factors in terms of growth is discussed briefly below.⁴

The *public institutions* with the greatest impact on economic growth

are those that help people and their businesses benefit from their productive efforts. This, in turn, encourages those who benefit to invest in education, technology, physical capital and improving the quality of the environment. These developments require the adequate protection of property rights, respect for the rule of law and of contractual commitments, and the absence of corruption. Although there are many difficulties in measuring the quality of institutions (Figure 1.10), most studies and quantitative indicators consistently show that many countries in the region have serious problems in the area of respect for the rule of law (Figure 1.11) and the prevalence of corruption (Figure 1.12). The most comprehensive summary of existing indicators shows that more than half the countries of Latin America and the Caribbean are below the world average with regard to respect for the rule of law and the suppression of corruption.

Unsuitable macroeconomic policies have proven to be especially harmful to growth when they jeopardize price stability and cause the level of public spending to be unsustainable or excessive in relation to the size of the economy. Starting in the early 1990s,

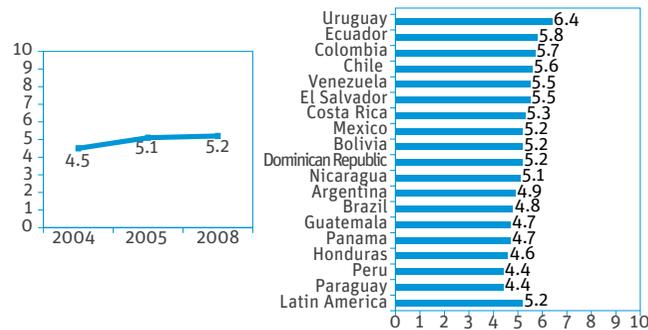
Figure 1.10 Good Functioning of Government Institutions, Latin America, 2002–08; Totals Per Country, 2008



Source: Latinobarometer (Latinobarómetro) (2002–08).

Note: The results for the figure were determined on the basis of the answers to the following question: “Generally speaking, what is your opinion of how well government institutions work? Would you say they work very well, well, okay, badly or very badly?” Only the “very well” or “well” responses appear here.

Figure 1.11 Compliance with Laws, Latin America, 2004–08; Totals Per Country, 2008



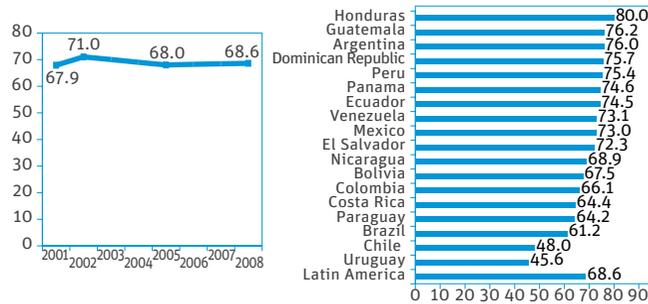
Source: Latinobarometer (Latinobarómetro) (2004–08).

Note: The results for the figure were determined on the basis of the answers to the following question: “On a scale from 1 to 10, where 1 is ‘The government is not achieving compliance with any law’ and 10 is ‘The government is achieving compliance with all laws,’ where would you rank (country)?” Only the “average” responses appear here.

measures were taken to control inflation, bolster public finances, reduce public indebtedness, and lend greater stability to financial sectors. However, despite the progress achieved with macroeconomic policies, these problems persist. In the IDB study *All That Glitters May Not Be Gold* (IDB, 2008a), it is emphasized that a good deal of the improvement in macroeconomic indicators in recent years was due to an exceptionally benign international environment. Setting aside the influence of this environment, the problems of fiscal and external fragility continue to afflict many countries. In the new international environment, these weaknesses have become evident.

The region’s *financial system* requires sound regulation and further development in order to meet the demand for resources from productive sectors. Strengthening regulation and financial oversight is vital for ensuring the stability of the financial system. There is a need for a system of standards and mechanisms enabling the financial system to properly manage the risks it has assumed, thus protecting the integrity of deposits. Although the region as a whole has made important strides in all of these areas, the financial

Figure 1.12 Prevalence of Corruption among Public Officials, Latin America, 2001–08; Totals, 2001–08



Source: Latinobarometer (Latinobarómetro) (2001–08).

Note: The results for the figure were determined on the basis of the responses to the following question: “Imagine that the total number of public officials in (country) is 100 and you have to say how many of these 100 officials you believe are corrupt. How many would you say are corrupt?” Only the “average” responses appear here.

industries of many countries continue to have a weak foundation and in some cases lack adequate regulation and oversight. The current crisis in the financial systems of developed countries has also called into question some international practices concerning certain aspects of risk regulation and the organization of regulatory systems.

Inadequate *physical infrastructure* can limit improvements in productivity, new investments and growth. An index that combines indicators of coverage and quality of telecommunications services, electrical utilities, ports and

roadways shows that 10 Latin American countries (out of a total of 21 for which information is available) do not meet international standards for countries in their income group. Starting in the early nineties, the region made the greatest progress in the area of telecommunications, with increased coverage and significant improvements in quality in many countries.

This improvement in telecommunications has facilitated the adoption of information technologies (IT), which in Latin America has occurred more rapidly on average than in other regions of the developing world, and at a level exceeding international standards for countries in their income group, although major disparities in access still persist. Although the level of coverage by the power industry is high, exceeding 85% on average, this coverage is not uniform for all countries. While in some countries coverage surpasses 95%, there are still nations where it is under 70%. More worrisome developments include the fragility of the reforms underway, the lack of interest of private business in investing in the capacity expansions required in conditions of regulatory and economic uncertainty, and the inability of state-run

companies—as well as of some private ones—to collect payments and deal with the losses caused by inadequate billing and distribution.

There are also major deficiencies in roadways and ports, which have a significant effect on the cost of transportation, limiting the region's ability to compete in international markets. Not only is the density of the road network very limited in most Latin American countries, especially in rural and marginalized areas, but the condition of their roads is precarious. Port efficiency indicators place Latin American ports in one of the lowest positions, only ahead of the poor countries of Asia and Africa.

The low levels of *education and human capital* have become an obstacle to growth in many countries because they limit the possibilities of technological modernization and increases in productivity, especially in the poorest countries. Indicators of education for Latin America and the Caribbean reveal a much slower rate of progress than in other regions of the world, in addition to serious deficiencies in terms of quality. In many countries, the educational advancement of the younger generations has been very modest (Figure

1.13). The problem in Latin America and the Caribbean is not lack of initial access to the education system, but poor attendance by children from middle-class and underprivileged families. Consequently, most countries in the region have high school graduation rates that are low for their income level.

Although deficiencies in the area of health are less generalized than in education, a characteristic shared by most countries in the region is the inequality, in terms of nutrition, illness and mortality, between low- and high-income groups, which constitutes a significant impediment to the productive inclusion of the poorest members of society.

An *unstable international environment* has chronically affected Latin America, limiting its growth. During the 1990s, terms of commercial trade fell by 7.6% and were subject to great instability. This trend came to an end in 2003, and from early 2006 to the middle of 2008, commodity prices experienced an extraordinary surge, comparable only to what occurred in the early seventies. This price surge recently came to an abrupt end with the worsening of the international financial crisis. Export revenues have been affected not only by price instability but also by severe

(Continued on page 26)

Interview with Pedro Pablo Kuczynski



Over the course of a prestigious professional career, Pedro Pablo Kuczynski has done outstanding work in the private as

well as the public sector. Having studied economics at Oxford University and Princeton, he has held important posts in multilateral organizations, leading banks, and the Peruvian government. The latter include President of the Central Bank of Peru, Minister of Energy and Mines, Minister of the Economy and Finance, and the role of Prime Minister.

Is it possible to give a brief summary of the changes that have taken place in Latin America and the Caribbean over the past half-century?

I would say that what has happened is most obvious. The region has grown and changed in many ways, but at the same time it has the world's worst income distribution with poverty rates that are still very high. In the same time period, not only has Eastern Europe emerged as an economic power, but Asia as well. Thus, global performance has had some very positive aspects, but in the same breath it has brought some letdowns.

On the positive side, what would stand out?

The fact that Latin America shows a sizable growth in its middle class, which wasn't the case in 1959 when the IDB was created. Also, social and health services have improved, as well as telecommunications. Overall, Latin America is a society on the road to modernization.

And on the negative side?

We have a wealth distribution that is measured in a Gini coefficient that's close to .055 and is behind other

regions of the world. There are different cases within Latin America with some countries better off than others, but also with some wealthy nations showing inconsistencies. I think the main cause for this inequality has to do with there being a lot of poor people, which goes without saying. And with few exceptions, governments have not learned how to provide services and succeed in including lower-income populations in the economy.

What do you think has happened with poverty?

There are two basic factors that explain it. The first is education, with levels of schooling that are still low and problems with quality. The second is infrastructure, which is still trailing behind, and that dooms millions of people to fall further behind.

Why did the gap with Southeast Asia widen?

There are a number of reasons. Without question, one very important factor in Asia was the high level of savings that allowed them to move ahead with sizable investments once the local economies opened up. It

must also be pointed out that Asian nations that were locked down tight 50 years ago have opened up more than Latin American ones. Likewise, we cannot ignore the impact of the debt crisis that caused us to lose everything in terms of growth during the eighties.

Have we not learned from past experiences in order to avoid repeating our mistakes?

Yes and no. Some countries have moved ahead while others wobble along. I would say the lessons prove that Latin America's setbacks have been due to government activities that were not well planned or well thought out as far as the consequences. There has been instability in fiscal policies and too much bureaucracy in public administration. It has been thought that price controls lower inflation, but in actuality they do the opposite, and there have been periods of nationalization that have massively set back investments.

Why was Latin America the region with the least amount of growth during the recent boom?

There is no one answer. In some cases Latin America needed more opening up, and I am not only referring to business but legal and labor standards. Generally speaking, there was a lack of competition.

How do you view the current crisis?

The crisis is going to have a differentiated impact. Those most vulnerable are nations that saw a considerable rise in their foreign debt, which grew overall in the case of the private sector. The other consequence is going to be a total reduction of exports. Exports have always been one of the driving forces for growth. In brief, this is going to be a rather slow year.

What would you like to see in the region?

Economic policies with common sense. Instead of talking about mod-

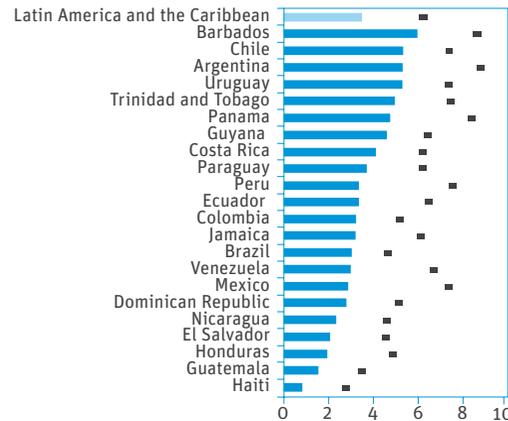
els, neo-liberalism and privatization, I would like to see government programs, and I repeat, common sense programs. This means promoting investment and savings, having open financial systems with a great deal of regulation and having more resources for infrastructure, including educational infrastructure. This is the area where Latin America is generally shaky.

How do you understand the role of an entity such as the IDB?

I believe the IDB is experiencing a renaissance because up to a short while ago, there were those who wanted to declare it dead on arrival. But now that capital markets have dried up, the IDB's role is essential. I think this is going to be a highly difficult period of transition where two strategies must be mapped out: one of creating bridges to promote business or support countries with their pressing problems, and another that will include issues related to the private sector or infrastructure.

(Continued from page 23)

Figure 1.13 Average Years of Schooling for People over the Age of 15, Latin America and the Caribbean, 1960–2000



Source: IDB (2006).

distortions in international markets caused by large subsidies given by developed countries to agricultural producers and by the restrictions they impose on the importation of products from developing countries. Access to international sources of financing has been very unstable and limited. Periods of abundance, such as those that occurred at the end of the 1970s, the first half of the 1990s, and from 2003 to 2007, have been followed by acute peri-

ods of distress. Sudden changes in the perception of a country's riskiness and the ripple effect of contagion are factors of instability that limit the growth of the region's countries.

NEW AND OLD CHALLENGES

The evidence from numerous studies and the half-century of experience that the IDB and other international financial institutions have had in developing countries has taught valuable lessons on the difficulty of achieving sustainable economic growth. The more general and obvious lesson is that there is no single formula that guarantees growth. Thus, the emphasis on maintaining adequate levels of savings and investment in the 1960s and 1970s proved to be insufficient as a strategic guide for development policies. The importance that was later given to the liberalization of trade and to the other precepts of the Washington Consensus formed an incomplete list, the effectiveness of which hinged upon a variety of factors.

The potential barriers to sustainable growth are many. Even when the basic conditions for sound macroeconomic management are in place and the main markets for goods and services func-

tion properly, sustainable growth may be hindered by such varied factors as the absence of institutional and policy mechanisms for responding to a crisis or explicitly identifying the social costs of exploiting natural resources and the degradation of the environment. In addition, it may be hindered by the absence of coordinating mechanisms that facilitate the optimization of competitive opportunities requiring joint action on the part of many economic agents. It may also be hindered by clashes over distribution and blocking strategies implemented by some ethnic, social or political groups against others, making it difficult to invest in public assets that are essential for development (such as safety, infrastructure and the conservation of natural resources). Inequality and social exclusion can also limit the potential for growth insofar as they slow the accumulation of physical and human capital, reduce investment yields, fuel social conflict and clashes over the redistribution of wealth, and make it difficult to adopt effective policies for handling external shocks.

These and other factors have led development analysts and experts to humbly recognize that there is no single formula applicable to all coun-

tries, and that each case requires a specific analysis. A recent current of thought that has been very influential in the region is being promoted by three academics, Hausmann, Rodrik and Velasco, in *Growth Diagnostics* (Hausmann, Rodrik and Velasco, 2005). They argue that an effective diagnosis must identify the most serious restrictions limiting growth in each specific country, instead of creating a long wish list of desirable conditions that would make the country in question a developed country if those conditions were fulfilled. Their method of analysis separately identifies the most serious restrictions, which naturally leads to the prioritizing of the economic policy measures that appear the most promising.

Such considerations are vital in light of the foreseeable impacts of the current international crisis, which threatens to condemn the region to reliving the eras of zero growth in per capita income, with an increase in Latin American GDP of only around 2% in 2009. Although various measurements show that fiscal and external debt ratios are the best in recent decades, vulnerability of the region's countries to lower prices for raw

materials, to limited investment flows and to the decrease in sources of financing is also clear.

Faced with the certainty that difficult times are at hand, the challenge confronting the nations of Latin America and the Caribbean is not only to maintain macroeconomic stability, but also to ensure that the brunt of the international economic crisis is not borne by their poorest citizens, many of whom personally suffered from the impact of higher fuel and food prices during the first half of 2008. Faced with this challenge, one hopes that the lessons of the past will be applied and that the Western Hemisphere as a whole will be capable of returning to the path of rapid growth, once recovery begins.

The certainty of better days to come, which are just as inevitable as economic downturns, should be heartening to those who view the current difficulties as insurmountable. However, the optimism of Latin Americans, who generally express satisfaction with their quality of life (IDB, 2008b), should not obscure the disappointments of the last half-century, during which the region grew, but at a slower pace than other regions.

Although per capita income (in 2000 prices) has more than doubled, going from US\$2,000 in 1960 to the current amount of around US\$4,500, and life expectancy is now 73 years, 17 years longer than when the IDB came into being, the road ahead is still very long. A promising future undoubtedly lies ahead for the region, but to a great extent it will be determined by whether the peoples of a continent that has teetered for decades between potential wealth and disaster also learn from their past.

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¹ In 1990 constant dollars.

² The term “Washington Consensus” was coined by economist John Williamson in a document made public in November 1989 and presented at a conference of the Institute for International Economics. The principles set forth in the Consensus were fiscal discipline, reordering public spending priorities, tax reform, liberalizing interest rates, competitive exchange rates, liberalization of international trade and of inward foreign direct investment (FDI), privatization, deregulation and the strengthening of property rights.

³ Note that these calculations rely on prices in terms of purchasing power parity (PPP), which is used to make income comparisons between countries. In the present case, the PPP prices used are from the historical data in the Penn World Tables 6.2. However, recent PPP price calculations indicate that mean per capita incomes for Latin American countries are currently 25% (not 15%) of developed-country incomes. In any event, it remains true that Latin America has fallen behind in relative terms compared to the developed countries, since the growth rates of these countries are not affected by these comparisons.

⁴ These diagnostic elements were included in the sustainable growth strategy guidelines approved by the IDB in 2003. The original text, which was used as a basis for the following paragraphs, has been updated and adapted especially for this publication.



Grass-roots democracy. Stakeholders meet to provide input on a large-scale sanitation project involving the cooperation of municipalities that share a common watershed. By participating in decision making, citizens are helping to build democratic institutions that go deeper than national elections and political parties. In this way, citizens join with local officials in taking on the responsibilities of planning for the future, deciding how money will be spent, and carrying out programs to improve social and economic welfare.

II Democracy: A Path of Learning

Between late 2005 and 2007, Latin America experienced the most intense electoral period in its history. During this time, 13 presidential elections took place, 10 of which occurred in late 2006. However, what is perhaps most striking is that these events failed to generate major headlines beyond the usual ones announcing a change in government. As noted by César Gaviria, the former Secretary General of the Organization of American States (OAS), “exercising the right to elect and be elected is no longer something out of the ordinary in the region.”

This, however, was not the case a half-century ago when, amid the tentacles of the Cold War and poorly understood nationalism, power was increasingly being exerted by civilians or the military, who resorted to violence in an attempt to direct the destinies of their respective nations. This trend only intensified over the decades that followed, until in 1977, only three Latin American countries (Venezuela,

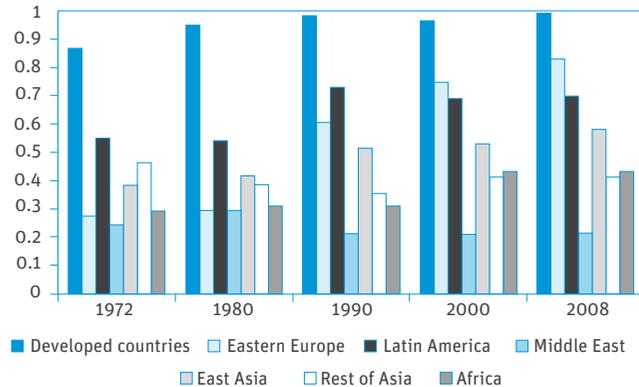
Colombia and Costa Rica) and a handful of Caribbean islands had functioning democratic systems.

Since then, the list of democracies has again begun to grow gradually, to the discredit of the totalitarian regimes that restricted not only economic freedoms but also the exercise of basic rights and were responsible for human rights violations that left a trail of suffering in a good part of the region. But changes on the international scene, combined with internal social pressures, allowed electoral practices to gain ground, and the pendulum swung to the side of democracy.

Nevertheless, the transition has not been easy, as illustrated on these pages, where the achievements and challenges of recent years are described. As the foundation for exercising the right to vote has continued to solidify, the tapestry of governments trying to respond to the aspirations of peoples who demand progress, equality and better-quality services from them has become more complex. This has occurred in the

Figure 2.1 Index of Political Rights and Civil Liberties, Regions of the World, 1972–2008

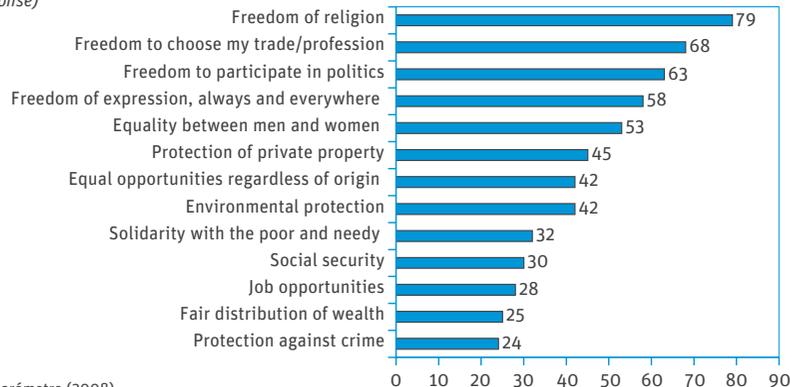
(Simple averages)



Source: Freedom House.

Figure 2.2 Democracy Guarantees, Latin America, 2008

(Percent response)



Source: Latinobarómetro (2008).

Note: Results are based on respondents' answers to the following question: "To what extent are the following rights, freedoms, opportunities and safeties guaranteed in your country?" Only the following answers are reflected here: "Completely guaranteed" and "Somewhat guaranteed."

context of a changing economic environment that has seen positive growth rates only in recent years and that is once again facing the uncertainty created by a complex international situation.

The challenge remains real. It is a hard truth that the quality of public institutions depends on the quality of politics and democracy (IDB, 2005). Politics is also the most sensitive thread in the tie between institutions and the economy. Simply stated, political systems matter, and they are critical for any economy (Carrillo Flórez, 2006). Affirmation is crucial in that free elections must be understood as a necessary but insufficient condition for democracy to function adequately in the region.

That said, in recent decades Latin America has made notable progress toward civil and political liberty. In the 1970s, the region was not in a particularly favorable position in this regard compared to other groups of developing countries and lagged far behind developed nations. By the 1990s, however, and more clearly in the early years of the 21st century, the gap had narrowed, and the region now boasts indicators of civil and political freedom that are higher than those of any other emerging area (Figures 2.1 and 2.2).



Community police in Bogotá, Colombia, break down the barriers that have traditionally separated local citizens from law enforcement institutions. Bicycles are their preferred mode of transport.

Progress toward democracy in the region over the past two decades is even more impressive if viewed from a long-term perspective. The available indicators, which cover nearly two centuries, effectively show that no other region on the planet has made a leap of this magnitude in a similar period. After the reversal of democracy in the region between the mid-1960s and late 1970s, the progress that followed

has been sustained and profound and has encompassed the vast majority of Western Hemisphere nations.¹

On the other hand, opinion surveys such as Latinobarómetro consistently show that, although the resounding majority of Latin Americans consider democracy the best form of government, there remains a sense of dissatisfaction intensified by the limited achievements of the system (Table 2.1).

Table 2.1 Attitudes Toward Democracy in Latin American Countries, 2008

	Support for democracy (Percentage)	Churchillian democracy (Percentage)	How democratic the country is (Index 0–10)	For the good of the entire population (Percentage)	Country in which democracy works best (Percentage)	Democracy is essential in order to be considered a developed country (Percentage)
Argentina	60	77	5.8	10	17	67
Bolivia	68	77	5.5	35	12	55
Brazil	47	82	6.0	37	33	57
Chile	51	70	6.0	23	44	58
Colombia	62	82	6.1	28	30	58
Costa Rica	67	78	6.5	18	42	60
Dom. Republic	73	79	6.8	10	17	77
Ecuador	56	60	6.0	29	12	62
El Salvador	50	63	5.4	28	8	63
Guatemala	34	58	5.2	23	8	64
Honduras	44	66	5.5	16	7	64
Mexico	43	69	5.0	19	23	67
Nicaragua	58	67	5.4	27	14	69
Panama	56	71	5.9	12	15	70
Paraguay	53	70	5.0	43	10	74
Peru	45	63	5.0	8	7	76
Uruguay	79	88	7.1	49	43	78
Venezuela	82	86	6.6	35	33	85
Latin America	57	73	5.8	25	21	66

Source: Latinobarómetro (2008).

The legitimacy of the democratic system, backed by undeniable popular support, has been accompanied by actions intended to strengthen the foundation of democracy. One of the most important initiatives was the adoption of the Inter-American Democratic Charter by the OAS on September 11, 2001.² It not only affirmed that “essential elements of representative democracy include, *inter alia*, respect for human rights and fundamental freedoms, access to and the exercise of power in accordance with the rule of law, the holding of periodic, free, and fair elections based on secret balloting and universal suffrage as an expression of the sovereignty of the people, the pluralistic system of political parties and organizations, and the separation of powers and independence of the branches of government” (Article 3), but it also stated that “transparency in government activities, probity, responsible public administration on the part of governments, respect for social rights, and freedom of expression and of the press are essential components of the exercise of democracy” (Article 4). It was also made clear that “democracy and social and economic development are interdependent and are

mutually reinforcing” (Article 11). In addition, the 34 nations that make up the OAS agreed that any infringement of democracy within any of the member states would result in its suspension from the organization upon an affirmative majority vote, as set forth in Article 21 of the Charter, an article that was adopted and adapted to the realities faced by other entities belonging to the inter-American system, including the IDB.

THE EFFECTS OF DEMOCRATIZATION

Democratization has generally involved a real redistribution of political power. Firstly, rights and liberties have seen enormous progress. Free and competitive elections have become the most important factor in the political process, at the very least giving the majority of the population the power to generate the uncertainty that characterizes change. Additionally, power has been geographically redistributed and democratized through an extensive process of decentralization aimed at regions and municipalities. This represents, however, some significant fiscal and administrative risks, and even, in

some countries, tensions. Lastly, ethnic minorities and women have achieved much higher levels of representation—something that a few decades ago would have been unthinkable—making a greater and greater impact on the political process (Payne, Zovatto and Mateo Díaz, 2006).

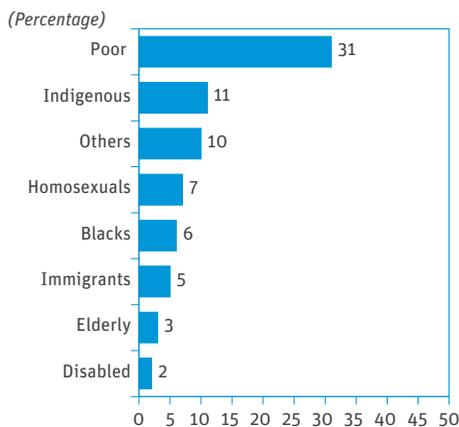
The relationship between the government and the market has also experienced important changes as a

result of the economic reforms implemented in recent decades, including the opening up of entire sectors of production that were previously dominated by inefficient, state-run monopolies. However, for those in the know, the transition toward a greater emphasis on the market has not been accompanied by sufficient development of regulatory frameworks that promote competition and protect consumer interests. Furthermore, the transition to a free market has been uneven and, in quite a few cases, has been a function of the ability of organized interests to take advantage of or resist the winds of change (Payne, Zovatto and Mateo Díaz, 2006).

Certainly, democracy has brought new opportunities for previously disadvantaged groups to organize, while increasing incentives for political parties and leaders to respond to their demands. Despite the formal equality and political rights guaranteed in the constitutions of these nations, the democratic system continues to limit the formal channels of influence for certain groups of citizens who continue to have a reduced presence in decision-making processes (Figure 2.3). Nevertheless, for the first time in some

(Continued on page 40)

Figure 2.3 Most Frequent Victims of Discrimination, Latin America, 2008



Source: Latinobarómetro (2008).

Note: Results are based on respondents' answers to the following question: "From what you know or have heard, who do you believe are the persons or groups most discriminated against in your country, or do you believe that no one is discriminated against in (country)?" This was an open-ended question. Only answers with a percentage of 2% or higher are reflected here.

Interview with Mario Marcel



Mario Marcel is the Manager of the IDB's Institutional Capacity and Finance Sector. He has held various positions through-

out his professional career, serving as Chairman of the Presidential Advisory Board on Pension Reform in Chile and lead researcher for CIEPLAN (Corporación de Estudios para Latinoamérica), Director of the Chilean Budget Office, President of the Government Internal Auditing Council and member of the Public Companies Administration System Council in Chile. He holds a master's degree in economics from the University of Cambridge, Great Britain.

How would you describe the changes taking place in democracy in Latin America and the Caribbean over the past 50 years?

The most evident and relevant change is that Latin America has gone through a period of authoritarian governments and dictatorships over the past 50 years that affected a good part of the continent, but for the last 20 years, democracy has returned to all of the region's countries. This is a major change that all of us who have lived under a dictatorship can appreciate. This change has come with significant involvement on the part of the citizenry, which shows that we don't just have formal electoral processes. Even when there have been problems in the region's countries, we were able to find a way out of those situations within the rules of the constitutional game. I believe democracy in the region at this point is irreversible. Moreover, democratic principles have been spreading to the local level in the region as a result of decentralization. Having said that, I believe there have also been advancements in the construction of governance by the rule of law, in the strengthening of civil and political rights, and the creation of institutions

to respond to voices like those of indigenous peoples, women or the regions.

What do you think the IDB's role has been in this process?

The IDB has recognized that democratic governance is a resource for ensuring sustainable economic and social development. This has manifested itself through loan programs where approved loans represent more or less 16 percent of the Bank's activity over the past 50 years. Among its many initiatives, the Bank has lent support to the control systems of the region's countries, to the processes of decentralization and to the modernization of governments and public authorities. What is also interesting is the role that the Bank has played in the dialogue process with the region's countries.

How do you see the future of democracy in the region? What should the IDB's role be?

I believe it's necessary to recognize and know how to respond to the changing demands of the citizens. For this reason it's necessary to support the region's countries for the purpose of improving how we integrate new actors, recognizing diversity and what

that means in terms of articulating and organizing more complex societies. This broadening voice is bringing about changes to standards of how institutions should behave. I'm referring to the fact that nowadays, many things once a part of doing business in financial management or in national congresses are now being rejected by the people. What I believe is essential, as far as what's required in order to face these challenges, is to understand that institutional capacity covers more than the simple management of certain agencies, it goes beyond our understanding of government or public administration. I think the Bank has an important place in these processes because the IDB's ability to understand the countries and be understood is possibly greater than that of any other multilateral agency in the region. This ability to get inside the logic of these countries, to understand what is happening, is of paramount importance for the Bank. I believe the institution also has to develop comparable advantages in certain areas, such as local development, safety for citizens, transparency and fighting against corruption, just to name a few.

Adults in a low-income neighborhood near Rio de Janeiro get literacy training that will enable them to participate in civic affairs and improve their lives.



Through mediation and arbitration programs, the IDB is helping countries to unclog their court systems by broadening the range of alternatives for settling disputes.

(Continued from page 37)

countries, new democratic systems have extended the right to vote to all citizens of legal age.³

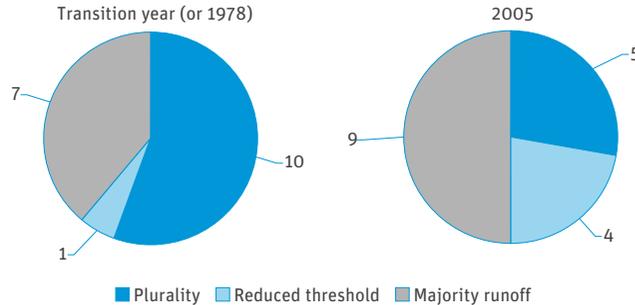
In light of the above, there have been moments of great instability in some of the region's countries: 16 governments did not complete their terms of office in the last decade. All have exited democratically, however, with the rules of the game being followed in replacing them (Mateo Díaz, 2007). The citizens have wagered on a peaceful way to resolve their conflicts, accepting the results of the ballot box, in many cases with high levels of voter participation. As such, the good news is that the citizens of Latin America are gradually recognizing this political system in terms of the immediate benefits or concrete satisfaction that they might receive: the seeds of a democratic culture are present.

Almost concurrently, a number of constitutional revision processes have taken place in which at least six different adopted lines of reform can be identified (Carrillo Flórez, 1999). The first is the transition from presidential systems with peripheral legislatures to more highly balanced and collaborative structures with an emphasis on modified supervisory missions for legislative

powers. The second is the move from centralist, closed state systems toward scenarios of political, administrative and fiscal decentralization with increased citizen participation. Third, democracies blocked by intermediaries and representatives from interest groups have evolved toward a resurgence of civil society and general interests within the framework of direct democracy. Fourth, a switch has taken place from rhetorical declarations of rights to basic rights charters that provide guarantees and immediate mechanisms for constitutional protection. Fifth, a transition has been noted from a weak interventionist state to a strong, capable regulationist state with autonomous economic authorities, such as central banks that are immune to the influence of petty politics, regulatory entities and commissions. Lastly, there has been a shift from inconsequential judicial systems to their resurrection in an environment of independence and great visibility, in some extreme cases representing what some are already describing as the "judicialization of politics."

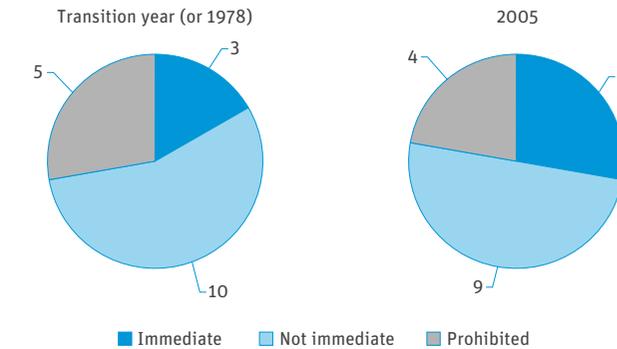
As a result of these changes, in presidential election systems there has been a clear shift from pluralistic

Figure 2.4 Trends in Presidential Election Systems in Latin America
(Number of countries)



Source: Payne et al. (2006).

Figure 2.5 Presidential Re-election Trends in Latin America
(Number of countries)



Source: Payne et al. (2006).

schemes (in which the candidate wins with a majority of the vote) toward first- and second-round systems, in which a selection is made among two or three finalists (Figure 2.4). For example, while in 1978, when democracy began its regression, the number of countries in the region with pluralist systems totaled around 10, this number had been reduced to five by 2005.

Moreover, the rules governing elections were changed in 11 countries during the period mentioned. In one out of every three Latin American countries with a presidential system, the president has the opportunity to repeat a term of office immediately, although this door was in fact almost completely closed three decades ago (Figure 2.5). The debate over the merits and disadvantages of this trend continues, as those who favor continuity remain concerned about the system of checks and balances needed to maintain equilibrium in governmental powers. There are also questions surrounding the relative weakening of political parties in favor of individuals, leading to warnings about a return to caudillismo (Prats, 2003). In addition, the decline of

political parties is also associated with corruption scandals, infrequent party reforms or platforms that have not earned the approval of voters.

Experts point to increasingly complex relationships between executive and legislative branches, which have made a fine art out of combining their capacity for action with their capacity for control (Payne, Zovatto and Mateo Díaz, 2006). Clearly, the latter must be an autonomous entity in relation to the former, without systematically blocking every action taken by the government as a result. Rather, parliaments must exercise constructive control and debate to help improve the quality of the proposals that come before executive branches by formulating concrete and viable alternatives. This skill is closely related to the elements mentioned above, such as the fragmentation of the party system and the ability to form coalitions and generate consensus.

Another notable phenomenon of recent times is the institutionalization of agencies of horizontal oversight, constituting one of the great advances in the process of democratic consolidation in Latin America (Payne, Zovatto and Mateo Díaz, 2006). The instru-

ments adopted by Latin American democracies for controlling abuses of power are multiple and diverse, but their institutional sustainability will depend on their efficient use as well as on the legitimacy that they must continue to gain as central agents of control. The independence of the judicial branch as well as the coordinated interactions among institutions of oversight, the attorney general's office and human rights advocacy groups confirm the need for concurrent, complementary systems.

THE IMPORTANCE OF POLITICAL PARTIES

Without a doubt, the concept of modern democracy revolves around a system of parties, where at least two of these compete freely for power. Consequently, the proper functioning of these groupings, which are crucial in the selection of candidates and in pushing through proposals, among other aspects, is essential to a functioning democracy (Payne, Zovatto and Mateo Díaz, 2006).

The last three decades have seen profound legal modifications to the institutional structures of most Latin

Figure 2.6 Party System Institutionalization and Degree of Programmatic Orientation

Index of programmatic parties, scale 0–8)



Source: IDB (2005), based on Jones (2005).

American countries, including constitutional reforms as well as changes to the laws governing electoral processes and political parties (Figure 2.6). However, in their early stages, these reforms skirted the issue of internal democratization of political parties, apart from token nods to democratization in national constitutions. In the second reform stage, carried out during the 1990s (particularly during the second half of the decade), the issue of the

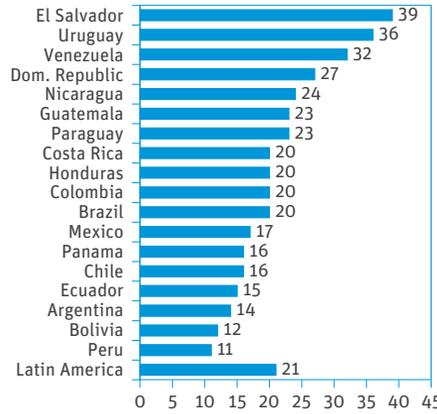
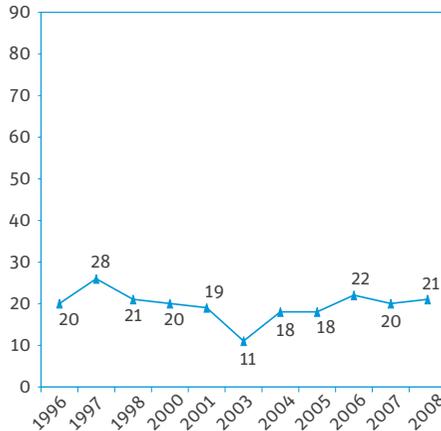
internal democratization of political parties gained importance in terms of both the election of partisan authorities and the selection of candidates by popular vote as well, particularly the presidents of the region's countries (Payne, Zovatto and Mateo Díaz, 2006).

In an ever-growing number of countries, the election of a candidate to the presidency, decided in the past by the top hierarchs of the party or internal conventions, now takes place through various types of internal elections that strengthen the legitimacy of whoever is elected. The idea behind these reforms is that greater intra-partisan competition provides greater levels of internal democracy, a greater capacity for representing the diverse interests of the party and society (assuming that internal party elections are open), the possibility of resolving conflicts between different administrations and improved legitimacy of the organization in the eyes of the public (Payne, Zovatto and Mateo Díaz, 2006).

The negative effects of this openness on the life of a political party manifest themselves primarily in terms of that party's internal cohesion

Figure 2.7 Confidence in Political Parties, Latin America, 1996–2008; Totals by Country, 2008

(Percentage)



Source: Latinobarómetro (1996–2008).

Note: Results are based on respondents' answers to the following question: "Please look at this card and tell me, for each one of the groups/institutions/persons mentioned on the list, how much confidence you have in it: a lot, some, very little or no confidence, in (...)" Only "political parties" and the responses "a lot" and "some" are reflected here.

and harmony. Certainly, adopting internal democratic practices has led to, in many cases, a surge in confrontations between different party factions, the fragmentation of parties and even their division. It is unclear whether this trend has improved the image of the parties in the eyes of the general public (Figure 2.7).

Thus, the parties of the region continue demonstrating clear weaknesses due to their low degree of

institutionalization, their growing fragmentation and a reduced ideological polarization that sometimes keeps them from standing out in the eyes of voters (Payne, Zovatto and Mateo Díaz, 2006). Although it is difficult to make generalizations concerning this issue due to the uniqueness of each country's situation, one of the reasons for this phenomenon may be the decreased programmatic focus of the parties, as their preoccupation with internal election mechanisms may have affected the level and intensity of proposal discussions.

THE DILEMMA OF POLITICAL FINANCING

With regard to political financing in the region, it is necessary to begin any discussion of the issue with two main points. First, the financing of political parties and electoral campaigns is a complex, controversial and unresolved issue, one in which there are no panaceas or silver bullets and where perfection is achieved through baby steps rather than through extensive and highly ambitious reform initiatives. Second, during the last two decades, important progress has been made

in this area, although to substantially different degrees among the different countries (Table 2.2). After being virtually absent from the region's political agenda for some time, the issue has been receiving increased attention, not just on a national level, where an intense reform process has taken place, but also in the form of specialized

Table 2.2 Beginnings of Public Financing of Political Parties in Latin America

Country	Year
Uruguay	1928
Costa Rica	1949
Argentina	1957 (indirect) and 1961 (direct)
Peru	1966 (indirect) and 2003 (direct)
Venezuela	Established in 1973 and eliminated in 1999
Nicaragua	1974
Mexico	1977
Ecuador	1978
Honduras	1981
El Salvador	1983
Colombia	1985
Guatemala	1985
Chile	1988 (indirect) and 2003 (direct)
Paraguay	1990
Brazil	1995
Bolivia	1997
Dominican Republic	1997
Panama	1997

Source: IDB (various years).

conferences of experts on the topic, and it has caught the interest of the hemisphere's heads of state and political parties themselves (Payne, Zovatto and Mateo Díaz, 2006).

In Latin America, a mixed system formally predominates, with a tendency toward favoring public financing and a proclivity for emphasizing legal limits on private contributions. Nevertheless, due to a combination of factors, such as inadequate regulation, the inefficiency of monitoring agencies and of systems for penalizing infractions of the rules, and political practices that have thus far favored violation of the rules, public financing has in many cases functioned as a complement to private financing rather than as a partial substitute for it. As a result, and despite its positive contribution, its impact thus far has been limited and has varied from country to country.

However, a trend has been observed in favor of controlling the triggers of electoral waste, establishing caps and shortening campaigns, with varying results in different countries. This trend has been accompanied by a reorientation of public resources, based on the concept of electoral in-

(Continued on page 50)

Interview with Julio María Sanguinetti



Julio María Sanguinetti, the former president of Uruguay, is one of the Western Hemisphere's most authoritative voices

on the subject of democracy. Not only was he the first democratic president elected in his country—in 1984 after a military dictatorship lasting more than a decade—but he returned to that post a second time in 1995 as a result of the popular vote. A renowned writer and analyst with a constant presence in the press, Sanguinetti talks about democracy in the region in this interview.

How would you describe the changes that have taken place in democracy in Latin America and the Caribbean over the past 50 years?

No one can objectively argue that the democratic system has not moved forward in Latin America in the last half-century. We are full of frailties and inadequacies, but we are no longer drowning in the instability of the Cold War, which not only encouraged guerrillas and handed them weapons, but gave its imprimatur to coups d'états. Fidel Castro's arrival in Havana in 1959 proved to be a key event of this period. It was the same way with the opposite camp, with the beginning of the Brazilian military dictatorship in 1964, which put an end to the developmentalist initiative begun by Juscelino Kubitschek and continued by João Goulart. In Argentina, after Perón was overthrown, another great developmentalist experiment led by Arturo Frondizi was thwarted and then abruptly cut off by a coup d'état in 1962. Mexico was taking its pro-PRI siesta and turned rather turbulent on more than one occasion, but in the end it opted for ensuring constitutional continuity instead of a monopolistic political hegemony. Lengthy dictatorships sprang forth during

those years, such as those of Somoza in Nicaragua, Duvalier in Haiti and Stroessner in Paraguay, while experiments of a very diverse nature took place in other countries like Peru. Peru went through democratic governments like that of Belaúnde Terry, and military dictatorships not just on the right but to the nationalistic left as well. More recently, around the time I came to power for the first time in Uruguay in 1985, Argentina had just returned to democracy under Alfonsín. Shortly thereafter, Brazil took the same steps under José Sarney. Two decades of military rule ensued. Then the democratization of Chile, Paraguay and Nicaragua came, beginning a democratic wave that has lasted to this day. We cannot ignore the fact that several elected leaders who couldn't finish their term in office have fallen, such as in Argentina, Ecuador and Bolivia; on the other hand, there have been no military relapses, and governments were able to re-establish themselves, though not without a lot of problems.

What was the most painful lesson taught by the presence of dictatorships in much of the Western Hemisphere?

The greatest lesson is that making a deal with the devil, to exchange liberty

for order, carries a curse. Once liberty is lost, true order, which is the rule of law, vanishes and the so-called commitment to progress never emerges. Add to that the consequences of hatred and the open wounds left by violence.

The most recent polls report that people in the region like democracy, but at the same time are very critical of it. What do you think about this?

Citizens are accustomed to confusing governments with the system itself. They usually judge from the outside looking in, as if they had nothing to do with it. Nobody voted for any presidents in any elections who managed to get re-elected. The political winds keep shifting, and these bouts of ill humor are very dangerous for our electorate. They speak poorly of our political parties and cast into doubt the worth of politicians in a dangerously razor-sharp generalization that strikes at the very heart of the system. Since it's all based on the popular vote, governments aren't going to be any better or worse than the citizens who elect them. Democracy cannot be managed by polls. Their legitimacy arises from the vote and voters. That's why these bouts of disenchantment make me really uneasy.

What has been the biggest failure of democracy over the past 50 years?

Democratic leaders are like prisoners chained by high expectations on the one hand and the need to maintain financial equilibrium on the other. Perhaps the greatest weakness lies in the fact that vast segments of our society persist in the stubborn notion that everything is possible. A greater civic-minded culture, a greater economic rationality must be at the center of democratic learning, because it teaches that social development is possible only within the framework of the rule of law and economic progress.

It's clear the focus has shifted from where it was in the beginning, which was having free and open elections. What is your interpretation?

Democratic governments that were unable to complete their term of office fell because of street uprisings, many of which were quite organized, expressing vague feelings of vindication. They generally coincided with tough economic times. The economic boom of the past five years, on the contrary, generated the opposite temp-

tation: to keep governments in power who were fortunate enough to be able to share the wealth. Today, the scenario is different: there is the danger that those who can no longer continue offering what they've been giving away will resort to authoritarian measures, attacking democratic legitimacy.

Do you think decisions such as those made at the heart of the integration accords or within regional multilateral organizations to make democracy a prerequisite in order to participate are meaningful?

It's essential, but we don't anticipate that there will be a great rush to enforce it.

Do you think that the government authority and the checks and balances system have developed appropriately?

World history tells us that true democracies can emerge only when Jeffersonian popular sovereignty is combined with Locke's concept of individual liberty and Montesquieu's checks and balances. In recent years, Latin America has experienced many imbalances. The courts do not always have the independence they need. Parliaments have continued to lose

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institutional prestige in many countries. And the consequence is a dangerous imbalance. Hence, the attempts to remake countries by methods outside of the scope of their constitutions or proposals to re-elect presidents for an undefined term. These are the most dangerous developments that exist today.

Are you concerned that there are so many obviously differing styles and approaches of governance? What would you like to see in the future?

Our perspective must be the same as that of those countries who share our culture and who have maintained democratic stability and reached outstanding levels of development. In other words, Spain, France and Italy. I'm not talking about Great Britain or the United States, the most stable democratic systems, simply because those cultures are different from our own. The fact is that countries like Spain and Portugal, who were archaic dictatorships with backward societies and closed economies only 30 years ago, have now achieved liberty and development. What I'm trying to say is that Latin America is not living under a death sentence, as we have heard so

many times. My dream for Latin America and the Caribbean is to see it reach those levels of maturity. But that is not to say the region should be unanimous. Christian democracies, social democracies and social liberal democracies have all been able to take turns without ill effects. And even with their nuanced differences, they have given Europe a remarkably high quality of life. My current hope would be to have democracy understood in that way and see the region acknowledge that there's no quick way or clever shortcuts to reach those results but the same tortured path they've been following up until now.

What do you believe the IDB's role has been with respect to democracy, and what should it do in the coming years?

The IDB has been a source of financing for mid-term objectives when nothing else like it was around. At the same time, it has been a calming influence in proposing sound economic, social and cultural policies. This has not always been understood, especially by the current crop of radicals who still dream of impossible revolutions and don't follow the path of democratic reform. Naturally, we at the IDB are

partners, so occasionally it goes astray and its decisions fall short of the mark, but from a broader democratic perspective, its contribution has been and continues to be essential.

Box 2.1 The IDB's Role Regarding Democratic Governance

From the beginning, the IDB has seen democratic governance as a requisite for ensuring sustainable economic and social development. Nevertheless, regional realities made it difficult for the IDB to work on those subjects until the beginning of the 1990s, when explicit decisions were made that allowed the Bank to expand its scope of action.

A notable example is the Bank's support of peace processes and democracy building in Central America, as in the case of El Salvador. After the 1992 peace accords that ended the civil war the country had been suffering since 1981, El Salvador faced some major roadblocks in its recovery. The war had devastating effects, including the virtual destruction of the economic base, a rise in poverty levels and a weakening of democratic institutions. The government immediately channeled its efforts to the task of the country's recovery under the National Reconstruction Plan (PRN), conceived as a tool that would take into consideration economic, social and political aspects that were critical dimensions of the challenge it faced. The Bank propped up this effort by providing support to the strategic design and offering the financing required to put it into operation.

More recently, the government's modernization strategy, approved in 2003, develops and reinforces the ideas that have been advanced in various processes. The strategy seeks to (i) provide a frame of reference for the Bank and its borrower countries for the construction of a democratic, modern and efficient government that promotes sustainable growth, the reduction of poverty and social fairness; (ii) adapt governmental modernization measures to the strategies of sustainable economic growth, the

reduction of poverty and social fairness; (iii) strengthen the emphasis on democratic governance as a means and as an end to development; and (iv) define areas of action with a broad-based approach. According to the strategy, the strengthening and reinforcement of government must be structured around the linchpins of any democratic system, the rule of law and judiciary reform, free market institutions, accountable public administration and a fifth area to be phased in over time, which is the support of decentralization processes and strengthening local governments.

From 1961 to 2008, the Bank approved loans in the total amount of US\$25,187,000 for governmental reform and modernization, representing 16 percent of total Bank activity. Nevertheless, it is worth noting that the IDB portfolio in the tax sector alone has reached 39 percent of the Bank's portfolio for the last 15 years, between 1990 and 2004, representing 963 projects for a total of US\$84,936,000.

The IDB has also published important books, studies and documents, some of which are worth mentioning: *La política importa: democracia y desarrollo en América Latina*, as well as *The Politics of Policies* (IPES 2006). IDB continues to delve into this subject with recently published works such as *Governing the Metropolis* (2005); *Informe sobre la situación del servicio civil en América Latina* (2006), available in English in 2008; *The State of State Reform in Latin America* (2006); *Justicia: Un vínculo pendiente entre Estado, ciudadanía y desarrollo* (2007); *¿Cuál es la salida? La agenda inconclusa de la seguridad ciudadana* (2007); *Policymaking in Latin America: How Politics Shapes Policies* (2008); *Civil Society and Social Movements: Building Sustainable Democracies in Latin America* (2008).

(Continued from page 45)

vestment, toward strengthening political parties by supporting research and training efforts (Payne, Zovatto and Mateo Díaz, 2006).

Nevertheless, transparency levels remain low even though a greater number of reforms directed at strengthening accounting methods and improving disclosure have been observed, with the media and civil society playing an increasingly positive role in this area.

Despite these advances, the vast majority of recent reforms have not been accompanied by the necessary strengthening of agencies of oversight and systems for penalizing infractions. This clearly appears to be an area where simply taking the path of legal reform is not enough. The system must be the product of a combination of effective legal frameworks and efficient monitoring agencies, underpinned by a vigilant attitude on the part of civil society and the media.

In sum, a good system of financing must guarantee open, free and equitable political competition and contribute to strengthening public confidence in parties, politics and democracy by improving transparency. Therefore, a mixed system (public and private)

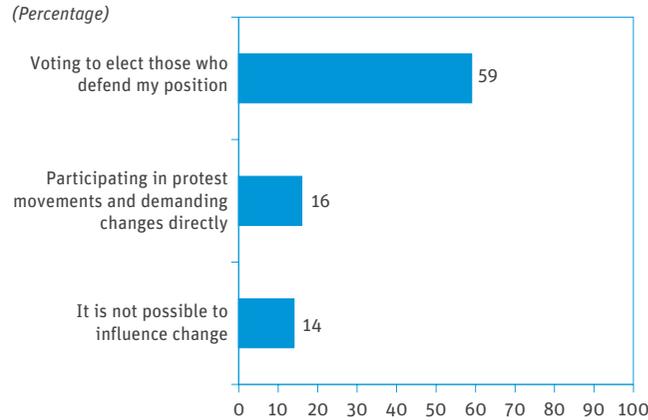
with full disclosure and strong government oversight backed by an efficient system of sanctions is essential for successful reform in this area (Payne, Zovatto and Mateo Díaz, 2006).

VOTER PARTICIPATION

On average, about 62 percent of the voting age population in Latin America and the Caribbean goes to the polls. In the most recent wave of presidential elections, nearly 36 percent of the voting population abstained from participation, a level higher than that of Europe (less than 30 percent), although lower than those recorded in North America and Africa (Payne, Zovatto and Mateo Díaz, 2006). Thus, a high percentage of Latin Americans now (as of 2008) consider voting an effective tool for solving their problems (Figure 2.8). Furthermore, according to Latinobarómetro, political participation among Latin Americans increased from 7 percent to 11 percent between 1998 and 2008 (Table 2.3).

In light of these results, one could consider the democracies of the region as being healthy, due to the fact that trends in their electoral behavior do not differ drastically from those of

Figure 2.8 Strategies Considered Effective by the Latin American Population in Order to Change Things, 2008



Source: Latinobarómetro (2008).
 Note: Results are based on respondents' answers to the following question: "What do you consider to be the most effective way to influence things: voting to elect those who defend my position, participating in protest movements and demanding changes directly, or do you believe that it is not possible to influence change?"

Table 2.3 Political Participation of Latin Americans, 2008
 (Percentage)

Country	Political participation
Dominican Republic	31
Panama	20
El Salvador	16
Honduras	15
Nicaragua	15
Venezuela	12
Colombia	11
Costa Rica	10
Mexico	9
Uruguay	9
Guatemala	8
Paraguay	8
Ecuador	7
Bolivia	7
Brazil	7
Argentina	6
Peru	4
Chile	3
Latin America	11

Source: Latinobarómetro (2008).

other regions with advanced democracies. Nevertheless, voter turnout is not enough to understand the whole story behind non-participation, a story that might truly serve as a measure of the democratic health of each system.

Underlying this regional figure are the realities of each country, in terms of both citizen and institutional participation. One must not forget that if competitive elections are the key

mechanisms by which one may identify democratic regimes, civic participation is essential to a functioning democracy. This implies that, if certain institutions surrounding the electoral process result in higher participation rates than others, reforms should focus on the former, based on the concept that if institutions can impact behavior, institutional changes of any kind could significantly affect electoral participation.

In terms of institutional design, it could therefore be said that (i) systems with automatic registration and compulsory voting with enforceable penalties produce the highest voter participation rates; (ii) the existence of concurrent elections (presidential and legislative) seems to lead to a significant increase in electoral participation; and (iii) systems in which political rights and civil liberties are greater draw more voters to the polls (Payne, Zovatto and Mateo Díaz, 2006). This factor could be linked to other results found at both the country and the individual level.

Along the same lines, it is worth noting the relationship between voter participation and the degree of distrust generated by democratic institutions, political parties, and the executive and legislative branches. Quite paradoxically, despite everything, people are still voting. The distinction between authorities as necessary, abstract entities for the functioning of the political system and the actual work performed by these authorities does not appear to be completely clear in the minds of the citizenry, which could explain a situation that may otherwise seem paradoxical: despite the almost system-

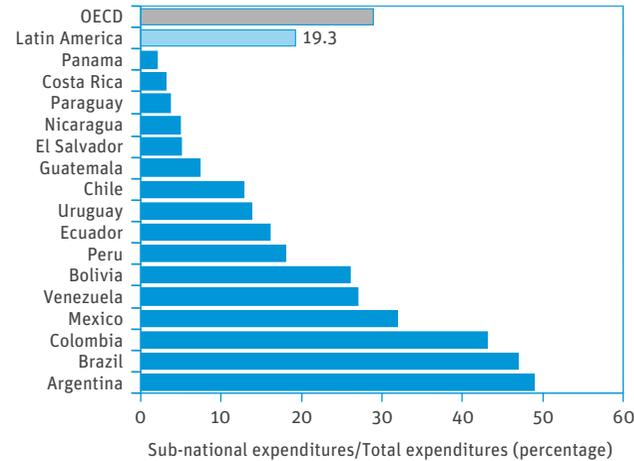
atic discrediting of political parties and other institutions that are identified almost methodically by the actors representing them, people continue to show up at the polls in support of democracy (Payne, Zovatto and Mateo Díaz, 2006).

DECENTRALIZATION

The expansion of democracy during recent decades in Latin America has not been limited to the popular election of national authorities. Each day, an increasing number of regional and local leaders are being elected by their communities, and the institutions that they represent are supporting the development of the phenomenon known as decentralization (Table 2.4). In this process, the central governments of numerous countries in the region are increasingly handing over responsibilities to sub-national governments (Lora and Cárdenas, 2006).

Most developed economies have a solid tradition of letting state and municipal governments play an important role in assigning public spending. Likewise, these administrations are largely responsible for collecting taxes and other income to guarantee

Figure 2.9 Local Government Expenditures Compared to Expenditures by Central Governments, the OECD and Latin America, 2004



Source: Daughters and Harper (2006).

the funding of services under their charge. In recent years, an emphasis on this behavior has been seen, with progressively greater spending and tax revenues for the sub-national public sector (Figure 2.9). In turn, many Latin American countries are taking similar paths, with a notably greater distribution of responsibilities among the different levels of government, gradu-

Table 2.4 Years When the First Mayors and Governors Were Elected in Selected Latin American Countries

Country	Mayors	Governor
Argentina	1983	1983
Bahamas	1997	n.a.
Belize	1981	n.a.
Bolivia	1985	2005
Brazil	1982/85	1982
Chile	1992	n.a.
Colombia	1988	1991
Ecuador	1983	1983
El Salvador	1985	—
Guatemala	1985	—
Honduras	1982	—
Mexico	1917	1917
Nicaragua	1992	—
Panama	1995	—
Paraguay	1991	1993
Peru	1980	2002
Uruguay	1984	n.a.
Venezuela	1989	1989

Source: Daughters and Harper (2006).
Note: n.a. = not applicable.

ally phasing out centralized forms of administration.

Responsibility is being transferred to sub-national governments in public services such as trash collection, urban zoning and transportation, water management, education, health, local police, irrigation and, to a lesser degree, highways, interurban highways, ports and airports. With regard to assigning

taxation responsibilities to sub-national governments, however, the region's countries have been much less active. In developed economies, states and municipalities are responsible on average for more than 34 percent of public sector revenues, corresponding to 80 percent of the revenues collected by sub-national governments. In contrast to this figure, the sub-national governments of Latin America's most decentralized countries collect only a bit more than 13 percent of total public revenue, corresponding to 53 percent of their own total revenues (Lora and Cárdenas, 2006). The relatively high dependence of sub-national governments in Latin America on the transfer of resources from national governments limits their autonomy and the incentives that citizens need to have for monitoring local and regional public administration (Daughters and Harper, 2006).

Despite the fact that Latin America still has a considerable way to go in the area of increasing the taxation responsibilities of sub-national governments as well as their responsibilities in terms of services, the level of progress seen in recent years suggests that the continent will continue to see

a growing process of decentralization in the near future (De la Cruz, 1998). This trend has been changing the relationships between the state and its citizens, generating new mechanisms for managing public services with the increased involvement of users in the design, management and evaluation of these services. It has rightfully been said that the region has made an extensive and profound commitment to a model of decentralized authority (Daughters and Harper, 2006).

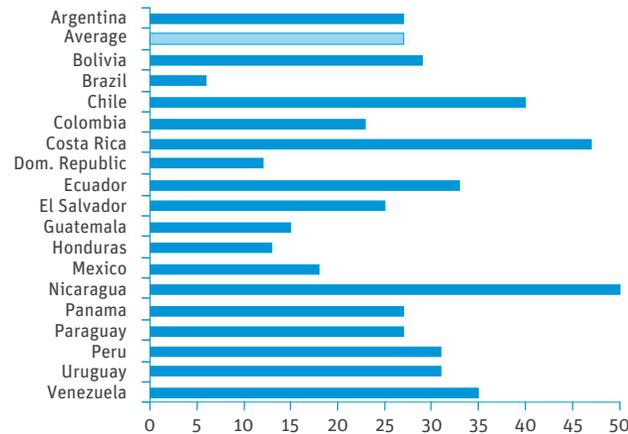
FEMALE LEADERSHIP

In recent history, a dozen women have been presidents or prime ministers of Latin American and Caribbean countries. Eight women have been designated as interim leaders for short periods of two years or less. More recently, the region has witnessed unprecedented changes in the level of women's political participation. For example, 2008 saw the greatest number of female state ministers in Latin American history, with women occupying 27 percent of all ministry posts (Figure 2.10).

In 1950, Panama became the first country in the region to appoint a

Figure 2.10 Gender Equality in Ministerial Cabinets, Latin America and the Caribbean, 2008

(Percentage that are women)



Source: Prolead (2008).

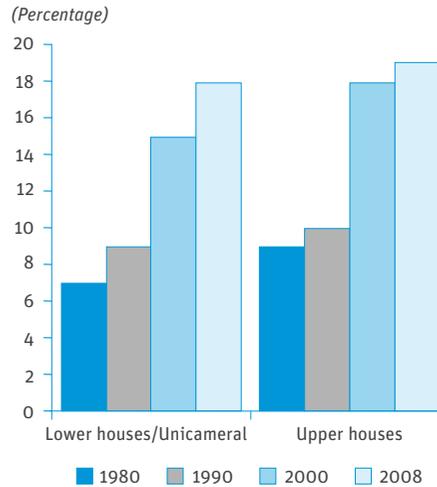
woman to an executive government position. After 1960, the presence of women became increasingly sustained and expanded into new sectors. Since 1990, more women ministers have been appointed than in all years prior. Historically, women's presence has been greater in social ministries, although since 2000 the participation of women in areas such as foreign relations, defense, interior affairs, justice and the environment has become increasingly common.

On the other hand, women's entry into national legislatures has been particularly slow; it was not until the 1990s that their participation significantly increased. From an average in both chambers of 9 percent in 1990, by 2008, female representation in Latin American and Caribbean countries had risen to 18 percent (Figure 2.11). That said, despite these successes, the gaps in equality between men and women in positions of political representation continue to be large.

Nonetheless, the trend is encouraging. On average, women in the region have made significant progress in the areas of education, health and labor, which has allowed them to acquire the capacities and opportunities to take on political leadership roles. The expansion of education in the region has given girls increased access to education and has likewise possibly contributed to reducing gender inequalities in employment and politics through education's direct effect on work and income, as well as its strong association with improved health conditions for women and decreased fertility.

In addition, the adoption of international agreements on human rights along with the creation of national leg-

Figure 2.11 Participation of Women in Parliaments, Latin America and the Caribbean, 1980–2008



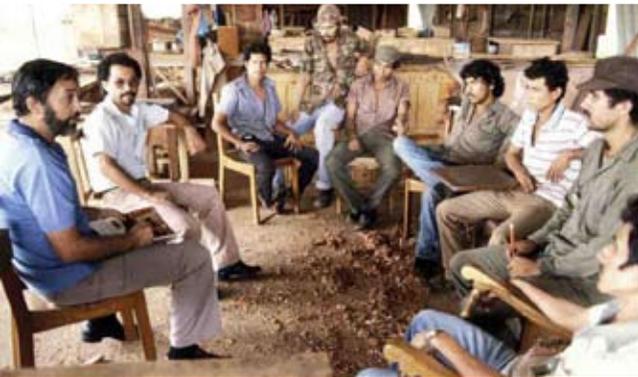
Source: Prolead (2008).

Note: The data for 1980 do not include Argentina, Belize, Chile or Uruguay with respect to upper houses; nor do they include Argentina, Belize, Chile, Guatemala, Guyana, Suriname, or Uruguay with respect to lower houses/unicameral parliaments.

islation on women’s rights has enabled women to enter and remain in politics. Governments have also created special bodies, institutions and instruments to propose legislation as well as supervise and implement policies related to women’s issues. Nevertheless, the progress achieved by women varies notably among different countries, regions, socioeconomic classes, and racial and ethnic groups.

AN ONGOING CHALLENGE

The above shows that although Latin America has seen much progress in recent years with regard to democracy and institutions, it has an extremely long road ahead of it with regard to giving greater efficiency to a system that enjoys majority support among the region’s inhabitants but which generates great dissatisfaction with regard to its functioning. These challenges ultimately have but one solution: a more active nurturing of democracy and an expansion of its mechanisms for achieving greater participation and transparency in decision making, all with the goal of promoting greater equality.



Members of a local labor group in Nicaragua exercise their rights as citizens to organize for better working conditions and a more secure future for their families.

Thus, the challenge continues. Just like the hiker who encounters a new hill when he believes he has reached the mountaintop, Latin Americans are facing a similar situation. While it is true that the right to vote is respected and exercised in the vast majority of the region and the number of people appointed by popular will, whether at a national or a local level, has certainly increased, it is also true that these changes must be accompanied by stronger and more transparent systems that respond to methods of citizen

control and that are effective in meeting the demands of the public. It is not just about hopeful voting but about seeing realities materialize in the form of progress and equality, in an increasingly more solid and, hopefully, more democratic framework. In other words, “a well-functioning democracy is indispensable for strengthening institutions and implementing efficient and sustainable public policies that allow for equitable and sustainable development” (Payne, Zovatto and Mateo Díaz, 2006).

Interview with Percival Noel James Patterson



Percival Noel James Patterson is one of the most respected politicians in the Caribbean. As Jamaica's sixth and longest serv-

ing Prime Minister, he was in charge of leading his country through times of challenges and progress. With a degree in law from the London School of Economics and after a long and illustrious career, The Most Honourable P. J. Patterson is now a member of the Global Leadership Foundation and is involved in regional and international issues.

How would you describe the democratic evolution of Latin America and the Caribbean over the past 50 years?

Fifty years ago, the islands of the Caribbean were yet to attain their independence and much of the South American mainland was ruled by totalitarian regimes. Today, democratically elected governments exist throughout Latin America and the Caribbean. This democratic evolution has been achieved by a number of factors: the end of the Cold War and ideological polarization; the fierce battles and unyielding determination of the people within the hemisphere against the oppression by military dictatorships of its citizens; and the sterling contributions of organized labor, the judiciary and the press. There have been spasmodic interruptions in the process, but the wind for democratic change has prevailed. The era of Stroessner, Somoza, Pinochet and Duvalier has finally come to an end. Within the nation-states of the Caribbean, we have now grown accustomed to the peaceful transfers of power from one political party to another. In Mexico, Central and South America we have witnessed the smooth changeover of the democratic baton.

How strong do you see democratic institutions in the region today?

Any working democracy, whether presidential or parliamentary, depends in part on the legislative apparatus and the institutions which its constitution creates, but no less on the underpinnings which must come from the operations of its political parties, judicial system and the flow of information. There are some countries, partly due to history, where the democratic institutions already appear firmly entrenched and others where they still seem somewhat vulnerable. In many places there exist the threats of terrorism and insurgency, but the diminution of democratic rights and responsibilities can never prove an acceptable response.

What dangers lie ahead?

Democracy rests on a number of pillars: the advancement of human freedom and personal liberty, and the rule of law and respect for human rights. But these are seldom found to exist in splendid isolation. The greatest dangers spring from poverty, hunger, ignorance and disease. Intolerable levels of poverty, the sparks of economic deprivation or social exclusion can easily ignite

fires that disrupt political stability and gradually undermine the foundations for a strong and lasting democracy.

Several presidential democracies in Latin America are discussing the possibility of giving a chance to parliamentary democracy. What is your view on the subject?

The substance of the democracy is immensely more important than the format, whether presidential or parliamentary. Everything turns on what will work most efficiently in securing the purposes of democracy. The whole body politic needs to have a full understanding of any constitutional structure to generate the appropriate response at every level in order to make it work.

Polls show that people from the region believe that democracy is the best form of government but some think that it is not very effective in addressing people's problems. What do you think?

No one can seriously dispute that the democratic machinery is not always geared to the most effective and immediate response. It has been a question asked throughout the ages,

and to which no satisfactory answer has yet been given. What is the alternative which will more consistently register a response that satisfies the human passion for choice and fulfillment? Until then, democracy remains the best available option.

Governments are also less centralized now. Do you think that is a good trend?

Definitely so! Everywhere people are seeking to assert more and more the right to make decisions which affect their daily lives. This search has been intensified in the new age of technology and instant access to communication. With the welcome liberation of private initiative has come an increased devolution of central responsibility. The empowerment of local communities and the greater role of civil society are irreversible. In building a democratic culture, there must be a deepening of its roots and a spreading of its branches.

What would you like to see in the future regarding democracy in the region?

A realization that democracy will not always produce the electoral results

which others want, but an acceptance that the voices of the people should always be heard and respected. Democracy demands that hegemony and the arrogant use of power can never be justified under any guise. Democracy should breed the environment within which different ideas will contend and yet serve as an engine to foster consensus where the interests of the nation so demand.

How do you see the role of IDB on the subject?

The IDB, as the hemispheric lending institution, should endeavor to ensure that the populace of member countries can move steadily along the pathway to releasing a wave of entrepreneurial initiatives, promote economic growth and accelerate social uplift in order to reap huge dividends from our democratic gains. Every dollar spent on education, health, justice, community development, urban renewal or microenterprise is money well invested to ensure that democracy will prevail.

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Stein, Ernesto, et al. 2008. *Policymaking in Latin America: How Politics Shapes Policies*. Washington, D.C.: IDB.

¹ The indicators on which these international comparisons are based come from an extensive series of questions posed to experts in an attempt to minimize the subjective aspects of these types of measurements. With regard to political rights, the questions evaluate the capacity and autonomy enjoyed by individuals and social groups (especially minorities) in participating freely in the political process through which they elect their leaders and representatives to legislative bodies, in forming political organizations and in exercising opposition to the party in power. With regard to civil liberties, the survey evaluates the capacity enjoyed by individuals to make personal decisions (of occupation, religion, residence, marriage, association, etc.), express their opinions, dissent publicly, create and develop organizations (civil, union, professional), benefit freely from their economic efforts and legal property ownership, have access to the justice system and be protected from arbitrariness or political persecution or terrorism. The democracy indicator uses more general categories that measure the competitiveness and regulation of political participation, competitiveness and openness in selecting the executive power, and the system of checks and balances that restrict the power of the latter.

² The complete text of the Inter-American Democratic Charter is available at: http://www.oas.org/charter/docs_es/resolucion1_es.htm.

³ In years prior, literacy requirements effectively excluded poor and indigenous people from participating in electoral processes.



On the job. Trainees put newly honed skills to work at a private firm participating in a Chilean program financed by the IDB to help unemployed people break into the job market. The IDB is helping to create opportunities for the region's low-income majority to join their countries' economic mainstream as suppliers of materials and equipment to private sector firms, as employees of companies, or as customers for products tailored to their needs.

III Progress and Goals in Social Development

If anyone's life can be said to have changed, it is that of the residents of Salinas de Bolivar, a small community in the Ecuadorian mountains where the indigenous Quechua coexist with mestizos. Three decades ago, the community was completely submerged in obscurity, poverty and marginalization. Child mortality at that time was at 45 percent, while illiteracy was at 85 percent. Homes were quite modest, constructed of straw and dirt, without running water, electricity, telephone service, sewer system or access to permanent roads (IDB, 2005).

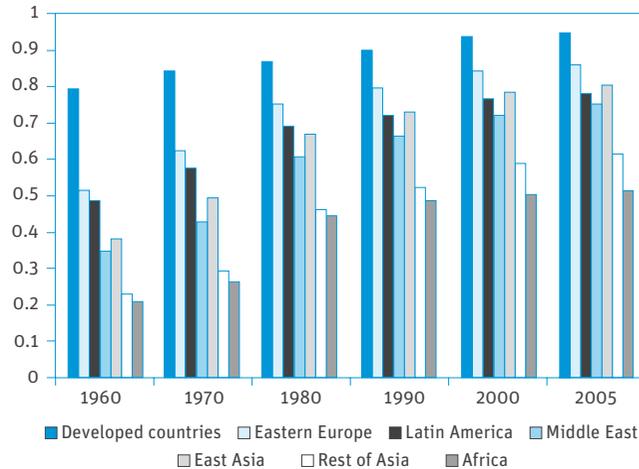
Today, however, the situation is different. Thanks to the actions of several productive projects and government support, 95 percent of those who live in Salinas now have electricity, 92 percent have access to the health care system, 100 percent are served by the aqueduct network, and only 8 percent of the area's young people are leaving for the country's major cities, primarily for educational purposes. Although the

list of needs remains long, progress is both undeniable and palpable.

Similar examples abound throughout Latin America and the Caribbean. Despite some reports of setbacks, various measurements reveal astounding advancements. Two examples are the progress made in achieving the Millennium Development Goals (MDGs) set by the United Nations and the rise in the Human Development Index (HDI), also from the UN, reflecting both economic and social aspects of development. Now, in the first decade of the 21st century, Latin America's HDI is only surpassed to a significant degree by the wealthiest of nations, and is on par with those of East Asian and Eastern European countries. Within the 0 to 1 range (used to measure this index), the 33 countries of the region that are included in the index averaged 0.803 in 2005, while developed countries scored an average of 0.94. The global average was 0.743 (Figure 3.1).

While this relative gap has remained virtually unchanged since the

Figure 3.1 Human Development Index, World Regions, 1960–2005
(Averages)



Source: UNDP, Reports on Human Development 1998 and 2007–08.

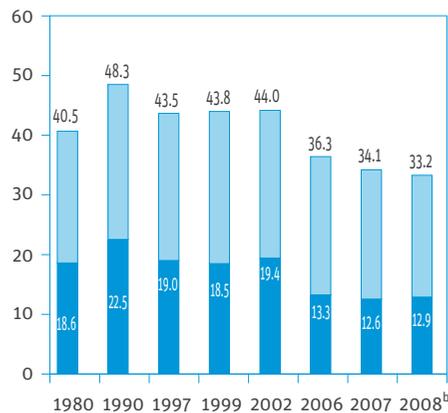
mid-1970s, it suggests a clear contrast between economic and social development trends. In fact, while the relative difference in per capita income between Latin America and other country groups has widened, the region has reached the same level as the most advanced nations in several aspects of social development. A typical case is that of life expectancy at birth. In the current five-year period, it is 73.4 years, a figure that not only

approaches that of the world's wealthiest regions but represents a 21-year jump over the regional average for the year 1950. Furthermore, life expectancy in Latin America is increasing and is expected to reach 79.6 years sometime between 2045 and 2050, according to projections by the Economic Commission for Latin America and the Caribbean (ECLAC) (Table 3.1).

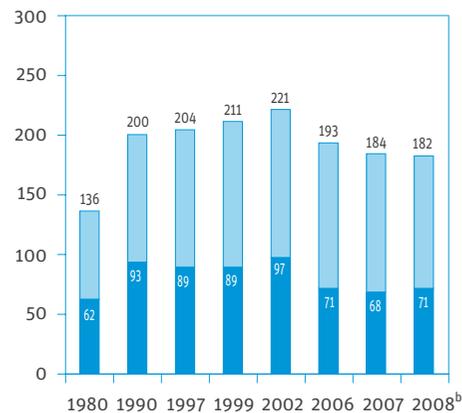
This does not mean that the region's inhabitants have been immune to economic changes. In fact, different studies have shown how the so-called "lost decade" of the 1980s affected social aspects as well—with an obvious backslide in the areas of poverty and indigence. According to ECLAC, the situation in Latin America during that decade was critical, with 40.5 and 18.6 percent of the population immersed in poverty or indigence, respectively. The decline that resulted from this period became evident in the 1990s, when the percentage of the population classified as poor and indigent increased by 7.8 and 3.9 percentage points, respectively (Figure 3.2). Nevertheless, these hardships do not take into account great advancements in such indicators as life expectancy, child mortality and literacy (Table 3.1). Enormous chal-

Figure 3.2 Changes in Poverty and Indigence, Latin America, 1980–2008^a

(Percentage of the population)



(Population in millions of persons)



■ Indigents ■ Non-indigent poor

Source: ECLAC (2008), based on special tabulations of surveys of households in the respective countries.

^a Estimate based on 18 countries of the region plus Haiti. The figures above the upper sections of the bars represent the percentage and the total number of poor persons (indigents plus non-indigent poor) respectively.

^b Projections.

lenges remain, of course, topped off by the struggle against inequality: Latin America, along with Sub-Saharan Africa, has the world's worst distribution of income. According to the World Bank (2008), 20 percent of the region's population receives 57 percent of the wealth, while the poorest 20 percent earns merely 3 percent (World Bank, 2008).

POVERTY: LIGHTS AND SHADOW

According to ECLAC estimates (2007b), in 2007 the number of poor people in Latin America and the Caribbean reached 190 million,¹ or 34.1 percent of the population. Of this total, 69 million (12.6 percent) would be classified as indigent² (Figure 3.2). While these figures are better than those reported in 1980 and, in the case of poverty, represent a drop of 14.2 percentage points versus the 1990 figures, the challenge is still formidable. Concerns are even greater in light of the vicissitudes of the global economy and the impact that the current crisis could have on the region, as it is clear that the advancements made from 2003 to 2008 were accompanied by the greatest increase in per capita GDP since the 1970s.

Table 3.1 Indicators of Demographic Dynamics in Latin America, 1950–2050

Indicators	1950–55	1975–80	2005–10	2025–30	2045–50
Global fertility rate (children per woman)	5.9	4.5	2.4	2.0	1.9
Life expectancy at birth (years)	51.8	63.4	73.4	77.1	79.6
Infant mortality rate (per 1,000 births)	127.7	69.7	21.7	12.0	7.9
Annual population growth rate (percentage)	2.8	2.3	1.3	0.7	0.2
Age brackets (percentage)	1950	1975	2005	2025	2050
0–14 years	40	41	30	23	18
15–59 years	54	52	61	62	58
60 years and older	6	6	9	14	24
Total	100	100	100	100	100

Source: Latin American and Caribbean Demographic Centre (CELADE, 2007).

Table 3.2 Unemployment Rate, Latin America, 1995–2007
(Average annual rate)

		1995	2000	2003	2004	2005	2006	2007 ^a
Argentina	Urban areas	17.5	15.1	17.3 ^b	13.6 ^b	11.6 ^b	10.2 ^b	8.4 ^{b,c}
Barbados ^d	National	19.7	9.2	11.0	9.8	9.1	8.7 ^e	8.1 ^c
Bolivia	Urban areas	3.6 ^f	7.5	9.2	6.2	—	—	—
Brazil	Six metropolitan areas	4.6	7.1	12.3 ^g	11.5 ^g	9.8 ^g	10.0 ^g	9.4 ^{g,h}
Chile	National	7.4	9.7 ⁱ	9.5 ⁱ	10.0 ⁱ	9.2 ⁱ	7.7 ⁱ	7.0 ^h
Colombia ^d	Thirteen metropolitan areas	8.8 ^j	17.2	16.7	15.4	14.0	13.0	11.6 ^h
Costa Rica	Urban areas	5.7	5.3	6.7	6.7	6.9	6.0	4.8
Cuba	National	7.9	5.5	2.3	1.9	1.9	1.9	1.9
Dominican Rep. ^d	National	15.8	13.9	17.0	18.4	18.9	16.2	15.6 ^p
Ecuador	Urban areas	7.7	14.1 ^k	9.8 ^k	9.7	8.5	8.1	7.6 ^c
El Salvador	Urban areas	7.0	6.5	6.2	6.5	7.3	5.7	—
Guatemala	Urban areas	—	—	5.2	4.4	—	—	—
Honduras	Urban areas	5.6	—	7.6	8.0	6.5	4.9	4.1 ^l
Jamaica ^d	National	16.2	15.5	11.4	11.7	11.3	10.3	9.9 ^m
Mexico	Urban areas	6.2 ⁿ	3.4	4.6	5.3	4.7	4.6	4.8 ^h
Nicaragua	Urban areas	16.9 ^o	9.8	10.2	9.3	7.0	7.0	—
Panama ^d	Urban areas	16.6	15.2	15.9	14.1	12.1	10.4	7.7
Paraguay	Urban areas	5.3	10.0	11.2	10.0	7.6	8.9	—
Peru	Metropolitan Lima	8.2	8.5	9.4	9.4	9.6	8.5	8.4 ^h
Trinidad and Tobago ^d	National	17.2	12.2	10.5	8.4	8.0	6.2	5.9 ^q
Uruguay	Urban areas	10.3	13.6	16.9	13.1	12.2	11.4	9.7 ^c
Venezuela	National	10.3	13.9	18.0	15.3	12.4	10.0	8.7 ^h
Latin America and the Caribbean^r		9.3	10.4	11.0	10.3	9.1	8.6	8.0

Source: ECLAC (2007a).

^a Preliminary figures.

^b New measurement since 2003; data are not comparable to previous years.

^c Estimate based on the January to September average.

^d Includes hidden unemployment.

^e Reference period: March.

^f Until 1999, data correspond to departmental capital cities.

^g New measurement since 2002; data are not comparable to previous years.

^h Estimate based on the January to October average.

ⁱ Beginning in 1998, data were linked with those pertaining to the sample applied since 2006.

^j Until 1999, data correspond to seven metropolitan areas.

^k The figures correspond to Quito, Guayaquil and Cuenca.

^l Reference period: May to July.

^m Estimate based on the January to April average.

ⁿ Data are not compatible to subsequent years.

^o National total.

^p Reference period: April.

^q Estimate based on the January to June average.

^r From 1991, includes an adjustment to the data for Argentina, Brazil and Mexico to take into account the methodological changes for 2002, 2003 and 2005, respectively.

Nevertheless, there are additional elements that explain what has occurred. According to ECLAC, one must also consider the increasingly high rate of dependency among poor families, which implies that income in these families is being distributed among a greater number of people, regardless of their income levels. Moreover, although the overall birth rate in the region has dropped, it remains elevated in the most vulnerable socioeconomic strata. As such, the rate of demographic growth, which reached 2.7 percent annually between 1950 and 1970 (Thorp, 1998), has fallen to less than 1.3 percent per year, although it is clear that in some areas, such as the rate of adolescent maternity in poor families, there has been no such decrease. By 2008, the region's population was expected to reach 579.4 million (ECLAC, 2008).

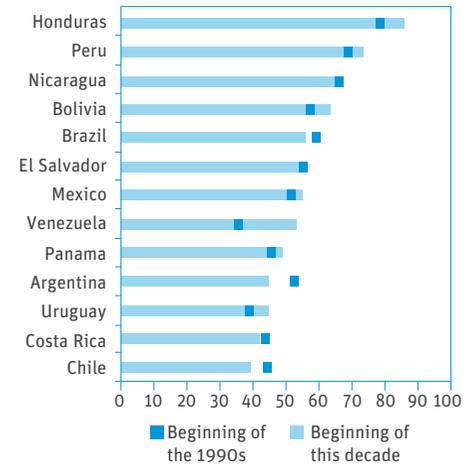
An equally important recent advancement in the fight against poverty has been a drop in the unemployment rate, which has led to both improved income levels and an increase in the proportion of the working population as well. Thus, from an average unemployment rate of 9.3 percent in 1995, rising to 11

percent in 2003, the average regional rate fell to 8 percent in 2007 (Table 3.2) and dropped to 7.5 percent in 2008. A detailed look at unemployment trends by country shows a rise in this variable during the 1990s and a decrease as of 2002, contributing to the reduction of poverty, as mentioned above.

One cannot, however, ignore rising informal employment in the region (Figure 3.3). Informality poses a problem in that it can increase poverty by leaving workers in a state of vulnerability and cause exclusion as a result of being left out of social security systems (especially health care and retirement pensions) without the option to register complaints or participate in union-based activities to improve working conditions (IDB, 2007a). That said, the belief that informal employment always implies lower pay than formal employment has been hotly debated, as the potential for income generation (in terms of capacity, effort and preference) may differ greatly between the two (IDB, 2007a).

Another aggravating factor of informality is the low productivity of this type of employment. As such, Latin America is a region that has experienced high rates of growth in

Figure 3.3 Workers with Informal Employment (Percentage)



Source: IDB (2008), based on the Center for Distributional, Labor and Social Studies (CEDLAS) and the World Bank (2008). Note: Informality is understood here as a modality that includes workers in small companies, non-professional workers and unpaid workers. The sample is comprised of adults from 25 to 64 years old. The years used for each country are: Argentina (1992–98), Bolivia (1993–2002), Brazil (1992–2003), Chile (1990–2003), Costa Rica (1990–2003), El Salvador (1991–2004), Honduras (1992–2005), Mexico (1996–2002), Nicaragua (1993–2001), Panama (1995–2004), Peru (1997–2003), Uruguay (1992–2004) and Venezuela (1992–2004).

its working population but deficient growth in labor productivity. This deficit is due to both greater informality and the low quality of jobs created at the general level (IDB, 2008). Nevertheless, publications such as *Beyond Facts: Understanding Quality of Life* (IDB, 2008)

(Continued on page 70)

Interview with Santiago Levy



Santiago Levy Algazi, a Mexican economist, is the IDB's Vice President for Sectors and Knowledge.

Before joining the

Bank, he served as General Director of the Mexican Social Security Institute (IMSS) and the Mexican Deputy Minister of Finance, becoming the main architect of the renowned Progres-a-Oportunidades social program. Levy has a Ph.D. in economics and a master's in political economy from Boston University, and was an honorary post-doctoral fellow at Cambridge University.

How do you view the changes that have taken place in the Western Hemisphere with respect to social issues over the past half-century?

There has been a constant concern with social development in Latin America since the IDB's inception. First, a lot of attention was given to the issues of access to basic services such as potable water, sewer systems and electricity. Then, I believe that a lot of attention was paid to the growth of education as one of the major facilitators of social inclusion and an engine of development, and advancements in coverage have been very significant, particularly with respect to primary education. Afterward—and this is a process that is still ongoing—there was a continuous review of which programs are most effective or most efficient to promote social development. I would say that there have been some important

achievements measured by coverage indicators such as health, basic health care, life expectancy, infant mortality, illiteracy, drinking water or electricity in the homes, although this does not mean that there are no deficiencies. If we could perhaps say what the greatest challenge has been to date that has not been possible to overcome in the region, it is that of reducing social differences and inequalities. The fact remains that Latin America, compared with other regions in the world, continues to lag far behind. So, while the final balance is clearly positive, we must also put some substantive challenges on the agenda that go beyond the elimination of extreme poverty. It is a matter of building more inclusive, more homogeneous societies; to put it another way, societies with a more equitable distribution of economic power and access to opportunities.

What would you point to as a positive achievement of the Bank throughout this period?

The Bank has always had this integrated vision of development, where it's not just about building dams, but also about building inclusive societies. The IDB has not been an institution with one vision only; it has balanced its analytical approach with a certain pragmatism that is always welcome in the design of public policies.

How would you describe the most recent phase of anti-poverty programs?

I think the IDB played a very important role 10 or 15 years ago when the new generation of anti-poverty programs was created, which are really programs for investing in the human capital of poor families where the mechanism for fighting poverty is a conditional transfer of resources. The

Bank has helped several countries with these programs, and in practice, they have turned out to be an effective instrument for achieving a reduction in extreme poverty and improvements in certain dimensions of human capital in poor families: nutrition, schooling, basic health indicators. But now, I'd go further than that and say that the IDB, like the region's countries, is confronting the challenge of designing the next generation of programs that go beyond conditional transfers, meaning that a child, even if he comes from a poor family, will have a better job when he reaches 20 years of age. A job with access to formal social security, in a productive company that can invest in his training, and where he has access to medical insurance, a pension, and—why not?—unemployment insurance. All this, so that his children will no longer be poor.

Do you think that this is the path the IDB will take over the next few years?

It will have many dimensions, including the great challenge of improving the quality of education and giving the population adequate health care services. We also have to think about how we design our job training programs so that the employees of a Latin American maquiladora can compete with a factory in Malaysia or Vietnam. That's what the region's social challenge is, in my opinion. It represents a huge effort in defining education systems, to understand the factors that limit the quality of education, to look at the design of health care systems and labor market institutions. That said, 50 years of achievements allow us to be optimistic and to believe that even better achievements are in store over the next 50 years.



A solid start in life is the goal of Mexico's acclaimed Oportunidades program, in which parents receive cash for sending their children to school and health clinics.

(Continued from page 67)

reveal that Latin Americans are more satisfied with their jobs than would be expected. In the specific case of informal employment it may actually be preferable due to several advantages it offers: freedom from the regulations typical of large companies, greater flexibility for students and workers with small children, and the ability to avoid paying taxes or contributions to the government, from which many workers believe they receive no direct benefit.

Various studies show that the successes achieved with regard to unemployment are relatively fragile, given the possibility of slow economic growth ahead. One of the questions that arise under the scenario of deceleration is the sustainability of social public spending, which rose from 12.9 percent of the regional GDP in 1990 to 15.9 percent from 2004 to 2005. There are also concerns regarding the effectiveness of this effort, as several Asian countries show better results in health and education despite having spent less per capita, suggesting that there is room to improve the efficiency of these expenditures (IDB, 2003a).

The crisis generated by the steep increase in the prices of food and

basic products of mineral origin, which peaked in the first half of 2008, served as a warning bell for the region, although a great number of countries saw an increase in revenue thanks to higher prices. Despite the significant backslide seen just a few months later as a result of the global economic slowdown, this increase, which took place over a relatively short period of time, became a challenge for the region's governments, one that could re-emerge once the global growth rate recovers. Various multilateral entities have warned of the effects that higher food prices could have on poverty and equity (Table 3.3), aside from the consequences of malnutrition, which are irreversible in the case of the youngest members of the population.

In a more immediate time frame, there are valid questions regarding what could happen with poverty in the region if the economic situation at the end of this decade ends up being worse than already expected. An analysis by the IDB shows that due to the lack of dynamic growth, poor families could face a drop in income as a result of loss of employment in the formal sector, pay cuts or lower

Table 3.3 Simulation of the Impact of an Increase in the Price of Food on the Incidence of Poverty and Indigence, Latin America, 2007 and 2008

	Percentages			Millions of Persons		
	Actual incidence	Simulated incidence ^a	Difference	Actual incidence	Simulated incidence ^a	Difference
2007						
Indigence	12.6	11.9	0.7	67.8	64.2	3.6
Poverty	34.1	33.4	0.7	183.9	180.0	3.9
2008 (projection)						
Indigence	12.9	10.9	2.0	70.8	59.6	11.2
Poverty	33.2	31.2	2.0	181.6	170.7	10.9

Source: ECLAC (2008), based on special tabulations of surveys of households in the respective countries.

^a It is assumed that the increase in the price of food was equal to the increase in the CPI for the rest of basic goods since December, 2006.

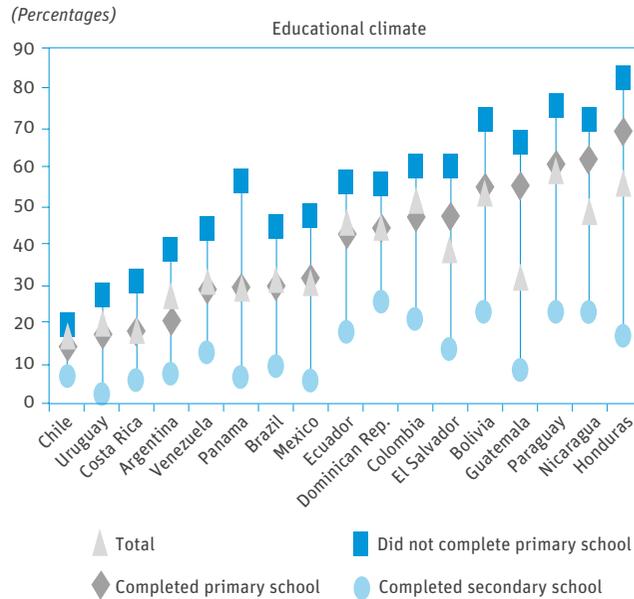
demand for work in the informal sector. Furthermore, if public spending is cut, poor families could be hurt by limited access to social services. In addition, the depreciation of local currencies could result in an increase in internal food prices. The situation could get even worse considering that the poor population of Latin America has an inadequate diversity of income sources, a low level of access to financial markets and a level of education that restricts their mobility in the labor market (Duryea et al., 2007).

In light of these prospects, it is worth reviewing some of the determining factors of poverty. First and foremost, poverty is associated with low

levels of education (IDB, 2003b). The incidence of poverty among households headed by those who have only completed primary education averages 41.3 percent in Latin America, a number eight times higher than the percentage for households headed by those with additional education through secondary school (Figure 3.4). Poverty rates are also higher among indigenous groups and people of African descent, as well as among households headed by women.

Phenomena like the one described above reveal broad disparities among countries, ethnic minorities, genders and urban and rural areas. In all cases, both general and focused policies are needed (Rodríguez, 2008). Consequently, it is worth noting the growing use of conditional transfers as a way to battle poverty and prevent its transmission from one generation to the next. Programs adopted include payment of a stipend in exchange for verifiable investments by poor families in their human capital, such as regular attendance of an educational institution by one or more family members or the use of specific nutrition systems or health services (Levy, 2006). To date, studies have shown

Figure 3.4 Incidence of Poverty in Latin America, According to Individual Household Characteristics, circa 2007



Source: ECLAC (2008), based on special tabulations of surveys of households in the respective countries.

Note: Educational climate means the average number of years of education of the head of the household and his spouse. In the case of Argentina, the data refer only to urban areas.

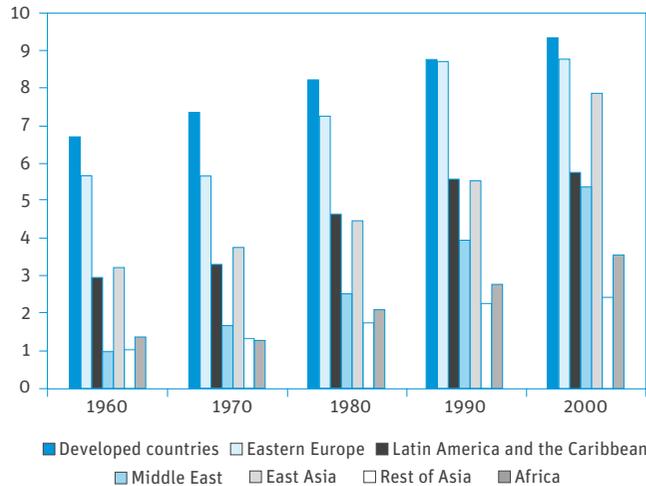
that the poor are increasing their consumption, as well as their levels of education and health, especially in countries where high inequity reduces the impact of elevated economic growth (IDB, no date).

PROGRESS IN EDUCATION: ADVANCEMENTS AND SETBACKS

Worldwide progress in education has been notable, and Latin America has been no exception. For example, the average literacy rate, which at the turn of the 20th century was barely 30 percent, rose to 63 percent in 1960 and nearly 90 percent by the middle of this decade (IDB, 2006). Perhaps the most encouraging circumstance of all is that more children are attending school than ever before in the region's history and that the goal of universal coverage in primary education appears to be attainable in a relatively short time, with a good number of countries already having met it.

In general, Latin American children are entering school at an earlier age than before, staying enrolled for more years, and completing increasingly higher grade levels. Furthermore, the gender gap that existed in the past has closed, with girls as well as boys attending school under similar circumstances. In fact, women are now completing more years of education than men (Duryea et al., 2007). There has also been a determined effort to improve access to information tech-

Figure 3.5 Average Years of Schooling for Adults Over 25, World Regions, 1960–2000



Source: Based on Barro and Lee (2000).

nology (IT) and introduce assessment systems for comparative purposes or to measure trends in competencies.

Nevertheless, the region has progressed more slowly than others, generating concern among specialists. For example, Latin Americans above the age of 25 had an average of only three years of schooling at the start of the 1960s (Schiefelbein, Wolff and Schiefelbein, 1998). By the start of the 21st century, the average had only

risen to five years. Meanwhile, in East Asian countries the figure grew from 3.2 to 7.9 years, in the Middle East from less than one year to 5.4 years, and in the former Communist countries from 5.6 to 8.8 years of schooling (Figure 3.5). Only in the rest of Asia and Africa did the number of years of schooling for the adult population grow more slowly than in Latin America.

Consequently, educational progress in Latin America has been inferior to that in other regions, particularly, but not exclusively, East Asian countries. As paradoxical as it may seem, the lag behind this region is a result neither of the percentage of people without an education, nor of the proportion of those with university degrees.³ The results are due, essentially, to the very low proportion of individuals with a complete or partial secondary education. Although access to primary education is quite high, a great percentage of people drop out before reaching secondary school or even completing primary school.⁴

The changes in the educational levels achieved by different cohorts are another reflection of the limited speed of educational progress in Latin



Though far from fancy, water “kiosks” in Haiti’s Grand’ Anse Department make life much easier for people who formerly had to walk to the nearest river to meet their daily needs.

America. For example, men born around 1960 had 7.5 years of schooling, while those born around 1930 had completed only 3.9 years. The evidence shows that women have experienced more rapid progress, advancing from 3.7 years of schooling in the case of those born around 1930 to 7.4 years of schooling three decades later.

Nevertheless, although the education gap between men and women later closed and even reversed, educational progress for generations born after 1960 began to decelerate. In fact, those born around 1975 received 8.6 years of schooling, an increase of only 1.1 years over a decade and a half in the case of men and 1.3 years for women (de Moura Castro and García, 2003). The speed at which education progressed from some cohorts to others in Latin America was much slower than in Indonesia or Taiwan, two representative Asian countries, where men and women born around 1930 received only 2.5 and 5.6 years of schooling, respectively, while men and women born around 1975 managed to complete 8.3 and 12.5 years of schooling.

In light of these data, some developments are encouraging. Around

2005, 92 percent of young people between the ages of 15 and 19 had completed primary schooling, while 71 percent had finished the lower cycle of secondary education, as opposed to 53 percent in 1990. In the same period, the proportion of young people ages 20 to 24 that had finished the upper cycle of secondary education jumped from 27 percent to 50 percent. In addition, more people were completing higher education, although this increase was not as dramatic. Thus, the percentage of young people ages 25 to 29 that had completed at least five years of secondary studies grew from 4.8 percent to 7.4 percent in the period described (ECLAC, 2008).

One topic that deserves special attention is the quality of educational test scores. One example is the results of the reading comprehension test of the Programme for International Student Assessment (PISA) administered by the Organisation for Economic Co-operation and Development (OECD) in 43 countries, including seven Latin American countries. The region’s countries received the lowest scores, with the highest percentage of students who did not meet the minimum requirements (Table 3.4).

Table 3.4 PISA Test Scores, Latin America and OECD Countries, 2000–06

Country	Average PISA score in reading			Average PISA score in mathematics			Average PISA score in sciences		
	2000	2003	2006	2000	2003	2006	2000	2003	2006
Argentina	418	n.d.	376	388	n.d.	381	396	n.d.	391
Brazil	396	403	393	334	356	370	375	390	390
Chile	410	n.d.	442	384	n.d.	411	415	n.d.	438
Colombia	n.d.	n.d.	385	n.d.	n.d.	370	n.d.	n.d.	388
Mexico	422	400	410	387	385	406	422	405	410
Peru	327	n.d.	n.d.	292	n.d.	n.d.	333	n.d.	n.d.
Uruguay	n.d.	434	413	n.d.	422	427	n.d.	438	428
OECD	500	500	500	500	500	500	500	500	500

Source: IDB (2008), based on the OECD (2001, 2004 and 2007).

Note: Scores on the Programme for International Student Assessment (PISA) tests are normalized at the statistical level, with the scores of the OECD countries taken as the median (500). The results show deviations from the median; a country's score can be above or below the median, so that a difference higher (lower) than the median represents a greater (lesser) difference between the performance of the students of that country and that of the students of OECD countries. n.d. = no data available.

A closer look at the numbers in each country suggests that significant differences exist depending on the students' position on the social scale and that economic resources determine the quality of education received by Latin American youth (ECLAC, 2008). Thus, greater effort is needed in areas such as school equipment, teacher training and public administration systems that are conducive to quality instruction. In other words, while advancements in this area have been significant, they have not been dramatic enough, because they somehow reproduce patterns of inequality that must be eliminated.

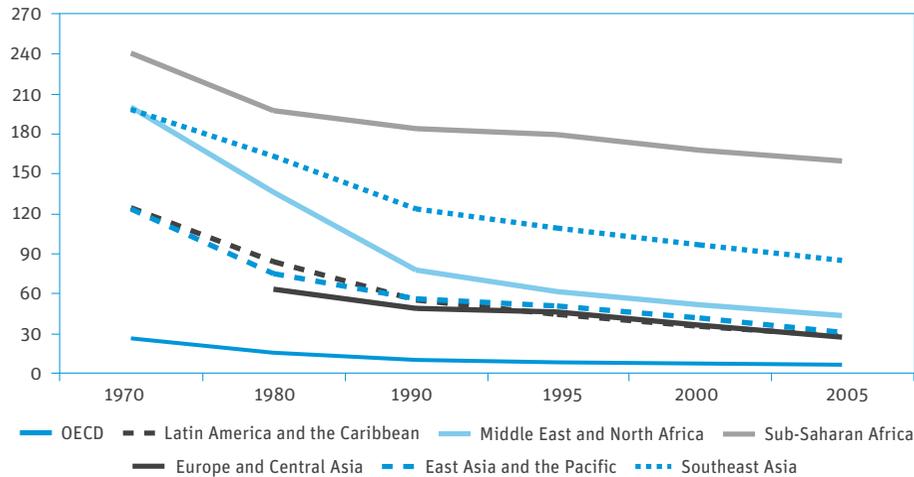
REMARKABLE PROGRESS IN HEALTH CARE

In looking at the region's history over the past half-century, it is clear that the population of Latin America is healthier than ever. This applies to almost every social group. In contrast with other aspects of development like education and economic growth, the region has done quite well in terms of health results. Today, the region enjoys the highest longevity rates and lowest child mortality rates of all developing regions. Over the past 50 years, global life expectancy has increased more rapidly than ever, with Latin America leading the trend. In 1960 the average Latin American country had a life expectancy of only 56.2 years, rising to 72.7 years by 2005 (IDB, 2008).

Historically, reductions in infant and child mortality have been the primary sources of increases in life expectancy (IDB, 2008). In Latin America and the Caribbean, mortality rates for children under 1 year of age have been dropping almost consistently since the end of the 19th century. In 1960, the average child mortality rate (deaths of children less than five years of age) in the region was approximately 150

Figure 3.6 Infant Mortality Rate, World Regions

(Deaths per 100,000 live births)



Source: IDB (2008) based on World Bank (2007).

deaths per 1,000 children (almost one out of every seven children). By 2005, the figure had dropped to 28 deaths per 1,000 children, or less than one child out of every 30 (Figure 3.6).

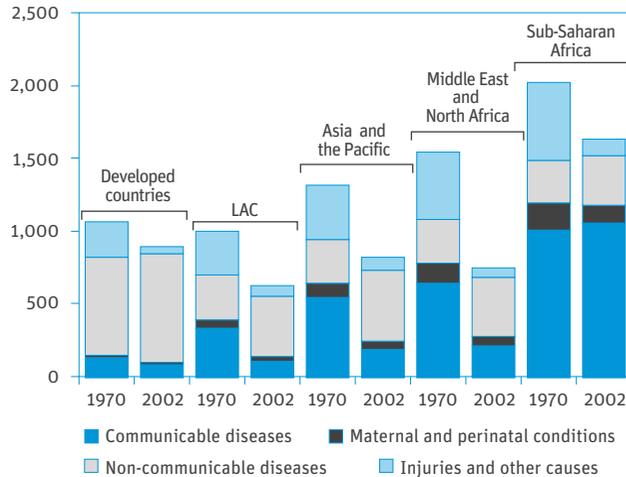
Hypotheses used to explain these events include the increase in the number of women in the workforce, the general decline in the fertility rate (from an average of 5.9 to 2.4 children per woman between 1960 and 2005), greater access to education, advancements in medicine and medications, and growing public investment in

vaccination, health, education and the construction of health care facilities. Likewise, the number of physicians per 1,000 inhabitants has nearly tripled over the past 50 years, from 0.33 in 1960 to more than 0.90 currently.

At the same time, the profile of diseases has changed radically (IDB, 2008). While in the 1950s most deaths were attributed to infectious diseases, today the most common threats are posed by other diseases such as diabetes, cardiovascular disorders and cancer (Figure 3.7). The spectacular reduction in infectious diseases, including diphtheria, poliomyelitis and smallpox, has been largely a result of the expansion in coverage of immunization programs in the second half of the century. One illustrative example is that of the triple vaccine or DPT (against diphtheria, pertussis and tetanus). In 1970 the DPT vaccine was administered to less than 10 percent of Latin American children, but this percentage grew to more than 90 percent by 2001 (IDB, 2008).

The spread of HIV/AIDS deserves special mention. According to the World Bank, over the past two decades the disease has taken the lives of 600,000 people in the region, while

Figure 3.7 Deaths by Type of Illness, World Regions, 1970–2002
(Deaths per 100,000 inhabitants)



Source: IDB (2008) based on Bulatao and Stephens (1992) and WHO (2004).
Note: The WHO international classification system was used for the classification of deaths from communicable diseases, maternal and perinatal conditions, non-communicable diseases, and injuries and other causes.

nearly 1.7 million were infected by the end of 2006 and another 140,000 become infected every year. The impact of HIV/AIDS is particularly worrisome in the Caribbean, with a quarter million people infected and the world's highest prevalence of the virus among adults after Sub-Saharan Africa.⁵ That said, efforts on the part of the region's governments with regard to both

prevention and treatment have lowered infection indices and mortality, although it is clear that total coverage in the distribution of retroviral drugs has yet to be achieved.

Moreover, there is a high incidence of mental illness and addiction as a result of increased rates of depression in women and alcoholism in men. Some believe that the region's rising crime should also be treated as a public health issue. Others point out that obesity has gradually become an illness that is showing signs of becoming an epidemic. In 1980, the proportion of overweight adults in most Latin American countries was lower than 20 percent. However, in 2008 this figure could exceed 50 percent due to a combination of economic and social factors, including changes in nutrition habits, increasingly sedentary lifestyles and higher income levels (IDB, 2008).

Another area in which many countries must still make substantial improvements in health care is financial coverage. This is of prime importance, because if receiving medical care requires families to empty their pockets, they will experience serious hardship, particularly if they are in a state of poverty. Although the region has overcome

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Interview with José Antonio Ocampo



With a prestigious professional career that spans more than three decades, José Antonio Ocampo is very familiar with the realities of Latin

America and the Caribbean. Whether in his current position as a professor at Columbia University in New York, or in his previous positions as United Nations Under-Secretary General for Economic and Social Affairs and Executive Secretary of the Economic Commission for Latin America and the Caribbean (ECLAC), or in the important positions he has held in the Colombian government, this economist with a Ph.D. in economics from Yale University has been a leading scholar on development issues.

How did Latin America and the Caribbean do during the past half-century?

There are three very different phases. Until 1980, there was dynamic growth. Then came the debt crisis and the “lost decade.” The implementation of economic reforms marks a third stage, in which the economy as a whole did not grow very much over the long term and became more sensitive to external events, both positive events such as those that occurred from 2003 to 2008, and negative events like what happened from 1998 to 2002. From the creation of the IDB until 1980, the region’s economy grew more quickly than the world economy. Since then, we’ve gone backwards in relative terms.

What was the most significant achievement?

Progress in human development, as reflected particularly in advancements in education and health care coverage. There was also important progress in other well-being indexes, such as access to aqueducts and sewers, and improvement in housing conditions.

What was the most notable failure?

The persistent high levels of social inequality, and even in several countries the intensification of inequality on various occasions. As a result of this and of slow economic growth, we lost a quarter of a century with respect to poverty reduction between 1980 and 2004.

Until 1973, the region experienced a period of rapid growth. What part of the import substitution model can be rescued?

Strictly speaking, rapid growth in the region occurred until 1980, although in several countries the slow-down started in 1974. I have written that the concept of “import substitution” is an inappropriate characterization of the model in the region before 1980. It is much more appropriate to characterize it as “state-managed industrialization,” as I suggested with Rosemary Thorp and Enrique Cárdenas in an economic history of Latin America that we prepared for the IDB. It was a period of success, not failure. What

was characteristic about that stage was active government intervention. In terms of insertion at an international level, it was not only about the substitution of imports but also about the diversification of exports and regional integration. We grew well, we diversified the productive structure, we began to diversify exports, and we experienced the greatest rate of progress in human development in our history. Inequality, however, continued to be very high.

Was the so-called “lost decade” inevitable?

In the second half of the seventies, there was a combination of high prices for basic products and abundant external financing that did not re-emerge until 2004 to 2007. The end of the boom required adjustments, but not a lost decade. The international response was what condemned Latin America. Two elements were decisive: the sharp rise in interest rates in the United States to combat inflation, and the greatly delayed response aimed at reducing our

excessive foreign debt, which exploded precisely when international interest rates rose drastically. In a sense, we can say that Latin America paid dearly for the contemporary banking crisis in the United States. In other words, the Latin American debt crisis was also a failure of the major commercial banks of the United States. If this had been openly recognized (for example, with market-price accounting, as is the standard today), the banks would have been saved and their portfolios would have been cleaned up. On the contrary, it was decided to refinance Latin American debt instead of reducing its amount. As a result of that, the banks did not have to openly recognize their losses and Latin America retained an excessive amount of indebtedness. The most positive step in the right direction came much later, with the Brady Plan. If a plan of this nature, or perhaps a more radical plan, had been adopted at the beginning of the eighties, there would not have been a “lost decade,” but rather a deep recession that would have lasted only a few years.

The reforms of the nineties brought a profound change. Were they essential?

It was essential to adopt measures to adapt the region’s economies to the new international context of globalization. But neither the severity nor the rapidity of the reforms was necessary. A more gradual commercial opening up that would have allowed for greater conservation of the productive apparatus inherited from the previous period would have been more appropriate. In some cases, in addition, the radical nature of the reforms was inadvisable. Financial liberalization left us a legacy of vulnerability to external financing cycles from which we have not yet been freed. And the apparatus of the government was weakened. Now we are trying to rebuild it.

Why, despite the volatility and the crises of 1995, 1997 and 2002, has the region succeeded in staying the course?

There have been many changes: in particular, a greater emphasis on social policies, progress toward macroeco-

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conomic anti-cyclical policies that is still incomplete, and the seeds of a return to industrial policy. In addition, the hegemony of neoliberal thought that marked this phase of world development has been eroding. In any case, as with commercial opening up, some reforms were kept, because they turned out to be suitable in the new world context.

What could you say about the boom that occurred during a good part of this century?

The combination of good prices for basic products and abundant external financing always produces accelerated economic growth in Latin America. This time around, it came with a third ingredient: high levels of remittances. This was the basis of the rapid growth experienced in Latin America between 2003 and 2008, as the IDB has acknowledged. The conditions that supported it have disappeared. There were, however, advancements in other areas, especially a step toward anti-cyclical

macroeconomic policies, as is reflected in treasury accounts and especially in the large accumulation of international reserves.

What advice would you give to the region's countries, looking toward the future?

That they should adopt a policy focus that is built on four pillars. The first is a very active social policy, focused on human development and on combating social inequality. I emphasize inequality and not poverty because our main problem is inequality. With our level of development, extreme poverty can be eradicated. The second pillar is made up of strongly anti-cyclical macroeconomic policies to manage boom periods as well as times of crisis. The third is based on productive development policies for today's open economies—that is, industrial policies modeled after East Asia, but promoting not only manufacturing but also services and sectors of the region that are abundant in natural resources.

The fourth pillar is greater investment in physical infrastructure, particularly road networks, where the region is experiencing severe deficiencies.

What do you think the IDB's role has been?

One of the Bank's main merits was its early promotion of the financing of social policy and of small businesses and micro-enterprises when the World Bank was focused on other things. In the eighties and nineties it grew a lot; it began to surpass the World Bank as a source of financing, and it expanded its analytical capacity. The majority participation of Latin American and Caribbean countries generates, in addition, a strong sense of belonging that, in a certain sense, other institutions lack.

Box 3.1 The IDB's Role in Social Development

Throughout its 50 years of history, the Inter-American Development Bank has invested more than US\$32 billion, or one-third of all of its loans, in the region's social development. Included in this portfolio are a broad spectrum of financial, cooperation and technical support efforts in the fields of health care, education, labor markets, innovations for social inclusion, gender-related issues, racial and ethnic matters, and poverty reduction.

The Bank's central mandate, which is to contribute to the general progress of its member countries, envisages an investment philosophy rooted in the idea that human development encompasses social and economic objectives, a vision that has remained intact throughout a half-century of loan and technical assistance operations. By emphasizing the importance of the economic returns of social investment, the IDB has been at the leading edge of thought on the development of social sectors since its founding in 1959. At that time, such operations were perceived as having a nominal return on investment, and their political and financial support was difficult to justify. However, improvements in labor productivity derived from advancements in health and education revealed a new directionality in the link between economic growth and social progress. In other words, "health produces wealth" is added to the traditional "wealth generates health" paradigm. The IDB's creation gave rise to a new era of investment in people, which has been instrumental in raising social development in Latin America and the Caribbean to an unprecedented level.

Today, the change in thinking has pushed the Bank to the front row with respect to social development. Apart from its traditional lending activities, the institution has assembled teams of front-line experts who work with member countries to create opportunities for the population. The current agenda of activities includes continuing work in the fields of social protection, health and nutrition, primary and secondary education, gender and diversity, and social security and work. In 2008 alone, more than US\$2 billion was earmarked for social investment.

That said, Latin America continues to be the region of the world with the most inequalities, and growth with equity is a top priority of sustainable development. The Bank is prepared to meet this challenge with modern initiatives and creative solutions. In taking this approach, it seeks to remain the social development pioneer it has always been.

In addition, the Bank has worked diligently on research and programs to promote social development in Latin America and the Caribbean. A list of publications and documents on this topic can be found at: http://www.iadb.org/sds/sdp_e.htm.

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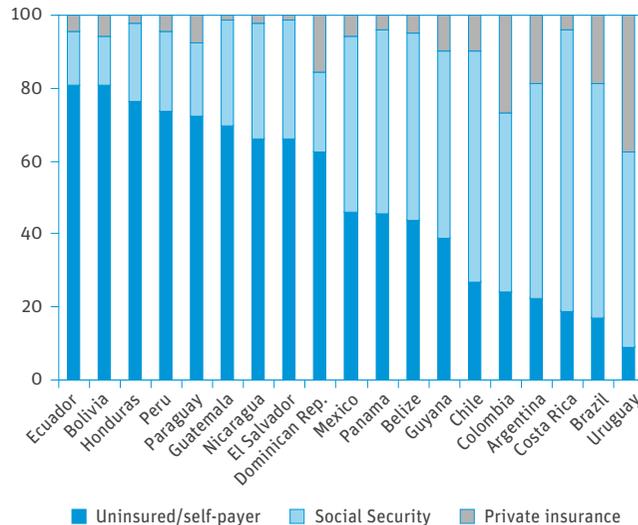
the low levels of financial coverage of the 1950s, current levels differ among the region's countries (Figure 3.8).

The region must therefore maintain the efforts made thus far, with additional emphasis on improving health care systems, eliminating their inequalities and promoting their use by the poorest segments of the population and the so-

cially excluded. Of special importance are preventive measures and primary care, including universal vaccination campaigns. One reason is that although the population growth rate in Latin America and the Caribbean is expected to fall from 1.3 percent per year between 2005 and 2010 to 0.2 percent between 2045 and 2050,⁶ people over 60, who today make up less than a fifth of the population, would then represent one out of every four inhabitants.

Figure 3.8 “If You Had to Go to a Hospital Because of an Accident or Illness, Who Would Take Care of the Expenses?”

(Percentage of respondents per country)



Source: IDB (2008) based on Gallup (2007).

GENDER AND DIVERSITY

Progress on women's issues is of particular note among the indisputable success stories of Latin America and the Caribbean over the past five decades (IDB, 2007b). According to available statistics, not only has parity been achieved in terms of education in comparison to 1960, when the proportion of men enrolled in study programs was substantially higher, but in some countries the female population represents the majority of those attending school. Consequently, the female illiteracy rate is still a couple of percentage points above that of men, although by 2010 it is expected to fall to 8.8 percent⁷ (Table 3.5).

Table 3.5 Illiterate Population Over 15, Latin America and the Caribbean, By Sex, 2000–10
(Percentage of the population over 15 years of age)

Country	Both sexes			Men			Women		
	2000	2005	2010	2000	2005	2010	2000	2005	2010
Argentina	3.2	2.8	2.4	3.2	2.8	2.5	3.2	2.7	2.4
Bahamas	4.6	4.2	3.8	5.5	5.0	4.7	3.7	3.3	3.0
Barbados	0.3	0.3	0.2	0.3	0.3	0.2	0.3	0.2	0.2
Belize	6.8	5.3	4.0	6.7	5.4	4.3	6.8	5.2	3.7
Bolivia	14.6	11.7	9.4	8.1	6.2	4.8	20.8	17.0	13.8
Brazil	13.1	11.1	9.6	13.0	11.3	10.0	13.2	11.0	9.3
Chile	4.2	3.5	2.9	4.1	3.4	2.8	4.4	3.6	2.9
Colombia	8.4	7.1	5.9	8.4	7.2	6.1	8.4	6.9	5.7
Costa Rica	4.4	3.8	3.2	4.5	3.9	3.3	4.4	3.7	3.0
Cuba	3.3	2.7	2.1	3.2	2.6	1.9	3.4	2.8	2.2
Dominican Rep.	16.3	14.5	12.9	16.3	14.7	13.2	16.3	14.4	12.6
Ecuador	8.4	7.0	5.8	6.8	5.6	4.7	10.1	8.3	6.9
El Salvador	21.3	18.9	16.6	18.5	16.4	14.4	23.9	21.2	18.6
Guatemala	31.5	28.2	25.2	24.0	20.9	18.3	38.9	35.4	32.1
Guyana	1.5	1.0	0.7	1.1	0.8	0.6	1.9	1.3	0.9
Haiti	50.2	45.2	41.1	48.0	43.5	39.8	52.2	46.8	42.3
Honduras	25.0	22.0	19.4	25.1	22.4	20.0	25.0	21.7	18.8
Jamaica	13.1	11.3	9.8	17.1	15.0	13.3	9.3	7.7	6.3
Mexico	8.8	7.4	6.2	6.7	5.7	4.8	10.9	9.1	7.6
Netherlands Antilles	3.5	3.1	2.8	3.5	3.1	2.9	3.4	3.0	2.7
Nicaragua	33.5	31.9	30.3	33.8	32.2	30.7	33.3	31.6	29.9
Panama	8.1	7.0	6.0	7.5	6.4	5.4	8.8	7.6	6.6
Paraguay	6.7	5.6	4.7	5.6	4.8	4.1	7.8	6.4	5.3
Peru	10.1	8.4	7.0	5.3	4.4	3.5	14.8	12.3	10.3
Puerto Rico	6.2	5.4	4.6	6.4	5.7	5.0	6.0	5.1	4.3
Trinidad and Tobago	1.7	1.2	0.9	1.1	0.8	0.6	2.3	1.7	1.2
Uruguay	2.4	2.0	1.7	2.9	2.5	2.1	2.0	1.6	1.3
Venezuela	7.5	6.0	4.8	7.0	5.8	4.8	8.0	6.2	4.9
Latin America and the Caribbean^a	11.1	9.5	8.3	10.1	8.8	7.7	12.1	10.3	8.8

Source: ECLAC (2007b).

Note: The illiterate population is defined as those persons who cannot, with understanding, both read and write a short, simple statement on their everyday life. Data correspond to the latest literacy estimates and projections by UNESCO revised in June 2000 and based on the information collected during national population censuses. Population data correspond to the 2000 revision of the United Nations World Population Prospects.

^a Includes 41 economies: Anguilla, Antigua and Barbuda, Netherlands Antilles, Argentina, Aruba, Bahamas, Barbados, Belize, Bermuda, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Cayman Islands, Turks and Caicos Islands, British Virgin Islands, Jamaica, Mexico, Montserrat, Nicaragua, Panama, Paraguay, Peru, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay and Venezuela.

This factor is both a cause and effect of the greater participation of women in the labor market. According to ECLAC, female representation among the region's working population grew from 35.7 percent to nearly 40 percent in 2005. Moreover, a disparity in income persists due to differences in types of employment as well as discriminatory practices, although an increasing number of laws are guaranteeing equality (Duryea, Cox Edwards and Ureta, 2005).

On the political scene, the region has a growing number of women presidents or prime ministers, while nearly one-quarter of cabinet positions and 18 percent of parliamentary posts are held by women. In the private sector, it is estimated that one-third of all top-level management positions are occupied by women.

Despite these advancements, challenges remain. Violence against women is high, with data for 15 countries indicating that 69 percent of women have suffered physical abuse by their husband or partner, while 47 percent have been victims of sexual abuse. On the other hand, the proportion of households headed by women has increased to nearly a

third of the total in the region's largest nations.

Great challenges also exist with regard to indigenous groups and people of African descent, groups for which progress has been less notable. People of African descent, for example, make up nearly 30 percent of the total population but 40 percent of those living in poverty (IDB, 2007a). Generally, both groups have higher indices of illiteracy, lower income levels, lower ratios of land ownership and lower life expectancy than other Latin Americans. Although in recent years some countries have made an effort to recognize and guarantee ethnic diversity, including the creation of government offices dedicated to serving the needs of indigenous groups and people of African descent, political exclusion and social marginalization persist.

FINAL CONSIDERATIONS

In September, 2000, the leaders of 189 countries belonging to the United Nations approved the "Millennium Declaration," which was to translate into a plan of action with eight specific, quantifiable objectives, including the eradication of extreme poverty and

hunger, ensuring universal primary education, promoting gender equality and the empowerment of women, reducing child mortality, improving maternal health, combating HIV/AIDS, guaranteeing the sustainability of the environment, and promoting a new development association. In a good part of these objectives, at least those related to social issues, Latin America and the Caribbean are steadily advancing toward the goal. Nevertheless, global figures hide profound differences among countries and specific regions.

Thus, while keeping in mind the success stories of the last 50 years, it is also clear that a sizeable share of the region's countries continue to lag behind the others, with less-than-satisfactory results. Some of the reasons outlined have to do with disparities in income levels, while others point to political and institutional aspects. However, beyond this explanation, it is clear that poverty levels in Latin America and the Caribbean are still too high and that not enough has been done to combat inequality, which in itself is one of the greatest obstacles to development. Beyond the support of multilateral entities like the

Child and maternal health has a high priority in an IDB-funded program in Guyana to extend basic health services to vulnerable population groups.



Farmers in Nicaragua go back to school in an IDB-financed program that included education on techniques to raise production while protecting natural resources.

IDB, the overall challenge is not only in spending more money but in spending it more wisely, with programs that more directly serve the needs of vulnerable segments of the population and that can break the cycle of misery that has plagued specific groups of people in the most diverse regions.

These concerns are even more valid in a scenario of global economic deceleration such as the one we are currently experiencing, in which the challenge

for Latin America and the Caribbean must be to preserve their achievements to date and continue making progress in an area where much remains to be done. The experiences of past crises show how social indicators have been hurt by periods of financial distress. Nevertheless, many countries are now fiscally stronger, with a broader assortment of successful policies in place to ensure that the same thing will not happen again.

Interview with Michèle Duvivier Pierre-Louis



Michèle Duvivier Pierre-Louis is the Prime Minister of Haiti. She received her primary education in Haiti and then earned a mas-

ter's in economics from Queens College in New York in 1976 and a doctorate in humanities in 2004 from St. Michael's College in Burlington, Vermont. Between 1995 and 2008 she was the head of Fokal (Foundation for Knowledge and Freedom), a non-governmental organization.

Would you agree that over the last 50 years, Latin America and the Caribbean have experienced significant social development?

Latin America and the Caribbean actually experienced profound changes over the second half of the 20th century. As early as 1959, the Cuban Revolution sent a shock wave through the region, sparking a passion in young people of my generation for utopias of freedom and change. We dreamed then of united, brotherly societies. Subsequent experiences in the Dominican Republic, Chile, Nicaragua, El Salvador, and Grenada came to form part of this same current: attempts to put an idea for social change into practice. Yet, at the same time, it was unrealistic to believe that the Cuban experience could be replicated in the region in the midst of the Cold War. We had to wait for the triumph of the ideology of human rights and the fall of the Berlin Wall for dictatorships like those of Duvalier, Somoza, or Videla to become obsolete. And this change of course, driven by new regional geopolitical realities, would unleash social forces in multiple sectors that the region's governments would tap into to promote economic and social development that was

increasingly focused on the needs of the concerned populations: education, health, justice, employment, communications, gender equity, culture, etc. These transformations occurred within the framework of a democracy-building process which included the definition of fundamental rights such as the right to free speech, freedom of association, and freedom of movement.

Nevertheless, disparities persist. Why?

All of the region's countries emerged from a long process of colonization by European powers based on the exploitation of natural wealth, and in many cases, on the free labor of slaves. The first disparities in our societies arose from this profoundly discriminatory situation of inequality. Successive political regimes over the course of the 19th and 20th centuries did not know how or were perhaps unable to conceive of citizenship in the modern sense of the word, based on inclusion and equal rights, thus driving the paradigm shifts that would necessarily follow from it. But, things change. The new types of leadership that have emerged in Brazil, Bolivia, and Ecuador, to name but a few, are clear manifestations of a social move-

ment that no longer accepts marginalization and exclusion, but rather demands a right to civic and political recognition and participation.

What can the region do to make up for these inequalities as quickly as possible?

First, governments must become aware of the multifaceted existence of these inequalities, and then take stock of the destabilizing effects they can have on the entire political process of building a democracy. This means paying attention to their populations, their needs, being able to establish a frank and open dialogue with all sectors of society, in order to build the trust necessary for the implementation of public policies based on shared interests and the common good. And if such internal processes prove necessary, regional meetings and exchanges can certainly help build local and national capacities. Efforts should be supported by the well-off sectors of society to allow the treasury to expand the tax base and to collect all taxes and duties, because democracy is also built on taxes. The state, the government will then have the resources necessary for investment and the creation of good jobs able to

improve people's living conditions. Access to government, education, employment, health, and justice are powerful means for combating these inequalities.

Among the many strategies that have been tried in the past, which do you consider most effective?

It is hard to say which strategy has been most effective. Despite all the progress made in these areas, the current financial crisis, which will have a negative impact on the region, has demonstrated the fragility of our societies, even the strongest ones. They have become so complex, and at the same time so dependent on our globalized world, that one sometimes wonders what safeguards to put in place to protect the gains we have made in the struggle against inequality and poverty. I am not a pessimist, but it requires a great deal of faith in the future to assure oneself of the irreversibility of things.

In your opinion, what are the main measures that should be taken to achieve concrete results in the fight against poverty?

I just cited a few examples. First and foremost, in a country like Haiti, we need to undertake an action that has

high significance and high symbolic content: access to government for all men and women, which is a recognition of citizenship; access to education (especially for girls) from primary school through university; and massive investment in job creation, agriculture, infrastructure, housing, industry, the arts and crafts sector, and new technologies. Emphasis must be placed on local development, strengthening territorial communities, and on young people. Good governance of public institutions and their opening to civil society can build the necessary trust between citizens and the state.

The spike in food prices had a negative impact on many countries, including Haiti. What can be done in the future to reduce this impact if prices rise again?

Deregulation in the 1980s and structural adjustment policies made ordinary people considerably poorer. These policies had a negative impact on traditional agriculture by cutting prices, and on cities due to intense migration to urban centers giving rise to communities of squatters around every city in the country. Now, we have to go back to national production, first, to reduce

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the country's food dependence, and then to recover some degree of food sovereignty, because today, this sector still represents the largest percentage of employment for the population. But we must increase productivity, select the channels that contribute the most, and invest throughout the value chain: inputs, credit, transportation, electricity, processing, packaging, and marketing. Only under these conditions can we restore a true national production process. A road network is also needed to allow land access to essential outlets: markets, ports, etc. We also need to establish strategic stockpiles held in reserve for hurricane seasons and potential spikes in prices. In a country like Haiti, regardless of national efforts, international aid, the work of the IDB, remains essential, indispensable, in the fight against poverty.

One concern analysts of the current international crisis have is an increase in poverty. Do you agree? What can be done to protect the most vulnerable populations?

The international crisis will have an impact on the region, and there is no doubt that the most vulnerable populations will be its first victims. For us,

the crisis will pose a crucial cash flow problem, and the paradox is that this will happen precisely when we will need access to a larger cash flow. The IDB has spoken to us about a cash transfer program that we consider an appropriate response to help vulnerable populations cover their day-to-day survival expenses. At these times, it is also important to inform the public of the need to mobilize and create a major national solidarity movement in order to help the poorest.

What do you see as the IDB's role in mitigating the crisis, particularly in the area of social development?

The IDB is an extremely important institution for the region. In 50 years—and this is my opportunity to express my best wishes for its continued success—it has already proven itself in every country in the region. With respect to Haiti, it remains our most important partner, both in terms of volume of aid, and also with respect to the flexibility it has shown in negotiating and renegotiating financial agreements. It is involved in many areas, ranging from institutional strengthening to concrete actions in sectors including agriculture, the environment, transportation infra-

structure, energy, etc. It also invests in the private business sector and civil society. In this regard, its contribution to social development is clear. With respect to its involvement in these times of international financial crisis, we are interested in planning the implementation of the cash transfer program for populations at risk. Our country needs aid in the form of budgetary support for the government, particularly now when it is just getting back on its feet after the series of shocks it endured in 2008, and when it is already anticipating serious problems related to its current precarious financial situation. In this regard, both on behalf of the Haitian government and personally, I would like to sincerely thank the IDB and I hope our work together continues to expand possibilities for development and progress for the country and for the Haitian people, as well as for the region.

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¹ Persons earning less than US\$2 a day based on purchasing power parity.

² Persons earning less than US\$1 a day based on purchasing power parity.

³ In Latin America, 8.6 percent of the workforce has higher education versus 8.2 percent in East Asia. See IDB (1998-99), Chapter 2.

⁴ The proportion of individuals with secondary education (complete or partial) in Latin America and East Asia equals 16.9 percent and 28 percent, respectively. Those with primary education (complete or partial) total 50.8 percent and 43.8 percent, respectively. See IDB (1998-99), Chapter 2.

⁵ For more information on this issue, see the following link: <http://web.worldbank.org/WBSITE/EXTERNAL/BANCOMUNDIAL/EXTSPPAISES/LACINSPANISHEXT/EXTLACREGTOPHEANUTPOPINSPA/EXTLACREGTOPHIVINSPA/0,,contentMDK:20560208~menuPK:792652~pagePK:34004173~piPK:34003707~theSitePK:783025,00.html>.

⁶ Based on ECLAC calculations.

⁷ Based on ECLAC calculations.



A sea of cargo. Bound for every corner of the world, Latin America's exports must compete in a global economy where national boundaries count for increasingly less. In addition to its historical status as producer of commodities and more recently of high-value agricultural foodstuffs, the region also exports industrial products and promises to be a major player in new sectors, such as biofuels. The IDB is helping countries improve transportation infrastructure to help exporters remain competitive.

IV Transformations in Integration and Trade

When Santiago Gutiérrez, an executive in Bogotá, was given the charge in 1991 of representing his company on the board of directors of a Venezuelan firm that met monthly, he asked to be relieved of this responsibility. The reasons, he recalls, were but one: “There were so few flights that sometimes you’d have to stay two or three days for a meeting that lasted just a couple of hours.”¹ Today, things are different. Many times a day, hundreds of people are making the same trek, even leaving in the morning and coming home for dinner.

Their reasons for going on this trip vary. Although a significant percentage of passengers on the Bogotá-Caracas route are traveling for pleasure or to visit family, a great many are making the trip for business purposes.²

Tangible examples like this one show how things have changed in a region where the terms “integration” and “trade” are becoming part of day-to-day reality. Thanks to the events of past de-

acades, more and more Latin American products are becoming available around the globe. Also, these sales have served to strengthen ties between neighboring or Western Hemisphere countries. As the numbers show, total exports from Latin America and the Caribbean grew from US\$130.214 billion to US\$761.959 billion between 1990 and 2007, while imports to the region jumped from US\$18.727 billion to US\$144.211 billion in the same period. As a result, the share of intra-regional sales increased from 13.9% to 18.9% of the total (ECLAC, 2008) (Table 4.1). Moreover, around 8% of foreign direct investment received in 2007 originated with companies from the region, known colloquially as *translatinas* (ECLAC, 2008).

THE FIRST STEPS

Despite the boom of recent years, the expansion of trade relations has been in slow incubation for quite some time. At the end of the 1950s, for example, Latin America and the Caribbean were

Table 4.1 Total Exports and Exports by Sub-Regional Integration Schemes, Latin America and the Caribbean, 1990–2007
(Millions of dollars and percentages)

	1990	1995	1998	2002	2003	2004	2005	2006	2007	January to March 2007	January to March 2008 ^a
LAIA											
Total exports (1)	112,694	204,170	251,345	319,807	346,145	427,835	506,557	602,803	675,139	154,001	189,416
Exports to LAIA (2)	13,589	35,471	43,118	36,164	40,872	56,777	72,979	91,757	107,586	22,664	29,678
Percentage of internal exports (2:1)	12.1	17.4	17.2	11.3	11.8	13.3	14.4	15.2	15.9	14.7	15.7
Andean Community											
Total exports (1)	31,751	39,134	38,896	52,177	54,716	74,140	100,089	126,112	139,102	29,596	44,213
Exports to the Andean Community (2)	1,312	4,812	5,504	5,227	4,900	7,604	10,313	12,719	12,909	2,622	4,012
Percentage of internal exports (2:1)	4.1	12.3	14.2	10.0	9.0	10.5	10.3	10.1	9.3	8.9	9.1
MERCOSUR											
Total exports (1)	46,403	70,129	80,227	89,500	106,674	134,196	162,512	188,188	221,498	46,749	56,718
Exports to MERCOSUR (2)	4,127	14,199	20,322	10,197	12,709	17,319	21,134	26,626	33,051	6,807	9,415
Percentage of internal exports (2:1)	8.9	20.2	25.3	11.4	11.9	12.9	13.0	14.1	14.9	14.6	16.6
CACM											
Total exports ^b (1)	4,480	8,745	14,987	17,006	18,117	19,767	21,849	24,493	26,036	6,795	7,257
Exports to CACM (2)	624	1,451	2,754	2,871	3,110	3,506	3,912	4,429	5,217	1,218	1,305
Percentage of internal exports (2:1)	13.9	16.6	18.4	16.9	17.2	17.7	17.9	18.1	20.0	17.9	18.0
CARICOM											
Total exports (1)	4,118	5,598	4,790	5,732	6,712	7,880	15,949	18,709	19,872	5,734.3	5,666.2
Exports to CARICOM	509	843	1,031	1,220	1,419	1,810	2,091	2,427	2,793	693.9	775.2
Percentage of internal exports (2:1)	10.3	14.2	18.6	17.2	16.5	17.4	13.1	13.0	14.1	12.1	13.7
Latin America and the Caribbean											
Total exports ^c (1)	130,214	227,922	280,065	347,610	376,590	472,444	568,798	679,713	761,959	167,356	203,061
Exports to Latin America and the Caribbean ^d (2)	18,727	45,180	56,644	53,424	59,635	79,952	99,839	121,923	144,211	30,600	39,063
Intra-regional percentage/total (2:1)	13.9	19.8	20.2	15.4	15.8	16.9	17.6	17.9	18.9	18.3	19.2

Source: ECLAC, based on official information from the listed sub-regional integration schemes and the IMF, *Direction of Trade Statistics*.

^a Preliminary figures.

^b Figures include external sales from *maquila* production.

^c Total exports include LAIA, CARICOM, Cuba, CACM, Panama, and the Dominican Republic.

^d Includes sub-regional trade among the Andean Community, MERCOSUR, CACM and CARICOM, and trade conducted by Chile and Mexico and by Cuba, Panama, the Dominican Republic, and Venezuela with the rest of the region, as well as among other groups of countries.



An IDB-financed project to build and improve highways in Brazil's state of Rio Grande do Sul also supports integration efforts in MERCOSUR common market.

an important frame of reference in discussions on economic integration, growth and development, even though those processes had been underway since the 19th century. However, the creation of the Central American Common Market (CACM) dates back to the early 1960s, the same decade that saw the establishment of the Latin American Free Trade Association (LAFTA), now known as the Latin American Integration Association (LAIA).

During that period, the model of regional integration was one of “looking within” based on import substitution, which contributed to the growth of the manufacturing industry. According to local popular theory, integration would help break bottlenecks created by narrow national markets, which in turn were limiting opportunities for industrialization in the face of rising barriers against developing countries.

That strategy failed due to the timid efforts of tariff liberalization as well as the rigidity of the programs adopted and the obstacles represented by the defense of public and private interests that maintained the status quo.³ Additionally, macroeco-

nomics instability, imbalances among member nations of regional and sub-regional groups and poor infrastructure hampered proper development of ties (IDB, 2002).

However, it wasn't until the debt crisis of the 1980s, considered by the region as its “lost decade of development,” that an opportunity arrived to shift the focus and adopt extensive reforms. Regional economies carried out far-reaching macroeconomic reforms in an attempt to control inflation, reduce volatility and future debt and open the region to the rest of the world.

NEW WINDS

Trade and integration constituted a central element of the framework for the new economic policy. The countries of the region gradually began shifting toward globalization in their development strategies, inserting their national economies into international markets. To that end, they made use of trade and liberalization as key tools, including tariff reductions that led to a drop in the average tariff for the region from 40% to less than 10% between 1985 and 2006 (IDB, 2006).



Strict quality control and market recognition ensure a consistent demand for bananas and other traditional exports that provide jobs and earn foreign exchange. (photo credit *El Tiempo*)

Latin America's strategy began to settle on a multi-pronged approach involving unilateral openness, reciprocal trade liberalization (through sub-regional integration), free trade agreements with partners around the world and multilateral negotiations within the framework of the World Trade Organization (WTO), to which the vast majority of the Western Hemisphere's nations now belong (Table 4.2).

Regional integration began gaining strength in the early 1990s with the redefinition or creation of schemes intended to become customs unions. Such was the case of the Andean Community, the Caribbean Community (CARICOM), the Southern Common Market (MERCOSUR) and the Central American Common Market (CACM). In 1994, the Summit of the Americas in Miami was the scene of negotiations between 34 countries to create the Free Trade Area of the Americas (FTAA) with the ambitious goal of breaking down barriers and narrowing ties among all of the continent's democracies.

While negotiations were taking place, bilateral agreements began to

Table 4.2 IDB Borrower Member Countries and Year of Entry in the GATT/WTO

Country	Year of Entry in the GATT/WTO System
Brazil	1948
Chile	1949
Dominican Republic	1950
Nicaragua	1950
Peru	1951
Uruguay	1953
Trinidad and Tobago	1962
Jamaica	1963
Guyana	1966
Argentina	1967
Barbados	1967
Suriname	1978
Colombia	1981
Belize	1983
Mexico	1986
Costa Rica	1990
Venezuela	1990
Bolivia	1990
El Salvador	1991
Guatemala	1991
Honduras	1994
Paraguay	1994
Ecuador	1996
Haiti	1996
Panama	1997

Source: IDB (2002).

Note: GATT: General Agreement on Tariffs and Trade, and WTO: World Trade Organization.

proliferate, whether between nations or between sub-regional associations. Many other countries also adopted a system of transcontinental integration

in an attempt to strengthen their relations in Asia as well as Europe.

In contrast to the “old regionalism” agreements signed in 1960 and 1970, current free trade treaties complement market liberalization with their characteristic “open regionalism” (Devlin and Estevadeordal, 2001). These treaties do not just mean low tariffs for outside countries; their complexity and ample coverage allows them to touch on matters such as investments, the exchange of services, policies for promoting fair competition, and more.

While the agreements of the previous generation were forged exclusively among developing countries, many of today’s agreements are of a North-South nature, including emerging and developed economies. In recent times, not only has the number of trade integration schemes increased, but their content has become more complex and their coverage has expanded as well. Most free trade agreements have gone even further, ensuring commodities market access to so-called “second-generation matters” such as services, investments, intellectual property rights and government procurement.

Sub-regional agreements have added a new dimension to cooperation by dealing with issues ranging from macroeconomic cooperation and labor mobility to coordination of positions in multilateral trade negotiations.

THE RATIONALE OF INTEGRATION

Although macroeconomic reforms gave a massive push to regional integration efforts, there were other national and international dynamics that led the nations of the Americas to sign free trade treaties in the midst of the challenges of an increasingly globalized world.

Part of the rationale had to do with the benefits of being a “first mover” in an expanding sea of agreements. The strategy of signing agreements of various types recognized that each country’s trade policy decisions hinged on the successful establishment of strategic interactions with other nations. Based on this rationale, early integration can allow a particular country to gain advantages in new markets and attract foreign investment. If, however,

these opportunities are not taken, a country can be left out of the network of trade agreements as well as the host of benefits that come from belonging to an integration scheme with multiple fronts.

Another explanation is the need for alternatives or contingency schemes that regional economies can opt for in any global trade policy scenario. For example, multilateral dialogue can be excessively prolonged or produce less-than-optimal results instead of leading to a substantial and significant agreement. Against the backdrop of scenarios like these, free trade agreements can function as an insurance policy for gaining access to certain markets. At the same time, countries that have guaranteed their access to the market by signing trade agreements have less to lose in global dialogue by using these agreements to their advantage in improving their negotiating positions.

An additional element is the flexibility to adjust to changes in competitive advantages and demand in global markets. Worldwide production and trade partnerships alike are evolving at an unprecedented speed, and the variety of goods exchanged has grown exponentially over just two decades.

Modifications in technology and the reduction of transport costs, in addition to the impressive increase in the exchange of electronic goods and the growing importance of services, will further increase the speed at which the global economy is changing. The multiple-agreement strategy allows for increased exploitation of trade niches that are important today but did not exist in the past.

Clear synergies also exist. Trade standards are generally based on the same set of disciplines, whether on a regional or global scale. Thus, knowing, negotiating and enacting agreements on one particular trade front can generate positive external effects on these processes on any other front. For example, negotiating the exchange of services via the WTO no doubt improves the capacity of governments to negotiate in the services sector within the framework of a free trade agreement. In addition, adopting mandatory measures for facilitating trade, such as modernizing customs processes or establishing a one-stop counter for processing exporter documentation, would result in immediate benefits for the country in question with all of its trade partners,



New highway construction helps to reduce transportation bottlenecks that boost costs for producers and diminish the ability of their goods to compete in the global marketplace.

not just those with which it has signed an agreement.

However, integration was brought about by many other factors. For example, in the early 1990s, with the rise of MERCOSUR, nontraditional advantages were a key motivator. Among these, the most vital was the need to consolidate peace and democracy in the continent's Southern Cone. In other cases, such as the North American Free Trade Agreement (NAFTA), the focus was on the lack of progress in the multilateral sphere. These agreements, and the many others that followed, would not have been possible without consensus on certain policies, such as macroeconomic reforms and the power of economic and trade liberalization. In addition, a type of "domino regionalism" has existed, frequently driven by the private sector in its search for new export markets, resulting in the signing of trade agreements.

BENEFITS

The benefits of integration go beyond a mere insurance policy in the face of multilateral difficulties or negotiation tactics. First and foremost are the economic benefits: agreements reduce

tariff and non-tariff barriers and are powerful tools for unleashing the expansion of trade and investment flows. When the principle of "open regionalism" is upheld, as has been the case in the Americas, integration schemes guarantee the creation, not the diversion, of trade and investment flows. This has helped to reinforce local economic reforms because current agreements contain numerous policies requiring members to adapt their internal legal frameworks and their frameworks for regulating established requirements.

Moreover, the trend of integration may contribute to the reinforcement of democratic values. The general line of thinking in free trade zones is to make democracy a prerequisite for entering negotiations. In addition, integration may inspire efforts to improve the quality of institutions in member states.

Additionally, a country's efforts in these areas can reinforce its preparedness to join a system of regional and multilateral liberalization. In fact, many current agreements can serve as pillars for more exhaustive hemispheric integration. There is a reason why Latin American countries were among

(Continued on page 102)

Interview with Antoni Esteveordal



Antoni Esteveordal holds the position of Manager of Integration and Trade at the IDB. He is an expert in trade policy,

economic integration and regional cooperation in Latin America and the Caribbean, Asia and Europe. In addition to having been a college professor, he has published numerous articles in specialized journals and has coordinated several of the Bank's reports. He holds a Ph.D. in economics from Harvard University and a bachelor's degree in economics from the University of Barcelona.

What is your impression of the hemisphere's progress with regard to integration and trade over the past half-century?

The region has seen a tremendous change and opening up over the last 50 years—a real turnaround. At the time the IDB was founded, Latin America and the Caribbean were leaders in regional integration but it was an integration that was inward-looking and based on the import substitution model. This model, however, caused a crisis and ended up leading to the “lost decade” of the 1980s. After that came a profound change in which integration and trade became part of the new economic scheme. This included trade liberalization and the signing of integration agreements. Since then the strategy has consisted of a multifaceted approach involving unilateral opening up and the search for reciprocal trade liberalization through sub-regional integration, bilateral trade agreements throughout the world and multilateral negotiations within the framework of the World Trade Organization (WTO). Unlike the “old regionalism” agreements of the sixties and seventies, the current treaties complement market liberalization and are evidence of an open regionalism; in other words, low tariffs for countries that are not part of the agree-

ments. These agreements are also complex and cover other areas such as investments, the exchange of services, and policies for promoting fair competition. In addition, they are not limited to developing countries but occur among wealthy and emerging markets as well. Sub-regional agreements also include cooperative items that go from macroeconomic cooperation all the way to labor mobility and the coordination of positions in multilateral trade negotiations. That's why we support these agreements. They give rise to a whole host of benefits and have a greater impact on development than what the countries signing them would have obtained had they acted on their own.

What do you think the IDB's role has been in relation to what has happened, and what positive aspects stand out as far as what has been done?

The Bank has had a long history of supporting these issues ever since it was founded. It has been a strategic partner of the region from the point of view both of development of physical integration, which includes roads and other networks to reduce the cost of exchange, and of reducing trade barriers and developing regulations that stimulate cross-border trade as well. The goal is now more complex

in light of the region's relative sophistication and the advancements made in the areas of trade and integration. We are trying to identify new strategic partners and use and obtain support from existing ones in order to achieve global competitiveness, and even deal with the short-term implications of trade liberalization. That is what we are focused on with the support of a dedicated team that provides technical studies, assessment and financial support.

How do you see the issue playing out in the near and distant future, and what should the Bank's role be?

Aside from technical and financial assistance in general, I would like to mention three areas. The first is taking advantage of Asian markets that are offering new opportunities for exporting Latin American products, an area we have already been working on. The second is to try to bring about convergence among the multiple trade agreements that exist in Latin America and the Caribbean so as to be able to create economies of scale and regional production networks. The third point refers to adjustments that will ensure that profits from trade make it to the region's poor populations and will allow for a greater

reduction in poverty. A major item in this area is the Aid for Trade initiative under the auspices of the WTO. The Bank has been a key player in this area worldwide and is leading its startup in

the region. In short, we have a broad agenda for ensuring that the competitiveness of the region's economies will be even greater in the global economy in the coming years.

Box 4.1 The IDB's role in integration and trade

Over the course of its 50 years of existence, the Inter-American Development Bank has played an important role in the areas of integration and trade for the purpose of strengthening the bonds among the countries of Latin America and the Caribbean and their bonds with the rest of the world. These activities cover a broad spectrum of the integration agenda and the promotion of trade and investments. They include projects to support trade negotiations and the implementation of bilateral, regional and multilateral trade agreements, as well as the development of regional infrastructures (IIRSA, Mesoamerica Project). They also entail institutional strengthening to support the public sector's ability to promote trade and attract foreign investment, build private sector export development, facilitate trade and modernize customs, speed the processes of adjusting the social and productive sectors in the transition toward the liberalization of trade, and more.

The Bank's support also includes helping countries to develop strategic regional and global integration agendas by providing policy studies, sector assessments, impact analyses and training programs. Activities include loans and technical cooperation programs on a national and regional level. There are also important initiatives and technical assistance programs. Other notable programs include the Regional Public Assets program for promoting collective action among the region's countries, as well as the IDB's participation in the Aid for Trade program under the auspices of the WTO. It is also important to mention the role played by the Institute for the Integration of Latin America and the Caribbean (INTAL), created in 1965 for the express purpose of promoting regional integration.

The Bank's activities are conducted in close cooperation with international and regional organizations such as the WTO, the Organisation for Economic Co-operation and Development (OECD), the World Customs Organization (WCO), and more. The IDB has worked actively in the production of research and programs to generate new knowledge in the area of trade and integration. Recent Bank reports on this topic include the following titles: *Beyond Borders: The New Regionalism in Latin America* (IDB, 2002); *FTAA and Beyond: Prospects for Integration in the Americas* (IDB/Harvard University Press, 2004); *The Emergence of China: Opportunities and Challenges for Latin America and the Caribbean* (IDB/Harvard University Press, 2006); *Trade and Poverty in Latin America* (IDB, 2009); *Unclogging the Arteries: The Impact of Transport Costs on Latin American and Caribbean Trade* (IDB/Harvard University Press, 2008); *Bridging Trade Agreements in the Americas* (IDB, 2009); *Regional Trade Agreements in the Global Trading System* (IDB/WTO, 2009); *Sovereign Remedy: Leveraging Trade Agreements in the Globalizing World* (Oxford University Press, 2009).

(Continued from page 99)

the most vocal supporters of a successful conclusion to the Doha Round.

Economic integration also provides a useful infrastructure for future cooperation, for the production of public goods like regional highway networks and power transmission lines, and for achieving a cleaner environment. The creation of policy frameworks for the regular flow of legal migration could be emerging as a regional public good of tomorrow.

The benefits provided by the various schemes are particularly important in the face of the rather problematic Doha Round. In fact, the problems faced by the Round underscore the importance of regional cooperation for trade and integration with regard to liberalization and facilitating trade, the multifaceted integration agenda, and the various bilateral and multilateral agreements.

Additionally, integration gives the region's countries a platform for coming together and building a consensus that can break down the obstacles that have come to light in Geneva. Furthermore, it can function as a vehicle for economic cooperation apart from what occurs on the global level. In other words, while these processes are

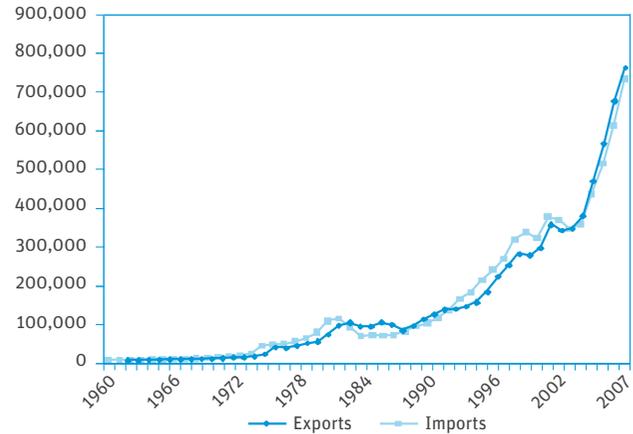
no substitute for the liberalization of trade, they serve as excellent complements to it.

THE PATH TOWARD TRADE LIBERALIZATION

The consequences of the process of regional integration are tangible. Early on, regional tariffs fell to levels between 10% and 20%, below the average 40% levels typical of the early 1980s. However, in recent years, integration agreements have been accompanied by more modest liberalization of external tariffs, making these lower and less widespread.

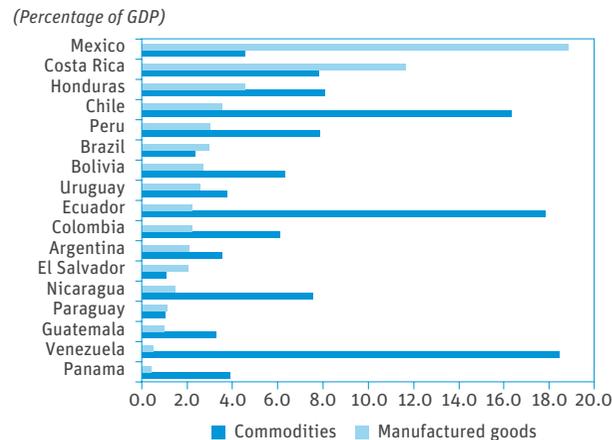
As a result of this process, exports became a fundamental component of Latin American economies, and direct investment grew massively in the 1990s, from 0.7% to 4% of the regional GNP in 2000. In turn, total exports for the region grew by an average of 10.1% annually between 1960 and 2007 while imports grew by 9.9%. Despite this effort, the ratio of exports from the region to exports from the rest of the world has not increased but has instead dropped slightly from 6.7% to 5.5% during the period mentioned. This reflects the persistent presence of

Figure 4.1 Growth of Trade, Latin America and the Caribbean, 1960–2007
(Exports and imports, in thousands of dollars)



Source: INT calculations based on World Development Indicators, World Bank.

Figure 4.2 Exports of Goods to Developed Countries, Latin America, 2006
(Percentage of GDP)



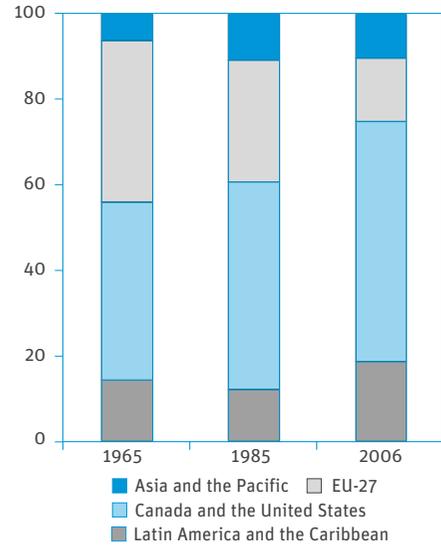
Source: ECLAC, based on official figures.

primary products in the export basket of Latin America and the Caribbean and the changes that have taken place in global competition (Figure 4.1).

Although trade in the region is inherently globalized, its geographical direction seems to have followed the same pattern as the early advancement of regionalism in the Americas (Figure 4.2). Today, the bulk of hemispheric trade is inter-regional. The most notable change in the profile of Latin American exports is the decline in importance of trade with Europe and the increase in importance of the inter-hemispheric market as well as the moderate rise in the participation of the Asia-Pacific region as an export destination.

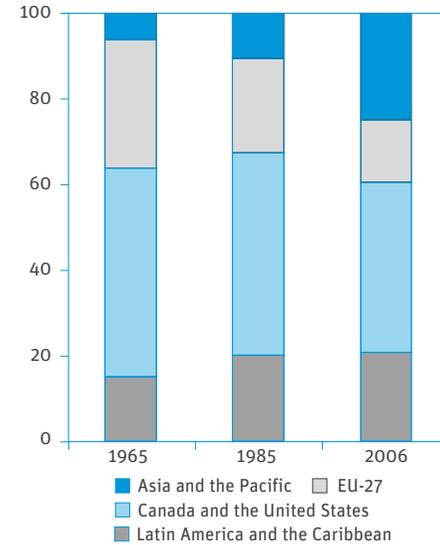
Some countries have experienced a rather marked increase in their exports of raw materials to China. On the imports side, Asia has energetically entered the Latin American market, nearly doubling its involvement during the period with respect to 1985 and acquiring a fifth of all purchases in the region. This phenomenon seems to have occurred at the expense of Europe, whose share has dropped to 14% (Figures 4.3 and 4.4).

Figure 4.3 Export Markets, Latin America and the Caribbean, 1965–2000



Source: INT calculations based on UN Comtrade database, DESA/UNSD.

Figure 4.4 Import Markets, Latin America and the Caribbean, 1965–2000



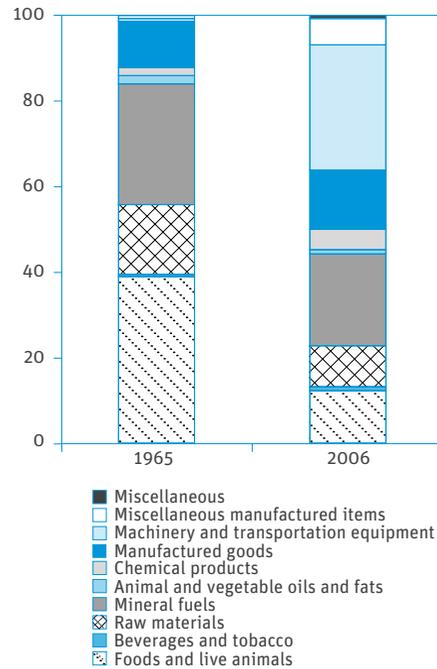
Source: INT calculations based on UN Comtrade database, DESA/UNSD.

Today, manufactured goods are enjoying growing, dominant participation in Latin America’s export basket. As a portion of the region’s external sales, these items grew from a fifth of the total in 1965 to more than 50% in 2006 (Figures 4.5 and 4.6). Meanwhile, the importance of other products such as food, non-food agricultural products, met-

als, minerals and fuels decreased, although the trend was no doubt slightly impacted by sharp increases in international prices, which ended in 2008.

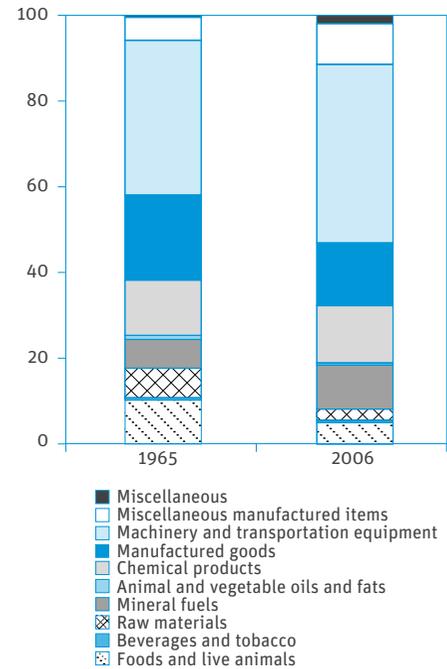
The growing importance of manufactured products in the export basket is more notable in deliveries from the region to the North American market. This has benefited

Figure 4.5 Composition of Exports, Latin America and the Caribbean, 1965–2006



Source: INT calculations based on UN Comtrade database, DESA/UNSD.

Figure 4.6 Composition of Imports, Latin America and the Caribbean, 1965–2006



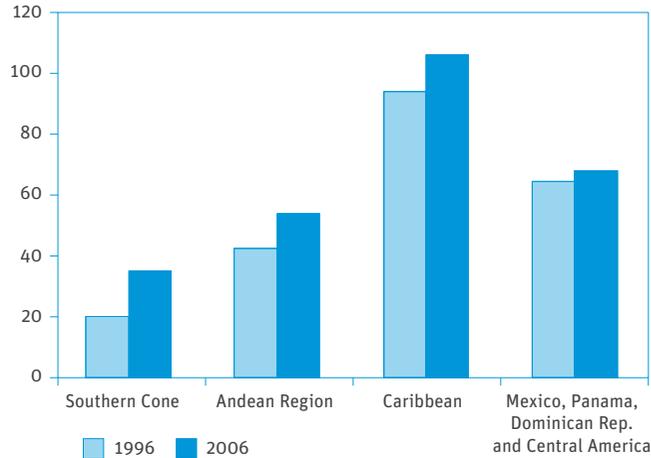
Source: INT calculations based on UN Comtrade database, DESA/UNSD.

countries in geographic proximity who have signed trade agreements. In contrast, MERCOSUR and the Andean and Caribbean regions have experienced much less pronounced growth in this category.

In general, trade has gained increasing importance in Latin American economies. As a proportion of the GDP of the countries of the region, its role in each sub-region over the past decade has increased significantly (Figure 4.7).

Figure 4.7 Expansion of Trade, Averages by Sub-Regions of Latin America, 1996 and 2006

(Trade as percentage of regional GDP)



Source: INT calculations based on World Development Indicators, World Bank.

LESSONS LEARNED AND CHALLENGES

The strategy of integration on diverse fronts and the appealing process of globalization have generated great benefits for Latin America along with new challenges. As has been seen, although liberalization and free trade agreements generate economic dynamism and increase future competitive-

ness, integration is only one part of the solution to the problem of reducing poverty. In other words, trade and integration are necessary but not sufficient. A set of complementary regional and national policies would be required in order to help them fulfill their promise of generating new economic opportunities.

One challenge to be met is that of coordinating negotiations and enacting different agreements, in addition to guaranteeing their mutual compatibility. For companies that must operate in different markets, multiple agreements increase the cost of doing business. The complexity of the trade agenda continues to increase due to the greater number of regional and multilateral negotiations taking place in sectors such as services, investment, standards, and intellectual property rights. Each new regulation included in an agreement represents a new policy that must be taken into account by players from the private sector when exporting, making use of outsourcing mechanisms or making investment decisions. Additionally, each regulation carries with it legal, administrative, and economic implications for countries that participate in a given agreement.

Small and medium-sized enterprises (SMEs) also incur higher learning and transaction costs when tackling numerous trade fronts. Due to asymmetries in information, SMEs are exposed to additional challenges: on the one hand, understanding the opportunities of the market in North America, Asia and Europe; on the other hand, becoming part of the production chains of multinational corporations and competing against the economic powerhouses of Asia.

Additional complementary efforts are needed to facilitate trade, because some traditional barriers continue to exist in certain sectors. Additionally, there are obstacles in the region that limit the integration of the goods and factor markets. Many of these turn into bottlenecks at the borders, to cite just one example. Identifying these types of residual barriers and their impact is a much more difficult task than determining the impact of known mechanisms such as tariffs.

Liberalization must therefore be recognized as having adjustment costs, implying that in the short term some players will lose while others win. If these costs are not adequately managed, they may end up causing a

protectionist reversal, counter to the strategy of liberalization.

CONSIDERATIONS FOR THE FUTURE

Beyond the events of past decades and the slowdown that is affecting the global economy today, there is no doubt that challenges remain. It is particularly important for the region to maintain a long-term vision that will allow it to reap the benefits of globalization and trade integration, thus gaining competitiveness in the world.

From this perspective, one must not forget that the Asian market is experiencing rapid growth, thereby generating opportunities for Latin American producers. Regional trade has shown great dynamism in recent years, with the rate of exports to China growing substantially in 2007. Recent trans-pacific treaties are aimed at expanding trade and investment ties and are inspiring ideas for deepening relations.

No less important is the search for convergence among Latin American countries through multiple overlapping agreements that promote the creation of future economies of scale and regional production networks. In

(Continued on page 112)

Interview with Moisés Naím



Moisés Naím, a native of Venezuela, is considered to be one of the sharpest analysts in the world today. With a

Ph.D. from the Massachusetts Institute of Technology, this former government minister in the Carlos Andrés Pérez administration has been the editor-in-chief of the prestigious *Foreign Policy* magazine in Washington, D.C., for the past decade. Author of the 2006 book *Ilícito (Illicit)* and a weekly columnist for the Madrid newspaper *El País* and leading newspapers in Latin America, Naím discusses trade and integration in the region in this interview.

How do you evaluate what has happened with Latin American integration?

It has been a process of ups and downs. I think the big breakthrough that led to Latin American integration was not so much the signing of free trade agreements between governments, or the establishment of the Andean Community, the Central American Common Market (CACM), or MERCOSUR. That was important. But what was even more crucial was the unilateral trade liberalization that occurred in the 1990s because it allowed the private sector to discover opportunities on its own. Trade increased, and this spurred investment among neighbors. The Chileans started to invest in Argentina, the Brazilians in Chile, the Colombians in Venezuela, and vice versa. So, there was as much trade as there was investment. The ability to grow by trading with or investing in one's neighbor became a reality, something that had only occurred very sporadically up until that time. If you look at statistics from before these reforms, there was very little intra-regional trade, but as a result of unilateral decisions made by several governments to reduce trade barriers and impediments to investment for companies from other countries, integration became more dynamic than ever before.

At the time these decisions were made, they were not very well received by the people. . . .

Well, that was because trade reforms tend to have direct, immediate and very tangible costs associated with them that are primarily borne by specific groups who may therefore lobby to try to prevent these changes from taking place. The benefits, on the other hand, are more broadly distributed among the population and in a way that is less noticeable. Taking tariff protection and government subsidies away from a country's textile industry, for example, negatively and directly affects the owners and workers of that sector's companies, but in a less noticeable way it benefits millions of consumers who have little incentive to lobby in favor of the reforms—unlike the negatively affected parties, who have a great incentive to fight against them.

Would you say, therefore, that the people were the ones who actually made integration happen rather than the governments?

That's right. I've got a story about this that made a big impression on me. Years ago, when I was a government minister, I was in Korea to promote in-

vestment in Venezuela. At the time we had hired a group of famous experts to provide us with an analysis of the country's competitiveness and the sectors that had the greatest potential for successfully competing in the global economy. I read their report and their recommendations on the plane. At the end of my talk in Korea, a man came up to me and said, "Look, I represent one of the world's biggest silk companies, and we're looking for a new location to set up our industry." Well, it turns out that silkworms require just the right amount of light and humidity and very specific and unique weather conditions in order to be able to produce efficiently. This man told me that after years of searching they had discovered that one of the best places in the world for producing silk was at a location in Venezuela and that they were planning to make a very large investment there. This was a pleasant surprise to me, but it also made me question the experts' highbrow report. It also got me thinking, and made me realize that no government or group of experts and planners had ever been capable of determining that one of Venezuela's competitive advantages was silkworms.

What lesson would you draw from this?

That governments should not try to "guess" the industries in which a country can be competitive, because not only does this exercise become a magnet for corruption and pressure tactics by groups that are interested in their industry being chosen, but also because there is no guarantee that the list they come up with will include the industries that really have the most competitive potential.

We've come such a long way, and yet we still have such a long way to go. What things would you point to that still need to be done?

Studies conducted by the International Finance Corporation (IFC) and by the World Bank's *Doing Business* report identify barriers to the creation of new companies in different countries, and they always mention the fact that Latin America is one of the most difficult regions in the world in which to set up a company. It should therefore come as no surprise to us to learn that half the region's jobs are in the informal sector. This is because being a formal employer is more expensive and complicated than it needs to be. What needs to be done is to eliminate barriers and red tape that inhibit the emergence of new

companies. I realize this is easier said than done. No doubt there are powerful political, institutional, technological, financial and perhaps even social and demographic forces that make it so difficult for governments to eliminate the conditions that prevent the creation and growth of new private companies.

It is striking how the region's integration efforts, particularly the last round of them, have survived changes in the countries' governments and political persuasions. Why is that?

First, because there aren't a lot of alternatives. Where these ideas have not survived are in countries that have been able to afford to subsidize alternative experiments in their political economy by using oil revenues. Also, the reality is that in several of the region's largest countries, there are already very large social groups who benefit from open trade systems and depend on them in their daily lives.

Can one categorically state that this change in the model has been more beneficial than harmful for Latin America and the Caribbean?

The problem is that this change took place together with many other changes, so it is very difficult to specifically isolate

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its effects. Reforms were brought into the region at the same time other parts of the world were undergoing profound changes. It occurred in conjunction with the information revolution that was taking place in communications and transportation, the process of political opening up, and the emergence of important economic players such as China and India on the world economic scene. Reforms definitely improved the situation in Latin America in terms of making it a little more competitive compared to what it had been in the past, but other countries advanced much more rapidly in this regard. The challenge is not just to run faster than you used to run, but to be faster than everyone else.

Why did this happen? Was it because even bolder reforms were needed but not enacted?

Partly. We see that in the case of India and China their competitiveness is inexorably linked to their very low labor costs, their unique demographic situation, their immense size and other similar circumstances. These countries which were economically isolated from the rest of the world began integrating at the same time that Latin America was launching its reforms. And then there

are other new competitors in Asia and Eastern Europe which also have more competitive advantages in the sectors with the greatest value added than many of the countries in our region that specialize in raw materials.

This also makes the trend toward greater global insertion inevitable.

Inevitable yet painful, because globalization has negative implications. There are costs that are inevitable and undesirable and that cause social dislocation and political friction. Unfortunately, aside from complaining, there is no way to escape from its effects. This does not mean you have to resign yourself to what's happening and say there is nothing you can do. Globalization can be managed, its costs can be mitigated, its opportunities can be maximized, and those who are most harmed by it can be protected.

What's in it for the average Latin American?

It is important to note that one of the most important groups of people as far as growth over the last decade is concerned, both in Latin America and throughout the world, is the middle class. This does not mean that our region is no longer an area where poverty

dominates, but it must be acknowledged that great progress has been made in reducing it. The very real threat is that the current economic crisis will wipe out the social progress that has been made in Latin America over the last decade.

Is this largely due to the trend toward global insertion?

That's part of it, but recent social progress has also occurred because, first of all, there hasn't been inflation and, secondly, there has been a certain amount of economic growth. The other factor is the popularization of very effective social policy programs involving conditioned transfers in which countries have earmarked a lot of money for low-income families who keep their children in school—a series of economic, nutritional and health benefits that have had a very clear and direct impact on improving the social situation.

What's coming down the road?

What's coming is protecting Latin Americans from the devastation that will be caused by the global economic crisis we're in right now. We must also try to keep the bad ideas that have already been tested in the past and that we know don't work from gaining popularity,

ideas which the crisis may cause to appear more valid than they really are.

What do you mean by bad ideas?

Closing down economies, setting up barriers to imports and exports, mistreating investors, limiting foreign investments, or thinking that the government can be a good businessman and manager of its workers' savings and pensions. Going back to exchange rate controls and to generalized price control systems, or imposing regulations in the labor market that inhibit job creation.

Looking back 25 years, what has surprised you the most?

That when economies are opened up, possibilities emerge that no one would have imagined. In Argentina, for example, with the Internet explosion, young entrepreneurs emerged and competed with the best in the world. This shows that business instincts, technical abilities, talent and creativity were there, and what was needed was to create the opportunities for them to flourish. I also continue to be surprised by the popularity of public policies that we know cause poverty, corruption, human suffering and inequality. There are ideas that sound good and are surrounded by a

halo of goodwill and solidarity with one's fellow man but which in practice always end up making the poorest segments even poorer. The disdain that certain political leaders show for the lessons experience has taught us never ceases to amaze me. They enact policies as if they were new and different when in fact they are the same ones that have caused so much misery and failure in the past.

What would you like to see in the future?

I'd like to see a large-scale agreement between the United States and Brazil where each country makes proposals that the other country can't reject because of how attractive they are, proposals that deepen their trade and economic integration. A bilateral agreement that is inclusive—in other words, one that any other nation can join, provided it is willing to accept the entry conditions: adopting open policies, creating economic stability, ensuring social protection, and conducting an effective fight against poverty. This would create a situation in which it would be very disadvantageous for any other country in the region not to be a part of this scheme. This type of agreement could very rapidly change the region's social and economic panorama for the better.

How do you see the IDB's role in what has happened and what would you expect from this organization in the next few years?

The IDB has gone through different stages, each of which reflected the changing situation in the region at that time. In the next few years, the Bank will have two big opportunities: one in the financial field and another in the realm of ideas. The financial crisis makes the IDB a more influential player than it was during times of plenty and great monetary liquidity when the region's countries and companies enjoyed easier access to credit and investments. This has now changed, and the IDB will be an important provider of funds to the region. To do so it must increase its capital and enhance the way it mobilizes its resources and its assets. But money without good ideas is dangerous, which is why the other opportunity the Bank has is to become a great producer of good ideas founded on the best available knowledge and experience with economic and social development, combined with a deep understanding of the specific realities of each country. In the next 10 years the IDB may become more important for Latin America than it has been over the last 10.

(Continued from page 107)

light of the globalization of production, advancing the creation of a wide regional base is a top priority. Private companies are dividing and scattering their manufacturing processes throughout national jurisdictions and forming global chains for lowering the costs of production, transactions, and the distribution of goods.

Another issue of great importance is the adjustments that the region must make to ensure that profits from trade reach the masses and contribute to reducing poverty in the future. Other important topics include strong regional homogeneities and, thus, the differing abilities of countries to enter trade flows and their impact on production structures and employment.

One of the ways in which the international community and multilateral organizations have successfully dealt with this issue is through trade-related capacity-building. This involves helping countries create and apply trade policies and negotiate and implement agreements on the subject. It also promotes the development of trade, including furthering exports and financial exchange.

On a broader scale, the initiative includes assistance for activity-related

infrastructures (transportation, communications, and energy) and other supply-side interventions, in the production sector, for instance, that allow a country to benefit from free trade. This assistance also encompasses adjustment programs related to the latter, including social security and employee re-education, as well as the availability of instruments for designing and carrying out complementary production development policies for greater openness and globalization.

Bilateral donors and financial institutions have granted trade assistance in the past, but the topic has been given center stage in the context of the Doha Round. Indeed, discussions in this area are crucial to the nations of Latin America and the Caribbean, as the region is primarily comprised of middle-income countries, many of which no longer have access to concessional financing.

Within this line of thinking, one of the most notable ways to optimize competition is by reducing the costs of trade. Even a one-day lag in supply, whether in supply chains or in production times, generates a 1% tariff increase for the good in question. Cost reductions require better transporta-



Chilean grapes and high-quality fruits and vegetables produced in the region find a ready market with North American consumers, particularly in winter months.

tion networks, transparent customs transactions, an exchange process free of excess paperwork, and the unhindered flow of information as well as fluid cross-border communications—hence the IDB’s focus on efforts aimed at physical integration of the region’s infrastructure.⁴

At the same time, policies within each industry as well as nationwide policies should also be aimed at integration. The high cost of energy, poor transportation infrastructure, an unstable macroeconomic environment and other factors decrease the private sector’s ability to optimize its opportunities for market access. Trade policies should be accompanied by complementary policies that promote the full development of this sector. According to a recent study by the IDB (Mesquita Moreira, Volpe and Blyde, 2008), a reduction of just

10% in Latin American freight charges would increase exports to the US by an average of 39%.

In conclusion, it may be said that trade integration is a profoundly transforming dynamic. It opens the markets of countries to new products and services, opens economies in the face of new economic and regional forces, and opens societies to the inflow of new cultures and influences. It also generates opportunities for trade and growth, although Latin America and the Caribbean may not be prepared to take advantage of some of these opportunities. Thus, the challenge for the region is to improve its preparedness, not only in order to maximize the benefits of the work that has been done in the form of trade agreements, but also in order to take advantage of new market strengths and opportunities offered by the global economy.

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¹ Material extracted from a conversation between Santiago Gutiérrez and the author of these pages, Ricardo Ávila, which took place on 26 November 2008.

² According to the World Tourism Organization, 51% of airplane passengers travel primarily for business purposes.

³ See Chapter 1 of this book.

⁴ See the case of the Mesoamerica Project and the IIRSA initiative (www.iirsa.org). An analytical discussion on the topic of physical integration and the importance of regional initiatives can be found in the works collected in IDB/INTAL (2008).



Waterscape with a warning. La Tomilla water treatment plant has served Arequipa, Peru, since it was rehabilitated at the start of the 1960s. The newly established IDB chose the project as the recipient of its first loan. Over the next 50 years the project would be followed by many other infrastructure operations designed to directly improve people's lives. Behind La Tomilla looms Misti Volcano, one of scores of ice-covered Andean peaks on which Peru depends for water. Today, global warming is threatening these icepacks.

V Sunshine and Shadows in Infrastructure

It was the year 1961, and loan applications were starting to arrive at the recently created Inter-American Development Bank (IDB) from the various countries of Latin America and the Caribbean. Once the requisite evaluations had been carried out, the Board of Executive Directors of the organization decided that the first objective would be to finance the Master Plan for the Potable Water and Sewage System in Arequipa, Peru, for which the sum of US\$3.9 million was approved.

Aside from the success of the project, which turned out to be a model that was imitated in other countries, the example serves to illustrate not only how infrastructure development was a key issue in the early days of the IDB, but that it has been an ongoing challenge for the region's different countries.

It is also clear that the large bottlenecks that existed a half-century ago with respect to drinking water have been largely overcome, at least in the

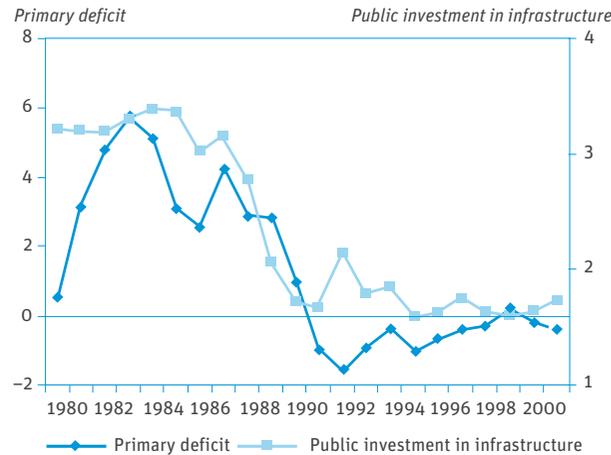
urban areas, where coverage was 91 percent of potential users in 2004 (IDB, 2007a), while at the beginning of the 1960s, coverage was closer to 40 percent.

However, if a broader prism is used, there is still much work to be done in the area, since not only is the regional infrastructure inadequate, but the gap has widened considerably in comparison with other areas of the world. Without ignoring the progress achieved, there are serious deficiencies in sanitation, waste treatment, energy, highways and ports.

Part of the explanation has to do with the periods of crisis that have limited the spending capacity of the region's governments. In this regard, when there have been periods of fiscal limitation, public works have experienced significant financial setbacks that could not be reversed during the boom periods. For example, in the area as a whole, public investment in infrastructure fell from more than 3 percent of GDP in 1988 to approximately 1.6 percent in 1998 (Fay and Morrison, 2007) (Figure 5.1).

Figure 5.1 Primary Deficit and Public Investment in Infrastructure, Latin America, 1980–2000

(Percentage of GDP)



Source: Servén (2005).

Note: Average for Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Mexico and Peru.

With things as they are now, experts believe that future efforts must be greater than in the past. On average, the countries of the region spend less than 2 percent of GDP on infrastructure when they would need between 3 and 6 percent to reach the level or match the rate of other countries that were previously lagging behind, such as China and the Republic of Korea (Fay and Morrison, 2007).

The potential rewards would be significant. Estimates calculated by

César Calderón and Luis Servén (2004) maintain that average economic growth in the region as a whole would increase by 2.6 percent if all the countries were at the same level as the leading Latin American country in this category (Table 5.1). One of the reasons is that both the quality and the quantity of infrastructure are key factors that determine a country's capacity to trade and compete in international markets (IDB, 2004). Also, empirical evidence demonstrates that income distribution tends to improve and poverty tends to decrease if there is adequate infrastructure (Table 5.2).

Much of the region's efforts to compensate for the lack of resources in this area have been focused on opening up to private capital, either through the mechanism of the transfer of ownership or through concessions for using a service over a specific period of time. As a result, in what has turned out to be a worldwide trend, the region's countries have received a large amount of money earmarked for activities that were once the exclusive domain of the public sector.

Thus, private sector investments in transportation, water, energy and telecommunications worldwide rose to US\$754 billion between 1990 and 2001; 48 percent of this money was earmarked

Table 5.1 Potential Increases in Per Capita GDP Growth, Latin America and the Caribbean (Percentages)

Country	Improvement that reaches the levels of the leading country in Latin America and the Caribbean (Costa Rica)			Improvement that reaches the median level for the East Asian Tigers (Republic of Korea)		
	Quantity	Quantity	Total	Quantity	Quantity	Total
Argentina	1.3	0.4	1.7	2.2	0.9	3.2
Bolivia	3.8	0.5	4.3	4.8	1.0	5.8
Brazil	1.5	1.4	2.9	2.4	1.9	4.4
Chile	1.3	0.0	1.3	2.3	0.6	2.8
Colombia	1.9	1.2	3.1	2.9	1.7	4.6
Costa Rica	—	—	—	1.0	0.5	1.5
Dominican Republic	1.3	0.1	1.4	2.3	0.7	2.9
Ecuador	2.0	1.0	3.0	3.0	1.5	4.5
El Salvador	1.6	0.4	2.1	2.6	1.0	3.6
Guatemala	3.3	0.4	3.7	4.2	0.9	5.2
Honduras	3.1	1.1	4.2	4.1	1.6	5.7
Mexico	1.4	0.2	1.7	2.4	0.8	3.2
Nicaragua	3.4	1.4	4.8	4.4	1.9	6.3
Panama	1.4	0.2	1.5	2.4	0.7	3.1
Peru	3.0	0.6	3.5	4.0	1.1	5.0
Uruguay	0.7	0.4	1.1	1.7	0.9	2.6
Venezuela	1.1	0.4	1.4	2.0	0.9	2.9

Source: Calderón and Servén (2004).

Note: Potential increases are due to improvements in the quantity and quality of infrastructure.

Table 5.2 Potential Decreases in Inequality, Latin America and the Caribbean (Gini coefficient)

Country	Improvement that reaches the levels of the leading country in Latin America and the Caribbean (Costa Rica)			Improvement that reaches the median level for the East Asian Tigers (Republic of Korea)		
	Quantity	Quantity	Total	Quantity	Quantity	Total
Argentina	-0.03	-0.01	-0.03	-0.05	-0.02	-0.06
Bolivia	-0.08	-0.01	-0.09	-0.10	-0.02	-0.12
Brazil	-0.03	-0.02	-0.06	-0.05	-0.03	-0.09
Chile	-0.03	0.00	-0.03	-0.05	-0.01	-0.06
Colombia	-0.04	-0.02	-0.06	-0.06	-0.03	-0.09
Costa Rica	—	—	—	-0.02	-0.01	-0.03
Dominican Republic	-0.03	0.00	-0.03	-0.05	-0.01	-0.06
Ecuador	-0.04	-0.02	-0.06	-0.06	-0.03	-0.09
El Salvador	-0.03	-0.01	-0.04	-0.06	-0.02	-0.07
Guatemala	-0.07	-0.01	-0.08	-0.09	-0.02	-0.11
Honduras	-0.07	-0.02	-0.09	-0.09	-0.03	-0.12
Mexico	-0.03	0.00	-0.03	-0.05	-0.01	-0.06
Nicaragua	-0.07	-0.02	-0.10	-0.09	-0.03	-0.13
Panama	-0.03	0.00	-0.03	-0.05	-0.01	-0.10
Peru	-0.06	-0.01	-0.07	-0.08	-0.02	-0.10
Uruguay	-0.02	-0.01	-0.02	-0.04	-0.02	-0.05
Venezuela	-0.02	-0.01	-0.03	-0.04	-0.02	-0.06

Source: Calderón and Servén (2004).

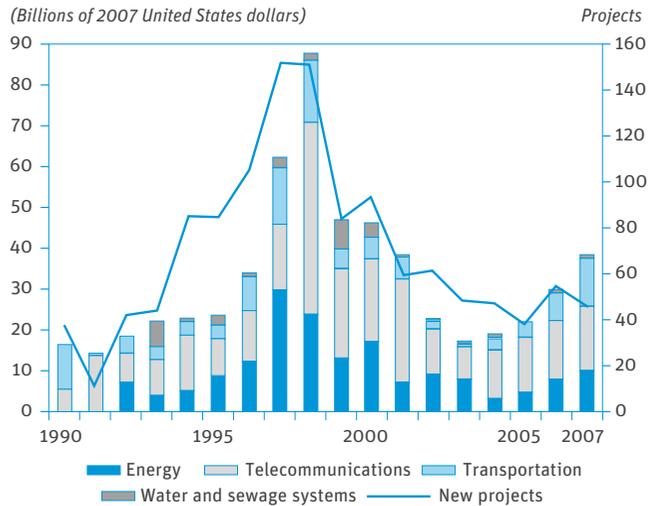
Note: Potential decrease due to improvements in the quantity and quality of infrastructure.

for Latin America and the Caribbean and was related, above all, to the sale of public assets (Guasch, Laffont and Straub, 2005). According to a database of the World Bank,¹ 29 Latin American and Caribbean countries received US\$474.5 billion for infrastructure distributed among 1,243 projects between 1990 and 2007. Of that amount, 47 percent went to telecommunications, 30 percent to energy, 18 percent to transportation, and 5 percent to water.

However, the experience of over two decades leads to disparate conclusions, depending on the specific field and the size of each country (Figures 5.2 and 5.3). In general, the most notable change is in telecommunications. According to the Economic Commission for Latin America and the Caribbean (ECLAC), 99 percent of the sales of companies in this field ranking among the region's 500 largest companies belonged to private companies in 2006 (ECLAC, 2008) as a direct consequence of the boom in mobile phone services and the provision of Internet-related services.

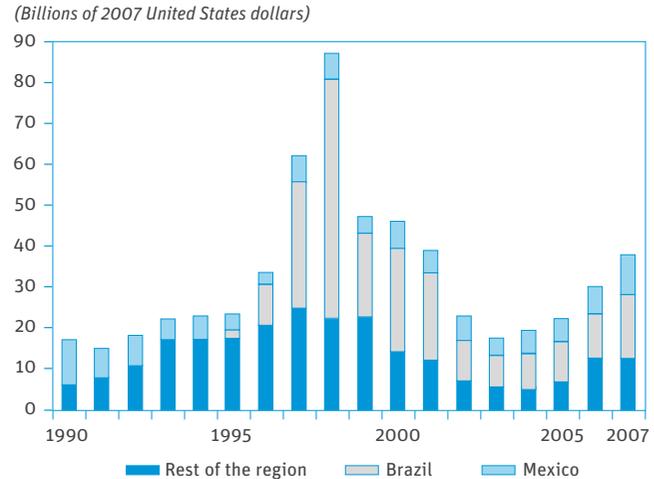
With respect to electricity, the proportion was 47 percent in the same year. Additionally, in the case of water accounts, the proportion reached 11 percent in 2003 (Fay and Morrison,

Figure 5.2 Investment Commitments to Infrastructure Projects with Private Participation in Latin America and the Caribbean by Sector, 1990–2007



Source: World Bank and the Public-Private Infrastructure Advisory Facility (PPIAF), PPI Project Database.
 Note: Dollars adjusted by the 2007 United States Consumer Price Index (CPI).

Figure 5.3 Investment Commitments to Infrastructure Projects with Private Participation, Main Recipients and the Rest of Latin America and the Caribbean, 1990–2007



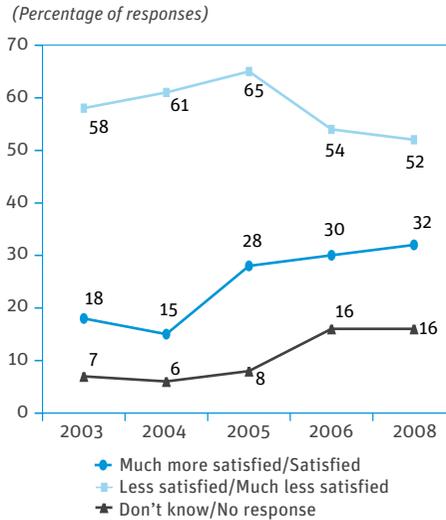
Source: World Bank and the Public-Private Infrastructure Advisory Facility (PPIAF), PPI Project Database.
 Note: Dollars adjusted by the 2007 United States Consumer Price Index (CPI).

2007). The ratio is apparently even lower with respect to highways, although it tends to be higher for airports and seaports as a result of a new wave of interest after 2005 (ECLAC, 2008).

That said, the involvement of the private sector has not been free of difficulties. In an analysis of 307 concessions granted in the water and transportation sectors, it was found that 162 projects

were re-negotiated in an average period of three and a half years after the contract was signed (Guasch, Laffont and Straub, 2005). There were also cases of re-nationalized operations, particularly in the field of water and sanitation. One of the reasons for this was the public's dissatisfaction with rate hikes and differences between the government and operators with respect to setting rates.

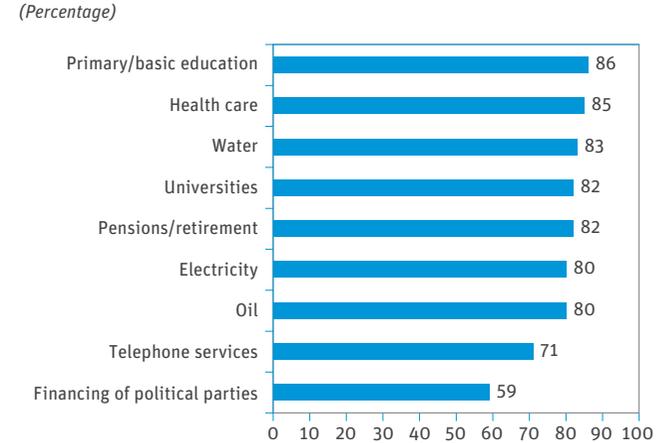
Figure 5.4 Satisfaction with Privatized Public Services, Latin America, 2003–08



Source: Latinobarómetro (2003–08).
 Note: The results in the figure are based on the responses to the following question: “Now that state-owned public services such as water and electricity have been privatized, and taking price and quality into account, are you much more satisfied, more satisfied, less satisfied or much less satisfied with these services today?”

This is probably one of the reasons why average Latin Americans continue to be critical of privatizations, despite the fact that the proportion of persons who say they are much more satisfied with the privatized service they receive rose from 15 percent to 32 percent between 2004 and 2008, while the proportion of those less satisfied decreased

Figure 5.5 Activities That Should Be Mainly in Government Hands, Latin America, 2008



Source: Latinobarómetro (2008).
 Note: The results in the figure are based on responses to the following question: “Of the following list of activities, which do you think should be mainly in government hands and which should be mainly in private hands: health care, oil, primary/basic education, electricity, water, pensions/retirement, telephone services, universities, financing of political parties.” The only response that appears here is “mainly in government hands.”

from 61 percent to 52 percent in the same period, according to Latinobarómetro (Latinobarómetro, 2008) (Figure 5.4). According to the same agency, when analyzing which activities should be in government hands, 83 percent say it should be water, 80 percent believe it should be electricity, and 71 percent say it should be telephone service (Figure 5.5).

(Continued on page 124)

Interview with Roberto Vellutini



Roberto Vellutini, a Brazilian citizen, is the Manager of Infrastructure and Environment at the IDB. For the past 10 years,

he was Head of Operations (Energy and Infrastructure) in the Bank's former Private Sector Department (now the Structured and Corporate Finance Department). The author of numerous articles and with many years of professional experience, he is a graduate of the School of Economics at the University of São Paulo and holds an M.Sc. and a Ph.D. in applied economics from Cornell University (United States).

How would you characterize the region's development with regard to infrastructure over the past half-century?

We've observed two different phases in Latin America with regard to infrastructure: the first one was the public financing era, which lasted for the first 35 years after the founding of the IDB, while the second one has been a period where investment in the public sector coexisted with increased investment in the private sector, with the latter also being active in providing the infrastructure services that were traditionally rendered by governments. Besides telecommunications, the first industry to open itself up to private investment was the electrical power industry. Several countries privatized power generation, followed by various electrical distri-

bution companies. The second area to open up was transportation, with the privatization of ports, airports and railways, and especially with the franchising of toll highways in various countries of the region. However, the water sector has fallen behind and hasn't been able to attract private resources in the same way. This has been due in many cases to a lack of interest on the part of governments, given its significance. Another issue that has gained importance in the context I've mentioned is the adaptation of the legal and regulatory frameworks for different industries for providing both public and private services related to infrastructure. The mitigation of environmental and social factors related to investments in infrastructure has also taken on enormous relevance over the past 20 years, with the goal of ensuring their sustainability.

What do you think has been the IDB's role in these events, and in what ways has it been positive?

The IDB has been a great partner of all the countries of Latin America and the Caribbean in the financing of public infrastructure over the past 50 years. This financing, at times countercyclical and at times complementary, has been accompanied by technical assistance with improving the environmental and social design and management of projects as well as developing the technical and institutional capacities of member countries. On the private side, the Bank's participation was key in supporting the first initiatives that were developing within budding, yet-unproven regulatory frameworks, which gave private investors and private commercial banking confidence in the "bankability" of projects. This has facilitated investments of more than US\$30 billion over the past 15 years.

Where do you see this issue going in the near and distant future, and what should be the role of the Bank?

In the near future, the Bank should strengthen its countercyclical role in order to mitigate the effects of the current financial crisis by financing infrastructure that improves the competitiveness of countries and generates employment and growth. Over the mid-term and long term, it should continue supporting public investment with technical assistance, institutional backing and financing. Also, it should complement this effort with actions aimed at supporting greater private investment in infrastructure. Two important issues for the future, in which the IDB has assumed and continues to assume great relevance and a leading role, are climate change and the water sector. The intent is to support things such as incorporating the effects of climate change in the design of relevant

projects as well as investment programs for preventing natural disasters. For the water sector, where the basic problem is the future scarcity of the resource, the Water and Sanitation Initiative was created for supporting things such as efficient water use as well as greater coverage and quality.

(Continued from page 121)

WATER AND BASIC SANITATION

Throughout the last half-century, the region experienced significant advances with respect to access to drinking water and sanitation services.

Table 5.3 Population with Access to an Improved Source of Water, Latin America and the Caribbean, 1990 and 2006
(Percentage)

Country	1990			2006		
	Urban areas	Rural areas	Total	Urban areas	Rural areas	Total
Argentina	97	72	94	98	80	96
Belize	100	n.d.	n.d.	100	n.d.	n.d.
Bolivia	91	49	72	96	69	86
Brazil	93	54	83	97	58	91
Chile	99	49	91	98	72	95
Colombia	98	68	89	99	77	93
Costa Rica	n.d.	88	n.d.	99	96	98
Cuba	95	n.d.	n.d.	95	78	91
Dominican Republic	97	66	84	98	91	95
Ecuador	82	61	73	98	91	95
El Salvador	90	48	69	94	68	84
Guatemala	89	72	79	99	94	96
Guyana	n.d.	n.d.	n.d.	98	91	93
Haiti	62	48	52	70	51	58
Honduras	91	60	72	95	74	84
Jamaica	98	86	92	97	88	93
Mexico	94	72	88	98	85	95
Nicaragua	91	46	70	90	63	79
Panama	100	n.d.	n.d.	96	81	92
Paraguay	78	28	52	94	52	77
Peru	88	46	75	92	63	84
Suriname	99	n.d.	n.d.	97	79	92
Trinidad and Tobago	92	88	88	97	93	94
Uruguay	100	100	100	100	100	100
Venezuela	93	70	89	n.d.	n.d.	n.d.
Latin America and the Caribbean	94	61	84	97	73	92

Source: Joint Monitoring Program (JMP) for Water Supply and Sanitation, WHO and UNICEF (2008).
Note: n.d. = no data available.

At the beginning of the 1960s, the level of coverage was very limited. Of an urban population estimated at 100 million, only about 40 million had household drinking water connections, while around 30 million had access to a sewage system that included waste treatment only in very few cases. The situation was worse in rural areas, where only 6 percent of the population had access to drinking water, while sanitation was practically nonexistent, with the exception of the construction of some rudimentary latrines.

Although universal provision of these services with adequate levels of quality, continuity and sustainability is still a long way off, the region has experienced significant improvements in this area. In urban locations, 97 percent of the population now has household drinking water connections, while 86 percent are connected to a sanitation network. In rural areas, 73 percent are connected to the water system and 52 percent are connected to a sanitation network out of a total of 126 million inhabitants (Tables 5.3 and 5.4). The main problem continues to be the scarcity of sewage treatment, which covers only 15 percent of such networks (IDB, 2007a).

For the first 20 years of the IDB's existence, a large part of the financing provided by the governments themselves, the Bank and other multilateral institutions was allocated to infrastruc-

ture projects aimed at developing and/or expanding water systems, mainly in the large urban agglomerations of the region. Beginning in the 1980s, a progressively greater emphasis was placed on improving the efficiency and effectiveness of these investments by incorporating cost-benefit analyses and other planning tools. In this decade planners also began giving greater importance to the financing of sanitation and sewage treatment works in order to reduce the levels of pollution generated by household waste.

At the beginning of the 1990s, however, it began to be recognized that financing infrastructure projects exclusively was not solving the region's water and sanitation problems and that in many cases, not addressing the institutional issues exacerbated the problems. Thus, institutional actions and variables began to be emphasized, such as the definition of the roles of planning, regulation and the provision of services, the introduction of standards and regulatory bodies, and the promotion of better business management among operators.

During this decade, the private sector's involvement in the provision of water and sanitation services

Table 5.4 Population with Access to Sanitation Services, Latin America and the Caribbean, 1990 and 2006
(Percentage)

Country	1990			2006		
	Urban areas	Rural areas	Total	Urban areas	Rural areas	Total
Argentina	86	45	81	92	83	91
Belize	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.
Bolivia	47	15	33	54	22	43
Brazil	82	37	71	84	37	77
Chile	91	48	84	97	74	94
Colombia	81	39	68	85	58	78
Costa Rica	96	92	94	96	95	96
Cuba	99	95	98	99	95	98
Dominican Republic	77	57	68	81	74	79
Ecuador	88	50	71	91	72	84
El Salvador	88	59	73	90	80	86
Guatemala	87	58	70	90	79	84
Guyana	n.d.	n.d.	n.d.	85	80	81
Haiti	49	20	29	29	12	19
Honduras	68	29	45	78	55	66
Jamaica	82	83	75	83	84	83
Mexico	74	8	56	91	48	81
Nicaragua	59	23	42	57	34	48
Panama	n.d.	n.d.	n.d.	78	63	74
Paraguay	88	34	60	89	42	70
Peru	73	15	55	85	36	72
Suriname	90	n.d.	n.d.	89	60	82
Trinidad and Tobago	93	93	93	92	92	92
Uruguay	100	99	100	100	99	100
Venezuela	n.d.	n.d.	n.d.	90	47	83
Latin America and the Caribbean	81	35	68	86	52	79

Source: Joint Monitoring Program (JMP) for Water Supply and Sanitation, WHO and UNICEF (2008).

Note: n.d. = no data available.

began to be encouraged through such modalities as concession and management agreements. The vast majority of companies that came to the region were large international operators with recognized experience in the field. However, this change did not bring the expected results. Shortly thereafter, a large number of these international operators began to leave and most services were re-nationalized.

Throughout this period, several countries also began implementing policies for the decentralization of their water and sanitation services, dismantling national organizations and transferring new responsibilities to regional, provincial or municipal levels. In many cases, however, the decentralization of responsibilities was not accompanied by the corresponding transfer of skills, so many municipal governments have not yet managed to develop the institutional, technical and financial strengths necessary to face and resolve the challenges imposed by the sector (IDB, 2007a).

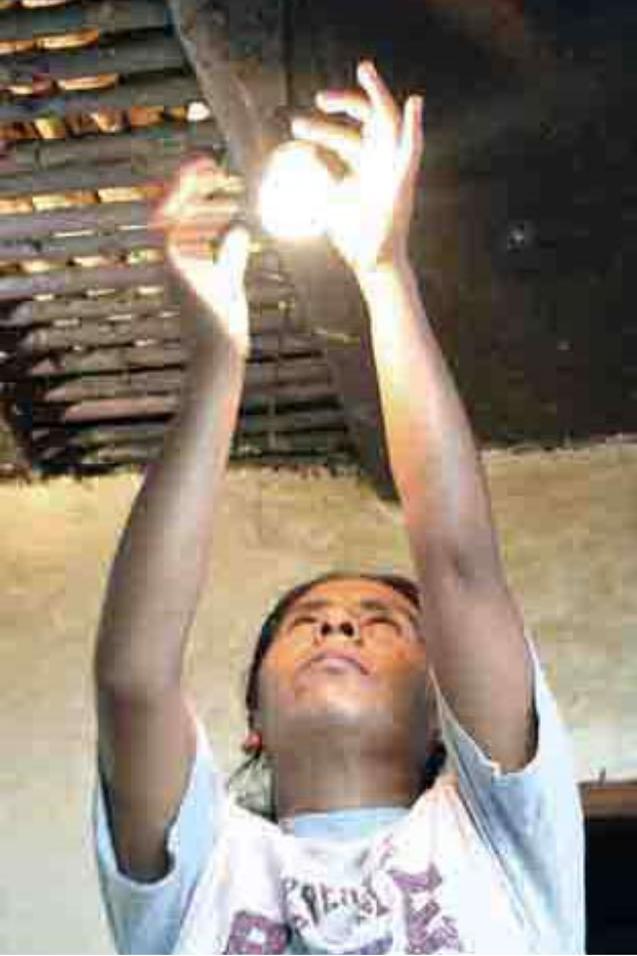
In this context, water and sanitation continue to be the most important items on the social, sanitation and productive agenda of the region's countries. This is evidenced in the

commitment made by the region's leaders in the Millennium Declaration (United Nations General Assembly, 2000), which includes the goal of halving the number of people without access to drinking water and sanitation by 2015.

The region's countries are on track to meet this goal. However, investments of around US\$30 billion will still be required up to 2015, without including sewage treatment. If the objective were to achieve universal coverage, the amount of investment required would be US\$50 billion, a figure that would rise to US\$75 billion if sewage treatment were included (IDB, 2007a).

Consequently, it is clear that increasing coverage levels requires a huge amount of resources which must be correctly evaluated for efficiency and effectiveness of use. In the case of rural areas, experience suggests that in order for the provision of water and sanitation services to be sustainable, it must be based on active community involvement in areas including project design, construction, and subsequent operation and maintenance.

Involving the private sector in financing and managing these ser-



A low-income rural family receives the precious gift of electricity thanks to a large-scale distribution system that links consumers with distant generation facilities.

vices is still an option, but it must be meticulously analyzed on a case-by-case basis. Beyond the trial model, no one can dispute that in order to avoid needlessly wasting resources, it is essential to improve efficiency in the administration of services.

It is imperative that recovery of costs through the payment of tariffs also improve, keeping in mind the needs of low-income families by developing properly designed and focused cross-subsidies. Lastly, continued political support for improvements in water and sanitation is a necessary condition for the achievement of long-term objectives. An attempt must be made to align this aspect with incentives governing service providers and with social issues. There is no doubt that room for action in the area is still quite broad.²

TRANSPORTATION CHALLENGES

If there is an area of infrastructure in which Latin America and the Caribbean have lagged behind with respect to the rest of the world, it is transportation. Slow development in this area has become more and more evident as the region has significantly

increased its interaction with the rest of the world. In addition to the international situation, an IDB study found that an improvement in logistics and a decrease in transportation costs would allow the region's different countries to be more competitive and increase their exports to other markets (IDB, 2007b).

Despite recent efforts, Latin American countries have not been able to close the gap that widened during the so-called "lost decade," when high levels of public debt, structural adjustments and fiscal inequalities led to a sharp decrease in investment in this area (IDB, 2002). Although the process of building stronger ties to private capital began immediately thereafter, the results have been varied.

While it is true that a good part of the region's largest airports and sea-port or river port operations are managed by private companies, which has cleared up some of the bottlenecks, and roadway concessions have been attempted with varying degrees of success, it is also true that Latin America continues to lag behind with respect to logistics. While the costs of this activity have been decreasing in the rest of the world since 1980, they have been

Table 5.5 Road Density, Latin America and the Caribbean, China and Mid-Income Countries

	km/1,000 km ²	km per 10,000 workers
<i>Total highways</i>		
Latin America and the Caribbean	148	110
China	177	22
Mid-income countries	180	180
<i>Paved highways</i>		
Latin America and the Caribbean	36	30
China	41	5
Mid-income countries	82	50

Source: Calderón and Servén (2004).

Note: Data are for the last year available (2000 or 2001). Per capita GDP in international PPP dollars corresponding to the time the chart was produced (2004) was US\$5,495 in China, US\$6,560 in medium-income countries and US\$7,920 in Latin America and the Caribbean. In current dollars, the difference is even more pronounced: US\$1,272 in China, US\$2,453 in medium-income countries and US\$4,013 in Latin American and the Caribbean.

increasing for Latin America and the Caribbean. Not only do export processes take up to five times as long as in developed countries, but the costs of transportation can represent between 10 and 20 percent of the total value of imported goods.

Thus, other areas of the world are clearly moving faster. In 1985, Latin America and the Caribbean had more highways than East Asia and more than the average mid-income country, but later that situation reversed. In 2001, normalized road density (paved highways and the total network),

taking the size of each country into consideration, had hardly grown, while road density in the Republic of Korea and mid-income countries had increased, thus causing this infrastructure variable to be much lower in Latin America and the Caribbean than in mid-income countries and China (Fay and Morrison, 2007) (Table 5.5).

The quality of the region's highways is generally deficient (Table 5.6). At the turn of the century, less than one-third of national road networks were in good condition in most of the countries for which data are available. The percentages of paved surfaces are also low: from 2000 to 2005, 24.3 percent of highways were paved compared to 44 percent in mid-income countries and 76.8 percent in the Republic of Korea (Fay and Morrison, 2007) (Table 5.7).

Factors such as these explain why the cost of logistics is a topic that crops up repeatedly in business surveys carried out in the region, and also explain why Latin American countries rank so low in the relevant ratings calculated by the World Economic Forum (IDB, 2007b). However, over the past few years there has been a notable fiscal effort reflected in government

Table 5.6 Highway Quality in Latin America and the Caribbean

Country	Total length of highway network (km)	National highways (percentage of total)	National highways in good condition (percentage)	Regional highways (percentage of total)	Regional highways in good condition (percentage)
Argentina	630,000	6.0	80	30	78
Brazil	1,611,000	4.5	24	14	n.d.
Colombia	166,233	10	29	40	n.d.
Ecuador	43,200	20	26	26	10
Guatemala	26,000	15	75	12	45
Haiti	3,400	20	16	44	4.0
Mexico	302,000	16	23	27	n.d.
Nicaragua	18,950	9.2	24	3.4	26
Peru	78,200	22	23	18	15

Source: World Bank.
 Note: Based on government evaluations.
 n.d. = no data available.

plans aimed at the development of road infrastructure which have gained currency as an anti-cyclical strategy to counteract the low rate of growth of the world economy as of 2008.

Also evident is the greater interest of private investors after available funds had decreased at the beginning of the decade. One of the reasons was that the first wave of route concessions generated a large volume of re-negotiation, making it necessary to develop new parameters to protect governments and investors. At the same time, reduced perceptions of risk lowered the internal rates of return on specific projects, making the system

Table 5.7 Paved Highways, Latin America and the Caribbean, 2000–05*(Percentage)*

Country	Percentage of paved highways
Argentina	30
Bolivia	7
Brazil	5.5
Chile	20.2
Colombia	n.d.
Costa Rica	24.4
Cuba	49
Dominican Republic	49.4
Ecuador	15
El Salvador	19.8
Guatemala	34.5
Haiti	24.3
Honduras	20.4
Jamaica	73.9
Mexico	37
Nicaragua	11.4
Panama	34.6
Paraguay	50.8
Peru	14.4
Trinidad and Tobago	51.1
Uruguay	10
Venezuela	33.6
Latin America and the Caribbean	24.3
Mid-income countries	44
Republic of Korea	76.8

Source: *World Development Indicators*, World Bank (2008).
 Note: n.d. = no data available.

less onerous for users and improving the viability of the initiatives. Whatever the reason, it is true that, according

(Continued on page 131)

Box 5.1 The IDB's role with regard to infrastructure

Since its creation, the Inter-American Development Bank has been very actively involved in the issue of infrastructure. As such, it has financed more than 700 projects and activities (including technical partnerships) in the area of water and sanitation, with an average US\$385 million invested per year and a total investment of nearly US\$17 billion.

A typical example of investment in this sector is the city of Medellín, Colombia. In the early 1990s, the Medellín River had a high concentration of wastewater and industrial contamination. To address these conditions, Empresas Públicas de Medellín (EPM; Public Utilities of Medellín), with the IDB's technical and financial backing, began working on projects with an estimated cost of US\$232 million, of which US\$130 million would come from a Bank loan and the remaining US\$102 million from local compensatory funds. The overall goal was to clean up the Medellín River and its tributaries, thus improving the quality of life in a metropolitan area that is home to more than three million people.

The results of these projects, which were begun in 1993 and concluded in 2000, included (i) construction of a plant that currently treats 23 percent of all waste water; (ii) construction of nearly 270 kilometers of waste water collector and interceptor sewers and 11,000 new connections to the sanitary drainage system; (iii) establishment of nearly 80 kilometers of aqueduct networks and nearly 26,000 household connections; (iv) purchase and installation of nearly 160,000 meters and an equal number of replacements in the field to reduce unaccounted-for water (UFW). Thanks to the joint efforts of the Bank and EPM, the quality of life of the city's more than three million inhabitants has significantly improved.

Moreover, over the past 50 years, the Bank has led in the development of the region's transportation sector. From 1961 to date, the IDB has approved a total of US\$17.819 billion in loans aimed at this sector, representing approximately 37 percent of all funds disbursed for infrastructure projects and 12 percent of all loans granted by the Bank.

One notable example is that of Curitiba, capital of the state of Paraná in southern Brazil, where nearly 1.8 million people reside and 3.3 million more from the outskirts move about the city on a daily basis. There are 1.6 million automobiles in the metropolitan area. However, more than 70 percent of the population chooses public transportation. In 1970, when most cities were concerned with implementing monocentric urban development models, Curitiba instituted a new model of linear expansion,

with priority given to public transport. Under this model, an integrated network was designed in which articulated buses travel in dedicated lanes along the city's main thoroughfares.

These buses, which have a capacity of 270 passengers each, travel over 72 kilometers of dedicated lanes to meet the demand. A decade later, a system of physical and fare integration was established that allowed the use of trunk and feeder roads in return for payment of a single fare. In 1995, the Bank joined in the support for this revolutionary mobility system, approving a loan aimed at developing specialized roadway infrastructure, building integrated terminals and implementing information support systems. In 2004, it approved a second loan for expanding the system to other areas of the city and improving service levels.

The IDB also played a relevant role in the development of the electrical power sector. The energy sector is the top category in the Bank's project portfolio at US\$22 billion, corresponding to 14 percent of the total volume of approved resources since its creation. Of this total, 90 percent was directed at projects in the electrical power industry, primarily the construction of hydroelectric plants and rural electrification, with 40 percent and 25 percent of total resources, respectively.

The Sistema de Interconexión Eléctrica de los Países de América Central (SIEPAC; Central American Electrical Interconnection System Project) is characteristic of the IDB's support for electrical integration in Central America. It is financing not only the construction of an 1,800 km, 230 kW transmission system, but also the creation of the Mercado Eléctrico Regional (MER; Regional Electricity Market), which, despite the regulatory differences among its six member countries, is succeeding in establishing a seventh supra-national market with one regional regulator and one regional operator, the Comisión Regional de Interconexión Eléctrica (CRIE; Regional Electric Interconnection Commission) and the Ente Operador Regional (EOR; Regional Operating Body).

Likewise, the IDB's most relevant operations in the area of biofuels have been the financing of three ethanol distilleries in the states of Minas Gerais and Goiás in Brazil which was approved in July of 2008 for a total of US\$269 million. Together, these three plants will require a total investment of approximately US\$1 billion and will be capable of producing 110 million gallons of ethanol per year and selling an amount of electricity to the grid that will be equivalent to the demand of 400,000 typical middle-class Brazilian households.

The IDB contributes to economic and social development in its member countries through loans and technical cooperation in the financing of projects that increase the availability and reliability of electrical power.



Toll-paying motorists increasingly become part of the financing mix in highway construction to ease urban congestion. In many cases, the toll roads are operated by private firms. (photo credit *El Tiempo*)

(Continued from page 129)

to the World Bank, private investment in transportation reached US\$12.052 billion in Latin America in 2007, almost double the figure reported the previous year and the largest amount in the region's history (Table 5.8).

UPS AND DOWNS IN ELECTRICITY

Around the middle of the last century, electricity service in the region was still being provided by private companies that concentrated their activity in

Table 5.8 Project Investment by Sector, 1990–2007
(Millions of dollars)

Year of investment	Energy	Telecommunications	Transportation	Water and sanitation	Total investment
1990	440	3,463	6,691	0	10,594
1991	0	9,101	610	75	9,785
1992	5,140	4,458	2,777	0	12,375
1993	2,857	6,141	2,252	4,071	15,321
1994	4,076	9,261	2,434	525	16,296
1995	6,457	6,528	2,786	1,293	17,064
1996	9,532	9,448	6,294	192	25,467
1997	22,912	12,690	10,767	1,933	48,302
1998	18,816	37,060	11,653	1,276	68,805
1999	10,611	17,832	3,558	6,011	38,011
2000	14,382	16,597	4,533	2,845	38,357
2001	6,265	21,861	4,019	1,165	33,309
2002	8,022	9,570	1,712	604	19,907
2003	7,146	6,951	940	296	15,333
2004	3,269	10,651	2,469	1,133	17,521
2005	4,524	12,615	3,286	190	20,616
2006	7,581	14,337	6,549	713	29,180
2007	10,078	15,613	12,052	539	38,282
Total	142,109	224,176	85,379	22,860	474,525

Source: Private Participation in Infrastructure Projects Database, World Bank (2008).



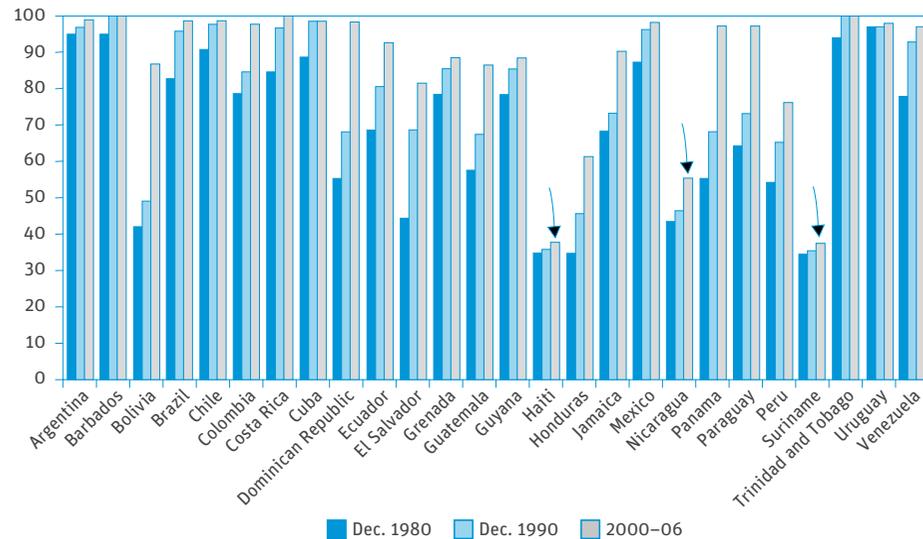
A ribbon of asphalt ensures all-weather transport between agricultural producers and consumption and export centers in an IDB-financed project in Argentina.

the most populated urban centers and had little interest in expanding their services to distant areas. In order to handle the deficiencies arising from the lack of investment in economic development, practically all the region's governments took on a business function through the nationalization of services. Thus, ambitious expansion plans were implemented with the support of

multilateral banking, and electricity coverage was expanded significantly.

This indicator changed favorably over time, reaching 42 percent coverage in 1971 and 70 percent in 1989; and today, on average, almost 90 percent of the Latin American population has access to electricity. Although some countries have achieved coverage of over 99 percent, great disparities

Figure 5.6 Progress in Electricity Coverage, Latin America and the Caribbean, by Decades
(Percentage)



Source: Millán (2006).

Note: The arrows indicate the Latin American countries with the least coverage of service.

persist among nations (Figure 5.6). It is estimated that more than 50 million inhabitants in the region still do not have access to electricity.

Installed generating capacity has been closely related to the increase in coverage. This growth has been moderated by the interconnection of the different systems in the region's countries, a process that began after the 1970s. Initially, the systems were isolated, and significant levels of reserves were required in order to provide adequate service reliability.

Almost at the same time, there was a significant increase in installed capacity thanks to the construction of large hydroelectric power stations that reduced the region's dependence on thermal power. While hydroelectric stations proliferated, for example, in South America at a rate of 5.5 percent per year between 1980 and 1995, the establishment of thermoelectric stations grew by only 2.2 percent.

Later on, however, when the private sector's involvement increased, the opposite occurred, in part due to climatic phenomena that intensified changes in the volume of water sources. Thus, between 1995 and 2006, the installation of thermoelectric stations

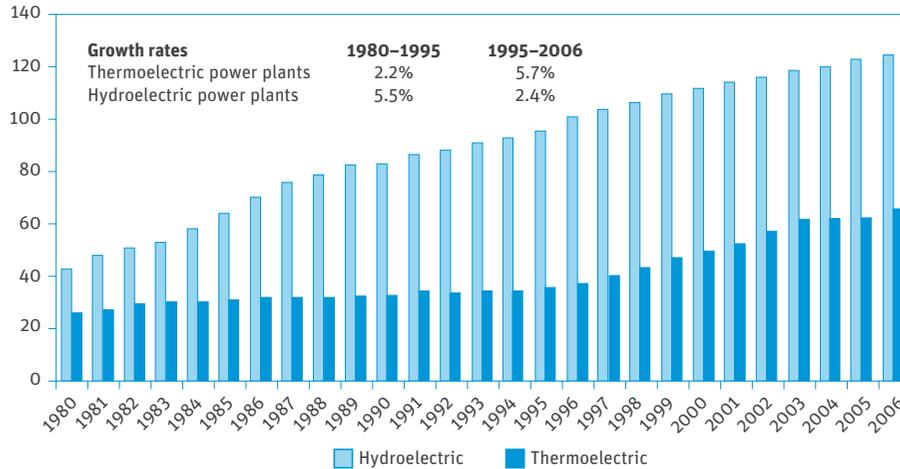
grew by 5.7 percent per year in the above-mentioned area, while hydroelectric station installations grew by 2.4 percent (Figure 5.7). Nevertheless, most of the region's countries depend significantly on hydroelectric power, with levels reaching as much as 85 percent in some cases.

Other technologies, especially renewable technologies (excluding hydroelectricity), were introduced in the last decade as substitutes for fossil fuels. Their share of the region's energy matrix is, in general, very limited, although it is expected to increase considerably over the next few years. Notably, power generation from geothermal sources, wind and sugar cane bagasse achieved a share of 12.6 percent in Central America in 2007.

This dynamic has been accompanied by the private sector's growing involvement in the provision of services. Some say that Latin America has been the leader worldwide with respect to tariff system and regulatory reforms and in opening up to competition (IDB, 2001), which has attracted a considerable volume of resources. According to the World Bank, between 1990 and 2007 US\$142.109 billion was invested in these activities, distributed among

Figure 5.7 Progress in Installed Capacity, South America, 1980–2006

(Gigawatts)



Source: Millán (2006).

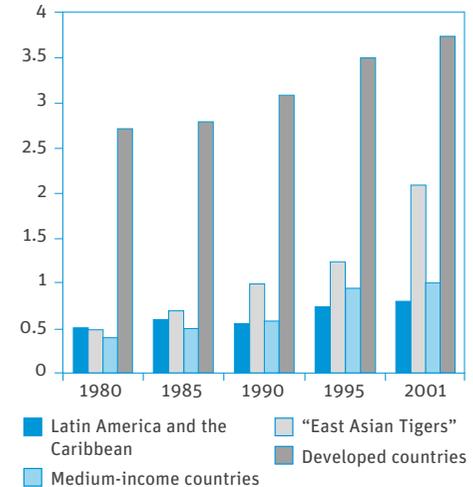
498 projects. Of this number, 10 were concessions, 174 were privatizations, 311 were new projects and 3 were leasing and administration contracts.³

An assessment of these efforts indicates that increased generating capacity had a big impact and that phenomena such as blackouts decreased, thereby increasing the reliability of service, although a considerable proportion of the region’s countries still operate under a public monopoly scheme and continue to suffer from the same

problems as before. Transmission losses have decreased, as well as tariffs, particularly for the largest buyers of electricity (IDB, 2001). However, the gap compared to other regions of the world such as Asia and the Pacific has continued to grow since 1980, when electricity generating capacity per

Figure 5.8 Electricity Generating Capacity by Region and Level of Development, 1980–2001

(Megawatts/1,000 workers)



Source: Calderón and Servén (2003).

Note: The sample includes 19 Latin American countries, the seven “East Asian Tigers” (Indonesia, Malaysia, Hong Kong SAR, Republic of China (Taiwan), Republic of Korea, Singapore and Thailand), 64 medium-income countries and 21 developed economies.

1,000 workers was practically the same in both areas (Figure 5.8).

In addition, regional integration has gone through several stages, beginning with inter-system links based on bi-national stations, especially in the Southern Cone in the 1970s. Years later, the Andean countries unified their transmission systems simultaneously in order to provide backup support to one another in the event of emergencies and to bolster reliability. Regional institutions and infrastructures were also created in Central America in order to form integrated markets.

A look at what has happened over the last few decades shows that the series of reforms that took place in the region's electricity sector led to alternating between nationalization and privatization. Moreover, the process highlighted the weak regulatory capacity of the region's governments, which in some cases led to the re-establishment or creation of new energy ministries, secretariats, commissions or national councils (Millán, 2006).

In a different field, environmental and social issues that did not receive much attention initially began gaining

importance, driven also by multilateral banking. Involvement of local communities, particularly those directly affected by the projects, began taking priority in the decision-making process. Environmental standards and regulations have been developing gradually in order to harmonize development objectives with the preservation of the environment and the customs and traditions of different populations, especially indigenous peoples.

These elements are key if one keeps in mind that according to the International Energy Agency (IEA), world consumption will increase by 56 percent in comparison to current levels by 2030, and Latin America and the Caribbean will not be an exception to that rule. Coping with greater demand, together with the need for alternative energy sources, will continue to be a priority. Given this scenario, one must keep in mind the IDB's estimate that the region could reduce its electricity consumption by 10 percent by the year 2018 through implementing regulatory policies and measures in a cost-efficient manner, which would be the same as saying that one-third of the expected expansion to meet demand could be paid for through energy savings.

(Continued on page 138)

Interview with Alberto Alemán Zubieta



Engineer Alberto Alemán Zubieta is the CEO of the Panama Canal Authority, the autonomous agency in charge of a key project for

regional and global trade and integration. With many years of experience as the head of this interoceanic waterway, Alemán is also overseeing expansion work on the Canal that will allow the route's cargo transport capacity to be doubled to up to 600 million tons per year by the middle of the next decade.

How would you describe what has been going on in trade in the Western Hemisphere over the past half-century?

I think what made this period unique was the integration taking place among different blocs at the regional and global levels. The various agreements that were signed allowed for increased trading and improved efficiency in marketing and distribution channels. We're also seeing far-reaching innovations in the way trade moves, as shown by the increasing use of containers for moving cargo. All of this has been accompanied by changes in the economic policies of Latin American and Caribbean countries as part of the growing process of globalization we're experiencing.

In what way have these changes been felt in the Panama Canal?

The Panama Canal is a bellwether of global trade that has registered not

only the changes in technology but also the emergence of China as an exporting and importing powerhouse. Both factors have required us to shift gears and find new ways of doing things. In our case, we've been feeling the effects since the mid-1980s. Also, in the last decade we've noted an increase in the demand for raw materials from the region.

Are you seeing global trade grow despite the worldwide crisis?

Throughout the history of the Canal, which began operating in 1914, we've seen slumps that, from a long-term perspective, seem manageable. The current expectation is that 2009 will be a very hard year that will require adjustments in every industry and segment, and we've been preparing for it. But further down the road growth will return, and it will bring with it greater volumes in commercial trade and cargo movement.

What does the Canal expansion involve?

It involves eliminating the restrictions we currently have on the global maritime industry. The maximum ship size we can accept is the well-known Panamax, which has a series of limitations. Meanwhile, there are cases of vessels that move, say, 12,000 containers or up to 150,000 tons or more of bulk cargo, depending on the type of craft. In our case, our limits are 4,500 containers and 60,000 tons, respectively. Our intention is, therefore, to break this bottleneck in the most important link between the two largest oceans. This will redefine the way cargo moves in this part of the world while providing great advantages to users by adding value to the client, to the economies that make use of this route and to neighboring locations, in addition to changing trade patterns in the region. In short, it's about being more efficient and developing economies of scale.

It's the most ambitious infrastructure project of the early 21st century.

In the region, definitely. The cost of expanding the Panama Canal is estimated at US\$5.25 billion and the project should be ready in 2014. This includes maintaining the current locks plus the ones to be developed. Also, the impact that this project will have on our country and on the region will be immense. In fact, we're already seeing ports and countries preparing themselves to adapt their facilities to the new realities and to offer complementary services that will generate a great deal of wealth and create jobs. Therefore, the investment involved will actually be much higher than what I've mentioned, but the benefits will be even greater.

In this entire equation, how would you characterize the role and challenges of the IDB?

I think the Bank is a mainstay in the region's development. In our case, the IDB played a leadership role because it understood the benefits of this project not only for Panama but for all the countries of the region. The future challenge will be to continue supporting the infrastructure while aiming at continuous and comprehensive development to make the project sustainable over the long term. Lastly, it's about obtaining a better quality of life for all the inhabitants of Latin America and the Caribbean.

(Continued from page 135)

BIOENERGY: A NEW DIRECTION

The region's experiences in the area of biofuels deserve special mention. Although this issue has lost a little of its strategic importance following the decrease in the price of oil after the peaks experienced in mid-2008, the progress that has been made is important and should regain visibility over the next few years. In particular, Brazil's experience with ethanol and the fact that sugarcane is cultivated in practically all Latin American and Caribbean countries sparked the region's interest in exploring this alternative for local consumption and/or for export (Rothkopf, 2007). In addition, there have been encouraging results with respect to biodiesel produced from raw materials such as palm oil.

In the mid-term, there is no doubt that when produced in a sustainable way, biofuels can offer, in addition to an affordable alternative to gasoline and diesel, a significant reduction in greenhouse gas emissions. The production of sustainable biofuels also creates jobs, reduces poverty, improves the quality of life in rural areas, and provides interesting opportunities in the area of co-generation. Although the

rise in food prices due to the diversion of agricultural supply gives cause for concern, the analysis depends on the raw material and the type of biofuel produced. Therefore, it is expected that regional strengths in this area will regain the world's attention once there is a return to world economic growth and a renewed demand for fossil fuels.

ADVANCES IN TELECOMMUNICATIONS

"Together with capital and labor, information has become a crucial part of production," states an IDB study carried out at the beginning of the decade (IDB, 2001). This paper also emphasizes how the emergence of new technologies had allowed the region to close the gap somewhat with developed countries in the field of telephone service, although the proportion was still five times greater for developed countries.

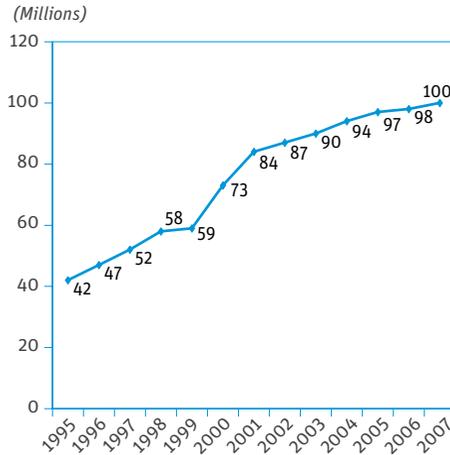
Six years later, the change was even more dramatic. According to the International Telecommunication Union (ITU), while the number of land lines in Latin America and the Caribbean rose from 87 to 100 million between 2002 and 2007 (Figure 5.9), cellular telephone subscribers increased from

Private investments in transportation in Latin America totaled over US\$12 billion in 2007, nearly double the previous year's figure and the highest in the region's history.
(photo credit *El Tiempo*)



Private companies administer a large portion of the region's airports and ocean and river ports, helping to reduce transportation bottlenecks.
(photo credit *El Tiempo*)

Figure 5.9 Land Line Telephones, Latin America and the Caribbean, 1995–2007

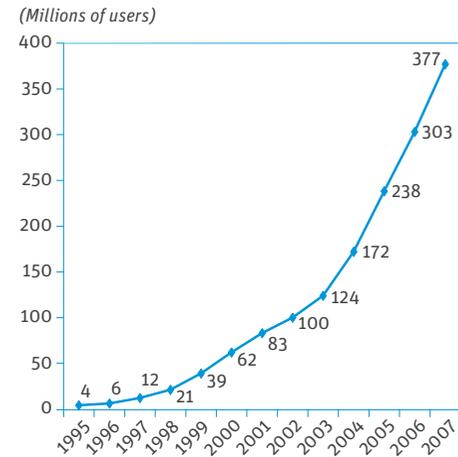


Source: Author's calculations based on the ICT Statistics Database of the International Telecommunication Union.

100 to 377 million compared to 1995, when they amounted to less than 4 million (Figure 5.10).⁴ As a result, overall density was about 82 percent in 2007 in comparison to 27 percent at the beginning of the decade. These figures keep changing continuously as the penetration of the service increases and the population pyramid changes.

Although what has happened in the region is part of a worldwide trend, since ITU estimates that there were 4

Figure 5.10 Mobile Cellular Telephone Subscribers, Latin America and the Caribbean, 1995–2007



Source: Author's calculations based on the ICT Statistics Database of the International Telecommunication Union.

billion active cellular telephone lines worldwide at the end of 2008, growth in Latin America is significant, with about 440 million lines in the region projected for that same year. As a consequence, and to cite one case in particular, the coverage gap compared to Europe has been reduced to less than two to one.

This technological change allowed one of the area's major infrastructure bottlenecks to be broken quickly. Part



An IDB-financed program to modernize power generation and distribution in The Bahamas has helped the Bahamas Electricity Corporation improve service while lowering costs.

of what happened had to do with the sale of public assets at the beginning of the 1990s, but no less important was the granting of licenses for new private operators to enter the different countries. As a result, the volume of investments has been considerable, rising to US\$224.176 billion between 1990 and 2007, distributed over 144 different projects.

Also of interest are developments related to Internet access. According to the ITU, the number of connections rose from 10 million to almost 24 million between 2002 and 2007, while the number of users increased from 48 to 147 million during the same period. Broadband connections increased eightfold in the same period, although the regional penetration index was 3.4 for every 100 inhabitants, significantly below the world average of 5.9. In light of these circumstances, companies such as IDC⁵ estimate that almost one-third of the region's households will have high-speed access to the World Wide Web by 2012.

In addition, given the high penetration of mobile telephone service, the expectation is that high-speed wireless connections through cell phones will prevail over cable. Possibilities such as

this will allow obstacles in connecting the region's most remote locations to be overcome, as long as there is coverage for this service.

Faced with the speed of these changes and the fact that a substantial part of the decisions to be made are in the hands of the private sector, government regulatory bodies have been pressed to set license prices and connectivity rates between operators, as well as defend the rights of consumers. However, in general, it has been possible to preserve an atmosphere of competition, resulting in better rates, more equipment and service options and, therefore, greater penetration.

That factor has allowed the most distant populations to break out of their isolation and enabled millions of people to be integrated into productive streams, and has enhanced the region's possibilities with respect to the outsourcing of voice and data services.

FINAL CONSIDERATIONS

The relative success of Latin America and the Caribbean with respect to progress in the telecommunications sector over the last few years should not, however, obscure the fact that

the region is greatly behind in infrastructure development. As noted by Marianne Fay and Mary Morrison, “approximately 2.5 percent of GDP (regional, annually over 10 years) would be sufficient to meet the projected growth in demand, maintain existing infrastructure and achieve universal coverage in water supply, sanitation and electricity.” But if one wants to take it further, “much more would be needed, approximately between 4 and 6 percent of GDP, in order for Latin America and the Caribbean to achieve, in 20 years, the same level of coverage as South Korea or simply to keep pace with China” (Fay and Morrison, 2007).

However, it is not just a question of spending more, but of spending more wisely. There are still deficiencies with respect to regulation or rate-setting that make it necessary to grant considerable subsidies to segments of the population that do not neces-

sarily need them. This lack of clarity hampers the inflow of private capital and raises the cost of the concessions granted, which delays the delivery of the works or increases what users pay for them.

Even if there is investor participation, the fact remains that the weight of infrastructure development falls on the public sector. In some cases, the role of the government must be to guarantee an adequate framework for the implementation and management of projects, while in others its role is that of co-participant, co-financing projects or guaranteeing minimum conditions to ensure the profitability of initiatives. However, in most circumstances, the weight of these undertakings will continue to be borne by public coffers, even when the private sector serves as a crucial complement, helping to close the immense gap that exists just a little bit faster.

Interview with Paolo Rocca



Paolo Rocca is the CEO of the Techint Group of Argentina, as well as Chairman, CEO and President of Tenaris S.A.

and Chairman of Ternium S.A., both headquartered in Luxembourg and leaders in the world steel market. With a degree in political science from the University of Milan, Italy, and additional studies at Harvard University, he took charge of the conglomerate in 2001. Rocca is extremely knowledgeable about the topic of infrastructure in the region, and he talks about it in this interview.

How would you analyze changes in Latin America and the Caribbean with respect to infrastructure over the past half-century?

Infrastructure has expanded significantly. During the first quarter-century of the IDB's existence, infrastructure was provided exclusively by governments. They participated not only in the definition of needs, but also in the financing, execution and operation of the projects. Although there was a significant increase in the coverage and quality of public services, there were also distortions, since infrastructure policies, which were influenced by short-term political factors, were not always congruent with economic and social development needs. After the great Latin American debt crisis of the eighties and especially during the nineties, there was a growing involvement of the private sector as well as of the public sector, which continued to reserve macro-planning and the definition of needs for itself. The experience of the nineties shows that coverage and the quality of services improved, particularly in the areas where private operators got involved. However, in the last 10 years, the involvement of these operators has been reduced in many Latin American countries. Changes in the rules of the game have created

uncertainty, and have distanced private investors from the infrastructure services sector.

The growing presence of the private sector in this issue has been remarkable. How would you describe this experience?

It's very nuanced and above all, varied. It ranges from the most successful cases in the most competitive sectors, like communications and energy, to complex and controversial sectors, such as that of drinking water and sanitation, where social variables have a very important role. The production of electricity with private backing practically doubled from 1990 to 2005, and at the same time we saw large growth in cellular and land line telephone services, so that today, thanks to investments by the private sector, more than 85 percent of the population has access to these services.

Foreign investment in infrastructure has also increased. Is this good or bad?

Foreign investment has permitted economies to incorporate technology, specific management skills and resources, accelerating the learning process. In addition, together with local partners, it has made possible the development of suppliers and clients, including in its role as

an exporter. As an example of this, since 2001 we have been participating—with the financial support of the IDB and jointly with other companies in Latin America and elsewhere in the world—in the development of the Camisea natural gas project in Peru, which includes two pipelines to carry the products from the Peruvian jungle to the coast and to Lima. An investment of US\$1.6 billion has been made in the project, generating employment for more than 2,000 persons (5,000 during construction), and an additional growth in Peruvian GDP of 0.8 percent per year.

What about regulation?

Government intervention must occur through clear and transparent regulations that are adapted over time to attract efficient and reliable participation from the private sector. I think that the functioning of the regulatory agencies has, in fact, improved in the region. It is no longer as common to see regulatory matters and the provision of public services converging in the same government area. The two functions are separate in many countries, and in these cases—where regulatory entities have greater autonomy—there is greater satisfaction with the provision of services.

Despite what has been done, the gap between Latin America and the rest of the world has widened in this area. Why?

Over the past 20 years, public investment in infrastructure has fallen significantly due to fiscal adjustments caused by the economic crises that affected the region's countries. Although private participation compensated partially for this decrease, it could not do so totally. In addition, private investment was concentrated in two sectors—energy and communications—where today the gap with the rest of the world is not great. Investment in transportation, on the other hand, has been relatively marginal.

What should the region do to make up for lost time?

The allocation of resources for infrastructure should be increased to extend its benefits to the fringes of the population that still lack them. Such expansion would favor social inclusion, improving competitiveness in the region in all sectors. Latin America and the Caribbean should spend more and better on infrastructure.

Does it worry you that the international economic crisis may affect infrastructure development?

Investment in infrastructure would have to be an essential component of the stimulus plan for the region's economies. Exports and private consumption are unlikely in and of themselves to compensate for a decrease in demand. The financing of an anti-cyclical plan on a large scale requires the ability to attract and channel government and private financial resources from all directions, in a context where investors can measure risk carefully. This is the challenge.

In this process, what would the IDB's role be?

The role that the IDB could play, just as with other international organizations, is key to financing, advising and monitoring in order to ensure that the increase in both public and private infrastructure investment is of greater economic and social quality and efficiency. The Bank's participation in financing, whether direct or indirect, creates confidence in the project and greater security with respect to its repayment. Additionally, it could contribute to supra-national projects, accelerating regional economic integration and developing shared regulatory frameworks.

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¹ Private Participation in Infrastructure Database. Available at: http://ppi.worldbank.org/explore/ppi_exploreRegion.aspx?regionID=4

² The launching in 2007 of the Water and Sanitation Initiative was the Bank's strategy in response to these new sectorial challenges. This initiative has set ambitious goals for the Bank's activity in the sector, together with proposals for changes in operating processes in order to make its work more dynamic and proactive. In addition, it renews the Bank's commitment to join forces with the countries in the region and support them in the fulfillment of the Millennium Development Goals, with the end goal of guaranteeing universal access. It also forms part of the IDB mandate as a development bank and it is an effort to position it as the best financing option for national and sub-national governments that seek to improve these services.

³ Data extracted from the Private Participation in Infrastructure Database. Available at: http://ppi.worldbank.org/explore/ppi_exploreRegion.aspx?regionID=4

⁴ Data extracted from the ICT Statistics Database. Available at: <http://www.itu.int/ITU-D/ICTEYE/Indicators/Indicators.aspx#>

⁵ Please see in this regard the note published at: <http://estrategia-de-negocios.blogspot.com/2008/05/avance-de-la-banda-ancha-en-america.html>



Parquet in Paraguay. It takes keen eyes and steady hands to make fine parquet flooring. The owner of this workshop in Paraguay used small loans extended through an IDB-financed credit program to expand production and hire more workers. The IDB has pioneered in microfinance, first supporting tiny credit-granting organizations, and now backing full-scale banking operations that meet the needs of thousands of customers. Microentrepreneurs have demonstrated that they not only use credit effectively, but also repay their loans on time.

VI The Private Sector: Tenacity and Success

Miguel Maccagno, who owns a small factory in La Matanza, a low-income neighborhood on the outskirts of Buenos Aires, is in his office examining plastic containers for the soft drinks he produces. Reducing the weight of the bottle by 14 grams, he believes, could lower costs enough to allow his business, Agroindustrias Río Tercero, to compete against the large United States, Brazilian and Chilean firms that are active in this segment of the local market (IDB, 2007).

Like this entrepreneur, whose company employs a dozen people, hundreds of thousands of Latin American and Caribbean private sector business executives are facing the challenge of competing and growing every day. Whether they own a mom-and-pop store or manage a large conglomerate with operations in several countries, in each case their overall objectives are the same: to sell more, maintain margins and grow in size. Although these are typical standards for a large

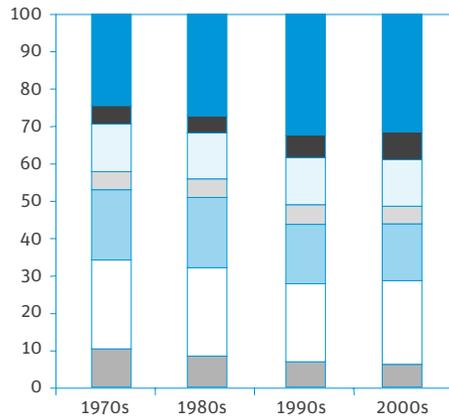
part of the world, such precepts have a well-defined and unique regional expression.

In fact, the private sector in Latin America represents nearly 90 percent of the economic activity of the region's countries (IDB, 2004a). Behind this proportion lies an important structural change. While in 1970 agriculture contributed 10 percent of added value in five major countries, with industry accounting for 18 percent (Figure 6.1), in 2007 these figures had dropped to 7.2 and 15 percent, respectively, in favor of the service sector.

Moreover, in terms of corporate entities, microenterprises clearly predominate, constituting 90 percent of all private firms, while small and medium-sized enterprises (SMEs) represent an additional 8 percent and large firms the remaining 2 percent (IDB, 2004a). SMEs also generate between 20 and 40 percent of all jobs in the private sector along with 10 percent of business activity, while the in-

Figure 6.1 Distribution of Added Value, Latin American Countries, 1970–2007

(Percentage)



- Other activities
- Transportation, storage and communications
- Wholesale and retail commerce, restaurants and hotels
- Construction
- Manufacturing
- Mining, manufacturing, public utilities
- Agriculture and livestock, housing, forestry, fishing

Source: United Nations Statistics Division.

Note: Average of Argentina, Brazil, Chile, Colombia and Mexico.

formal sector conducts more than half of all economic activity (IDB, 2004a).

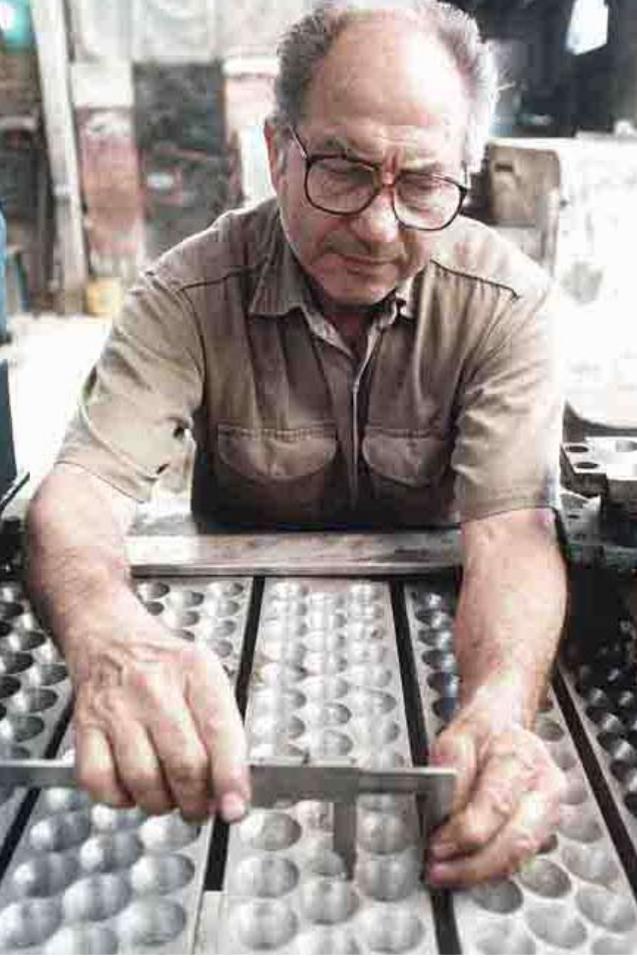
These changing proportions are the result of an increasingly urban population whose productive base has changed, becoming more highly skilled and increasing its involvement in the

global economy. But perhaps the most noteworthy element of all is the greater room afforded to private activity in the region over the last half-century, beyond the property rights traditionally guaranteed by law.¹

In other words, the context for the development of the private sector has changed dramatically throughout the region in recent decades. The wave of reforms of the eighties and nineties was intended to improve the efficiency of markets, opening economies up to international competition by lowering trade barriers, broadening access to international capital and transferring ownership of certain assets to the private sector.

Thanks to these policy changes, the environment for firms has become more dynamic and stimulating (IDB, 2004a). Evidence of this includes the rise in foreign investment, the increasing presence of transnational Latin American firms or *translatinas*, and booming entrepreneurship favored by regulatory changes and lower barriers to entry, especially with regard to access and use of technology.

There has also been a clear intent to build progress among micro-,



High quality standards and credit from an IDB-financed microfinance program enabled the owner of a small business in Mendoza, Argentina, to expand production.

small, and medium-sized enterprises through training and stimulus plans aimed at formalizing them and aiding their growth. A deciding factor in this equation has been the emergence of new financial products geared toward providing loans to smaller or newly established productive units.

However, this process has led to bottlenecks and weaknesses at all levels. Surveys conducted by various sources show that the region's business environment falls in the category of "less favorable" overall (Batra and Mahmood, 2003). The cost of doing business remains high in many countries, while the public institutions necessary for providing support to a dynamic private sector are classified as inadequate.

The combination of weak credit frameworks, rigid bureaucratic procedures and complicated labor laws translates into higher transaction costs. Fragile public institutions are not able to provide the legal, educational, health and infrastructure services required for doing business. The combined effect of these factors on the corporate environment has been a higher degree of uncertainty

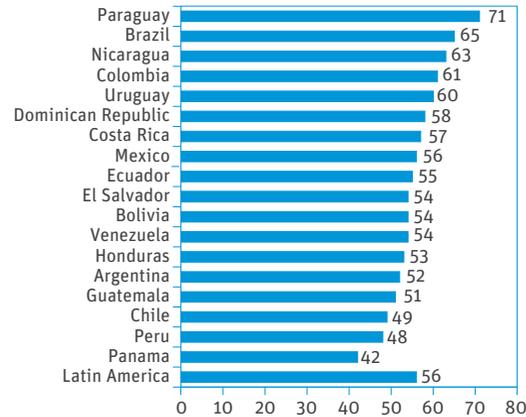
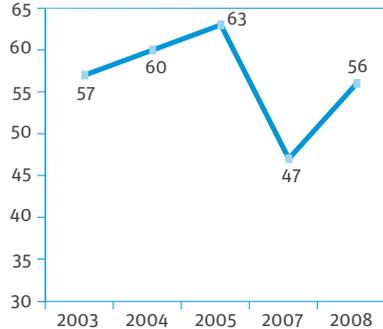
and risk, shorter-term investments, the low availability and high cost of financing (both external and internal), a lower productivity per worker and, generally, greater difficulties and fewer mechanisms to help firms seeking business opportunities (IDB, 2004a).

The realities mentioned above are also in contrast with public perception. According to Latinobarómetro, statism continues to be quite prevalent in the region, and in those nations where various services have been privatized, a significant majority feels that they should be in public hands (Latinobarómetro, 2008). Additionally, 41 percent of the population expresses confidence in private firms, while 44 percent of those surveyed classify the work conducted by business owners as "very good" or "good."

That said, 56 percent share the opinion that a market economy is the only system that will lead to development (Figure 6.2). These surveys were taken at a time when most of the region's countries were experiencing an important economic boom, with average annual growth rates of nearly 5 percent between 2003 and 2008. This dynamic was accompanied by an

Figure 6.2 Approval of the Market Economy, Latin America, 2003–08; Totals by Country, 2008

(Percentage)

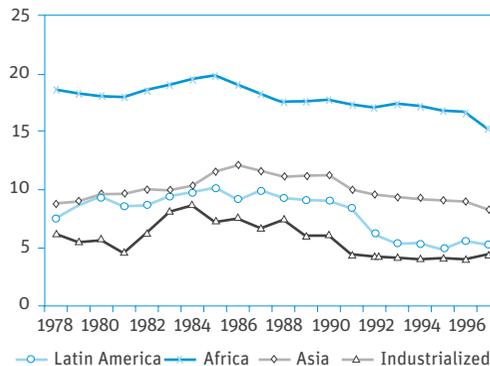


Source: Latinobarómetro (2003–08).

Note: The results in the figures have been determined based on the responses to the following question: "Do you strongly agree, agree, disagree or strongly disagree with the following statement? 'The market economy is the only system under which (country) can be developed.'" Here, only the responses "strongly agree" and "agree" appear.

Figure 6.3 Involvement of State-Owned Companies in the Economy, Selected Regions, 1978–1996

(Percentage of GDP)



Source: Chong and López de Silanes (2003).

appreciable decline in the employment rate and poverty indices.²

THE DEBATE OVER PRIVATIZATION

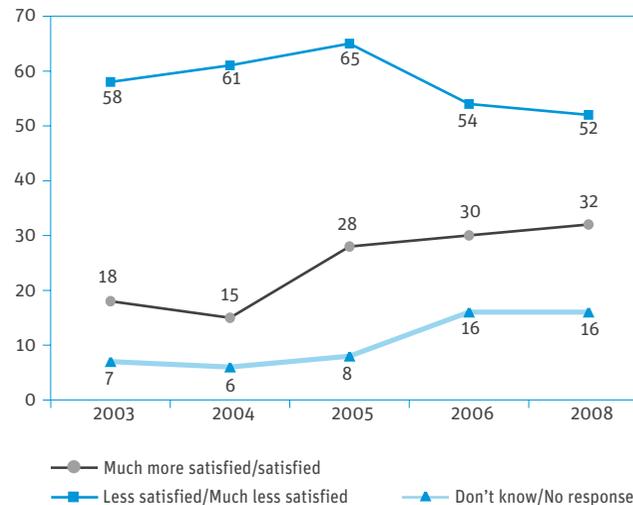
Throughout a good part of the last century, the region's governments played a prominent role as business managers, whether in the area of public utilities or in activities deemed as strategic, including the development of natural resources. According to experts, the results of this experience were not favorable, as companies "often were instructed to keep their prices below the cost recovery level" (Chong and Benavides, 2007). Such distortions led to rescue operations and budgetary pressures, a system that became ridden with conflict upon the explosion of the foreign debt crisis in 1982, when state-run firms accounted for nearly 10 percent of the region's economy (Figure 6.3).

Consequently, only a few years later several Latin American and Caribbean countries decided to sell off public assets in certain areas or allow the private sector to enter to develop new projects related to infrastructure, industrial activities or services. Although this trend was global, income from

privatization in the region accounted for 55 percent of the total generated by privatization throughout the entire developing world (Chong and Benavides, 2007), with the amount collected totaling US\$117.839 billion between 1990 and 1999 (Chong and López de Silanes, 2004).

Figure 6.4 Satisfaction with Privatized Public Utilities, Latin America, 2003–08

(Percentage of responses)



Source: Latinobarómetro (2003–08).

Note: The results in the figure have been determined based on the responses to the following question: “Now that state-owned public utilities such as water, electricity, etc. have been privatized, taking into account price and quality, are you much more satisfied, more satisfied, less satisfied or much less satisfied with these services today?”

This led to notable changes. In early 1990, only 3 percent of telephone and electric power customers were served by private firms, a proportion that grew to 86 and 60 percent, respectively, in 2003 (Chong and Benavides, 2007). However, the process was not homogeneous, nor was it exempt from changes in direction. One example was that of aqueduct services, where cases of re-nationalization were seen. There were also complaints resulting from the layoffs that followed the restructuring of sold-off firms, as between 20 and 30 percent of workers lost their jobs (Chong and López de Silanes, 2003).

These problems have likely made it difficult for the public to support the decisions made, although support has been higher in recent years (Figure 6.4). Studies have also shown that the regional balance is positive and that the failures were the result of poorly transparent processes or deficiently designed contracts due to the lack of an appropriate regulatory system (Chong and López de Silanes, 2003).

Based on this point of view, privatization not only generated

(Continued on page 154)

Interview with Steven J. Puig



Steven J. Puig is the IDB's Vice President for the Private Sector and Non-Sovereign Guaranteed Operations. Before

his appointment, he was Head of Trade Products for Latin America at Citigroup and had headed up Citigroup operations in different countries throughout the region. He holds a master's degree in international management from the American Graduate School of International Management in Arizona, and is a graduate of Georgetown University's Edmund A. Walsh School of Foreign Service in Washington, D.C.

What's your opinion of the change that has taken place in the private sector in the region over the last half-century?

Undoubtedly, the view of businesspeople in Latin America and the Caribbean has changed significantly with respect to the nature of competition, social responsibility and the scope of their activities. In terms of competition, these days they are aware that their organizations must be competitive at an international level, not just in order to defend their domestic markets, but also in order to conquer neighboring regional markets and, in some cases, extra-regional markets. Therefore, our businesspeople are very focused on continually improving the efficiency of their operations. Given the globalization of our region's countries, this focus is essential for business success. With respect to social responsibility, we have seen that over time businesspeople have taken on multiple commitments alongside the generation

of profits. Moreover, our societies and the international community demand it of them. There has been a very positive change in internal business management, in environmental responsibility and civil responsibility. Lastly, I would add that the scope of business activities has expanded significantly. Many activities that were once the exclusive domain of the public sector have been transferred to the private sector, or have become a joint effort of both. I'm referring to telecommunications, roadway construction and maintenance, electricity generation and transmission, and the administration of ports and airports, among other sectors.

What role do you think the IDB has played in these events, and what would you emphasize as positive with regard to what has been done?

The Bank has played multiple roles in this change. It has supported businesses and productive public institutions directly through its windows to

the private sector by way of loans and technical assistance. In addition, we have continued to emphasize backing for infrastructure projects with the support of the private sector. Well-conceived projects yield benefits for all users, reduce costs for our consumers, and contribute to the competitiveness of businesses and economies. Many initiatives take place within the framework of public-private partnerships created with IDB assistance. The Bank has been a leader in promoting social responsibility among the region's companies, demanding sound management of IDB-financed projects and promoting ongoing dialogue on the topic through the annual Inter-American Conference on Corporate Social Responsibility. The projects that we finance undergo an environmental review. In some cases we receive requests precisely because the sponsors or the government of a country is looking for a reliable and independent assessment of the potential environmental risks. I

would close this answer by highlighting the Opportunities for the Majority initiative through which we support business models that include the poorest people of the region.

How do you see this issue playing out over the short and long term, and what should the Bank's role be?

In the immediate term, the IDB has an anti-cyclical role of great importance in dealing with the international financial crisis. This situation obligates us to focus on ensuring that the most basic elements of our economies are functioning well to allow for a general recovery. I'm referring to liquidity for trade and the systemic liquidity of the banking systems. The recession also forces us to ensure, now more than ever, that our activities are closely aligned with the economic programs of each borrowing country in order to achieve a greater impact with the set of actions to be taken. In addition, many countries have announced broad

infrastructure programs for contributing to economic recovery in the short term and to competitiveness. We want to support these initiatives too. In the medium term it's logical to assume that the world will thoroughly evaluate this economic crisis. The IDB will have an important role in this task and in identifying recommended measures and policies for the future. With regard to the long term, I anticipate that the Bank will continue playing a key role as a go-between among its member countries, civil societies and business-people. It will continue to be a catalyst, promoting the development of projects with a high impact on the region's development by contributing loans and technical cooperation. We will seek to provide initiatives, reforms and projects that could not happen without a multilateral institution like the IDB.



A shoemaker in a modest neighborhood of Santa Cruz, Bolivia, used credit extended through an IDB microenterprise program to purchase leather and other supplies.

(Continued from page 151)

greater income, but also increased production levels, productivity growth, tax benefits and improvements in quality and access for low-income individuals (Chong, 2006). Also, the belief that governments that sell off businesses are relinquishing a positive flow of income is refuted by the argument that state-run enterprises were losing money prior to privatization, the magnitude of which is difficult to calculate due to enormous cross-subsidies from other public enterprises and government loans (Chong, 2006). In addition, the data suggest that tax revenues from sold-off companies have improved in many Latin American countries thanks to privatization, resulting in a favorable tax balance.

With regard to job losses, even if layoffs explain part of the increase in profits following privatization, the evidence shows that salaries, adjusted by industry, actually rose in the average firm and that the higher profits seen by companies are largely the result of greater productivity (Chong, 2006).

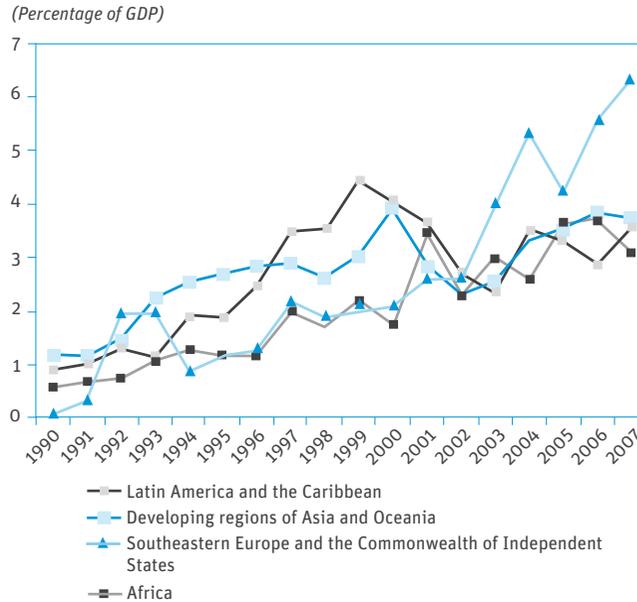
Thus, the solution has more to do with improving regulation than with refocusing efforts. In other words,

regulation related to privatization must be carefully reviewed, at least in two cases: industries characterized by natural monopolies or where oligopoly market structures exist, and industries where the government owns most of the industry's assets, especially if no one firm carries sufficient market weight (Chong, 2006). However, placed in perspective, proper regulation can make privatization work, benefiting both the government and consumers (Chong and Duryea, 2008).

THE FOREIGN INVESTMENT BOOM

According to ECLAC, in 2007 the region was the world's most dynamic emerging economy, receiving US\$105.9 billion in foreign investment, an unprecedented figure in the region (ECLAC, 2008), equivalent to 7 percent of investment activity worldwide during that period. Although the previous decade had seen a significant amount of revenue, this time around things were different in that resources were linked not to privatization as a key source of funds but to the sale of privately owned firms, the development of extractive industries and

Figure 6.5 Income from Foreign Direct Investment, Developing Regions, 1990–2007



the creation of new companies, both industrial and service-related. Thanks to a 46 percent increase in funds received versus the previous year, foreign investment accounted for 3.6 percent of the region's GDP (Figure 6.5), a rate not quite as high as the previous decade's peak levels but similar to that of the early 1970s and double the

amount reported in the 1980s.

This dynamic shows a fundamental shift of focus in a good part of a region that for half a century has oscillated between indifference, hostility and receptiveness to foreign capital. Depending on each country's political situation and what was fashionable at different moments in history, there have been episodes of openness to foreign investment which in certain cases have been reversed. Nevertheless, in most economies the free movement of resources continues, and the number of sectors allowed to be the recipients of these resources has increased (ECLAC, 2008).

With regard to the events of recent years, there are two different explanations for the observed boom. A significant part of investments was aimed at markets in response to internal economic growth and the emergence of an increasingly broad group of consumers. Thus, important expansion projects took place in the automotive sector, the consumer goods industry, the retail sector, the financial industry, electrical power services, and construction to meet the demand for real estate and infrastructure. There was also a renewed interest in natural

resources, particularly mining and hydrocarbons, as well as in the development of biofuels (ECLAC, 2008).

Without a doubt, these circumstances changed in late 2008 after prospects for the world economy soured and prices for basic products dropped sharply, making a reduction in investment flows foreseeable. Nevertheless, the perception is that once the depressive part of the cycle has passed, Latin America will once again become an attractive destination as an internal market or as a supply source for other regions of the world, especially if regulatory stability and flexibility are maintained to facilitate the entry and exit of capital.

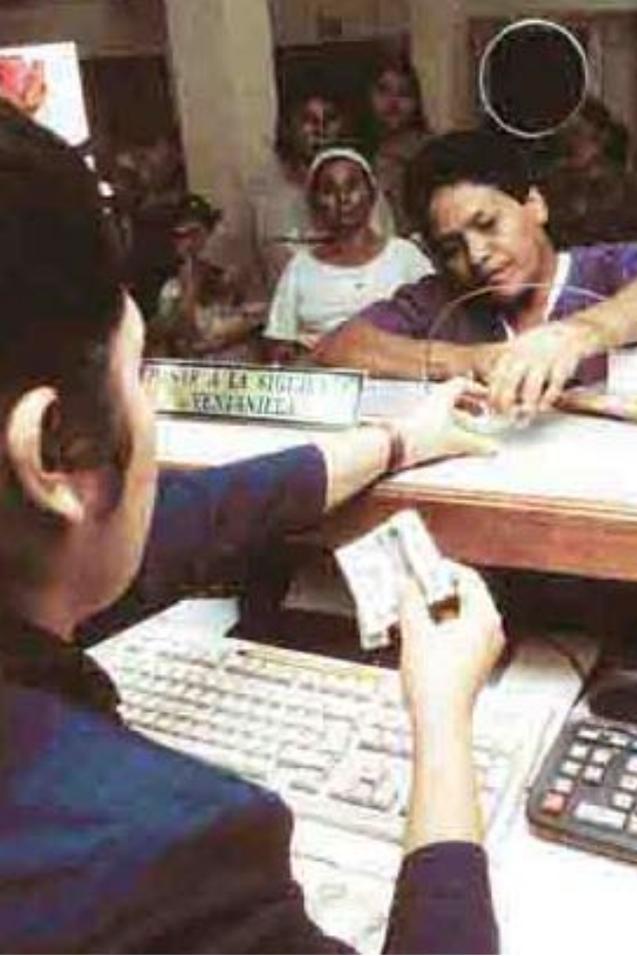
That said, some trends appear to be irreversible. One of them is the increasingly important role being played in the region by the *translatinas*, firms that are headquartered in the region and specialize in certain sectors that are of interest to overseas investors. Thus, industries such as telecommunications, hydrocarbons, mining and metals, cement, food and beverages, and retail have been particularly dynamic, with US\$20.619 billion in resources invested in 2007. Although conglomerates operating in multiple

countries have been formed on all continents, the bulk of these firms' operations has been concentrated in Latin America.

MARKET FLUCTUATIONS

Having a solid, efficient financial system has been considered to be one of the bedrock principles for achieving adequate performance in the private sector. Various analyses indicate that in countries where credit restrictions are tightest, whether in the form of reduced access to loans or very high costs, growth in the productive sector is more difficult (Galindo, Micco and Panizza, 2007).

The region's financial markets have oscillated significantly in past decades. During the 1970s, a large part of the credit system was repressed and the state was playing a prominent role in financial activities (IDB, 2004b). In the 1980s, after a brief period of liberalization and a few cases of privatization, the majority of financial systems faced profound crises, forcing governments to intervene and increase public ownership. At the end of the decade, a strong focus on banking regulation and supervision had become glob-



A customer makes a payment at a branch office of El Salvador's Financia Calpia, one of Latin America's largest microfinance institutions and a regulated bank since 2002.

ally widespread, strongly impacting the region. At that time, a new series of financial sector privatizations and reforms took place, this time in a context of greater and more prudent regulation and supervision.

In the mid-1990s, bank lending was growing at historic rates after a burgeoning inflow of capital. Nevertheless, shortly thereafter many countries once again saw themselves affected by crises, and at the start of the new century banks remained weak and credit continued to stagnate (IDB, 2004b). Once again, this trend was to be reversed in 2003 thanks to a notable boom across various economies.

In simple terms, a shift has occurred from systems of direct ownership, establishment of quotas by the productive sector and a high level of restriction with regard to interest rates or permissible activities at the end of the 1970s toward the current system of less government ownership combined with stricter regulation and supervision (IDB, 2004b). In 1970, for example, public banks managed 64 percent of industry assets in the region, a proportion that dropped to 55 percent in 1985 and 40 percent in 1995. In other words, the level of gov-

ernment ownership in Latin American banks is similar to that of other developing countries and is showing strong decreasing tendencies (IDB, 2004b).

Also, in contrast with the global financial crisis that forced various developed nations to inject public capital into a large number of credit institutions at the end of 2008, the region seemed free of causes for alarm, although a decline in the number of credit approvals is to be expected. This process has been accompanied by long-term inertia indicating greater expansion of financing, with loans to the private sector growing from around 15 percent to nearly 40 percent as a proportion of the region's GDP over the past 50 years.

This relationship, however, differs quite a bit from the one observed in developed nations as well as the emerging economies of Asia. Although the global financial crisis that began in 2008 may alter the gaps between regions, the evidence shows a clear correlation between the level of credit-related activity and the performance of the productive sector. It is also important for a majority of the population to have access to financial

institutions, something that occurs in less than 40 percent of Latin American families (Demirgüç-Kunt and Levine, 2008).

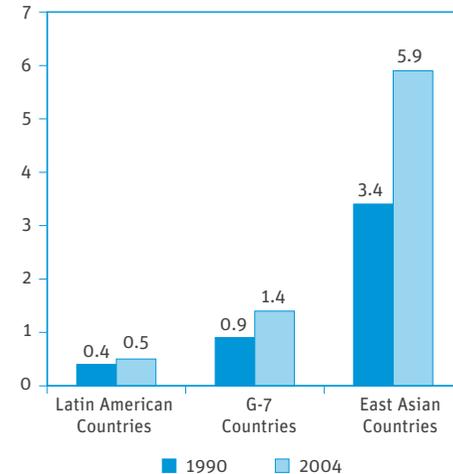
Despite these advances, the perception exists that the decisions that have been made have not been as fruitful as expected, despite more flexible legislation (De la Torre, Gozzi and Schmukler, 2006) and greater macroeconomic stability thanks to the victory over hyperinflation. However, this diagnosis is much more convincing in the case of stock exchanges and bond markets, the indicators for which continue to lag behind those of other regions. The development of the capital market is still, therefore, precarious (De la Torre, Gozzi and Schmukler, 2006). In other words, vigorous capital markets have not been developed in the region's countries, and the primary source of external financing for the region's companies is bank loans (IDB, 2004b).

Although there are those who believe that a long period of gestation is needed and that the decisions that have been made recently are the right ones, a different line of thinking suggests the need to review and change the sequence of adopted policies

(De la Torre, Gozzi and Schmukler, 2006). But beyond this debate, several advancements are worth recognizing. For example, between 1990 and 2004, the market capitalization of companies listed on the region's seven stock exchanges (Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela) tripled, while in the region as a whole it went from 0.4 to 0.5 percent (Figure 6.6). However, it is also true that the same indicator reached 92

Figure 6.6 Capital Raised Domestically, Selected Regions, 1990 and 2004

(Percentage of GDP)



Source: De la Torre, Gozzi and Schmukler (2006).

percent in countries belonging to the Group of Seven (G-7) and 104 percent in Southeast Asia (De la Torre, Gozzi and Schmukler, 2006).

Even more worrisome is the fact that the number of companies listed on the stock exchange fell from an average of 232 to 174 during the period. Although the bond market saw an important increase in issues by public entities, private issuers did not react the same way, accounting for only 10.7 percent of GDP in the nations analyzed, while in Asia this indicator was two and a half times greater. All of this took place despite the emergence, over the last two decades, of private pension funds, which have become increasingly important in some regional economies. In fact, innovations in this area were a central component of state reforms during the 1990s (Mesa-Lago and Márquez, 2007). In practical terms, this involved modifying a public system based on contributions linked to employment and designed to cover the risks of old age, disability and death.

However, as life expectancy increased, it became difficult to expand the base of active, contributing workers in order to finance the retired

population, and systems began to accumulate considerable deficits. Thus, structural transformations took place, including the creation of private systems to substitute for or supplement public systems. Some also argued for promoting the creation of long-term financial instruments that could contribute to expanding the capital market (Mesa-Lago and Márquez, 2007). Thus, 12 of 20 Latin American countries adopted reforms ranging from completely replacing the public system with a private one to adopting a parallel system (where public and private coexist) and a mixed system (where private supplements public), although in general, modifications were passed by all national legislations. Changes also included an increase in the number of contribution weeks, a revision of contribution amounts, and raising the retirement age.

Without getting into the justification for these measures, the aggregate impact was great. By 2004, 160 million people were insured under pension systems, with two-thirds of these systems belonging to the public sector and the remainder to the private sector (Mesa-Lago and Márquez, 2007). Toward the middle part of the decade,

(Continued on page 162)

Interview with Dionisio Gutiérrez



As President of Corporación Multi Inversiones, Dionisio Gutiérrez manages one of Guatemala's largest and one of the region's most

powerful corporations. The conglomerate, whose origins date back to the beginning of the last century, now boasts six divisions: milling, fast food restaurants, livestock operations, renewable energy generation projects, real estate and construction, and financial services. With a presence on 3 continents and in 14 countries, the company employs 32,000 people and is an example of successful globalization. Its best-known brand is Pollo Campero, whose restaurants are located in Madrid, Jakarta, Shanghai, and throughout Central America and the Caribbean.

What was the reason for forming a transnational group?

I think it was mainly because the region is made up of relatively small markets, with a few exceptions. Due to this, globalization is inevitable for certain countries, such as those of Central America. So, business groups have been set up despite the difficulties and contradictions. But it is due to the small size of the markets and the lack of an integration scheme along the lines of the European Union.

What is that process of going across borders like?

It is still traumatic, costly and inefficient, and causes companies to lose their competitive edge. The reason is that there are incompatible laws and policies, which is really regrettable because the growth that we should experience is not there. This lack of standardization makes the process traumatic. There's no doubt that all of this makes us less competitive in a globalized world.

What are the rewards?

For those of us who are used to this system, it is sometimes easier for us to operate within the cultural identity of the region. However, I want to emphasize that we're facing some big regulatory problems.

Is the Latin American businessperson more globalized now?

Yes, there is much more awareness of the issue. Unfortunately, businesspeople haven't made the necessary level of commitment with respect to civil or legal matters in order to promote policy change. That is what we need, and until we change it, we will continue to see only large companies moving across borders, while we will still remain underdeveloped.

How has your group changed over the last half-century?

We started the group's international expansion more than 35 years ago, first in neighboring Central American

countries and then in the Western Hemisphere and other latitudes. We were able to expand because we kept saturating the markets, and we had a drive to succeed and move forward. We generated the opportunity, and we took advantage of it.

What is your opinion of Latin American businesspeople?

I think that the Guatemalans as well as others from Latin America and the Caribbean are the result of a process. We move in weak democracies that don't give us the regulatory security that we would like and that haven't fulfilled people's expectations. Over the last few decades, only Chile has managed to sustain its growth, while the rest have fallen behind. Part of what has happened has to do with the absence of unified government policies. For this reason, I hope to see the region's businesspeople helping to decisively piece together that complex puzzle that holds the solution to the problems of poverty and backwardness.

What would you like to see in the region?

I really hope that the elite of Latin America will take action. The region needs a new awakening that includes profound political reforms that will give back institutional security and strength in the rule of law to its democracies and institutions. I see the need to strengthen the bonds of integration, and I'd like to see us have a single passport and a single currency. This would give us economies of scale and would drive the development that we need to rescue millions of fellow Latin Americans who still live in poverty.

How do you see the IDB's role in all this?

I think that the IDB is an institution that has made significant inroads in Latin America and the Caribbean. But I would like it to show more strength in the region without funding excesses or irresponsible activities. Otherwise, we will continue to be a lost continent, one that has a lot of potential and talent but

fails to take advantage of what we have in our favor.

(Continued from page 159)

the volume of managed resources grew to US\$147 billion, or nearly 12 percent of the region's GDP at that time. Nevertheless, around half of all investments were deposited in government bonds, while a little over 20 percent went into local stocks, corporate bonds and mutual funds (De la Torre, Gozzi and Schmukler, 2006); as such, the impact on the development of the capital market was limited.

In light of the magnitude of the crisis that rocked the globe in 2008, it was clear that no market would be immune to the situation and Latin America was no exception. Consequently, average share prices on various stock exchanges fell by nearly half, while the price of internal and external debt securities suffered due to the increased perception of risk across the region. This does not negate the fact that, despite the magnitude of these events, seeking the greater development of capital markets remains a valid objective. The question, of course, is whether the experts will find the right path toward meeting this objective once the situation returns to normal.

THE RISE OF MICROFINANCING

As a virtual parallel to the efforts aimed at driving capital markets, support for microfinancing has gained force as a way to break the chains of poverty that surround one of every three Latin Americans and to battle informality. Even though this phenomenon is relatively recent, the results are already encouraging. An analysis of 23 countries in the region showed that between 2001 and 2005 the number of entities dedicated to microfinancing grew from 184 to 447, while the number of clients rose from 1.8 to 5.9 million and portfolio values increased from US\$1.189 billion to US\$5.442 billion during the above period (Table 6.1) (Navajas and Tejerina, 2006).

The chances of achieving these figures were slim at the start of the 1970s, when the first initiatives were launched in countries as diverse as Bangladesh and Brazil. The driving factor behind the first tested models was the conviction that the poorest households could and should have access to credit (Navajas and Tejerina, 2006). These models evolved over time and began to include loans to groups of individuals or even

communities, a good portion of such loans being managed by non-governmental organizations. By 1990, however, personal loans and the formation of entities specialized in microfinancing began to predominate; commercial banks also began channeling resources in this direction.

The current decade has seen particularly rapid changes. According to available data, between 2001 and 2005, average annual growth in the number of clients was 35 percent, with

46 percent for loans. During the same period, regulated entities specialized in microfinancing had the greatest number of clients and the highest volume of loans. No less remarkable is the fact that these operations remain profitable, with indicators nearly equal to those of traditional banking. This is one of the reasons why the movement is attracting growing numbers of individuals and institutional investors, who typically participate through an increasing number of specialized funds that chan-

Table 6.1 Microfinance Institutions, Latin America and the Caribbean, 2005 and 2001

Type of Institution	Number of Institutions	Portfolio (US\$ millions)	Borrowers	Average Loan (US\$)
Data from 2005 (23 countries)				
Regulated microfinance institutions	98	4,407	3,851,765	1,144
<i>Downscaling</i> (banks and financial institutions) ^a	31	1,810	1,233,873	1,467
<i>Greenfields</i> ^b	30	1,005	738,671	1,361
<i>Upgrading</i> ^c	37	1,592	1,879,221	847
Nonregulated MFIs	238	1,030	2,100,951	490
All MFIs—2005	336	5,437	5,952,716	913
Data from mid-2001 (17 countries)				
Regulated microfinance institutions	60	901	936,936	962
<i>Downscaling</i> (banks and financial institutions) ^a	21	343	365,171	939
<i>Upgrading</i> ^c	39	558	571,765	976
Nonregulated MFIs	124	288	869,509	332
All MFIs—2001	184	1,189	1,806,445	659

Source: Navajas and Tejerina (2006).

^aRegulated financial institutions that added microcredit as a new line of business.

^bMFIs operating as regulated financial institutions since inception.

^cNGOs that have transformed themselves into regulated financial institutions.



A bed frame gets a colorful coat of paint as workers gain experience in a program to prepare job seekers for a place in the workforce.

nel money to microfinancing agencies through loans or capital investments (Miller-Sanabria and Narita, 2008).

COMPETITIVENESS AND THE EASE OF DOING BUSINESS

However, these favorable developments must be imitated on other fronts. One example of the road that lies ahead was given in a study conducted by the IDB comparing the business environment in Latin America and the Caribbean with that of Asia. The data indicated that the region's business owners were at a clear disadvantage. According to the study, East Asian countries have more highly integrated societies, greater income levels, and more highly articulated and sophisticated productive structures and innovation systems (Kantis, Ishida and Komori, 2002).

Latin American entrepreneurs also pointed to the lack of necessary financing as one of the barriers impeding development and the growth of new firms, leading them to seek different ways of reducing their initial investment, such as purchasing second-hand machinery, obtaining credit from suppliers, or starting out on a smaller scale. Asian entrepreneurs, on the

contrary, enjoy better access to external financing, especially during the launch phase and the initial development of their firms, with a greater variety of financing sources (Kantis, Ishida and Komori, 2002).

Such weaknesses have been highlighted by other measurements, such as those maintained by the World Economic Forum in its competitiveness rankings (Table 6.2) or by the World Bank in its Doing Business program. In both cases, the results have been useful in re-evaluating the belief that the more devalued a country's currency becomes or the greater its trade surplus, the more competitive it will be. This has been displaced in recent years by a more comprehensive vision that takes into account the factors that contribute to generation of added value at both the microeconomic level and the aggregate level.

Thus, an economy is more competitive when firms are able to function in an environment that encourages sustained growth in productivity and per capita income levels. The drive for greater competitiveness in a global economy forces countries to create better conditions for the development of firms than those that reflect

Table 6.2 Global Competitiveness Index, 2008

Country/ Economy	GCI 2008– 2009 rank	Score	GCI 2008–2009 rank (among 2007 countries) ^a	GCI 2007–2008 rank	Country/ Economy	GCI 2008– 2009 rank	Score	GCI 2008–2009 rank (among 2007 countries) ^a	GCI 2007–2008 rank	Country/ Economy	GCI 2008– 2009 rank	Score	GCI 2008–2009 rank (among 2007 countries) ^a	GCI 2007–2008 rank
United States	1	5.74	1	1	Slovak Republic	46	4.40	45	41	Libya	91	3.85	90	88
Switzerland	2	5.61	2	2	Barbados	47	4.40	46	50	Trinidad and Tobago	92	3.85	91	84
Denmark	3	5.58	3	3	Jordan	48	4.37	47	49	Kenya	93	3.84	92	99
Sweden	4	5.53	4	4	Italy	49	4.35	48	46	Nigeria	94	3.81	93	95
Singapore	5	5.53	5	7	India	50	4.33	49	48	Moldova	95	3.75	94	97
Finland	6	5.50	6	6	Russian Federation	51	4.31	50	58	Senegal	96	3.73	95	100
Germany	7	5.46	7	5	Malta	52	4.31	51	56	Armenia	97	3.73	96	93
Netherlands	8	5.41	8	10	Poland	53	4.28	52	51	Dominican Republic	98	3.72	97	96
Japan	9	5.38	9	8	Latvia	54	4.25	53	45	Algeria	99	3.71	98	81
Canada	10	5.37	10	13	Indonesia	55	4.25	54	54	Mongolia	100	3.65	99	101
Hong Kong SAR United Kingdom	11	5.33	11	12	Botswana	56	4.25	55	76	Pakistan	101	3.65	100	92
12	5.30	12	9	Mauritius	57	4.25	56	60	Ghana	102	3.62	n/a	n/a	
Korea, Rep. of	13	5.28	13	11	Panama	58	4.24	57	59	Suriname	103	3.58	101	113
Austria	14	5.23	14	15	Costa Rica	59	4.23	58	53	Ecuador	104	3.58	102	103
Norway	15	5.22	15	16	Mexico	60	4.23	59	52	Venezuela	105	3.56	103	98
France	16	5.22	16	18	Croatia	61	4.22	60	57	Benin	106	3.56	104	108
Taiwan, China	17	5.22	17	14	Hungary	62	4.22	61	47	Bosnia- Herzegovina	107	3.56	105	106
Australia	18	5.20	18	19	Turkey	63	4.15	62	53	Albania	108	3.55	106	109
Belgium	19	5.14	19	20	Brazil	64	4.13	63	72	Cambodia	109	3.53	107	110
Iceland	20	5.05	20	23	Montenegro	65	4.11	64	82	Côte d'Ivoire	110	3.51	n/a	n/a
Malaysia	21	5.04	21	21	Kazakhstan	66	4.11	65	81	Bangladesh	111	3.51	108	107
Ireland	22	4.99	22	22	Greece	67	4.11	66	65	Zambia	112	3.49	109	122
Israel	23	4.97	23	17	Romania	68	4.10	67	74	Tanzania	113	3.49	110	104
New Zealand	24	4.93	24	24	Azerbaijan	69	4.10	68	66	Cameroon	114	3.48	111	116
Luxembourg	25	4.85	25	25	Vietnam	70	4.10	69	68	Guyana	115	3.47	112	126
Qatar	26	4.83	26	31	Philippines	71	4.09	70	71	Tajikistan	116	3.46	113	117
Saudi Arabia	27	4.72	27	35	Ukraine	72	4.09	71	73	Mali	117	3.43	114	115
Chile	28	4.72	28	26	Morocco	73	4.08	72	64	Bolivia	118	3.42	115	105
Spain	29	4.72	29	29	Colombia	74	4.05	73	69	Malawi	119	3.42	n/a	n/a
China	30	4.70	30	34	Uruguay	75	4.04	74	75	Nicaragua	120	3.41	116	111
United Arab Emirates	31	4.68	31	37	Bulgaria	76	4.03	75	79	Ethiopia	121	3.41	117	123
Estonia	32	4.67	32	27	Sri Lanka	77	4.02	76	70	Kyrgyz Republic	122	3.40	118	119
Czech Republic	33	4.62	33	33	Syria	78	3.99	77	80	Lesotho	123	3.40	119	124
Thailand	34	4.60	34	28	El Salvador	79	3.99	78	67	Paraguay	124	3.40	120	121
Kuwait	35	4.58	35	30	Namibia	80	3.99	79	89	Madagascar	125	3.38	121	118
Tunisia	36	4.58	36	32	Egypt	81	3.98	80	77	Nepal	126	3.37	122	114
Bahrain	37	4.57	37	43	Honduras	82	3.98	81	83	Burkina Faso	127	3.36	123	112
Oman	38	4.55	38	42	Peru	83	3.95	82	86	Uganda	128	3.35	124	120
Brunei					Guatemala	84	3.94	83	87	Timor-Leste	129	3.15	125	127
Darussalam	39	4.54	n/a	n/a	Serbia	85	3.90	84	91	Mozambique	130	3.15	126	128
Cyprus	40	4.53	39	55	Jamaica	86	3.89	85	78	Mauritania	131	3.14	127	125
Puerto Rico	41	4.51	40	36	Gambia	87	3.88	86	102	Burundi	132	2.98	128	130
Slovenia	42	4.50	41	39	Argentina	88	3.87	87	85	Zimbabwe	133	2.88	129	129
Portugal	43	4.47	42	40	Macedonia, former					Chad	134	2.85	130	131
Lithuania	44	4.45	43	38	Yugoslavia	89	3.87	88	94					
South Africa	45	4.41	44	44	Georgia	90	3.86	89	90					

Source: Porter and Schwab (2008).

^aOne country that was included last year is not shown (Uzbekistan) because of the lack of survey data. Thus, the lowest rank in this column is 130 instead of 131.

Interview with Nicolás Trociuk



Nicolás Trociuk is the Chairman of the Board of Directors of Banco Regional, one of Paraguay's most important finan-

cial institutions, as well as a director of Trociuk y Compañía, a company specializing in agriculture and livestock production, agroindustry and the sale of foodstuffs. In this interview, he indicates that the current global crisis must be met with a mixture of perseverance and optimism.

How has the environment changed for a company like yours over the years?

In my experience I have noticed constant, cyclical changes, because we are in a country, Paraguay, with an economy that is very dependent on the climate, on primary production and on international markets, as well as on neighboring countries, mainly Brazil and Argentina, with whom we have many ties. We were constantly growing until the global crisis exploded, and we don't know how deep it will be or how long it will last.

Is it more difficult to compete in a globalized world?

Without a doubt. But I also see globalization as a positive thing, because it forces us to be efficient and competitive. Otherwise there would be stagnation in quality and cost, which is not healthy at all.

What are the opportunities that this new reality brings?

In crises, there are also opportunities, and this is particularly true in a globalized world. It's all about creativity, willingness and work that is efficient and well done. Of course, we must make the necessary effort, since challenges can be met if we approach opportunities responsibly and seriously. It's a matter of confidence.

There are many companies in the region that have decided to go into other countries. What do you think about that?

From my point of view, diversifying risks, investments and work is prudent, although you don't always achieve the results you were expecting. However, a globalized world is a reality that we can't ignore or escape. Sound investments for sound purposes are and will always be embraced and welcomed. It doesn't matter where or in what country you are, or what country you come from.

Are Latin Americans in today's business community better prepared? If so or if not, why?

I sense that they are; there is greater capability and experience. The region's businesspeople have already carved out their space in the global market. But with what has happened lately, we have seen that those who up to now were considered the best and most reliable can also fail and make mistakes.

In your opinion, what's the main challenge facing the private sector in the region?

Right now, it's to get out of this crisis without too much irreparable damage, although undoubtedly there will be some. We hope to get around the situation and look at the future optimistically and with confidence, without losing hope. Although we can't ignore that there are problems, the challenge is to generate work and productivity to move forward.

How do you see the business sector handling things in the global crisis?

I'm concerned, but I'm also highly optimistic, because the crisis has to end one day. It is better not to get depressed and realize that life will go on and that companies must continue operating. We are going to go through some very hard times. Although the bomb exploded in another place that had nothing to do with us, the shock wave hit us all, and we have a heavy cross to bear. It's a matter of resistance and time.

What change would you like to see occurring in the region's business community?

I'd like us to soon be able to see the light at the end of the tunnel in this crisis that we still haven't been able to measure. I'd like to see this crisis come to an end quickly so that we can get down to work, repair the damage and rebuild our economies. Of course, I'd also like the regional and world economies to stabilize so that we can begin

working. In this current environment of fear, re-establishing confidence as quickly as possible is crucial.

How do you analyze the IDB's role in this matter?

We applaud the IDB's decision to support its member countries with an ambitious program to confront and mitigate this crisis to a certain extent. In Paraguay, the IDB has always been viewed as a good partner to have in development programs. It's my understanding that this institution is the one that has supported Paraguay the most with loans and development programs. My perception is that it has played and continues to play an extremely important role.

current income levels (IDB, 2001). Ultimately, this involves staying ahead of the pack, an important consideration for a region that has failed to close the gap or lost ground in the race against other areas of the world.

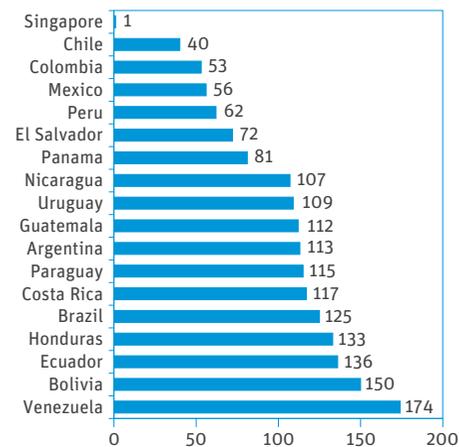
Despite the advancements of recent years, the results for the region are not good. According to the Global Competitiveness Index,³ in 2008 only one Latin American nation was among the top 30 in a group of 134 countries, while seven of the region's countries were in the top half and 16 were in the bottom half. A 2001 analysis of 75 countries, including 20 from the region, showed similar results despite changes in the measurement methodology that make the numbers not completely comparable. It was clear at that time, as it is now, that Latin America was in fifth place among the seven major regions of the world with regard to competitiveness, only slightly outstripping the poor countries of Asia and the small number of African states included in the study (Porter and Schwab, 2008).

Although some individual classifications differ, the results published by the World Bank in its annual *Doing Business* report show clear similarities in terms of where the nations of the

region rank⁴ among a sample of 181 economies (Figure 6.7). Beyond specific success stories, the general perception is that even where progress has been made, it has been slower than on other continents.

The obstacles to be overcome are broad and diverse in nature. One of them is the regulatory framework and the high cost of dealing with government entities. Other factors include the lack of modern infrastructure, low labor productivity, the relatively

Figure 6.7 Ranking in the Doing Business Index, Singapore and Latin American Countries, 2008



Source: World Bank (2008).

small size of local firms, a low capacity for innovation, and bottlenecks in the finance sector, just to name a few. Improving this reality is essential in light of the challenges generated by the global deceleration reported since late 2008. Beyond the complex nature of the crisis, recovery will no doubt be faster in areas where the private sector can function in a more favorable and flexible environment.

Thus, while it is clear that private initiative in Latin America and the Caribbean has made enormous strides over the past half-century, the task is not yet done. On the one hand, the sale of public enterprises or the arrival of new capital in areas that were previously off-limits requires a massive effort in establishing standards and regulations

to guarantee both the rights of the public and the development of the projects involved. On the other hand, with regard to the financial sector, a greater expansion has occurred that nevertheless lags behind the indicators for other regions of the world.

It is equally important to emphasize that while the rise in foreign investment reported during this decade may suggest otherwise, the region's business climate is not the most optimal. Consequently, there is no choice but to tear down barriers and make procedures more efficient while working on issues like education or physical infrastructure. In the industry's own terms, an effort of this magnitude will guarantee greater returns for all of the region's inhabitants.

Interview with María Otero



María Otero is president and CEO of ACCION International, a leading global microfinance institution and a microfinance pioneer in

Latin America and the Caribbean. Throughout her career, she has worked with the U.S. Agency for International Development, the Centre for Development and Population Activities, the Development Group for Alternative Policies, and the Inter-American Foundation. She has earned numerous awards and is currently an adjunct professor at the Johns Hopkins University School of Advanced International Studies (SAIS). A native of Bolivia, she holds a master's degree in literature from the University of Maryland as well as a master's degree in international relations from SAIS.

Aside from the significant growth of microfinance throughout the region, its role in rebuilding the social fabric has been remarkable.

Yes, indeed. We've seen that in some contexts, in certain regions in conflict, the possibility of bringing in a source of new jobs through microenterprises makes the difference. We've also seen that in countries that are coming out of conflict, incorporating microfinance programs really helps along the reconstruction process. It's an element that helps countries create all the threads that have to be tied together to build a stable society under the conditions that will allow their citizens to live a better life. Microfinance hasn't been the answer to everything. It's not the solution, but it helps expand our capacity to heal a society.

Not all microfinancing happens through banks, but through non-governmental organizations, correct?

Yes, and the reason is that NGOs have more options for addressing certain types of situations. Donors play a different role in that they must recognize that, in some cases, the work being done isn't for creating a financially viable entity or new business

models, but simply for providing assistance. Nevertheless, in a good part of Latin America and the Caribbean, the model is sustainable, which explains its significant growth.

What impact do you think the financial crisis will have on microfinance?

We're still in an environment of uncertainty. We're aware that this is a crisis situation, but we're not sure yet what the impact will be. We know that it's affecting economic growth, along with production and demand. This definitely impacts the micro-entrepreneur and raises the cost of food and other basic household necessities for poor families.

And how will it affect microfinance organizations?

The thing that will be affected the most is their liquidity, which is a concern because they need resources to expand their portfolios. What we're going to see is that those organizations that were using capital markets will be forced to look for other sources of funding, which will result in a significant slowdown in their growth. We have to remember that in Latin America they've grown at 20 percent

per year, with some of the more well-established ones growing at 35 or 40 percent per year. These rates will drop, in a context where many people still don't have access to financial services. Overall, the crisis will impact the momentum at which microfinance has been implemented in recent years.

What is your opinion regarding the assertion that lending rates for micro-credit are too high?

Our experience, after working 30 years in this field, is that you can't compare the interest rates of a microfinance entity with market rates, because micro-entrepreneurs don't have access to the market. Instead, you have to compare them with moneylender rates, which can be as high as 10 or 15 percent per day. Any micro-entrepreneur who compares those rates, which can be up to 600 percent per year, with the maximum 40 percent offered by microfinance organizations, won't hesitate to choose microcredit for that reason, because his other option isn't the bank that will lend him funds at 20 percent, but the moneylender. The reason for the higher rates is that it's very expensive to grant small loans and make them available on demand in an efficient manner.

But couldn't they be lower?

If they charged less, microfinance institutions wouldn't be able to sustain themselves and they'd start decreasing in size. You can ask any micro-entrepreneur whether he'd rather pay a higher interest rate and have the security of knowing that he'll have access to financial services two or three years down the road, or pay a lower rate and live with the risk that we may not be around in three years. Micro-entrepreneurs will always go for the first option, because they need secure access to credit.

What is your view of the interest rate caps on microloans that exist in some countries?

They worry us, because establishing caps creates a situation where microfinanciers will have less of a chance of becoming self-sustainable or -regulated. If regulators in a particular country want to maintain a cap on interest rates but decrease financial services for the poor, though, unfortunately, that's their choice.

Do you worry about the level of consumer indebtedness that is being promoted to many low-income people?

That's one of the issues that caused the current financial crisis—people

were financing out-of-control consumption with credit cards. Having access to consumer goods through plastic is helpful, but the key here is to improve the financial literacy of low-income people, helping them comprehend their economic situation so that they understand how overindebtedness can lead to enormous losses. I think if that had been done in the United States, we wouldn't have this crisis today. Commercial entities that work with the lowest-income segments of the population not only have a responsibility to be transparent, but they also have a responsibility to help improve the financial knowledge of their clients.

What would it take in regulatory terms to provide greater incentives for financing?

The answer differs from country to country, and in general, we're seeing that it's not just about taking regulatory steps, but about creating incentives for banks to view microenterprises as clients and educating banks on how to work with people who don't keep books and are used to informality.

Box 6.1 The IDB's Role in the Private Sector

The Inter-American Development Bank has worked alongside the private sector in the region throughout its history. However, such activities have intensified over the last few years, thanks to a more favorable business climate and decisions that have expanded the range of loans beyond national or regional public spheres. A concrete example of these efforts is the Inter-American Investment Corporation (IIC), founded in 1989 as a separate entity of the IDB with its own accounting department and Board of Directors. From its creation until 2002, the IIC approved loans for the small and medium-sized enterprises of Latin America and the Caribbean. In 2008, the IIC approved a new business plan that included new definitions and market segmentation between financial institutions and companies in other sectors. Thus, between 1989 and 2008 the Corporation approved 560 operations with an aggregate value of US\$3.3 billion, not including another US\$1 billion for co-financing activities.

It is also necessary to point out the Multilateral Investment Fund (MIF), founded in 1992 for the purpose of delivering funds for research, developing partnerships with the public or private sectors, and even investing in risk capital. As a result of this effort, the MIF has carried out trailblazing work in the area of remittances in order to calculate their volume and to determine more effective uses for these funds. It has also supported the transformation of non-governmental organizations into regulated microfinance institutions. The MIF's goal for the next five years is to triple the resources delivered under this modality in Latin America and the Caribbean so that it may reach 25 million clients. During its existence, the Fund has approved 1,200 projects for the delivery of money and 160 joint investments for an overall total of over US\$2 billion.

In 1994, the Private Sector Department was created within the structure of the Bank, and in 2006 its name was changed to the Department of Structured and Corporate Finance. Loans and partial guarantees approved for the finance, productive, infrastructure and service sectors have totaled almost US\$18 billion since 1995. Also worth mentioning is the Opportunities for the Majority initiative. Created in 2007 with an initial allocation of US\$250 million, its purpose is to apply market-based strategies to incorporate the millions of people who are still excluded from the region's economic activity.

Some of the Department's most notable projects include successful programs for investing in different microfinancing entities like Bancosol in Bolivia or Financiera Calpia in El Salvador. In the latter case, by the time the Bank sold its share in Financiera Calpia in 2000, the institution had 10 times more clients than when it began, as well as eight additional offices, 61 new loan officers, and nearly three times as many clients per officer.

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¹ The private sector has been defined as "a basic organizational principle for economic activity in which private property is an important factor, markets and competition drive production and private initiative and the assumption of risks set activities in motion." See OECD (1994).

² See Chapters 1 and 3 of this book.

³ The Index is the result of individual measurements in 12 areas or "pillars": institutions, infrastructure, macroeconomic stability, health and primary education, advanced education and training, efficiency of the goods market, efficiency of the labor market, sophistication of financial markets, technological readiness, market size, business sophistication and innovation.

⁴ The World Bank measures 10 stages in the life of a business: starting a business, dealing with licenses, employing workers, registering property, obtaining credit, protecting investors, paying taxes, trading across borders, enforcing contracts and closing a business.



Putting science to work. Growing out new genetic material, a lab worker in São Paulo takes an initial step in developing varieties that will not only help farmers but also fuel a chain of agroindustries that has made Brazil a world leader. In general, however, most Latin American countries have lagged in science and technology critical for creating a modern industrial sector capable of competing in the global marketplace. The IDB has been a leader in supporting programs to strengthen links between research and industry.

VII Science and Technology: A Wise Investment

When Geraldine Mlynarz graduated with a degree in agronomy, choosing the detection of viruses in fish as the topic for her biotechnology thesis, she didn't expect to become, along with her professor Ana María Sandino, a prosperous entrepreneur in genetic technology as a result (IDB, 2005a). After creating a new diagnostic method using chain reaction polymerization, a research technique never before applied in Chilean aquaculture, both women decided to transfer this innovative technology to the commercial sector. They held extensive meetings with various Chilean salmon producers, and in 1997, they formed their own company, Diagnostec, offering pathogen diagnostic services for salmonids. Eventually, the company opened an office in Santiago, and shortly thereafter joined forces with a new partner to open a branch in Puerto Montt, the center of Chile's salmon industry.

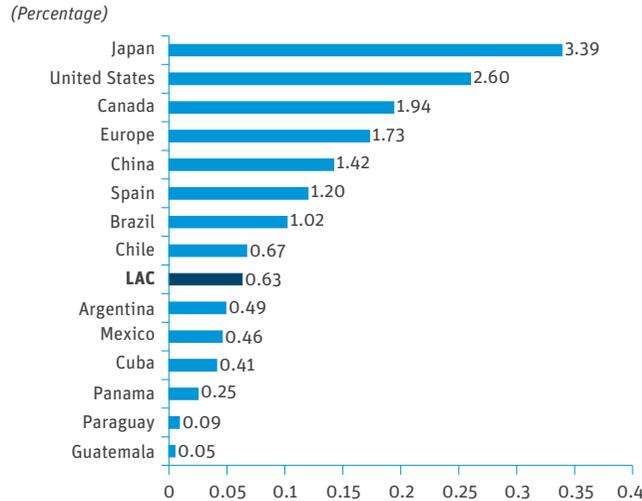
Today, the company has expanded to provide quality control for foods

such as salmon, pork and poultry.¹ But beyond the particular case of Diagnostec, the moral of the story is that there are opportunities and room aplenty for science and technology in Latin America.

One explanation is that as education indices increase, so does the number of scientists in the region. According to the Network on Science and Technology Indicators (RICYT), the number of full-time investigators and technologists grew to 234,661 in 2006 or 85 percent more than in 1997, one of the highest rates in the world (RICYT, 2008). Investments in science and technology reached US\$18.3 billion in the same year, nearly 60 percent more than at the end of the previous decade.

That said, in reality, the road ahead is still extremely long. Total investments in research and development are between less than 0.1 percent and 1 percent of the gross domestic product (GDP) for most of the region's countries (Figure 7.1) (RICYT, 2008), with no drastic changes in recent times (IDB,

Figure 7.1 Investments in Research and Development as a Percentage of GDP, Selected Regions and Countries, 2006, or Last Year Available



Source: Ibero-American Network on Science and Technology Indicators (RICYT, 2008).

2000). Not only is this proportion low compared to the 2 to 3 percent of GDP invested by high-income nations, but total investment by the region in the field is nearly half the amount spent by South Korea (IDB, 2005b). Furthermore, the public sector accounts for almost 70 percent of spending for

this purpose, while in the emerging economies of Asia, this figure totals 25 percent (IDB, 2000). On the other hand, Latin America's share of the worldwide total grew to 1.9 percent in 2006, placing the region above Africa and Oceania, but lagging far behind Asia, Europe and North America.

A great sacrifice is implied. According to experts, innovation in advanced economies is positively correlated with economic activity, training of highly skilled labor, and the commercial and competitive expansion of innovative firms, in addition to higher Human Development Index (HDI) levels (RICYT, 2008). Economies committed to innovation pay higher salaries and tend to create more rigorous demand, forcing companies to offer differentiated, technologically advanced products of higher quality. This scenario compels the private sector to move continuously toward more aggressive strategies with regard to its competencies and to redesign its product offerings constantly.



Students in a well-equipped classroom learn research fundamentals and develop curiosity about the world around them that could lead to a career in science. (photo credit *El Tiempo*)

ORIGINS

A wide variety of reasons are cited in explaining the relative technology deficit of Latin America and the Caribbean. According to one point of view, the reduced size of national firms and little competition in local markets, the result of a long and strict policy of import substitution, favored a course of action that culminated in the importation of technologies with no effort focused on generating knowledge applicable to creating domestic technologies. This strategy, despite having achieved the establishment of diversified industrial structures, created an environment of excessively protected business activity in most Latin American countries (Erber, 2000).

Although this situation was abruptly modified at the start of the 1990s, it is worth noting that during the period of import substitution, most of the region's countries created a scientific and technological infrastructure. The first Latin American organization dedicated to science and technology was founded in 1950 in Mexico. Other institutions emerging during this period include the National Council on Scientific and Technological Development (CNPq),

founded in 1951 in Brazil, and the National Council for Scientific and Technological Research (CONICET), established in 1958 in Argentina. In the decades that followed, the issue was further incorporated into regional agendas based on support for creating infrastructure in universities and human resource training in specific sectors, such as nuclear energy, telecommunications, petrochemicals, information technology, microelectronics and biotechnology.

At the start of the 1990s, despite the heterogeneity of their economies, most of the region's countries opted for a homogeneous policy supported by the opening of markets to international competition and an intense program of privatization, in which a large number of historically government-run enterprises were transferred to the private sector.

These measures produced drastic and irreversible changes in many production chains, provoking the fear that the region would go through a process of generalized de-industrialization, particularly in Argentina and Brazil. The technological progress and organizational changes underway in developed countries forced Latin



The latest electronic technology purchased through an IDB-financed program in Chile helps fishermen fill their ship's hold and return safely to port.

American companies to operate on a more competitive scale in light of competitive standards existing outside the region with regard to the price and quality of products (Radaelli, 2002).

After two decades, the entire region failed to see any abrupt changes in productivity indicators, which remained much lower than those of developed economies. As a result, the opinion emerged that the tacit and cumulative nature of knowledge and the countless forms of interaction-based learning require a complex and dynamic set of policies to support and develop the business sector that the free market had been unable to establish locally. Thus, the incorporation of technology in products and processes and its subsequent incorporation in companies, already occurring with greater intensity at the start of the new century, created a set of instruments for promoting local long-term development (Katz, 2006).

A series of incentives with varying degrees of intensity were conceived as a catalyst for local innovation and joint cooperation between public research institutes and private

companies. These included not only tax-related incentives, but also those aimed at financing basic and applied research, promoting collaborative associations between universities and firms, protecting intellectual property, and developing aspects related to public sector acquisition policies (Iglesias, 1999).

It was believed that these mechanisms could be effective in creating access for private investment, primarily because scientific and technological advancements utilized are not fully accessible to the investor. They instead spread through the social fabric as a result of external benefits utilized by other firms in other public and private projects and by entities involved in a wide variety of sectors.

Thus, a new perspective arose in Latin America in which industry, government and universities were seen as having specific competencies that can expand when combined. Nevertheless, in some countries, many innovation-centered industrial policies took too long to be developed and implemented, largely due to a lack of consensus regarding their importance.



The IDB has consistently supported research and development.

REGIONAL IDIOSYNCRASIES

Science and technology policy in Latin America reflects characteristics derived from a broader historical perspective, one in which institutions and concepts were assimilated. Its scope is generally limited due to a decision-making process concentrated in various public institutions, where a low level of coordination tends to generate a loss of adherence to, and focus on, the plans and goals of the policy (Herrera, 1995).

Furthermore, support for research occurs primarily through public research institutes and universities, generating a concentration of resources and creating a level different than that observed in advanced nations whose resources for this purpose are concentrated in private firms.

Moreover, in Latin American countries, firms tend to interact with foreign technology providers rather than with those that are available in the local market. The relationships are thus unidirectional in nature. The origin of this behavior seems to involve a lack of clarity with regard to defining national and business strategies. The continuation of this process may

be accepted solely as a condition for transition or as a way of nourishing local markets with the technologies that they lack, with an eye toward gradually enabling the industry in a structured manner through numerous channels of transfer.

With regard to research and development investment as a percentage of GDP, it is clear that most Latin American countries allocate few resources to this area. In fact, while practically every single country classified as developed showed an increase in investment between 1996 and 2006, only a handful of nations in Latin America dedicated more resources to this field in 2006 than in 2001 (Figure 7.2). In absolute terms, the level of investment carried out by the region's countries represents only 4 percent of that of the United States and 6 percent of that of Europe (OECD, 2008).

This reality contrasts strikingly to that of countries on the cutting edge of technology. In emerging economies, adherence to innovation policies has been marginal and regarded as yet another item on the agenda of individual politicians. In advanced economies, however, increasing formal research is a priority in govern-

(Continued on page 184)

Interview with Conrado Varotto



As Executive and Technical Director of the National Commission on Space Activities (CONAE) in Argentina, Conrado Varotto has been at

the forefront of one of Latin America's most prominent scientific organizations. With a bachelor's degree and a doctoral degree in physics from the Balseiro Institute of Universidad Nacional de Cuyo, Professor Varotto has served as a Research Associate in the Department of Materials Science and Engineering at Stanford in the United States. He has been General Manager of INVAP, an Argentine company that develops nuclear, aerospace, medical and industrial technologies, and National Director of Planning, Evaluation and Monitoring for Argentina's Ministry of Science and Technology.

How would you analyze what has happened in Latin America with regard to science over the past half-century?

I believe Latin America hasn't done so badly compared to the rest of the world. It depends on the country, the issues and the circumstances. What I do believe is that over the past half-century there has been a bit of confusion. When decisions had to be made with respect to promoting science and technology much more aggressively in our countries, sometimes mistakes were made or there were misunderstandings. The proof is that whenever our graduates in the hard sciences went to other countries, they played a very important role.

What happened after that point?

I believe everything has happened. For one thing, lasting educational and research institutions were created. Possibly the greatest error committed in the area of scientific research—and this didn't just happen in Latin America—consisted of trying to reproduce the United States model after the end of the Second World War. Their model

was substantial and almost all-encompassing. It was made for a country that had an enormous amount of resources. It took us a long time to understand that we had to focus our resources on selected issues because, as we say in Argentina, we don't have enough skin to cover everything.

What is the benefit of changing one's focus?

It gives you the ability to be better in clearly defined areas. Afterwards, like a virus, interest spreads and starts to grow in other areas. In this way you develop a spectrum of knowledge in a few strong areas, separated from one another, and those strengths grow so much that other areas get carried along with them.

Do you believe the economic crises that have occurred in the region have affected progress in this area?

The substantial budget cuts implemented after the crises that occurred affected everything. But in my opinion, what is really causing a major change is the understanding that you have to focus on specific types of issues.

What about the private sector's role?

A few years ago, I was invited by the Italian government to study this in cooperation with other colleagues. Beyond the differences with Latin America, what was interesting was finding something that applies to all our countries: you have to understand the economic structure. The conclusion was quite simple: generally speaking, the greater the private investment that is placed in research and development, the greater the impact on the productivity structure. In countries with a sizable measure of small to medium-sized enterprises, governments have to compensate for the lack of investment to a greater proportion than in other nations where larger-sized businesses predominate.

Does a scientific community exist in Latin America?

There are many issues that are being worked on jointly. One example is the space situation, in which Argentina is promoting a regional model similar to the European experience. In other words, the goal is to do it at the international level more than working together at the personal level.

Are people better trained nowadays?

I don't know how to answer that. I've had to work through very difficult projects in my professional life, and I've never had the problem of not having someone to work with. People have shown in all cases that they are capable and their training is quite good.

What would you like to see in this field, going forward?

I would really like to see a regional space agency, one that's equipped and operational, because this deals with a very critical issue. For that purpose, what is most important is brain power. Every country can contribute something. If we were able to design joint projects among countries, we would see some outstanding achievements in Latin America.

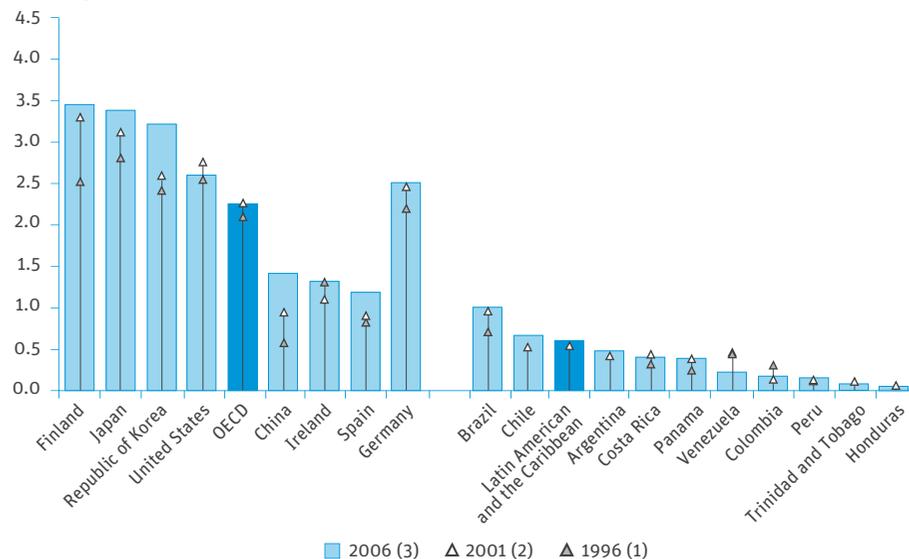
And in the area of science in general, what would you like to see?

I believe Latin American countries have understood the importance of science and the region is working hard on it. But no less important is the fact that the Inter-American Development Bank itself has made the decision to support projects with heavy scientific and

technical content. The IDB's decision to take on a project with a broad scope on the frontiers of science and technology, which was the case with us, was very significant. Therefore, over the next 10 years, I'd like to see the Bank increase this type of support considerably and spark interest in other banks and other sources of financing along the same lines.

Figure 7.2 Investments in Research and Development, Selected Regions and Countries, 1996–2006

(Percentage of GDP)



Sources: OECD (2008) and RICYT (2008).

(Continued from page 181)

ment strategies, with clearly defined goals and objectives (Table 7.1).²

The reasons why it has been difficult to explore and develop innovation-focused policies in Latin America include the fact that most of the region's infrastructure has been geared toward the production of natural products exported as raw or semi-processed

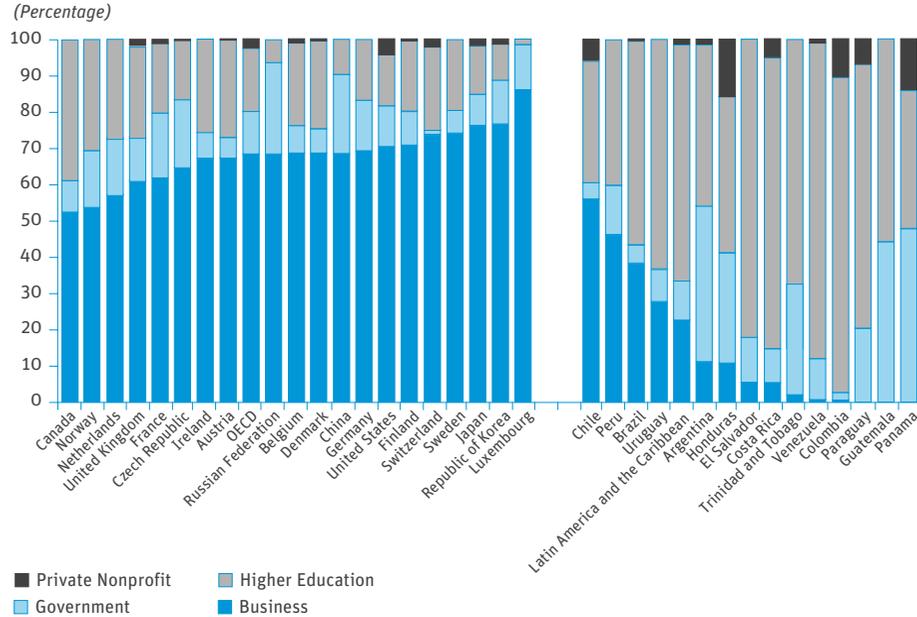
materials, while the incorporation of machinery and equipment occurred through imports from more developed nations. In many Asian countries, the importation of technologies has formed part of their industrialization strategies. In Latin America, however, there is a disconnect between strategies and the activities of the region's firms (IDB, 2001).

Table 7.1 Targets for National Investment in Research and Development (Percentage of GDP)

Country/Region	Target (Percentage)	Target Year
Austria	3.0	2010
Belgium	3.0	2010
China	2.0	2010
Czech Republic	2.1	2010
Denmark	3.0	2010
European Union	3.0	2010
Finland	4.0	2011
France	3.0	2012
Germany	3.0	2010
Greece	1.5	2015
Holland	3.0	2010
Hungary	1.4	2010
Ireland	2.5	2013
Norway	3.0	2010
Republic of Korea	5.0	2012
Russia	2.0	2010
Spain	2.2	2011
Sweden	4.0	2010
United Kingdom	2.5	2014

Source: OECD (2008).

Figure 7.3 Total Investment in Research and Development, Selected Regions and Countries, by Financing Source



Sources: OECD (2008) and RICYT (2008).

Thus, another characteristic of Latin American science and technology systems becomes clear. There is a dependence on public spending injected into institutes and universities for conducting innovation work without the

involvement of private firms in directing internal research and development activities. This is in sharp contrast to advanced economies, where investments are primarily financed by firms (69 percent); in Latin America, public investment is mostly responsible for funding activities aimed at dynamizing innovation-related issues (62 percent) (Figure 7.3).³

On a much different path, in some advanced countries, private investments are reporting significant growth. In the United States, annual growth between 2001 and 2006 totaled 1 percent; in the European Union, it reached 1.4 percent; in Japan, 4.4 percent; and in China, 23 percent. Despite the varying intensities with which advanced countries are involved in corporate research and development activities, they all share a common characteristic: decreased government financing. This decrease reflects a change in the style of government support from direct to indirect backing (tax incentives and economic subsidies). These methods of financing are now starting to be used in Latin America.⁴

A NEW PLAN

The concentration of innovation financing in the hands of the government has significant implications with regard to the investment dynamic and the capacity to generate investments over the long term. This is due to the fact that, despite advancements in the regulatory systems of these countries, restrictions on the participation of the private sector remain in place. It has been difficult to adapt public financing to the internal research activities of the private sector, especially in the case of small and medium-sized enterprises (SMEs). Taking into account only those firms that developed a product or process innovation in Brazil between 2000 and 2003, only 16.5 percent of Brazil's 30,000 innovation-focused companies attributed significant importance to internal research activities (IBGE, 2003).

Wherever innovative efforts are being made, Latin American firms tend to opt for modernizing machinery and equipment that already exist on the market. Process innovations tend to be superior to product innovations as they are generated by their own providers. The reduced interaction between scientific knowledge as embodied in

universities and research institutes, the industrial application of this knowledge and the meager efforts undertaken by industrial firms in conducting internal research activities reinforces vicious cycles where no improvements of any kind take place.

The low level of corporate research and the reduced importance given to this activity and to the processes for incorporating new technologies, along with the risks associated with innovative activities, tend to discourage investments in innovation and increase the distancing of public institutions, as reflected in the growing difficulties in accessing public financing.

The interaction between industry and academic institutions is much lower than it should be. Researchers must generally divide their time between routine class activities and administrative tasks, leaving them little time for research and even less time for searching out or partnering or interacting with businesses.

In fact, few firms maintain frequent contact with universities and research institutes. Among the few that cultivate a reasonable level of interaction, there are frequent complaints that the pace at which the university moves lags behind

(Continued on page 188)

Box 7.1 The IDB's Involvement in Science, Technology and Innovation Projects

Throughout its 50 years of operation, the IDB has closely followed the scientific, cultural, social and competitive changes in the area of science, technology and innovation (STI). The guidelines and action strategies in the science and technology policies of the member countries were reviewed systematically with an eye toward incorporating new mechanisms or tools capable of stepping up competition and social well-being in the Western Hemisphere. The importance of the IDB's involvement in this area stems from the affirmation that activities in scientific innovation are a significant part of the changes that have recently emerged on the competitive scene, and such activities are based on the ability of businesses to create new products and processes from internally accumulated knowledge and knowledge that is available outside their countries' borders.

Science and technology, as an exclusive field of analysis and project management, became a specific division of the IDB in the mid-1990s with a dedicated technical team. This factor has created several challenges. The first challenge stems from the diffuse, interdisciplinary nature of science and technology, which can be employed in the most diverse projects, including those in agricultural research, biotechnology, infrastructure, the environment, education and health. This feature requires that the internal divisions have the ability to integrate and work together on the same scale proposed for industrial and innovation policies. The second challenge is for countries that apply for support to be able to identify the most representative projects in terms of increased scale and scope in the incorporation of self-sustaining competencies. This is no mean effort for countries with such diverse characteristics as those of Latin America and the Caribbean. Highly trained technical teams are required: teams that are focused on projects and that have a great ability and willingness to establish joint bodies with the private sector and the countries with which they share projects.

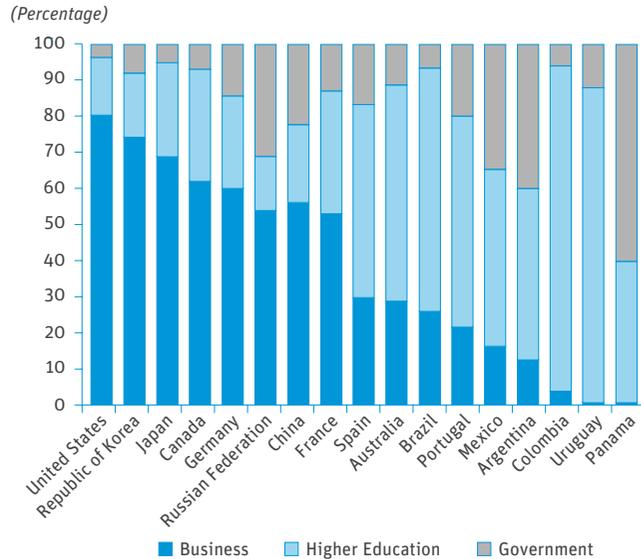
It is possible to group the IDB's performance into three key periods, starting with the first STI-related loan approved in 1962 for Peru, which was planning to create the Basic Science Department of the Universidad Nacional. The emphasis for projects during the first period was placed on creating science and technology infrastructure at universities and research institutes.

Time	Objectives	Primary performance
1961–87	Develop research capacity	<ul style="list-style-type: none">• Physical and human infrastructure (primarily in universities).• Laboratories and research institutes.
1988–98	Achieve institutional strengthening	<ul style="list-style-type: none">• Applied and experimental research development.• Programs focused on university-business interaction.• Financing of development agencies.
1999 to present	Develop national innovation systems	<ul style="list-style-type: none">• Technological competitiveness.• Innovation in the private sector.• Technology infrastructure and research networks.• National and regional innovation systems.

Departments such as physics, chemistry, mathematics and biology received support for purchasing books and setting up laboratories. During the second period, the focus was on institutional strengthening and the establishment of public institutions geared to support and coordinate scientific activities in the region, and technology transfers to support the diffusion of technologies and innovation.

The IDB's third phase is in full swing. The emphasis is now on strengthening national and regional innovation systems: projects focused on articulating a combination of needed policies and institutional advancements with regard to the support of innovation and the catalytic mechanisms of scientific advancement for key areas tied to each country's technologies and projects. The priority is to modify, establish and accelerate private investment in research and development, to build consortiums among businesses, especially among small and medium-sized enterprises, and to develop standards, metrology and quality control systems.

Figure 7.4 Researchers by Sector of Employment, Selected Countries, 2005



Sources: OECD (2008) and RICYT (2008).

the speed of business activity. This discourages some firms from establishing long-term contracts and cooperative associations. More frequently, universities look for support and very specific solutions from companies, and when they do find a solution to a problem, the solution will often be specific, precise, sporadic and unsuitable for building a long-term process of interaction based on contracts that clearly define the roles

to be performed and the mutual benefits associated with interaction.

Most researchers in the region are involved in research activities led by public institutes or are assigned to universities. Also, it is clear that Latin American researchers receive only a small fraction—between 40 percent to 60 percent—of what an equally qualified professional receives in Europe or Japan, for example (Figure 7.4). Due to the financial and institutional fragility of Latin American economies, it is extremely difficult to guarantee a continuous and stable flow of resources. This tends to negatively affect the type of research conducted and the ability to keep well-qualified professionals in the local market.

Furthermore, these types of activities demand long-term planning. When they are not carried out or if resources are restricted, long-term projects become unfeasible. In a macroeconomic crisis environment, projects tend to be postponed or interrupted as they lose their priority in comparison to more urgent events. Alongside these waves of interest in science and technology policy, there has been a backslide in terms of the de-motivation of work teams, the obsolescence of



With the help of a US\$3.5 million IDB loan, The Bahamas is using the latest technology to modernize and expand land administration and to strengthen tax collection through improved registration and taxation of real property.

equipment, and an increase in the gap between Latin America and other more advanced countries.

Although some indicators are intangible, multidimensional and practically impossible to quantify in economic terms, the strength of the data on patent registrations and scientific production cannot be ignored. Their analysis yields another paradox when observing the structure of science and technology in Latin America. In an environment of scarce and volatile resources, the concentration of funds in government bodies, scarce investment in the private sector and the concentration of qualified human resources in public institutions where their productivity is measured by the production of scientific articles, the expected occurs: copious scientific production fails to translate into patent registrations.

For instance, scientific production in Brazil now represents nearly 2 percent of the worldwide total and 48 percent of Latin America's (CAPES, 2007). In 1990, Brazil's share of global scientific production was only 0.63 percent. The substantial increase was achieved thanks to the government's efforts to expand the human resources involved in science and technology by granting scholarships.

Nevertheless, despite the advancement of scientific production, a smaller part of it is being converted into practical products and processes in firms. The factors that explain the low level of patent registration are cultural, structural and financial in nature. Nevertheless, the data show which companies are more disciplined in making use of advancements in knowledge in its most varied dimensions. A study conducted by the World Intellectual Property Organization (WIPO) in 2007 showed that, while patent registration activity worldwide grew by 7 percent in 2005, in Brazil, the country with the highest number of recorded patents in Latin America, this figure dropped by 13.8 percent in 2005 versus 2004.

Another comparison of the efforts made can be drawn by analyzing the number of patent applications submitted. Despite an increase in absolute numbers, the region demonstrates little stamina with regard to patent registration. In 1980, South Korea had submitted 33 patent applications to the United States Patent Office. In the same year, China submitted 7 applications, while Brazil sent in 53, Argentina submitted 56 and Mexico sent in 79. In 2004, the number of applications grew consider-

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Interview with Flora Montealegre Painter



Flora Montealegre Painter is Chief of the IDB's Science and Technology Division. With more than 20 years of experience in the

field of economic development, she joined the IDB in 2000 after having worked at Coopers & Lybrand (now known as PriceWaterhouseCoopers). Painter holds a master of business administration degree from the University of Maryland and a master of science in economic development degree from Georgetown University in Washington, D.C. She is also a graduate of Harvard University's Science, Technology and Innovation Policy Program.

What is your interpretation of the changes that have taken place in the Western Hemisphere with regard to science and technology over the past 50 years?

On the whole, the changes have been positive, particularly with regard to the institutionalization of science and technology policies in many countries in the Western Hemisphere and the creation of a public infrastructure for the promotion of research and development (R&D). Nevertheless, when progress indicators for the region are compared to those of countries with more developed economies, the technology deficit is noticeable and, unfortunately, it's increasing. Minimal R&D investment from the business sector is particularly noticeable. The past 50 years have seen some profound technology transformations and changes that have occurred at an increasingly faster pace. Support for development of Latin America's innovation capacity unfortunately hasn't been commensurate with the needs or challenges this scenario presents either. A concerted

effort to increase investment in science, technology and innovation significantly is required from the region's political leaders, international development agencies and the private sector in order to be able to turn this situation around.

What do you think the IDB's role has been in what has happened, and what positive things would you emphasize?

Since its creation, the IDB has been a very important player in the region's science and technology development. In the beginning, from the sixties to the eighties, the Bank's policy placed a high priority on investments in human and physical infrastructure, especially in universities and research facilities. By the nineties, this approach became more focused on support for institutional strengthening, with an emphasis on supporting applied research and joint academic-business research through competitive funds. Now, our approach stresses the systemic features of technological innovation and its relationship with productivity and competitiveness. I would point out

that the IDB has played a significant role in technological and scientific development in the region, not only through its loans, but also through its technical assistance, program evaluations and studies that have allowed for sharing experiences and best practices with other countries and generating new policy approaches and promotional design tools.

Looking to the future, how do you see this issue developing, and what should the IDB's role be?

A greater investment in science, technology and innovation (STI) is a must for future economic development and the generation of prosperous societies in the Western Hemisphere. Nowadays, science and technology permeate all fields of human development, from the way we communicate with each other to the clothing we wear and the food we eat. The food crisis and the energy crisis are just two examples of the pressing need to drive R&D in critical areas like the generation of renew-

able energies and biotechnology. If the region's countries don't improve their capacity for science, technology and innovation, in the near future, it will be hard for them to take advantage of technological revolutions and acquire and apply cutting-edge technologies such as nanotechnology, biotechnology, computer technology and materials technology in order to enhance economic development and the common good. Therefore, I believe that supporting STI must not be an isolated exercise, but rather a vital part of the development policy of each country. The IDB's role must be consistent with this and lend a strong push to investment in science, technology and innovation, within its development strategies in the region's countries. I am concerned that the impact of the financial crisis may result in a reduction in STI investment in the near future, as has happened in other crises. It would affect future development in the region, since continuity in investment is crucially important for its cumulative effect.



The owner of a bottling plant discusses his firm's operations as part of an IDB program that fostered knowledge sharing among private enterprises in different countries.

(Continued from page 189)

ably, especially among the first two countries mentioned, South Korea (13,700) and China (1,700), but less so in Brazil (287), Argentina (103) and Mexico (179) (WIPO, 2007).

Recent macroeconomic performance indicators for the region's countries are generating positive expectations with regard to programs, organizations and objectives in the area of science, technology and innovation. Taking only Latin American countries into account, this analysis confirms the establishment of a scenario in which significant progress has been made compared to the situation a few decades ago. The primary challenge, and perhaps the primary measure of the success or failure of these policies, is the increase in innovative activity driven by firms, as this is where innovation should occur, with the growing incorporation of skilled labor (IDB, 2001).

FINAL CONSIDERATIONS

Some studies show that the skill levels built by Latin American firms are remarkable. Several countries have been successful in improving products, processes and technologies for organiz-

ing production. Despite the fact that these technological efforts are less technically sophisticated in comparison to those of OECD members, they are associated with countless forms of learning through reverse engineering. There have been important advancements during crucial phases in the process of creating local competencies and technological knowledge, but little has been achieved in advancing toward more sophisticated stages, where new technological knowledge resides. That is precisely what the region needs: a move toward more sophisticated stages in which the scale of production is universal, not confined to the internal market, and closer to the cutting edge of science and technology (Figure 7.5).

Firms that eagerly absorb knowledge and technologies through countless channels, including the combination of specialized suppliers with internal research, do indeed exist; ignoring them is a short-sighted and dangerous position to take. In some industrial sectors, innovation activity has become imperative. In activities closer to the cutting edge of technology, such as information science, software development, custom-made

Box 7.2 The Importance of Innovation

*By Ana María Rodríguez**

In 2008 Latin America and the Caribbean completed a six-year cycle of expansion, the greatest and most long-lasting of any since 1980, and the second most significant since 1950. But despite this encouraging development, the gap between the region and more developed regions did not close; in fact, it may be widening. For this reason, it is essential to draw on the experience of recent decades to put in place better means for achieving solid gains in productivity.

With the experience of other economies, as well as economic theories that emphasize innovation and entrepreneurial capacity, there are now solid tools available for accelerating productive development in the region. A brief look at recent history can help show the way.

In the 1960s and 1970s, policies for directly intervening in the market proved the ineffectiveness of price setting at the central level, general subsidies, and market protection. Direct controls, which seemed at first like a good idea, discouraged innovation, weakened the entrepreneurial spirit, and encouraged businesses to pursue profits rather than productivity. The informal sector continued operating on the fringes of these interventionist policies, but with serious limitations on the full development potential of its businesses and entrepreneurs.

Shortcomings of the direct interventionist model were becoming clear in the 1970s, but it was the financial crisis of the 1980s that ultimately sparked demands for new policies to support production. In the midst of debt and fiscal crises, and with poor results from price and market interventions, policies tended to swing the other way, relegating all decision-making to an invisible hand, despite market imperfections.

Structural reforms put in place at the end of the 1980s and in the 1990s helped to reestablish the region's economic growth. The benefits of better macroeconomic management became evident, but not the hoped-for productive transformation. With few exceptions, the region did not move from an economic structure based on sectors of low productivity to one led by sectors capable of adding value and knowledge. In the economies that stood out as exceptions, gains in productivity achieved through free market reforms and free trade quickly began to diminish.

Globalization, technological change, and the growth of technological and service markets, among others, once again put the spotlight on private firms and entrepreneurs. By their very nature, economies are dynamic, and entrepreneurs and innovators are the ones with the power to drive the process of sustained growth.

History has provided the region and the IDB with basic lessons on how to fashion policies for achieving productive development: direct market intervention is inefficient and paralyzes the most productive and efficient economic agents; balanced macroeconomic management is fundamental for economic growth and to provide suitable conditions for the economic agents that drive this growth; productivity gains are primarily achieved by entrepreneurs and innovators who accept risks and seek profits; regulation (not intervention) helps to reduce market flaws that impede competition among innovators and entrepreneurs; and microeconomic policies can encourage firms and business leaders to adjust to changing economic conditions.

In the future it will be necessary to design policies that combine evenhandedness with selectivity, making it possible to leverage market reform with instruments and policies that mitigate externalities associated with the process of change and breakdowns in coordination and information, and which encourage those sectors best capable of generating productivity gains. Since many of the elements responsible for productivity are not distributed evenly, it will be necessary to apply a territorial approach.

There will always be innovators and entrepreneurs, people who hold the potential for dynamic and sustained economic growth. This enormous potential will be realized through the application of policies that encourage innovation and productivity to take advantage of market reforms and opportunities in the global market.

* Ana María Rodríguez is the IDB representative in Peru. A graduate of the Universidad de Los Andes, in Bogotá, Colombia, and with a master's degree in economic development from Williams College in the United States, she worked in a number of financial institutions in Colombia before joining the IDB in 1991.

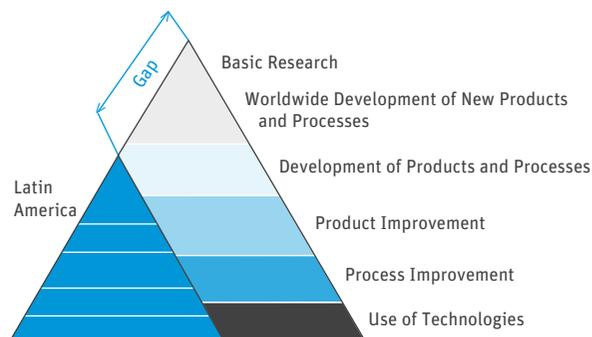
capital goods, aeronautics, medical equipment and applied biotechnology, firms must contract with suppliers that use cutting-edge machinery and equipment while maintaining an adequate internal base for managing such increasingly sophisticated machinery and equipment.

Recent advancements in regulatory frameworks for innovation in the region cannot be denied. They synthesize efforts and demands from different industrial and academic areas, which will favor innovation during the coming years. Meanwhile, important adjustments will be needed so that a

greater number of firms will understand the real necessities of organizational restructuring, innovation and management, training and modernization. Likewise, it will be necessary to improve agencies that support and encourage innovation in order to debunk the idea that innovation only occurs in more dynamic sectors with greater technological content.

The countries of Latin America have an impressive number of professionals working in science and technology, but they need to do more. Firms need to accept that current practices require economic agents to adopt and disperse new technologies and processes that apply to production. While companies must be conscious of their technical and financial fragility and respond rapidly in order to correct distortions and avoid an inefficient allocation of resources, the importance of public action also cannot be overemphasized.

Figure 7.5 Levels of Technology Training in Latin American Companies



Source: Adapted from Katz and Bercovich (1993).

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- ¹ For more information see the Diagnotec Internet page: http://www.diagnotec.cl/Sitio_web/index.php?fuseaction=Espublico.Servicios&expand=yes&azul=productos_servicios.
 - ² Between 1992 and 2002 the Finnish government carried out a national technology initiative that selected areas that would receive government support to improve competitiveness: investment in research and development and in training in human resources and digital inclusion policies, among others. Ireland is another example where, despite its small territory, more than 1,000 foreign firms operate in highly advanced areas such as software, electronics, pharmaceuticals, and biotechnology.
 - ³ For more information, see the RICYT Internet page: www.ricyt.org.
 - ⁴ Meanwhile, important mechanisms to encourage innovation are still lacking, or are in their earliest stages, in the countries of Latin America. Among them is risk capital, which is a powerful instrument for supporting, for example, the creation of technology-based firms. Brazil, in partnership with the IDB, recently undertook major initiatives at the national level through the Brazilian Innovation Agency (FINEP) and the Brazilian National Development Bank (BNDES).



Shades of green. Seedlings from a nursery in southern Mexico are planted on denuded hillsides in a reforestation program carried out by a local conservation organization. Rural people see for themselves that environmental protection preserves the soil and water sources on which they depend. The IDB supports projects to protect water, soil and biodiversity, as well as large-scale programs to strengthen institutions that have the legal and technical responsibility to protect resources for future generations.

VIII The Future of the Environment

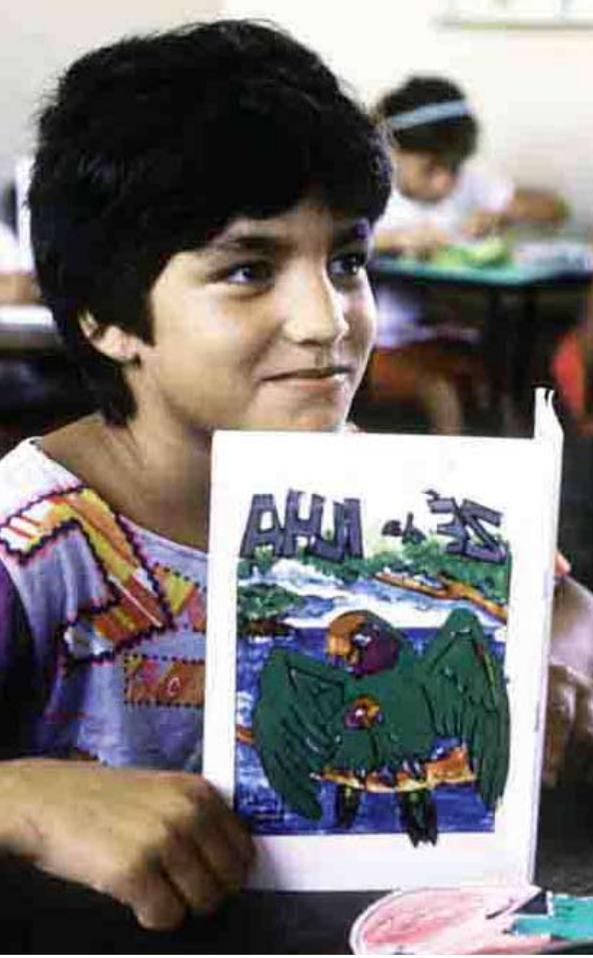
The article appeared in Lima's *El Comercio* at the end of May 2008. In her report, journalist Nelly Luna told of how the snow cap on Mount Pastoruri, the most visited snow-covered mountain of Peru's Cordillera Blanca mountain range, could no longer be considered a glacier.¹ "I don't think it will be more than 10 years before it melts completely," said a geologist quoted in the article. Similar stories, supported by documentary evidence, are told in other countries of the region that have or have had snow-capped mountains or glaciers. In all cases, not only is thawing undeniable, but its pace has quickened over the last few years.

Evidence such as this constitutes one more example of the impact of global warming on the region, a phenomenon that has become more and more noticeable over the last half-century and that is of increasing concern to academics, leaders and the general public. Without a doubt, climate change caused by increasing

concentrations of greenhouse gases in the atmosphere, and the degradation of ecosystems and loss of biodiversity, represent the most significant environmental problems of the twenty-first century and some of the greatest global challenges facing humanity today.

As paradoxical as it may seem, this process has been accompanied by a greater institutional strengthening in many Latin American countries, characterized by the emergence of environmental protection agencies, developing regulations and greater awareness among the region's inhabitants. This does not mean that degradation has been avoided, but the occurrence of isolated, successful experiences gives cause for hope that the region can make significant contributions to the fight against global warming as it continues to make progress in the environmental arena.

Such objectives are especially significant in light of the crisis affecting the world economy as of early 2009. In the face of the financial difficul-



Children discover a new world of nature in a school program financed by an IDB national environmental fund in Brazil.

ties experienced by countries and the private sector, there is valid concern that efforts to promote clean energy and moderate the use of fossil fuels might fail due to cutbacks in programs and subsidies and the noticeable reduction in the price of energy inputs. The change in the relative prices of fuels may dilute the sense of urgency concerning a matter that requires more action than talk.

That said, the evidence that proves the reality of global warming is alarming. The fourth report of the Intergovernmental Panel on Climate Change (IPCC) confirmed that the warming of the atmospheric system is unmistakable, as already shown by the increases observed in average air and ocean temperatures throughout the world, the general thawing of permanent snow and ice, and increased sea levels (IPCC, 2007).

Additionally, the report indicates that world emissions of greenhouse gases as a result of human activities have increased since the pre-industrial age—by 70 percent between 1970 and 2004—and that much of the rise observed in average global temperatures since the middle of the twentieth century is very likely due to the increase

in these man-made emissions. Should a rate of change equal to or higher than the present one continue, warming will further increase and the world's climate system will undergo numerous changes in the twenty-first century (IPCC, 2007) (Table 8.1).

This scenario would be disastrous for the planet in general and for Latin America and the Caribbean in particular. According to projections formulated for the region up to the middle of this century, increases in temperature and the corresponding decrease in soil humidity would cause a gradual substitution of grasslands for tropical forests in the eastern part of the Amazon. Moreover, semi-arid vegetation would gradually be replaced by the vegetation of arid lands and, in general, significant losses of biodiversity could occur, with the extinction of species in many tropical areas of Latin America.

As if all of this were not enough, the yield for some important crops would diminish, and with it livestock activity, with adverse consequences for the stability of the food supply. Although the yield of products such as soybeans would improve in temperate areas, the number of people threatened by hunger would increase overall. In

Table 8.1 Examples of Climate Change and Extreme Climatic Phenomena

Projected Changes	Projected Effects
Higher maximum temperatures, more hot days and heat waves in nearly every area of the planet.	<ul style="list-style-type: none"> ▲ Mortality and incidence of serious illnesses among the elderly and the rural poor. ▲ Heat stress affecting livestock, wildlife and vegetation. ▲ Risk of damage to various crops. ▲ Demand for electricity to power refrigerators and air conditioners. ▼ Reliability of energy supplies.
Higher minimum temperatures, fewer cold or freezing days in nearly every area of the planet.	<ul style="list-style-type: none"> ▼ Human mortality and birth rates related to the cold. ▼ Risk of damage to various crops. □ Distribution and impact of certain pests and disease vectors. ▼ Demand for energy.
Increased intensity of rainfall.	<ul style="list-style-type: none"> ▲ Flood damage. ▲ Soil erosion. ▲ Flood surges could overload the aquifers of some flood plains. ▲ Pressure on public and private disaster relief and security systems in the event of flooding.
Drier summers in most mid-latitude continental areas, with an increased risk of drought.	<ul style="list-style-type: none"> ▼ Crop yields. ▲ Structural foundations damaged by soil contraction. ▲ Risk of forest fires. ▼ Quality and quantity of water resources.
Increase in the maximum intensity of tropical hurricanes and in the intensity of mean and maximum rainfall.	<ul style="list-style-type: none"> ▲ Risk to human life; risk of epidemics and infectious diseases. ▲ Coastal erosion and damage to coastal infrastructure. ▲ Damage to coastal ecosystems such as coral reefs and mangrove swamps.
More severe droughts and flooding in many regions in connection with El Niño.	<ul style="list-style-type: none"> ▼ Productivity of farms and pastures in drought- and flood-prone regions. ▼ Power generation potential of drought-prone regions.
Greater variability of rainfall during the summer monsoons in Asia.	<ul style="list-style-type: none"> ▲ Magnitude of damage caused by flooding and droughts in the temperate and tropical areas of Asia.
More severe storms in the middle latitudes.	<ul style="list-style-type: none"> ▲ Risks to human life and health. ▲ Loss of property and infrastructure. ▲ Damage to coastal ecosystems.

Key: ▲ Increase ▼ Decrease □ Expansion

Source: UNEP and SEMARNAT (Secretariat of the Environment and Natural Resources, Mexico) (2006), on the basis of the IPCC's *Third Assessment Report*, 2001.

addition, changes in precipitation patterns and the disappearance of glaciers would seriously affect the availability of water for human, agricultural and hydroelectric consumption. An even greater impact would be felt in an increased occurrence of natural disasters brought on by drought or periods of more intense rain, and in the increased vulnerability of coastal areas as a result of elevated sea levels and extreme climatic phenomena (IPCC, 2007).

However, despite the environmental degradation and destruction that have been reported throughout Latin America and the Caribbean over the past few decades, the region continues to be very rich in renewable natural resources. Seven of the world's 12 most megadiverse countries are located there.² Of the eight nations of the world that retain more than 70 percent of their original forest cover, six are in South America, specifically in the Amazon River basin: Brazil, Colombia, French Guiana, Guyana, Suriname and Venezuela. The vast abundance of natural forests found in these states, which are ecologically intact and experience relatively low levels of disturbance (also found in

Central America and Mexico), have a unique significance for the earth's survival (Rodríguez Becerra, 2002).

Additionally, the region has the world's largest reserve of arable land, with an agricultural potential estimated at 576 million hectares, equivalent to 29 percent of its total territory. Latin America could feed its entire population in the year 2030 by cultivating only 4 percent of its surface with high-ratio land production and input techniques and using traditional production technologies on another 20 percent (Rodríguez Becerra, 2002).

The region is also rich in water. With only 15 percent of the world's territory and 8 percent of the world population, it receives 29 percent of global precipitation and has one-third of the world's renewable water resources. However, there are notable differences in the supply of water and its availability throughout the territory. Three of its main hydrographic areas—the basins of the Gulf of Mexico; the Brazilian South Atlantic; and Parana, Uruguay and La Plata—concentrate 40 percent of the region's population in 25 percent of the territory, with only 10 percent of total water resources. Many areas in Mesoamerica, the Andes,



On Colombia's coast, a project to plant mangroves will reestablish the role of these important ecosystems in preventing erosion and providing sanctuary for marine life.

northeastern Brazil and the Caribbean suffer from a recurring or chronic lack of water (UNEP and SEMARNAT, 2006).

INSTITUTIONAL CHANGE

Such a scenario lends a clear sense of urgency to an issue that is relatively new for Latin Americans, despite the fact that during the Colonial period and after independence different pro-conservation decrees and laws were enacted; for example, the decrees promoted by Simon Bolivar for Bolivia, Colombia, Ecuador, Peru and Venezuela, which included one issued in Chuquisaca, Bolivia, on December 19, 1825, pertaining to “conservation measures and the good use of water” and one issued in Guayaquil, Ecuador, on July 31, 1829, pertaining to “measures of protection and better use of the nation’s forest wealth” (UNEP and SEMARNAT, 2006).

During the nineteenth century and the beginning of the twentieth century, regulations relating to the exploitation and use of renewable natural resources were enacted, and public agencies specializing in the management of these resources were created. These agencies

were frequently set up as divisions or entities attached to ministries, most frequently Agriculture and Public Works. In the 1930s and 1940s, legislation was introduced to protect forests, soil, water and fauna—particularly fishing resources—pointing to a push toward regulation.

Special mention must be made of the 1940 approval of the Convention on Nature Protection and Wildlife Preservation in the Western Hemisphere in Washington, D.C., within the framework of the Pan-American Union, which would later become the Organization of American States (OAS). The objective of this convention is “to preserve in their natural habitats all species and genera of native American flora and fauna from extinction, and to preserve areas of extraordinary beauty, striking geological formations or regions of aesthetic, historic or scientific value.” This agreement was instrumental in driving the creation of nature parks throughout the entire continent.

The years that followed the end of the Second World War were marked by a growing effort to regulate the issue. However, it was not until the United Nations Conference on the

(Continued on page 206)

Interview with Janine Ferretti



Janine Ferretti is the Chief of the Environmental Division of the Sustainable Development Department, Inter-American Development Bank.

A Canadian by birth, Ferretti has been responsible for the development and execution of a series of initiatives, including the new Environment and Safeguards Compliance Policy and the Sustainable Energy and Climate Change Initiative, as well as for distributing information on sustainability. Ferretti joined the Bank after finishing her term as Executive Director of the North American Commission for Environmental Cooperation (CEC).

How have you viewed the change that has taken place in Latin America regarding environmental awareness during the last half-century?

Environmental awareness has undergone several changes over the past 50 years, because at first the issue was seen as a problem of rich countries, one of the expected results of economic growth. Today, the governments of Latin America and the Caribbean have adopted sustainable development as a conceptual framework in their efforts to achieve a better quality of life. Additionally, remarkable progress has been made in most of the region's countries. Legislation has been passed and environmental institutions have been created. Also, there are more legal requirements regarding the assessment of environmental impact, emissions of contaminants, land management, citizen participation, and the use and conservation of natural resources. Protected areas have been established in response to the need to conserve the region's biological heritage. Public opinion in the region is getting stronger and more informed on this topic.

What's more, concern about environmental deterioration has spread. Farmers are seeking green alternatives

for managing their crops, businesses are incorporating eco-efficient innovations in their manufacturing systems and fishermen are more and more concerned about the effect that pollution has on water. Urban populations themselves are aware of the costs of air pollution and the implications it has for public health, and many municipal governments have begun to respond to this situation by improving public transportation systems and taking other measures. Public-private associations have sprung up between companies and organizations of civil society that are cooperating to develop solutions ranging from forest conservation to monitoring environmental quality.

What do you believe the IDB's role has been thus far and what would you emphasize positively about what has been done to date?

The Bank has played an important role in helping countries develop environmental institutions and programs. In 1979, the IDB unequivocally recognized the importance of the environment by approving its Environment Policy and was the first multilateral bank to do so. The IDB has been known for its support of environment-

focused programs in such areas as watershed management, regional management of natural resources and protected areas and, more recently, renewable energy and climate change. In addition, the IDB has supported efforts that have contributed to the development of regional awareness. There is also the creation of the Central American Commission for the Environment and Development and the creation of high-level permanent forums like the Forum of Ministers of the Environment of Latin America and the Caribbean.

In looking to the near and distant future, how do you see this issue playing out and what must the IDB's role be?

Climate change is an enormous challenge for the region. Without a doubt, the availability of water and productive areas will be a key concern for various countries since they are deeply involved in development issues. Therefore, one of the Bank's most significant actions in this area is its support of cost studies and what

change would represent in terms of economic and social development for the region's countries. These analyses will help countries make more appropriate decisions regarding their options for energy sources, investment in agricultural infrastructure that takes into account the region's vulnerability to the effects of climate change, the prevention of natural disasters, water use and conserving natural resources. The IDB should strengthen its capacity to support the region's countries in examining these options.

It's also necessary to recognize a challenge that the entire region shares: despite advancements in the institutional and legal framework, the application of environmental regulations is relatively weak. Another challenge is the integration of environment and the economy in policies and programs so as to allow countries to establish and achieve joint objectives. The Bank should be able to help countries forge this new path of advancement in the region's development. The future depends on it.



Forests provide a wide range of environmental services, including resin extracted for the production of turpentine, as in this IDB project in Colombia.

(Continued from page 203)

Human Environment in Stockholm in 1972 that the discussion came to the awareness of the general public. Despite that, the event highlighted the divergence of the positions of the countries that were gathered there, according to their income levels. According to the United Nations, “Stockholm thus marked a polarization between the priorities of economic growth and environmental protection, which has dominated the debate between rich and poor countries and between interest groups within countries for many years, and is still not fully resolved.”³

Despite this circumstance, Latin American countries responded with new regulations and institutional reorganization initiatives⁴ that were later affirmed at the Earth Summit in Rio de Janeiro in 1992. By this time, scientists had already confirmed the existence of the hole in the ozone layer and global climate change, and the concept of sustainable development was adopted.

This position, with some differences, was endorsed by the region’s countries at the Summit of the Americas on Sustainable Development held in Bolivia in 1996 and at subsequent Summits of the Americas, as well as at

the Monterrey Conference on Financing for Development in 2002 and at the World Summit on Sustainable Development in Johannesburg that same year. In addition, although the Kyoto Protocol did not establish gas emissions parameters for developing countries, regional representatives played an active role in the process.

Meanwhile, it was obvious that environmental issues were acquiring a higher profile (Table 8.2). For example, since 1992, 18 countries in the region have “constitutionalized” environmental protection and, in some cases, sustainable development. Also of note was the enactment of new laws and regulations or the updating of existing ones and the criminalization of environmental crimes in some legislation (Rodríguez Becerra, 2008).

Although different reports suggest that enthusiasm for the topic has diminished in the region and, in fact, several countries have gone backward during this decade (Rodríguez Becerra, 2008), Latin American countries rate well on certain lists such as the Environmental Performance Index constructed by Yale University. According to the measurements for 2008, 11 of the 13 developing coun-

Table 8.2 Signatories to International Conventions for the Protection of the Environment
(Year of ratification, acceptance, approval or adherence)

Country	Basel ^a	Cartagena ^b	Biological Diversity ^c	Climate Change (UNFCCC) ^d	Desertification (UNCCD) ^e	CITES ^f	Migratory Species (CMS) ^g	Stockholm ^h	Kyoto ⁱ	Law of the Sea ^j	Montreal ^k	Ramsar ^l	Rotterdam ^m	Vienna ⁿ	Heritage ^o
Antigua and Barbuda	1993	2003	1993	1993	1997	1997	2007	2003	1998	1989	1992	2005	—	1992	1983
Argentina	1991	—	1994	1994	1997	1981	1992	2005	2001	1995	1990	1992	2004	1990	1978
Bahamas	1992	2004	1993	1994	2000	1979	—	2005	1999	1983	1993	1997	—	1993	—
Barbados	1995	2002	1993	1994	1997	1992	—	2004	2000	1993	1992	2005	—	1992	2002
Belize	1997	2004	1993	1994	1998	1986	—	—	2003	1983	1998	1998	2005	1997	1990
Bolivia	1996	2002	1994	1994	1996	1979	2003	2003	1999	1995	1994	1990	2003	1994	1976
Brazil	1992	2003	1994	1994	1997	1975	—	2004	2002	1988	1990	1993	2004	1990	1977
Chile	1992	—	1994	1994	1997	1975	1983	2005	2002	1997	1990	1981	2005	1990	1980
Colombia	1996	2003	1994	1995	1999	1981	—	—	2001	—	1993	1998	—	1990	1983
Costa Rica	1995	2007	1994	1994	1998	1975	2007	2007	2002	1992	1991	1992	—	1991	1977
Cuba	1994	2002	1994	1994	1997	1990	—	—	2002	1984	1992	2001	—	1992	1981
Dominica	1998	2004	1994	1993	1997	1995	—	2003	2005	1991	1993	—	2005	1993	1995
Dominican Republic	1999	2006	1996	1998	1997	1986	—	2007	2002	—	1993	2002	2006	1993	1985
Ecuador	1993	2003	1993	1993	1995	1975	2004	2004	2000	—	1990	1991	2004	1990	1975
El Salvador	1991	2003	1994	1995	1997	1987	—	—	1998	—	1992	1999	1999	1992	1991
Grenada	—	2004	1994	1994	1997	1999	—	—	2002	1991	1993	—	—	1993	1998
Guatemala	1995	2004	1995	1995	1998	1979	—	—	1999	1997	1989	1990	—	1987	1979
Guyana	2001	—	1994	1994	1997	1976	—	2007	2003	1993	1993	—	2007	1993	1977
Haiti	—	—	1996	1996	1996	—	—	—	2005	1996	2000	—	—	2000	1980
Honduras	1995	—	1995	1995	1997	1985	2007	2005	2000	1993	1993	1993	—	1993	1979
Jamaica	2003	—	1995	1995	1997	1997	—	2007	1999	1983	1993	1998	2002	1993	1983
Mexico	1991	2002	1993	1993	1995	1991	—	2003	2000	1983	1988	1986	2005	1987	1984
Nicaragua	1997	2002	1995	1995	1998	1977	—	2005	1999	2000	1993	1997	—	1993	1979
Panama	1991	2002	1995	1995	1996	1978	1989	2003	1999	1996	1989	1990	2000	1989	1978
Paraguay	1995	2004	1994	1994	1997	1976	1999	2004	1999	1986	1992	1995	2003	1992	1988
Peru	1993	2004	1993	1993	1995	1975	1997	2005	2002	—	1993	1992	2005	1989	1982
Saint Kitts and Nevis	1994	2001	1993	1993	1997	1994	—	2004	—	1993	1992	—	—	1992	1986
St. Lucia	1993	2005	1993	1993	1997	1982	—	2002	2003	1985	1993	2002	—	1993	1991
St. Vincent and the Grenadines	1996	2003	1996	1996	1998	1988	—	2005	2004	1993	1996	—	—	1996	2003
Suriname	—	—	1996	1996	2000	1980	—	—	2006	1998	1997	1985	2000	1997	1997
Trinidad and Tobago	1994	2000	1996	1994	2000	1984	—	2002	1999	1986	1989	1993	—	1989	2005
Uruguay	1991	—	1993	1994	1999	1975	1990	2004	2001	1992	1991	1984	2003	1989	1989
Venezuela	1998	2002	1994	1994	1998	1977	—	2005	2005	—	1989	1988	2005	1988	1990

Source: ECLAC (2008).

^a Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal.

^b Cartagena Protocol on Biosafety of the Convention on Biological Diversity.

^c Convention on Biological Diversity.

^d United Nations Framework Convention on Climate Change.

^e United Nations Convention to Combat Desertification in Those Countries Experiencing Serious Drought and/or Desertification, Particularly in Africa.

^f Convention on International Trade in Endangered Species of Wild Fauna and Flora.

^g Convention on the Conservation of Migratory Species of Wild Animals.

^h Stockholm Convention on Persistent Organic Pollutants.

ⁱ Kyoto Protocol to the United Nations Framework Convention on Climate Change.

^j United Nations Convention on the Law of the Sea.

^k Montreal Protocol on Substances That Deplete the Ozone Layer.

^l Convention on Wetlands of International Importance, Especially as a Waterfowl Habitat.

^m Rotterdam Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade.

ⁿ Vienna Convention for the Protection of the Ozone Layer.

^o Convention for the Protection of the World Cultural and Natural Heritage.

Table 8.3 Environmental Performance Index, Latin America and the Caribbean

Ranking	Country	Score	World Ranking
1	Costa Rica	90.5	5
2	Colombia	88.3	9
3	Ecuador	84.4	22
4	Chile	83.4	29
5	Panama	83.1	32
6	Dominican Rep.	83.0	33
7	Brazil	82.7	35
8	Uruguay	82.3	36
9	Argentina	81.8	38
10	Cuba	80.7	41
11	Venezuela	80.0	45
12	Mexico	79.8	47
13	Jamaica	79.1	54
14	Peru	78.1	60
15	Paraguay	77.7	63
16	El Salvador	77.2	65
17	Guatemala	76.7	69
18	Honduras	75.4	73
19	Nicaragua	74.4	77
20	Belize	71.7	84
21	Trinidad and Tobago	70.4	89
22	Guyana	64.8	108
23	Bolivia	64.7	110
24	Haiti	60.7	119

Source: Yale Center for Environmental Law and Policy (2008).

tries with an index greater than 80 are in the region (Table 8.3).

With all that has happened, there has been a striking increase in citizen participation, due not only to legally defined mechanisms such as referendums, but also to the rise of civil society and more frequent public demonstrations. Examples of commu-

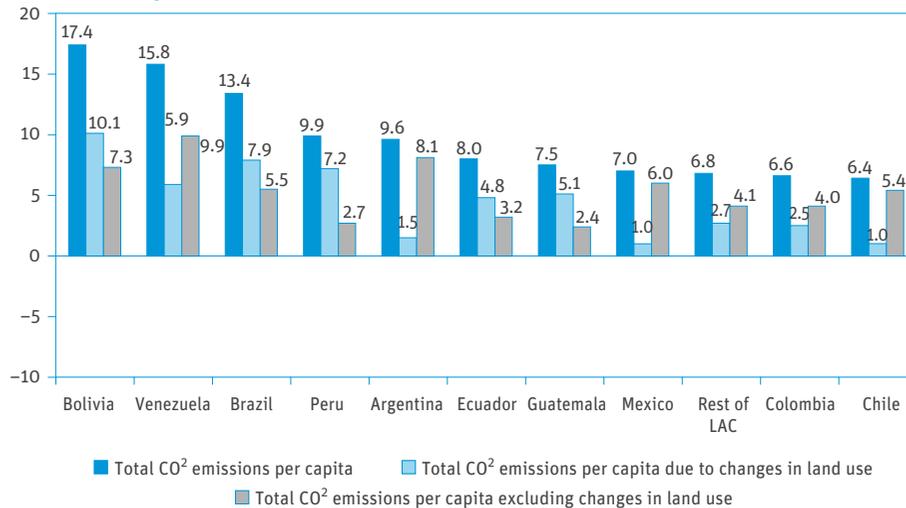
nities questioning projects or forcing an industrial initiative to include environmental mitigation plans abound and have much to do with the growing awareness that the region is rich in natural resources, but that these assets deserve to be protected since they are not inexhaustible.

CHALLENGES

However, aside from the progress made on that front, the challenge is enormous. Available indicators show a serious degradation of the environment and the depreciation of the natural capital in all its forms, which are in turn reflected in the deterioration of public health, diminished productivity and income, physical vulnerability, and a reduction in the quality of life, as shown by calculations prepared specifically for the Caribbean. Statistics confirm that although the region has made considerable efforts to reduce environmental pressures, the actions of governments, the private sector and civil society have not been enough to lessen the negative effects of development and correct the process of environmental degradation. This can be observed in the changes that have

Figure 8.1 Per Capita Emissions of Greenhouse Gases (GHGs), Countries of Latin America and the Caribbean, 2000

(Total CO₂ per capita, 2000)



Source: Climate Analysis Indicators Tool (CAIT, Version 5.0) and World Development Indicators Online (WDI).

taken place in the main environmental indicators (IDB, 2003) (Figure 8.1).

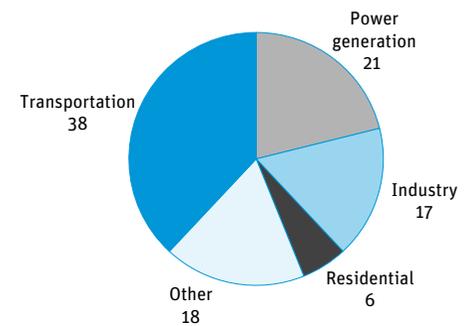
For example, the region is experiencing a constant process of deforestation, soil degradation and loss of biodiversity. It is estimated that in the 1990s alone, the region lost around 4.7 million hectares of forest per year. The scenario resulting from the growing demand for energy (Table 8.4) is no less complex. Especially important is

the environmental impact of the consumption of fossil fuels for transportation, which uses one-third of primary energy and 55 percent of petroleum derivatives in the region. This sector is the main party responsible for the rapid increase in atmospheric pollution in the region's large cities (PM₁₀, CO, NO_x and SO₂), causing 36 percent of greenhouse gas emissions (IDB, 2003) (Figure 8.2).

In addition, the region faces growing limitations in the water supply: 15 percent of the general population—and as much as 30 percent in rural areas—lacks access to drinking water. The

Figure 8.2 Carbon Dioxide Emissions Per Industry Latin America, 2001

(Percentage)



Source: IEA (2001).

Box 8.1 The Role of the IDB Regarding the Environment

The Inter-American Development Bank was the first multilateral financial institution to adopt an Environment Policy. The 1979 Policy contained an inclusive mandate to ensure the environmental quality of its operations and lend support to environmental projects in the region. Since the end of the eighties, the Bank has actively accepted and supported the sustainable development principles that led to the 1992 Rio Declaration on Environment and Development. As a result of this, in 1994, the environment, along with poverty reduction and social development, were declared priority areas for Bank support, and several specific mandates were included that have continued to guide the Bank's work in this area to this day. These mandates contained provisions aimed at (i) building legal and regulatory frameworks regarding the environment; (ii) strengthening environmental agencies; (iii) improving the environmental quality of the Bank's operations; (iv) promoting conservation and efficient energy use in the Bank's projects; (v) improving the urban environment; (vi) encouraging sustainable management of natural resources, especially in reference to sustainable environmental practices in the management of water resources, forest use, biodiversity, and agricultural and marine resources; (vii) dealing with the subjects of transparency and access to environmental information and providing information to interested parties; (viii) guaranteeing quality control and executing environmental impact assessments (EIAs); and (ix) encouraging environmental education and training.

The IDB's Board of Executive Directors backed a new environmental strategy in 2003 that established the direction for actions geared toward improving the results of efforts in sustainability, which defines the environment as a vital and all-encompassing component of economic and social development. In this context, the Bank's Environment Strategy was developed to support two fundamental objectives: achievement of sustainable economic growth and the reduction of poverty and inequality. With the 2006 approval of the Environment and Safeguards Compliance Policy, the Bank sought to provide the necessary directives to set

and reinforce key priorities identified in the Environment Strategy. This new policy took into consideration the actual changes and realities that impact environmental development, including the development of institutional capacities that had taken place in borrower countries; the ever more predominant role of civil society in the context of democratic processes; the process of convergence of policies and harmonization among multilateral and bilateral development agencies; the need to improve the effectiveness of development; the ever-increasing role of the private sector and public-private partnerships; the commitments to sustainability made by the major financial institutions of the private sector through the Ecuador Principles; and the growing importance of regional and global opportunities and challenges. This policy also recognizes the links between poverty and management of the environment and the need to improve social and economic conditions based on rational management of natural resources and the environment (IDB, 2006).

The IDB's Board of Executive Directors approved the Sustainable Energy and Climate Change Initiative (SECCI) in March 2007 as a response to the request from the countries of Latin America and the Caribbean to expand the role of sustainable energy and climate change in the region. SECCI is proving to be an exceptional generator of new operations, and a solid mechanism for adding value to the current ones. Its current structure has allowed for its incorporation in the Bank's work through its different departments. The IDB and many other multilateral development banks have been involved in the process of reforming the region's policies for the purpose of promoting not only sound policy development, but also an appropriate institutional structure that results in the desired effect. In this process the Bank has spearheaded policy-based loans (PBLs) in a wide variety of sectors such as education, health and pensions. Along the same lines, the IDB is supporting innovative PBL programs such as policy-based loans related to climate change. In these cases, loans do not aim to reform existing institutions, but to promote the creation of others that allow for the adoption of principles established in international agreements.



A wind farm in Costa Rica that received IDB funding is part of a growing movement in the region to adopt innovative energy sources to reduce hydrocarbon consumption.

Table 8.4 Total Energy Consumption, Latin America and the Caribbean, 1995–2006
(Equivalent in thousands of barrels of oil)

Country	1995	2000	2003	2004	2005	2006
Argentina	273,039.9	298,924.4	291,537.1	335,002.9	335,265.5	361,886.4
Barbados	1,745.8	1,795.6	1,896.8	1,949.4	2,027.6	2,067.8
Bolivia	18,976.9	19,284.5	19,598.5	24,009.1	24,820.2	26,613.4
Brazil	924,204.0	1,100,175.7	1,146,393.6	1,240,992.2	1,314,679.4	1,355,368.3
Chile	113,880.7	143,595.3	148,737.8	156,152.9	151,430.6	159,150.7
Colombia	171,661.5	165,683.9	168,337.9	155,776.9	166,788.3	169,013.9
Costa Rica	14,842.1	17,013.8	18,381.2	21,505.1	21,177.1	24,049.3
Cuba	51,569.2	60,861.1	61,983.6	62,812.6	66,499.9	69,005.5
Dominican Rep.	26,684.7	39,079.0	38,587.4	38,741.2	37,868.4	36,935.4
Ecuador	41,021.7	45,969.3	48,622.1	55,852.5	58,905.7	60,132.2
El Salvador	18,366.8	21,123.6	23,113.5	23,760.2	23,115.5	23,961.5
Grenada	311.8	418.3	479.3	465.3	489.9	507.0
Guatemala	36,665.2	46,208.4	50,522.6	50,842.6	52,610.9	53,938.4
Guyana	5,000.4	5,490.7	5,294.8	5,312.4	5,483.8	5,519.4
Haiti	9,956.4	12,559.5	12,534.2	16,520.6	16,818.0	17,238.4
Honduras	18,306.5	19,970.6	23,636.7	23,960.0	23,996.2	24,674.9
Jamaica	13,131.8	16,490.3	17,554.3	20,676.3	27,637.0	28,843.1
Mexico	641,918.8	703,210.2	693,545.7	761,309.2	775,492.2	800,331.5
Nicaragua	12,192.9	15,281.0	16,308.3	17,358.3	18,205.9	18,570.2
Panama	11,376.9	13,727.5	16,678.2	21,194.9	21,457.7	22,809.1
Paraguay	26,978.3	26,414.8	26,948.9	26,249.5	26,580.9	26,674.3
Peru	72,340.7	80,026.1	77,056.0	80,649.3	83,234.0	86,612.0
Suriname	4,105.7	4,333.9	4,188.3	4,400.8	4,373.3	4,495.5
Trinidad and Tobago	33,722.2	49,009.5	65,582.4	68,782.9	78,654.1	79,015.0
Uruguay	16,306.6	18,067.4	16,035.4	16,966.3	17,848.6	18,390.0
Venezuela	232,221.8	233,838.1	256,398.9	269,727.5	289,813.3	326,320.3
Latin America and the Caribbean ^a	2,790,529.1	3,158,552.4	3,249,953.3	3,500,970.9	3,645,274.1	3,802,123.3

Source: ECLAC (2008).

^aIncludes the countries shown in this table.

elimination of wastewater effluents continues to be a serious problem, since only 14 percent of the volume collected was being treated at the beginning of the decade. Moreover, the problem of solid waste management is an issue

of concern in urban centers because uncontrolled sewage deposits affect drainage basins, the course of rivers and coastlines, and more (IDB, 2003).

In coastal areas, the destruction of mangrove swamps and coral reefs, the

(Continued on page 215)

Interview with Mario Molina



When Mexican scientist Mario Molina received the 1995 Nobel Prize in Chemistry, the vast majority of fellow Mexicans and Latin Americans did not

know who he was. Today, he is regarded as one of the most outstanding scientists of the region thanks to his experiments demonstrating how the buildup of CFCs causes a reduction in the ozone layer of the stratosphere. Molina's accomplishments have sparked interest in the importance of the global atmosphere, protecting the environment and mitigating the "greenhouse effect" associated with climate change. Dr. Molina is currently a professor at the University of California in San Diego and an advisor to the Mexican government.

Your work helped humanity to understand the serious nature of environmental deterioration on the planet. What is your interpretation now?

All indications are that the world is becoming more aware of the subject of climate change every day; nevertheless, the solutions are behind schedule. The hope is that there will be a greater awareness so we may arrive at an international consensus on reducing greenhouse gas emissions, one that allows for an effective solution to the problem. This is the first step that urgently awaits us. Even so, there are sizable differences in levels of development and the promises each country has made, above all the most polluted ones. In particular, with regard to the United States, it still maintains the position of considering only voluntary measures to limit greenhouse gas emissions. But change is afoot, spearheaded by the new administration of President Barack Obama, so hopefully that nation will soon join the international community in taking measures and forging the necessary agreements.

And China?

Almost the same thing is happening there. China did not participate

with limiting its greenhouse gas emissions in the first phase of commitments to the Kyoto Protocol. But now, China already has a gas emissions level as great as that of the United States—not cumulative, but per year. Therefore, it must participate, the same as India, Mexico, Brazil and other emerging economies of the world. It's possible that China's contribution will not be to the extent of imposing emissions limits, but it will at least make certain its economic development is very efficient from the energy point of view. China is still taking great measures, investing considerably in employing clean technologies in electrical power generation plants that use coal and in applying energy-efficient regulations for automobiles.

Is it inevitable that greater action in this area will put a damper on economic growth?

No. Of course it's possible to control the climate control problem and stimulate economic growth at the same time. The two are compatible, although there is a cost. We are talking about a relatively small economic impact. According to the most widely accepted studies, all the economic efforts to

mitigate the effects of climate change would be on the order of 1 percent or 2 percent of the world's GDP. By contrast, the damage would entail a much greater cost. Thus, from the economic point of view, it turns out that it's more cost efficient to try to prevent climate change than try to adapt to it. In addition, there's a very important ethical factor: we cannot afford to do extensive damage to the Earth's natural systems because we've got to leave the planet in good shape for future generations or at least leave it with the same quantity and quality of natural resources that we had.

Do you share the apocalyptic view that strong measures must be taken now, given the magnitude of the damage?

I do not. But I do believe this is a threat that compels us to act soon, because the risk is clearly alarming. It consists of changes which, if not apocalyptic, are large enough to seriously harm society, such as hurricanes and severe droughts, and extreme meteorological phenomena in general that will affect millions of people. The changes that could come would be abrupt, sudden and very hard to predict. Neverthe-

less, we can reduce the risk of these things happening if we take action during the next decade and continue during the rest of the century. In other words, we have time to make an orderly transition toward true sustainable development where clean technologies are applied to improve quality of life for people. We must take a very serious look at this subject.

What role does Latin America play in all of this?

Latin America has many opportunities to take on the climate change challenge. For example, in the field of energy, as regions make progress and there is greater economic development, demand for energy will increase. The goal is to satisfy that demand with energy source that have low carbon intensity. If we use fossil fuels, their use has to be limited and made more efficient. At any given moment, we can apply new technologies for the capture and geological storage of carbon dioxide to generate electricity, instead of only sending it into the atmosphere as we have done since the beginning of the Industrial Revolution over 150 years ago. There are clean technologies being introduced in developed coun-

tries, and at any given moment we can adapt or apply them in our countries. The solution is to take many measures at once, especially in sectors with greater greenhouse gas emissions, such as transportation and housing. Also, you have to start making extensive use of renewable energy such as wind and solar power. These energy source have a lot of potential in the region. There's potential for biofuels as well, if they have a positive effect on the environment and energy, because there are ways to produce and use them that don't benefit the environment. Also, if nuclear energy keeps improving in order to be even safer and with fewer problems regarding the proliferation and storage of radioactive waste, it too can be one of the solutions we can apply. There is no one technology that can solve all our problems given the magnitude of the climate change we are facing.

What is your interpretation of what countries in the region are doing?

We are lagging behind. Nevertheless, I see certain things with a more positive outlook because there is a willingness, and we are starting to take action, but first you have to come to

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an agreement. In the case of Mexico, for example, President Felipe Calderón wants to take significant measures that will clearly help solve this problem. Other nations can follow in Mexico's footsteps and make it clear that we are going to sit down to discuss seriously our goals for reducing greenhouse gas emissions, which is exactly what we must begin to do in order to figure out how we can help solve this problem. In the final analysis it is up to us to turn up the pressure within the body of the UN so that an actual international agreement is established.

What would you like to see with regard to this issue in the coming years?

I'd like to see a very clear international agreement in which goals and commitments are established to reduce greenhouse gas emissions so as to avoid, in this century, an increase in the Earth's average temperature of more than 2.5 degrees Centigrade. I'd like to see all countries being charged for gas emissions that harm the envi-

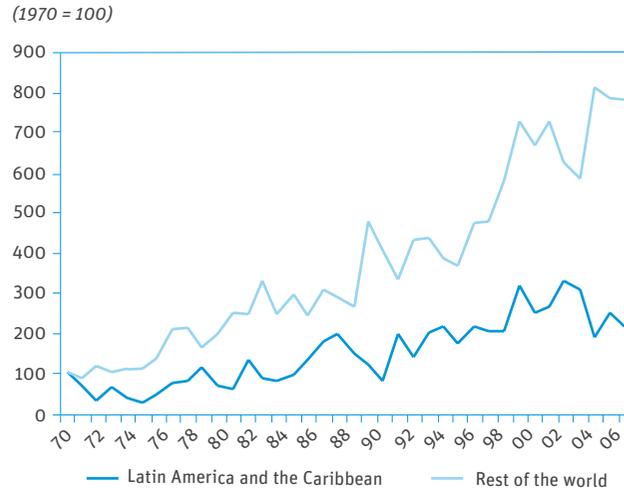
ronment. But at the same time, there must be a transfer of resources from developed countries to the developing ones to help them to apply new technologies without sacrificing economic growth, but rather, ensuring that sustainable growth takes place. This has to be a cooperative effort on the global level. This can all be done in the next decade.

What role should the Inter-American Development Bank play regarding this subject, and what would you emphasize as far as what the Bank has done?

The IDB must financially promote and support relief measures in Latin America, primarily in productive sectors that require new investments and technologies in order to be more competitive on the international market, but at the same time cleaner and less intensive in the use of fossil fuels. The IDB must also support countries that are more greatly affected by climate change, such as the insular countries or countries where extreme

meteorological phenomena and a loss in productivity in agriculture and livestock are anticipated. The creation of the Sustainable Energy and Climate Change Initiative (SECCI) is a very positive development; it's a clear sign of how important this subject is to governments in the region.

Figure 8.3 Index of Climate-Related Disasters, Latin America and the Caribbean Compared to the Rest of the World



Source: World Bank EM-DAT database calculations.

(Continued from page 211)

loss of fishing resources due to overfishing, the pollution caused by effluents and solid waste, and the serious risk of flooding and erosion are causes for concern, as well as the deterioration of air quality. More than 100 million persons in the region's cities are exposed to air pollution levels that exceed those recommended by the World Health Organization (WHO), and more than 100,000 persons die each year due to exposure to vehicular emissions (IDB, 2003).

To this list one must add the constant threat of natural phenomena (earthquakes, floods, tropical storms and hurricanes, droughts and landslides) that cause serious economic and environmental damage (Figure 8.3). Between 1990 and 1998, to cite just one example, the region experienced a total of 40.7 disasters per year that caused direct and indirect economic losses of nearly US\$20 billion (IDB, 2003).

Thus, the scenario for the region is a complex one. It includes the loss of biodiversity, deforestation, soil loss and desertification; deterioration of coastlines and the marine environment; water pollution from industrial, agricultural and local sources; a need for proper solid waste management, especially household waste; environmental deterioration in the region's large cities; and disasters caused by natural phenomena and human intervention (Rodríguez Becerra, 2002). Climate change deserves separate mention.

CLIMATE CHANGE

Global warming has touched all parts of the world, and the region's countries are not immune to this reality. According to the IPCC, regional temperatures



A dust storm signals the need to improve stewardship of land and water resources, particularly in the face of future uncertainties related to the effects of global warming.

(Continued from page 215)

increased by nearly one degree Centigrade during the twentieth century, while sea levels rose between two and three millimeters per year starting in 1980. At the same time, increased rainfall in certain areas and drought in others are well documented.

These realities contrast with the moderate impact the region has made with respect to this topic. According to the UNEP (UNEP and SEMARNAT, 2006), with regard to global greenhouse gas emissions, Latin America's contribution was on the order of 7 percent in the year 2000, and its share is expected to rise to 9 percent by the year 2050. The region as a whole produces 4.3 percent of total carbon dioxide emissions worldwide due to industrial processes, and 48.3 percent of the emissions caused by changes in soil use. Methane emissions derived from human activities represent 9.3 percent of the world total. Average carbon dioxide emissions per inhabitant in 1995 were 2.55 tons, less than the 11.9 tons calculated for high-income economies and below the world average of 4 tons (UNEP and SEMARNAT, 2006).

In this context, experts identify four urgent problem areas for the region. The first is the gradual thaw-

Table 8.5 Potential Value of Services Lost Due to the Loss of Coral Reefs
(Millions of dollars)

	Low estimates	High estimates
Coastal protection	438	1,376
Tourism	541	1,313
Fishing industry	195	319
Biodiversity	14	19
Pharmaceutical uses	3,651	3,651
Total	4,838	6,678

Source: Vergara (2008).

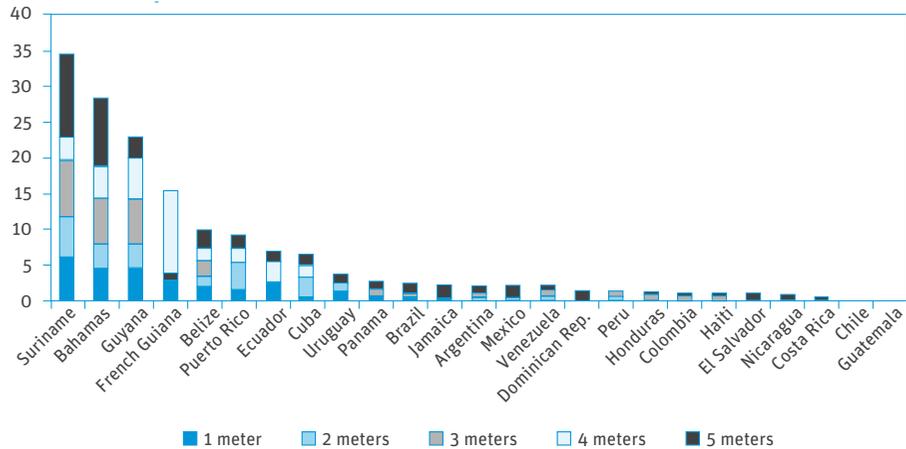
Note: Scenario for 2040–60, projected in 2008, assuming a loss of 50% of Caribbean coral reefs.

ing of the Andean glaciers and the effect that this may have on related ecosystems, as is demonstrated by the case of Mount Pastoruri in Peru. The second problem is the bleaching of Caribbean coral reefs, upon which 65 percent of the region's marine species depend for their survival (Table 8.5). A third problem is the damage to swamplands in the Gulf of Mexico and the disappearance of mangrove swamps, which are indispensable to maintaining ecological equilibrium in the region. A final source of concern is the risk of deforestation of the Amazon jungle due to natural causes (de la Torre, Fajnzylber and Nash, 2009).

The concerns are even greater when looking to the future. According to the IPCC, the increase in temperatures in

Figure 8.4 Projected Impact of Rising Sea Levels on GDP, Latin America and the Caribbean

(Percentage impact on GDP)



Source: Dasgupta et al. (2007).

the region could range between 0.4°C and 1.8°C by 2020 and between 1°C and 4°C by 2050. In addition, sea levels could rise between 18 and 59 centimeters this century, without considering catastrophic scenarios such as what might happen to Greenland’s glaciers or an accelerated thaw in Antarctica (Figure 8.4).

Such scenarios would be cataclysmic for Latin America and for the world. One cannot forget that five of the world’s 10 most biodiverse countries

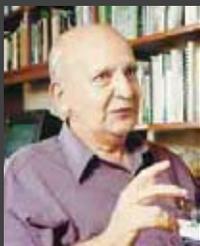
are in the region, which is home to 27 percent of the world’s mammals, 34 percent of all plants, 37 percent of the world’s reptiles, 43 percent of all birds and 47 percent of the world’s amphibians (de la Torre, Fajnzylber and Nash, 2009). Equally devastating would be the effects on agriculture, the availability of water and disaster prevention. With respect to health, it is estimated that 76,641 additional cases of dengue fever and malaria will appear over the next six years, due to an increased number of vector mosquitoes (de la Torre, Fajnzylber and Nash, 2009) (Table 8.6).

WHAT LIES AHEAD

The previous discussion makes it clear that the issue of the environment and a concern about climate change will be constants in the region for a long time to come. Interest will be fueled by the unfortunate effects expected to occur over the next few decades, which include catastrophic natural disasters and dramatic changes in rain and crop patterns. As a result, the agenda of possible actions is broad, and in some countries a few initiatives are already in progress, although a more far-reaching, forceful emphasis is desirable.

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Interview with Rodrigo Gámez



Rodrigo Gámez is the President of the National Biodiversity Institute of Costa Rica (INBio), which preserves biodiversity by using

the opportunities it provides to achieve a better quality of life for mankind. Gámez holds a Ph.D. in plant virology from the University of Illinois. He was a research professor at the University of Costa Rica, and he has received numerous national and international awards, such as the OAS Bernardo Houssay Award in Sciences, the Rainforest Alliance Green Globe Award (1997), the Distinguished Scientist Award from the Ministry of Science and Technology of Costa Rica (2004), and the Interscience Award in Ecology and Biodiversity (2005).

How would you describe what has happened in Latin America and the Caribbean with regard to the environment over the last half-century?

The process of global change has naturally affected the region. The factors of global change are population growth; changes in the way land is used in favor of agriculture and the extractive industries; environmental pollution; climate change due to greater greenhouse gas emissions; the proliferation of invasive species, particularly in some Caribbean islands; and the over-exploitation of wildlife, on the land as well as in the oceans, including forests, fishing and hunting.

As an expert on biodiversity, do you think the region's wealth in this area is in serious danger?

It is in very serious danger, because human beings are very dependent on nature. Not only that, but the region's biological wealth is at stake as well. Our region is one of the world's richest, in terms of both biodiversity and megadiversity. We mustn't forget that this biological wealth was used here by the pre-Columbian populations, who were responsible for making this area one of the cradles of agriculture.

Moreover, according to the experts, at the current rate of destruction, half of the biological wealth of Latin America and the Caribbean could be lost by the end of the century, with one-quarter of this loss due to climate change alone. Therefore, we must defend this natural asset and not squander it.

What would you take away from the events of the last 50 years?

Certainly, there has been a growing awareness of the problem in an increasing number of sectors at the national, international and multilateral levels. The 1992 Earth Summit in Rio de Janeiro, the Convention on Biological Diversity and the Framework Convention on Climate Change were just a few of the landmark events that took place. Protected wildlife areas have increased. The causes of environmental damage are better understood, and certainly more action has been taken, but it hasn't been enough to reverse the trends because losses continue to occur.

What do you wish had happened?

I wish there had been much more commitment and action. The data confirm that after the Rio de Janeiro summit, there was increased biodi-

versity loss throughout the world and in the region. In addition, developed countries provide less support for the conservation efforts of poor countries that are rich in biodiversity. It is necessary, therefore, to work harder toward stabilizing the population and rationalizing consumption. Moreover, we need to expand protected areas as well as urban and agricultural areas that are more hospitable to biodiversity and administer them more effectively. Finally, we need to work harder to restore degraded habitats, educate the people, and empower the population and communities. We must change human attitudes toward nature.

What do you feel is the future of biodiversity?

The situation is very serious because of its adverse consequences for the well-being of the region's people. The loss of species threatens the food supply and health. We must also improve protec-

tion against natural disasters while we work on climate stabilization.

What would you like to see happen in this area?

I would like to see a greater commitment from all the sectors that are in a position to act and influence the processes. These sectors include government, the private sector, business, religion and education. There is no doubt that greater action is needed to solve such a large problem. In other words, we must take things much more seriously and not treat this issue as if it were the exclusive domain of the environmentalists.

What, in your opinion, should be the role of an organization like the IDB under these circumstances?

Every crisis is an opportunity. As a development bank, the IDB can communicate its perception of the impact of global change on the region's

development process. I would like the Bank to have a greater influence on the above-mentioned sectors to make them understand the serious consequences that global change holds for humanity and the quality of life. The Bank must work on reinforcing the concept of natural assets, particularly in support of education and bioliteracy. We must help everyone understand how much we depend on nature and how we can take advantage of the opportunities it offers us. In the final analysis, our well-being and development are at stake, and we must protect them through the proper use of science and technology.

Table 8.6 Additional Cases of Malaria and Dengue Fever, Future Scenarios

Disease vectors	Historical number, 2000–2005	Additional number of cases per six-year period	
		Scenario in 50 years	Scenario in 100 years
<i>Plasmodium falciparum</i> malaria	184,350	19,098	56,901
<i>Plasmodium vivax</i> malaria	274,513	16,247	48,207
Dengue fever	194,330	41,296	123,445
Total	653,193	76,641	228,553

Source: de la Torre, Fajnzylber and Nash (2009).

(Continued from page 217)

We must also prepare ourselves for the scenario that will play out after the expiry of some of the provisions of the Kyoto Protocol in 2012, because one topic of discussion that will definitely emerge will be that of adaptation to climate change in developing countries. On the other hand, according to UNEP (UNEP and SEMARNAT, 2006), the instruments now existing under the Protocol will probably be used more and more. It is important that clear signals be given for the continuity of the mechanisms and for the emergence of new tools, strategies and partnerships.

In conclusion, the future is alarming, but not inevitably so. Several organizations, including the IDB, have

identified precise action areas to tackle so as to correct or mitigate the trends. These consist of the development of renewable energy and greater energy efficiency, the push toward biofuels, carbon financing and adaptation to climate change.⁵ Specific examples involve the increased use of hydroelectricity and alternative energy sources, reforestation programs, the use of alternative fuels for transportation, the proper management of waste and harmonized decision making among the region's governments. In all cases it is clear that success is not guaranteed, especially in light of the region's complex social, political and economic realities. But to do nothing is a sure recipe for failure.

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- ¹ To view the complete article, go to: <http://www.elcomercio.com.pe/edicionimpresa/Html/2008-05-25/pastoruri-agoniza-hecho-pedazos.html>.
 - ² In decreasing order of megadiversity, the world's 12 most megadiverse countries are Brazil, Colombia, Indonesia, Peru, Mexico, China, Australia, Ecuador, India, Venezuela, Bolivia and Madagascar.
 - ³ Cited in Rodríguez Becerra (2002).
 - ⁴ "In 1973, Brazil created the Special Secretariat for the Environment and Mexico established the Subsecretaría para el Mejoramiento del Medio Ambiente (SEMA; Sub-Secretariat for the Improvement of the Environment), setting a trend for the construction of environmental agencies elsewhere on a national and sub-national level. The establishment in 1974 of the Colombian Code of Natural Resources and the Environment and the creation in 1976 of Venezuela's Ministry of the Environment were pioneering creations in comparison to the advancements made by other developing countries elsewhere in the world."
 - ⁵ Proposals contained in the IDB's Sustainable Energy and Climate Change Initiative (SECCI). For more information, go to <http://www.iadb.org/SECCI/?lang=es>.



A landscape of challenges. The most urbanized developing region, Latin America faces a major challenge of unsnarling traffic to make its cities livable. With IDB support, metropolitan areas have taken innovative approaches to meeting needs for infrastructure and social services. Often working with private sector partners, cities have expanded funding available for mortgages for new housing, undertaken massive projects to collect and treat sewage, improved law and order, and strengthened the ability of municipal agencies to carry out their responsibilities.

IX The Urbanization of Latin America and the Caribbean

They called it the *burroducto*. Until a few years ago, it was the only source of drinking water for tens of thousands of people who live on the handful of hills overlooking Cartagena de Indias, in the Caribbean region of Colombia. “My family used to pay around 3,000 pesos a day (approximately US\$40 per month) for water from the *burroducto*,” recalls Delfina Díaz Pereyra. Born in Loma Fresca, one of the sprawling neighborhoods located at the city’s edge, Díaz Pereyra became a sort of water activist in 1995. “I got tired of waiting for the municipality to install water service in my house,” she says. “So I started showing up at the mayor’s office to demand an explanation.”

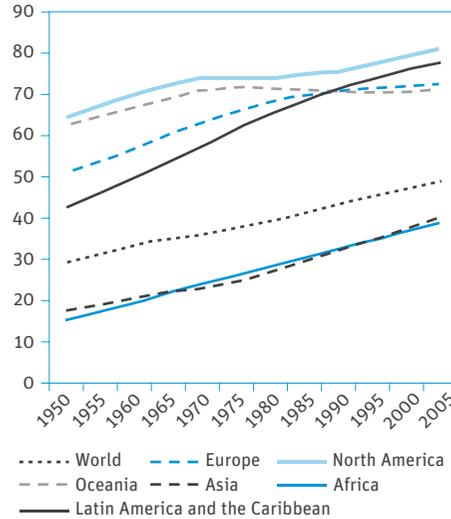
Today, it’s a different story. Díaz Pereyra has been paying about US\$8 a month for drinking water that flows 24 hours a day, since the local water company, Acuacar, went under private management. According to the company, 99 percent of residents have household water connections and 82 percent

have access to the sewer system. These numbers would be impressive in any context, but they are especially notable in a city like Cartagena, where 85 percent of the population is classified as poor (IDB, 2006).

Cases such as this one reflect the profound contradictions of the cities in a good part of the Western Hemisphere, where efforts toward a better quality of life for a constantly growing population are the exception and not the rule. The reason is very simple. Latin America and the Caribbean is now the most urbanized region in the world, which is surprising when one considers that in 1900 none of its capital cities had more than one million inhabitants, and that in 1950 there were barely seven cities with at least that number of people.

According to the most recent figures, 77 percent of the area’s inhabitants live in these types of settlements¹ (Figure 9.1). In addition, four of the 20 cities in the world with more than 10 million inhabitants and 55 of the

Figure 9.1 Urban Population, by Continent
(Percentage of total population)



Source: Cristini and Moya (2008).

414 cities with more than one million inhabitants are located in the area. These 55 cities are home to a total of 183 million individuals, one-third of all Latin Americans (IDB, 2008).

Moreover, in recent times medium-sized cities (those with a population of between 200,000 and one million persons) have experienced vigorous economic and demographic growth, with increases greater than those for any other group. This process is expected to continue; by 2030 it is estimated that 84.3 percent of Latin Americans, approximately 609 million people, will be living in urban areas (Table 9.1) (UN-Habitat, 2007).

This trend has been evident since the middle of the twentieth century, because the process of urbanization in Latin America and the Caribbean has been more intense than in any other region

Table 9.1 Urbanization Trends, 1950–2030, and Projections
(Population data in thousands of inhabitants)

	1950	1950–75	1975	1975–2000	2000	2000–30	2030
Total population	179,050		319,893		522,929		722,377
Increase in total population		140,843		203,036		199,448	
Urban population	74,484		196,094		394,212		608,968
Increase in urban population		121,610		198,118		214,756	
Urban population as a percentage of total population	41.60%		61.30%		75.38%		84.30%

Source: UN-Habitat (2007).



Squeezed in a narrow valley, La Paz, Bolivia, faces the challenge of controlling development on surrounding hills whose unstable slopes are prone to landslides.

of the world. According to analysts, migration from rural to urban areas is attributable in some cases to problems of personal safety, but above all to the miserable living conditions in the countryside, a consequence of the concentration of land ownership in the hands of but a few families and of the low productivity of agricultural workers and rural tenant farmers (IDB, 2008). At the same time, growing industrialization in the urban centers opened up opportunities for employment and higher incomes, thereby increasing the gap between the city and the countryside (Thorp, 1998).

From that point of view, it can be argued that urbanization has been good for the different economies. This would have been the result of greater productivity among companies and workers due to the emergence of large centers of consumption. However, it is clear that even under this scenario, the region's cities have not been able to absorb the large amount of labor available. Because of this, two out of every three new jobs belong to the informal sector. Apart from that, the cities, many of which form part of metropolitan agglomerations, account for more than half of the productive capacity of their respective

countries and it is estimated that they will generate more than 80 percent of their future growth (Rojas, Cuadrado-Roura and Fernández Güell, 2008).

Additionally, such a drastic change met with insufficient institutional capacity to respond to the avalanche of people. In other words, urbanization was accompanied by disorderly growth, human settlements (often illegal), and scarce infrastructure and social services. Although over time a large part of the needs have been met, there are still challenges. At the same time, the response from municipalities has been slow because, among other reasons, de facto metropolitan areas have been created in many cases that exceed the boundaries of established administrative limits, creating conflicts between different authorities. That factor affects overall decision making and prevents the adequate development of fiscal resources.

Nevertheless, there is a clear trend toward greater political and administrative independence achieved through popular elections to appoint mayors, councilmen, and local administrators in the majority of the region's cities. There is also an obvious effort toward decentralization that includes the transfer of

national taxes to local administrations, along with greater responsibilities.

This is a key dynamic when the region's urban centers account for a good part of the challenges confronting the different countries. These include the high incidence of poverty, elevated rates of unemployment and informal employment, environmental problems caused by vehicular congestion and the handling of garbage, and rising organized and non-organized crime.

Resolving such challenges in turn impacts each city's possibilities for progress in specific ways, in a world that is becoming more and more globalized, where competitiveness is increasingly important for establishing businesses or attracting investment resources.

URBANIZATION OF POVERTY

It can be said that the high levels of internal migration that took place in Latin American countries have led, in turn, to the urbanization of poverty. Today, although these indexes are higher in the countryside (one out of every two households, compared to one out of every three in the cities), the region's poor are concentrated in urban areas. According to ECLAC, of the 190 million people with income of less than two dollars per day in 2007, about 121 million lived in towns and cities (ECLAC, 2007) (Table 9.2).

Such circumstances create a type of vicious circle that lays traps from which it is hard to escape. These include

(Continued on page 232)

Table 9.2 Latin America: Poor and Indigent Population 1980–2007^a

	Millions of persons					
	Total	Poor ^b		Indigent ^c		
		Urban	Rural	Total	Urban	Rural
1980	135.9	62.9	73.0	62.4	22.5	39.9
1990	200.2	121.7	78.5	93.4	45.0	48.4
1997	203.8	125.7	78.2	88.8	42.2	46.6
1999	211.4	134.2	77.2	89.4	43.0	46.4
2002	221.4	146.7	74.8	97.4	51.6	45.8
2005	209.0	137.9	71.1	81.1	41.8	39.3
2006	193.5	127.2	66.3	70.6	34.7	35.9
2007	183.9	121.0	62.9	67.8	33.9	33.9

Source: ECLAC, based on special tabulations of household surveys in the countries listed.

^a Estimate for 18 countries in the region plus Haiti.

^b Persons with incomes below the poverty line. Includes indigent persons.

^c Persons with incomes below the indigence line.

Box 9.1 The IDB's Role in Urban Development

In its five decades of activity, IDB loans earmarked for urban development—including urban infrastructure and social services, housing, municipal development, renewal and heritage preservation projects, transportation, health care and environmental conservation—have grown exponentially. This has been tied to the need for investment to sustain the expansion of infrastructure and urban services capable of maintaining the growth of the population and of booming local economies.

In the first phase, the IDB focused on the critical needs generated by rapid urbanization, such as the issues of health care and housing construction. Thus, a large part of the Bank's portfolio was centered on housing and health care loans during the 1960s and 1970s. During the 1980s, there was increased interest in urban loans, especially those aimed at sustaining municipal development, as a response to the decentralization processes taking place in the region. The 1990s brought greater complexity to the loan portfolio, with the addition of urban development. In this decade, in addition to a significant increase in municipal loans, a new interest arose in revitalizing urban centers, preserving national heritage, generating modern public transportation systems, and promoting programs to deal with growing social programs such as urban violence; other social services in general began to be managed through integrated initiatives designed to handle several problems simultaneously.

Consequently, direct Bank loans to cities represent 15 percent of all loans granted and 12.5 percent of all approved projects since 1961.

In figures, the aggregate total amounts to US\$33,781 billion (in 1997 dollars).

Of particular note are the changes with respect to housing; at the beginning, the Bank was actively involved in housing by financing construction projects. Today, its support is more complex, including backing for both the supply and demand of units in addition to urban improvement programs.

Loans to municipalities and other subnational levels are no less remarkable. In response to the trend toward decentralization in Latin America and the Caribbean, the IDB expanded its service portfolio to include syndicated loans and guarantees for private companies involved in municipal infrastructure, particularly in sanitation, transportation and electricity.

Another important area is that of support for the integrated urban development projects carried out by dozens of cities in the region. These projects are aimed not only at the revitalization of run-down areas, but also at the conservation, restoration and preservation of historic centers.

Finally, the Bank has maintained an active technical cooperation program to support the preparation of loan applications or the institutional development of cities. More than 120 transactions worth US\$22 million overall have been processed under this category. Work in this field has been supplemented by a thorough research program whose published findings have served as a basic tool for municipal managers and the academic sector throughout the Western Hemisphere.

Interview with Vicente Fretes-Cibils



Vicente Fretes-Cibils is the Chief of the Fiscal and Municipal Management Division of the Inter-American Development Bank

(IDB). Throughout his professional career he has worked at the World Bank and the IDB, and has taught as a university professor on several occasions. After receiving a degree in economics from the Universidad Nacional del Nordeste in Argentina, Fretes-Cibils completed postgraduate studies at the University of Pennsylvania and North Carolina State University, where he obtained a Ph.D. in economics.

How do you see the changes that have taken place in the region with respect to urban development over the past half-century?

Over the past 50 years, urban development in Latin America and the Caribbean has had a remarkable history. The explosive growth experienced by the cities in the region beginning in the second half of the twentieth century led to the current advanced urban structure, which is responsible for a large part of overall economic growth and of increased integration with global markets. From a population of 74 million persons in the 1950s, the cities have grown to become home to more than 400 million inhabitants, which represents 75 percent of the total Latin American population. In addition, more than one-half of the region's GDP is generated in the urban areas, and that share is expected to rise to 80

percent in the future. The region's best resources, in terms of human capital, technology and entrepreneurship, are found in the cities. Despite the benefits offered by the cities, however, this growth presents significant challenges that affect the quality of life. The large scale of the cities exacerbates social, environmental and transportation problems. And their management continues to be one of the key challenges, given their size and the jurisdictional conflicts that arise when regional solutions are required.

What do you think the IDB's role has been in these events, and what would you highlight as a positive development with respect to what has been done?

Throughout its history, the IDB has supported urban development in the region. It has promoted, for example,

decentralization programs that have brought additional resources to the municipalities as well as greater responsibilities. The IDB has also been a partner in the mobilization of technical and financial resources required at the municipal and regional levels in order to deal with the challenges arising from urban growth. This support has been aimed at specific sectors such as water and sanitation, transportation, environmental protection and housing, as well as multi-sectored plans that include integrated urban development, revitalization of downtown areas, improvements in housing and the provision of urban services. Over the past 50 years, Bank loans to benefit the cities have represented 15 percent of all loans and 12.5 percent of all approved projects.

Where do you see the issue going over the short and long term, and what should the Bank's role be?

Challenges include helping local governments mobilize both financial and technical resources to deal with the critical issues related to urban growth. Improving the quality of life in the cities will remain on the public agenda, since issues such as congestion, environmental degradation, violence and governance will be at the center of the debate. In this regard, the Bank will increase its support of integrated programs related to priority issues in each city. This support will include critical financial investments for improving the quality of life and providing social services, as well as technical assistance to increase the effectiveness of fiscal management and governance capabilities, including

in the private sector. In short, the Bank recognizes that Latin America and the Caribbean constitute an urban region and is ready to cooperate to improve the quality of life in the cities and make them safer and more productive.



The Bank has financed the construction of affordable housing throughout the region.

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different types of scarcity that are exacerbated by poor living conditions, poor health, crime, violence and vulnerability to natural disasters. Such conditions create pressure on the nuclear family, as expressed in the high incidence of teenage pregnancies in the cities, where 8 out of 10 Latin American young people live. According to ECLAC, almost one-quarter of the region's young women ages 15 to 24 years old have become mothers before the age of 20. Among the higher-income socioeconomic groups, less than 5 percent of young women have had children at the age of 17, while among lower-income groups the incidence has risen to between 20 percent and 35 percent of young women, depending on the country (ECLAC, 2008).

There is also the matter of spatial segregation. Although it is not a phenomenon exclusive to Latin America and the Caribbean, implicit in real estate market operations is the fact that the price of urban land rises because it is a scarce commodity, thus relegating the poor to areas that are distant, unsafe, inaccessible, and afflicted with serious problems in the supply of public utilities. This factor tends to create

a dichotomy between metropolises with modern areas and good infrastructure and other areas that are in a backward state. Such a situation also exacerbates transportation problems because the commute time between home and work tends to increase, thereby affecting the general competitiveness of cities and barring hundreds of thousands of persons from access to broader opportunities (Rojas, Cuadrado-Roura and Fernández Güell, 2008).

This situation does not obscure the fact that progress on certain indicators is considerable. For example, the availability of electricity is practically universal in the region's urban areas, with electricity reaching 95 percent of all homes. In addition, the availability of running water is high, with 86 percent coverage, although the sewage system barely reaches 60 percent of homes. Landline telephone service coverage, however, is low at 61 percent, but this proportion increases to 87 percent when mobile telephone service is included. There are gaps in the figures mentioned according to socioeconomic level that tend to be moderate for electricity and water services, but are much more substantial for sanitation services and landline telephone service (Table 9.3) (IDB, 2008).

Table 9.3 Public Utilities Coverage in Urban Areas and Gaps between the Two Highest and Lowest Quintiles, Latin America

	Year	Sanitation		Water		Electricity		Telephone		Telephone/cell phone	
		Coverage	Gap	Coverage	Gap	Coverage	Gap	Coverage	Gap	Coverage	Gap
Argentina	2003	60.4	39.2	98.4	4.0	99.5	1.2	64.8	39.5	93.0	11.1
Bahamas	2001	12.8	-0.1	86.7	12.4	96.1	5.7	n.d.	n.d.	n.d.	n.d.
Belize	1999	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.	62.7	38.9	93.3	n.d.
Bolivia	2003-04	61.2	-3.2	90.2	9.7	92.5	6.1	45.5	27.0	86.6	11.0
Brazil	2005	65.5	30.2	95.6	9.9	99.6	0.9	95.7	7.0	98.0	4.0
Chile	2003	91.8	11.2	99.3	1.3	99.7	0.6	69.8	24.9	93.1	13.0
Colombia	2004	87.6	10.4	89.9	5.2	90.4	4.6	76.2	13.7	94.9	4.8
Costa Rica	2005	43.4	5.8	98.9	0.6	99.9	0.2	74.1	15.0	87.8	14.2
Dominican Republic	2006	32.3	14.6	80.6	18.9	94.4	4.7	40.6	43.8	84.9	20.1
Ecuador	2003	67.4	28.7	91.1	9.7	99.3	1.2	49.3	39.2	77.9	31.5
El Salvador	2004	50.6	30.7	73.7	23.8	90.7	14.4	59.0	19.2	87.2	8.9
Guatemala	2004	66.7	23.9	77.9	0.8	96.0	11.0	42.9	25.1	84.3	14.0
Guyana	1992-93	1.6	-3.3	88.7	7.3	91.0	14.6	83.3	1.6	95.2	0.4
Haiti	2001	n.d.	n.d.	23.2	11.1	61.9	28.7	n.d.	n.d.	n.d.	n.d.
Honduras	2006	63.8	31.1	n.d.	n.d.	97.0	10.1	51.3	5.8	70.5	6.7
Jamaica	2002	32.9	1.3	65.3	12.0	92.3	6.3	n.d.	n.d.	n.d.	n.d.
Mexico	2005	69.5	37.1	94.9	8.9	99.6	1.0	68.4	20.3	81.4	23.3
Nicaragua	2005	36.4	23.8	89.5	13.4	95.5	12.8	37.1	32.4	79.5	18.8
Paraguay	2005	15.0	14.7	89.7	20.1	98.4	3.8	40.1	48.0	82.6	28.9
Peru	2006	77.6	34.3	83.4	23.8	96.3	12.6	58.2	50.5	82.2	29.1
Suriname	1999	97.8	0.1	87.3	7.4	99.3	0.2	n.d.	n.d.	n.d.	n.d.
Uruguay	2005	66.2	38.3	98.8	1.5	99.3	1.9	71.9	42.1	90.1	21.4
Venezuela	2002	95.1	5.7	93.9	6.7	99.1	0.9	69.2	24.5	89.8	12.6
Average		56.9	17.8	85.6	9.9	94.9	6.5	61.1	27.3	87.0	15.2

Source: Cristini and Moya (2008). Data on telephone coverage derived from Gallup (2007).
Note: n.d. = no available data.

MORE HOMEOWNERS ²

The expansion of Latin American cities over the second half of the twentieth century democratized homeownership at an unprecedented rate in the region, and possibly worldwide. In 1950, approximately one out of every four families in Buenos Aires, Mexico City and Santiago, Chile, were homeowners; now, about two-thirds of those families own their own homes. According to the most recent surveys of urban areas undertaken in 22 countries, the average homeownership rate is 68.4 percent (Table 9.4). This figure is higher than that of other developing countries and comes close to that of the United States (69 percent), where mortgage markets are very well developed and there is a long tradition of incentives

for homeownership. In the region as a whole, the homeownership rate is higher among higher-income families (71 percent compared to 64 percent), but this difference conceals deep gaps in some cases (Table 9.5).

These indexes are striking if one keeps in mind that a good part of the region's original settlements were illegal due to being established in areas that had not been designated for housing, as they were outside of the urban limits at the time and did not have the appropriate permits. However, not all of the region's irregular settlements are the result of illegal occupation. Currently, a large part of this illegality is purely nominal in the sense that regulations are breached with respect to planning, or there are no property titles confirming the voluntary transfer of ownership on paper. In order to resolve this problem, many governments in the region have carried out programs to issue property titles. But even now, about 20 percent of homeowners in the lower socioeconomic brackets of Latin America and the Caribbean do not have titles, and in some countries those levels are much higher (Figure 9.2).

Despite the fact that the lack of property titles has contributed to the

Table 9.4 Homeowners, by Latin American City, 1947–2002
(Percentage of families who own their own homes)

	1947–52	1970–73	1990–93	1998–2002
Bogotá	43	42	54	52
Buenos Aires	27	61	72	75
Mexico City	25	43	70	76
Guadalajara	29	43	68	62
Medellín	51	57	63	56
Rio de Janeiro	33	54	63	75
Santiago	26	57	71	73

Sources: Gilbert (2001), UN-Habitat (2003), DANE (1998–2002).

Table 9.5 Index of Homeowners by Income, Urban Areas, Latin America and the Caribbean

	Low income	High income	Average
Argentina	58.4	70.6	66.0
Bahamas	51.9	61.8	57.7
Bolivia	55.4	55.0	53.9
Brazil	65.3	73.1	69.9
Chile	59.8	69.2	65.9
Colombia	57.8	64.1	60.0
Costa Rica	69.1	74.2	72.2
Dominican Republic	59.3	58.3	59.3
Ecuador	70.6	69.5	69.4
El Salvador	56.3	71.0	66.0
Guatemala	71.1	70.0	70.0
Guyana	31.3	42.9	40.6
Haiti	47.3	45.2	46.0
Honduras	57.2	62.0	59.2
Jamaica	57.2	48.5	52.5
Mexico	67.3	71.8	69.5
Nicaragua	67.6	79.6	76.6
Paraguay	75.6	74.2	74.4
Peru	55.1	70.0	65.7
Suriname	65.4	67.1	63.7
Uruguay	43.9	75.5	64.0
Venezuela	77.2	74.3	75.3
Latin America and the Caribbean (weighted average)	63.6	71.3	68.4

Source: Cristini and Moya (2008).

Notes: "Low income" refers to the two lowest quintiles, and "high income" refers to the two highest quintiles. The data come from household surveys and may not coincide with census data.

disorderly development of housing construction in the region's large cities, a relatively high percentage of homes have been built in compli-

ance with acceptable construction standards and with access to basic services, half a century after the great urban expansion.

What does or does not constitute an acceptable home has been the subject of intense debate among the region's economists, architects, urban planners and sociologists for several decades. All agree that no universal standard can be defined because basic requirements vary depending on climate, construction methods, customs, and in the final analysis, individual needs and preferences. A simple standard, imposed more by available information than by conceptual rigor, defines "unfit housing" as that which has been built with poor-quality materials according to each country's standards. Using this criterion for a set of 65 cities in the region that, as a group, include over half of the urban population, 18 percent of homes are considered unfit. However, this average represents some uneven distribution, with rates of unfit housing ranging from 5 percent to almost 20 percent in 17 of the region's 22 largest cities. It is also important to mention that the majority of unfit housing is reflected in the lowest income deciles,

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Interview with Jaime Lerner



Born in Curitiba, Brazil, architect and urban planner Jaime Lerner has thrice been mayor of his native city and

twice governor of the State of Paraná. Lerner implemented reforms ranging from urban transit to planning in general, which have been imitated on every continent. In this interview, Lerner discusses a topic he is passionate about: cities.

How would you analyze what has happened over the past half-century in Latin American cities?

It has been a period marked by several events: disorderly growth, ever-increasing urbanization and improvements in the urban quality of life. A positive event is that the population growth rate has decreased over the past few decades, which demonstrates that the expected density bomb did not materialize. One of the most important lessons to draw from this is that it's a mistake to treat economic development, quality of life and human settlements separately. When this occurs, it's a disaster for cities, for the regions, for the provinces, and for the countries.

What have we learned?

We've learned that cities are the last refuge of community. For this reason, we must replace the pessimistic view of cities that prevails in some countries and adopt a more generous view with respect to people in the areas of health care, education and child care. When we speak of the whirlwind that is the global economic crisis, it's time to try another New Deal that must aim to improve the quality of life of the people. It's not a question of delivering abstract

resources, but rather of taking advantage of the opportunity to invest money in programs that benefit the citizens.

In Latin America, there are some countries in which a large part of the population is concentrated in one city, while in others, the population is distributed across several urban centers. Is it more difficult to serve the needs of the population in the first case?

Undoubtedly, it is more difficult when there are fewer hubs of development, because it is more difficult to establish a balance and offer the same quality of life throughout the country. It's always better to have more hubs of development.

Everything indicates that the gap between the countryside and the city has widened. Do you agree?

Yes. It's my understanding that the lack of opportunities in the countryside and in small towns has caused the mass migration to the large urban centers. But now the trend has changed, and job sources have diversified, thanks in part to technology, because wireless communications have made it possible to provide services anywhere. This should reduce the pressure on large cities. We

also have to work to reduce the area of land that is occupied and follow the example of the tortoise, which is an example of how to live, work and move in one. The tortoise's shell is designed like an urban structure. If we cut it into several parts, the tortoise will die. This is exactly what we're doing in our cities: we live in one place, we work in another place, and spend our leisure time in a third place. This is a big mistake, and it is harming the quality of life of the cities.

What are the most important problems, apart from the obvious ones?

One problem is mobility, the second is sustainability, and the third is coexistence. To begin with, it's a big mistake to think that the problem of mobility can only be solved by using a car or taking the subway, because the city just isn't viable for cars, and waiting for a complete subway network like the kind that was set up more than a century ago in London, Moscow, Paris and New York is impossible. So, my position is that everything is important. If it's the subway, we have to build a smart subway; if it's the bus, we have to build a smart bus; if it's the bicycle, we have

to make a smart bicycle. What, then, is the secret of successful mobility distribution? It's to use all your options, but never to let one system compete in the same space as the other.

And what about sustainability?

Everybody's discussing it, but they're in a state of perplexity because nobody knows what they should do. Many believe that the solution is to be found in new sustainable materials, and that's indeed important, but it's not enough. People are also promoting new forms of energy or recycling, which are equally important, but they're not enough. First of all, we must understand that 75 percent of carbon emissions come from cities. Therefore, it is in the conceptualization of cities where we can most quickly and effectively resolve the problem of climate change, and this means making some commitments. One, use the car less, which will force us to have good public transportation systems. Two, separate garbage. Three, live closer to work, or bring your work closer to home. Four, take the concept of multi-use into consideration, because a city cannot have areas that remain empty for 16 hours a day or a sports

arena that is used 10 times a year. We must understand that sustainability is an equation between what we save and what we waste.

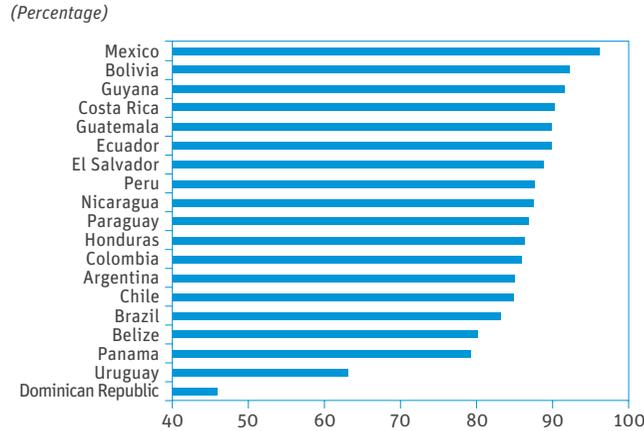
What do you have to say about coexistence?

We can't have ghettos of very wealthy people or very poor people. It is an illusion that you can build bigger walls to have a safer life, because this doesn't solve anything. The higher the wall, the greater the stimulus it gives to violence. There will come a time when whoever is inside the wall will realize that he is a prisoner, and that when he wants to get out, they will be waiting for him.

How do you see the role of an organization like the IDB in all this analysis?

The Bank was the first institution that opened up the topic of quality of life. It was where we found the first sources of financing for cities. It was the first bank that invested in urban transit and opened up this perspective of non-bureaucratized response. I hope it will continue this way, as a key partner of the region's cities.

Figure 9.2 Latin American Homeowners with Deeds of Ownership in the Two Lowest Quintiles, 2007



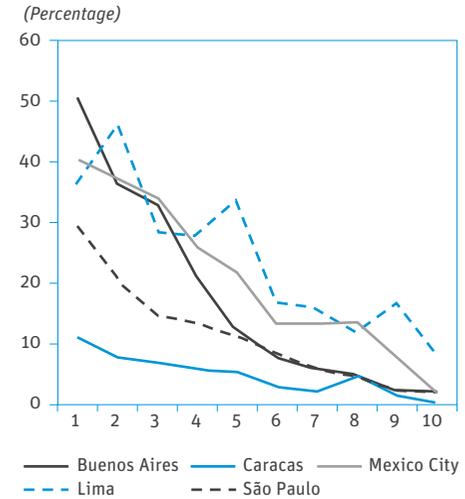
Source: Gallup (2007).

(Continued from page 235)

a fact that provides evidence of the problem of inequality in Latin American urban areas (Figure 9.3).

How far are the cities of Latin America and the Caribbean from solving the most basic deficiencies of housing construction and the provision of water, sanitation and electricity services? This has been a recurring question that is usually answered on the basis of calculations of “quantitative” and “qualitative” housing deficits. The

Figure 9.3 Unfit Housing in Latin American Cities, by Income Deciles



Source: Cristini and Moya (2008).

former is the difference between the number of households and the number of homes, while the latter is a measure of the quality of housing based on the type of building materials, access to services, or other criteria. The Economic Commission for Latin America and the Caribbean (ECLAC) and the Latin American and Caribbean Demographic Center (CELADE) estimated that in 1995, the total (quantitative and qualitative) deficit in all countries in Latin

America and the Caribbean was 53 million homes, which was equivalent at that time to 54 percent of available housing. The quantitative deficit was calculated at 28 million homes and the qualitative deficit (defined simply as a lack of connection to running water) at 25 million homes. A more recent study

carried out on 17 large cities in the region showed quantitative deficit ranges of 3 percent to 12 percent of households, while the unfit housing index ranged from 5 percent to 50 percent (Table 9.6).

Table 9.6 Qualitative and Quantitative Housing Deficits, and the Cost of Policies Required for Improving Urban Infrastructure in Latin America

Country	City (ordered by population size)	Housing deficits		Quantitative deficit			
		Inadequate dwellings		Inadequate dwellings		Homes without water or sanitation	
		Percentage of households	Cost (percentage of the city's GDP)	Percentage of households	Cost (percentage of the city's GDP)	Percentage of households	Cost (percentage of the city's GDP)
Mexico	Mexico City	3.6	1.7	15.8	3.6	6.2	0.3
Brazil	São Paulo	4.8	3.0	12.4	2.5	13.7	0.7
Argentina	Greater Buenos Aires	3.7	2.6	13.5	4	41.2	2.5
Brazil	Rio de Janeiro	6.1	6.2	12.7	5.5	9.4	0.8
Colombia	Bogotá	12.1	7.5	n.d.	n.d.	n.d.	n.d.
Peru	Greater Lima	4.8	2.2	17.3	3.4	15.8	1.7
Brazil	Belo Horizonte	6.5	4.6	19.2	5	14.4	1
Mexico	Guadalajara	5.4	2.2	10.5	2	4.5	0.3
Brazil	Porto Alegre	5.3	4.6	10.9	3.5	15.3	1.3
Mexico	Monterrey	4.5	2.6	9.3	0.4	0.9	0.04
Brazil	Recife	10.3	8.7	50.6	18.5	56	5.2
Brazil	Brasília	3.3	1.5	10.3	2.0	17.1	1
Brazil	Salvador	9.2	6.3	20.5	6.0	14.6	1
Brazil	Fortaleza	10.2	6.6	41.7	11.6	49.2	5.1
Colombia	Medellín	4.1	2.8	n.d.	n.d.	n.d.	n.d.
Venezuela	Caracas	n.d.	n.d.	5.6	1.6	4.2	0.3
Brazil	Curitiba	4.9	3.8	17.6	5.8	20.5	1.3

Source: Cristini and Moya (2008), based on household surveys and national census data.

Note: n.d. = no available data.

GREATER AUTONOMY, MORE CHALLENGES

One of the most notable aspects of recent developments in the management of Latin American cities has been the growing transfer of functions by national governments to local governments. This decentralization process is aimed at improving the provision of services and the quality of basic infrastructure, giving municipal governments (or regional governments, in some cases) decision-making responsibilities with respect to the use of resources, based on general coverage parameters. Thus, many of the region's countries have transferred the management of areas such as health care, education and sanitation to the cities, with the understand-

ing that their greater proximity to the area's residents facilitates better decision making and more effective control by the local community (Table 9.7). In this respect there are a wide variety of models for this process, as well as a heterogeneous reality. In Latin America and the Caribbean, there are more than 15,000 towns and cities of different sizes, with different systems of government and administrative capacities.

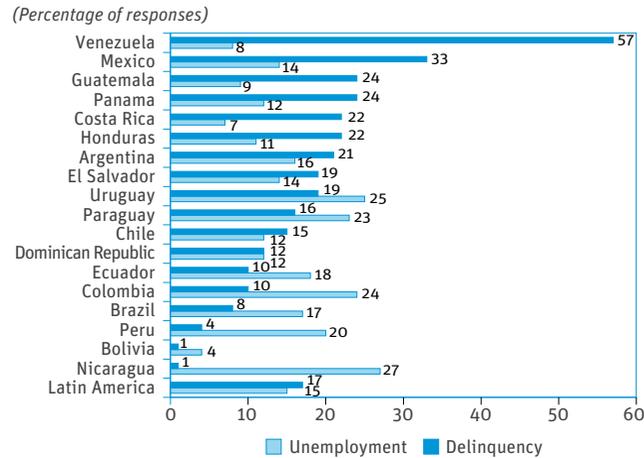
Part of what has happened has to do with the strengthening of democracy in the region. As dictatorships were replaced over the last three decades by governments chosen by popular vote, the election of local authorities—mayors, councilmen and, in some cases, the heads of regulatory bodies—gradually increased as well.

Table 9.7 Decentralization Levels by Country
(Percentage of public expenditures reported by subnational governments)

Focus of decentralization effort	Level of decentralization		
	More than 20%	Between 10% and 20%	Less than 10%
Intermediate level (states and provinces)	Argentina (49.3) Brazil (47.0) Mexico (31.8) Venezuela (27.0)	Peru (19.0)	
Local level (municipalities)	Colombia (44.7) Bolivia (25.1)	Ecuador (17.5) Uruguay (13.7) Chile (12.8) Honduras (12.3) Guatemala (10.3)	El Salvador (5.1) Nicaragua (5.0) Paraguay (4.0) Costa Rica (3.1) Panama (1.0)

Source: Daughters and Harper (2006).

Figure 9.4 Delinquency and Unemployment as the Most Important Problems, Latin America, 2008

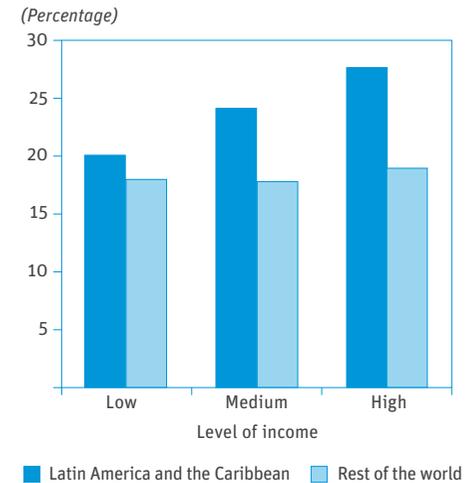


Source: Latinobarómetro (2008).

Note: The results were determined on the basis of the answers to the following question: "In your opinion, what do you consider to be the country's most important problem?" Only the two problems considered to be the region's most important ones are reflected in the figure.

The accelerated growth of the population and economic activity in urbanized areas has brought about the creation of communities that are unified, but divided into several municipalities. This situation leads to problems of coordination among authorities, institutional vacuums, and disparities in the management of resources. A reduced capacity for the development of taxation when the standards are

Figure 9.5 People Who Have Been the Victims of Theft or Robbery in the Last 12 Months, by Level of Income



Source: Di Tella and Ñopo (2008), based on Gallup (2007).

different in neighboring territories is a concern arising from such a situation. This is occurring in the case of taxes on property, motor vehicles and corporations (Rojas, Cuadrado-Roura and Fernández Güell, 2008).

However, the matter of personal safety is what generates the greatest concern among the population. According to Latinobarómetro (2008), crime is now the most serious problem for many of the re-



The sound of horses' hooves sends the message that historic preservation can play an important role in fostering civic pride and attracting tourists. (photo credit *El Tiempo*)

gion's inhabitants, more worrisome than unemployment (Figure 9.4). In addition, the proportion of persons who say they have been victims of theft or robbery is significantly higher than in the rest of the world (IDB, 2008) (Figure 9.5).

There is also a growing concern with respect to the lack of an effective response to the deterioration of the environment. One of the negative impacts arising from the accelerated growth of Latin America's urban areas has to do with the degradation of natural resources. As cities grow, the demand for environmental resources and services increases: land for development, water and energy to serve the needs of the population and the business community, and space to deposit or dispose of waste.

Despite the efforts expended, the fact that only 15 percent of liquid or solid waste undergoes any type of treatment is a reason for concern. The growing rate of motorization resulting from the recent economic boom, the expansion of the middle class and the relative decrease in the price of vehicles do not help, either. They impact the air quality and noise levels in a region where acute respiratory illnesses constitute the third most common cause of death (Rojas, Cuadrado-Roura and Fernández Güell, 2008).

FINAL CONSIDERATIONS

The growing urbanization of Latin America and the Caribbean is more than desirable; it is inevitable. In some cases, it has been accompanied by mushrooming urban sprawl, as observed in the region's large metropolises. That process has made things difficult to manage, especially when it comes to eliminating the strong social segregation and fragmentation that are typical to the region. Although improvements in coverage with respect to public utilities have been notable, it is undeniable that great challenges still lie ahead, as is the case with problems in personal safety, mass transit, traffic congestion and the deterioration of the environment.

Things being as they are, duality is one of the characteristics of Latin American cities. Not only do persons of the highest income levels live side by side with a large number of poor persons, but formal and informal economies often exist side by side as well. This simultaneous reality of modernity and backwardness is faced with an institutional structure that is sometimes weak and, on occasion, inadequate to service the needs of the population.

Table 9.8 Satisfaction with Housing and Cities, Regions of the World
(Percentage)

	Satisfaction with their dwellings	Satisfaction with their cities	Their city is improving
East Asia and the Pacific	82.1	87.2	68.6
Eastern Europe and Central Asia	75.2	79.8	60.5
Latin America and the Caribbean	79.7	79.5	52.9
Middle East and North Africa	80.0	79.4	72.5
North America	n.d.	88.0	57.9
South Asia	87.6	87.5	67.3
Sub-Saharan Africa	62.2	69.7	55.2
Western Europe	89.9	92.4	50.2

Source: Gallup (2007).
Note: n.d. = no available data.

Consequently, the challenge continues to be that of reducing social inequalities and minimizing the impact on the environment, while bearing in mind that the migratory flow from the countryside to the city is ever-present in the region. The competitiveness of a specific urban area, an element that is increasingly important to globalization, depends in large part on how successfully the unknown factors that emerge are resolved. The region's cities, like its countries, depend on a high rate of investment in order to accelerate their growth and expand the space of the formal economy.

A key element of that objective is the so-called “governability of metropolitan areas” (Rojas, Cuadrado-Roura and

Fernández Güell, 2008), which has to do with the decision making and resource-management process in areas where different municipalities or levels of government sometimes converge. In this regard, it is advisable to develop systems that facilitate the resolution of differences among authorities and the harmonious definition of common purposes. Such a model also allows for improvements in fiscal efficiency and tax collection for the purpose of implementing redistribution and community development policies.

Even when one acknowledges that the list of tasks to be accomplished in Latin American cities is long and that the size of the challenge to meet the public's expectations is formidable, it is still worth noting that nearly 80 percent of the region's inhabitants say that they feel satisfied with their homes and with their cities (IDB, 2008) (Table 9.8). This statistic is close to that in other areas of the world, and does not necessarily bear any relationship to the objective conditions of each metropolis. But beyond the details, there is no doubt that Latin Americans like to live in urban areas and that, apart from the known problems, the trend toward larger and more numerous human settlements is part of an inescapable reality.

Interview with Juan del Granado



Juan del Granado, the mayor of La Paz, Bolivia, has held the office since early 2000 and was re-elected in 2005. An at-

torney with a lengthy career in public service, del Granado has distinguished himself as a transformative force at the helm of the Bolivian capital. In this interview, he talks about Latin American cities from the perspective of the city under his management.

How would you analyze what has occurred in the cities of the Western Hemisphere over the past half-century?

The phenomenal growth of cities is universal and irreversible. Those of us in charge of managing municipalities would like this process to benefit the population in terms of quality of life, equity and preservation of the environment, all in the direction of building communities with a fabric that incorporates these factors.

Despite their difficulties, are people living better in cities?

In Latin America, we find that cities, despite their drawbacks, are an enormous draw for populations living in rural areas where extreme poverty is the rule and not the exception. So what we're seeing is people arriving with a suitcase full of dreams as well as needs. This makes planning and creating opportunities for growth more difficult.

What is the impact of this process on the demand for services?

The challenge is enormous. In the case of La Paz, over the last three decades we've gone from a population of

500,000 to a population of one million, not including the residents of El Alto, our neighboring municipality. This represents an enormous additional burden that affects everything from infrastructure and basic services to issues related to education, health and the environment, without necessarily increasing tax revenue.

What can be done to meet these growing needs?

We have an urban development program that includes everything from citizen participation to major coverage expansion projects. We've concentrated on neighborhoods with the goal of improving quality of life as well as humanitarian and health care facilities, among other things. This allows us to combine various strategies and achieve progress despite the challenges.

What can you tell us about the informal economy?

It's an immense challenge, without a doubt. For example, in La Paz we have 45,000 reported street vendors who provide sustenance to an equal number of families and who conduct their work in an unorganized fashion. In response to this challenge, we've

tried to harmonize this type of commercial activity with the protection of public spaces. This includes various programs, such as establishing more indoor commercial centers to make coming into the city center more appealing. At the same time, we're attempting to provide dignity to the working conditions of these vendors.

What are your most complex challenges?

I'd have to be very specific due to the particularities of each case. But in our case I'd start with the geology and hydrology of the city, two factors that increase the risk of soil instability and flooding during rains. We've invested US\$60 million with the support of the IDB, but we need more. We must also consider the problems of urban marginalization and informal commerce, as well as the issue of transportation, since the lack of a mass transit system complicates our relationship with the private firms that own the vehicles. Last but not least, we have the issue of water and the sewer system. In our case, this service is handled by a company that reports to the national government, not the municipal government.

What would you like to see occur in cities?

I'd like to see all the people who live in our cities have the same opportunities with regard to urban development. I'm talking about basic services, road improvements, health care centers, education centers and recreation sites. We must add to that the issue of access to jobs, which is outside our area of responsibility but which has to do with equity and inclusion.

Critics have pointed to weak tax collection efforts at the local level.

Taxation capacity involves various components, including a technical one in the case of La Paz in that we do not yet have a complete property register. This generates tax evasion on top of the fact that people's income levels are low to begin with. That's why many of us depend on fund transfers from the national government, despite the efforts of the private sector and the support we receive through cooperation.

Has city management become professionalized?

Without a doubt, an important level of institutionalism has been achieved, especially in medium and large mu-

nicipalities. We're continuously seeing better teams and systems.

What do you see happening in the future of the region's cities?

It's difficult to generalize, but I see a trend toward greater concern for social rights. I'm deeply hopeful that this process will turn out well.

How is the Inter-American Development Bank participating in this process?

It's been very important for us to be able to count on the Bank's support, which includes resources from the Fund for Special Operations, a fund that grants 40-year loans with very low interest rates. These funds allowed us to develop our downtown revitalization program, and since then we've been able to design other initiatives. Personally, I really believe in the value of this collaboration and can attest to how important it's been to the city that I manage.

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¹ An urban area is defined as a settlement of 2,000 or more inhabitants.

² The text of this section has since been adapted by IDB (2008).



A new beginning. A coat of paint puts a new shine on the historic center of Quito, Ecuador. The IDB-financed renovation project, a model for Latin America, joined architects, builders, experts in art restoration, private entrepreneurs, and many others to transform this formerly run-down district into vibrant neighborhoods. Today, tourists come to see the museums and the monuments, and growing numbers of Quiteños are choosing this exciting urban environment as a place to live and work and educate their children.

X The Growing Importance of Culture

In February, 2007, the 79th Annual Academy Awards created a buzz in Latin America, and not just among movie lovers. The reason was that three Mexican directors—Alejandro González Iñárritu, for *Babel*; Guillermo del Toro, for *Pan's Labyrinth*; and Alfonso Cuarón, for *Children of Men*—together earned 16 Oscar nominations in various categories in the film industry's most prestigious ceremony. Their success is yet another example of the increasing impact of culture in the region, both inside and outside the hemisphere. Whether literature, fine art, music, or audiovisual media, the work coming out of this area of the world is no longer confined to narrow geographical boundaries. In fact, it is becoming a part of the everyday enjoyment of millions of people, regardless of where they live.

However, this was not always the case. In the words of Argentine

anthropologist Néstor García Canclini (2003):

The inter-relationship among countries in the Americas and the rest of the world began changing around the middle of the 20th century, thanks to the cultural industries. Until about 50 years ago, inter-American integration, or the integration of each region, especially of Latin America, was a political and cultural project with weak economic support that was of interest to some elites in certain countries, without the means of communication with which to share it with the rest of the general population. Latin Americanist movements, although they invoked geographic, linguistic and historical unity, sometimes in confrontation with extra-regional powers, were rather rhetorical actions that mobilized few resources. Their greater expression and diffusion was achieved through fine art, literature and some iconic figures in film and music, thanks to the handful of Argentine and



Mexican films, boleros, tangos and Andean melodies that made it across national borders.

Thus, the growing importance of Latin American and Caribbean culture is one of the most encouraging outcomes of the last half-century. This affirmation may sound contradictory in a globalized world where outside influences have increased and where concerns sometimes arise regarding the quality of language or the decline of certain activities, caught in the whirlwind of changing technology. At the same time, however, the region's cultural phenomena are reaching more and more corners of the world, be they Jamaican reggae, Brazilian soap operas, or Argentine cinema. Not surprisingly, Colombian singer Juanes says that over the past two years he has given more concerts in Finland than anywhere else, and that his most loyal fan base is in Germany,¹ despite the fact that neither of these nations has a large number of Spanish speakers.

This is happening despite the fact that "Latin America is a living contradiction of material poverty and extreme cultural wealth" (López Morales, 2000). Elements such as geographical diversity, the blend of ethnicities and the evolu-

tion of national identities have combined to create the right environment for artistic cultivation, the potential of which has not been fully tapped. For this reason, there are some who say that "the region's cultural legacy, characterized by its great diversity and common historical roots, is its most important resource for the future" (López Morales, 2000).

This affirmation does not detract from the importance of the topic in today's world. Various studies show that the relative weight of culture ranges from 1 to 7 percent of the gross domestic product (GDP) in several countries in the region and that its growth rate is higher than that of the economy (Machicado, 2004). In concrete terms, the most prominent activities are those related to communications, followed by the publishing, recording and audiovisual industries (Machicado, 2004).

Evidence that the cultural sector is a dynamic element of the economy has been accompanied by developments in the business community, many of which are a result of transnational processes. In sectors such as book and music production, cases

Student members of a clarinet chorus learn not only about music but also about being part of a team, taking responsibility, and the value of hard work.

of mergers have appeared, partly in response to the challenges that the development of technology has brought to the traditional content distribution model. Nevertheless, in other areas, interesting partnerships have formed, as is the case with television production companies that have developed series aimed at Hispanic minorities in North America and Europe. Cultural tourism has also gained growing momentum, encouraging investment in hotel or communications infrastructure.

CAUSES AND EVOLUTION

According to the analyses of various experts, culture began to evolve more quickly with the advent of technological advancements, spurred by the growing rate of urbanization in the hemisphere and the region's increased earning power. The increased exchange of products and advancements in telecommunications facilitated by the culture industries has created a situation that was very different from that of a half-century ago. Although press, radio and film had exerted a certain impact on societies since the start of the 20th century, their widespread dissemination came as a result of geographic and

educational changes. Once again, in the words of García Canclini (2003):

While these three media helped integrate disconnected regions within each nation, they also helped create conditions for each country to learn more about the others. The development of television since the 1960s, satellite and cable transmission starting in the 1980s, the miniaturization of computers, and the merging of telephone services and IT created a multimedia system of networks that has taken the integration of Latin America to new levels.

This situation may have been complemented by other factors, such as international migratory patterns. In the case of Latin America, the last 50 years have seen significant displacements of native populations to other regions of the world. Though modest at first, migration began accelerating in the early 1980s and spread throughout the region as a result of economic volatility, the search for opportunities for progress, and the ease of travel. Without getting into the effects of or justification for this phenomenon, there is no doubt that culture plays a role in everything, nurtured through the act of giving and receiving.

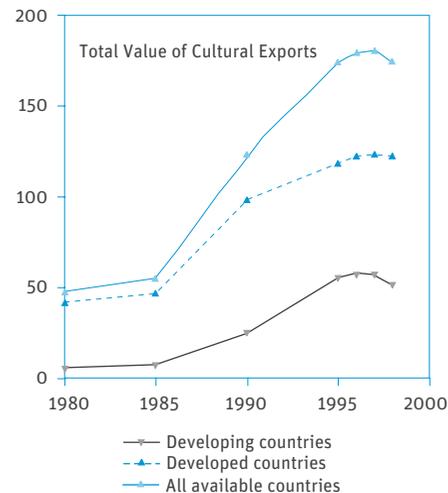
According to Mexican writer Carlos Fuentes (1992), not only is this process inevitable, but it also includes some very positive elements:

The United States brings its own culture, its influence in film, its music, its books, its ideas, its journalism, its politics and its language to Latin America. This does not scare Latin Americans, as we believe that our own culture is sufficiently strong and that in effect, the enchilada can coexist with the hamburger, even if the former, in our view, is definitely superior. It is a fact that cultures only flourish in contact with others and perish in isolation.

Such situations are, in fact, part of a global trend; despite relative gaps in progress among regions, similar events have taken place in all corners of the globe as a result of similar factors. Several objective measurements seem to confirm the trend. According to the United Nations Educational, Scientific and Cultural Organization (UNESCO), worldwide imports of cultural goods grew from US\$47.8 billion in 1980 to US\$213.7 billion in 1998, equivalent to a per capita increase from US\$12 to nearly US\$45 (UNESCO, 2000). Although most

Figure 10.1 Growth of Cultural Exports, 1980-2000

(In billions of dollars)



Source: UNESCO (2000).

of this trade took place among developed nations, the poorest countries experienced considerable proportionate growth, from US\$5.5 billion to US\$57 billion in traded goods (Figure 10.1).

Consequently, it is worth noting the growing weight of economic activities related to the production and circulation of symbolic goods and services, the essential worth of which is derived from their cultural value (Carranza Valdés, 2003). Such activities include

The many faces of culture in the region add up to an economic powerhouse that provides livings for millions of people, from traditional artisans to international superstars. (photo credit *El Tiempo*)



The ancient Zapotec capital of Monte Albán, in Oaxaca, Mexico, is one of many pre-Columbian sites included in IDB projects to preserve heritage and foster tourism. (photo credit *El Tiempo*)

those aimed at producing and marketing symbolic goods and services based on intangible content of a cultural nature, generally under the protection of intellectual property laws. These include the so-called “classic” cultural industries: radio, television, film, publishing, the recording industry, design, architecture and new media such as the Internet. There are also the so-called “traditional arts” such as the visual arts, handicrafts, theater, musical productions, literature, museums and galleries (Carranza Valdés, 2003).

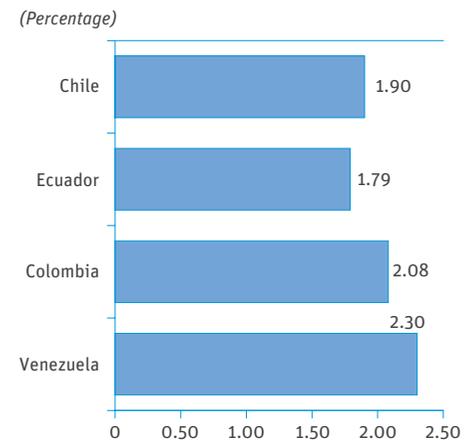
Thus, it is clear that some activities linked to culture also generate an economic impact similar to that produced by other sectors of the economy. In short, culture—besides being an essential element for social cohesion and the creation of an identity—is of equal importance to or even greater importance than any other productive sector. Commercial transactions related to culture produce positive economic effects, such as learning and knowledge. In other words, the cultural sector contributes to development, not only within its own social and identity-building context, but with regard to generating income as well (Machicado, 2004).

A GROWING PRESENCE

This affirmation is encouraging for Latin America and the Caribbean, given their immense cultural wealth. The region still has a long way to go, however, to increase the role of culture in its GDP to levels similar to those of more developed areas of the world. In the case of the United States, for example, culture accounts for more than 7 percent of its economy, while in countries of the region the impact is much lower (Figure 10.2). Such differ-

(Continued on page 256)

Figure 10.2 The Weight of the Cultural Sector in Selected Economies



Source: Andrés Bello Convention (2003).

Interview with Fernando Botero



Fernando Botero is not only the most distinguished artist of Colombia, but also one of the world's most recognized painters

and sculptors. Born in Medellín, he held his first exhibition in 1948 at the age of 16, and has since embarked on a career that has taken him to Bogotá, Europe and the Americas. His work is found in major museums and adorning streets and parks in dozens of cities on every continent. Accustomed to speaking candidly, whether it be with his voice, his brush or his hands, in this interview he talks at length about the outlook of art in the region.

In your view, how has Latin American art evolved over the last 50 years?

Well, the truth is that Latin American art is unfortunately quite colonized, in the sense that many artists are very closely following the styles of Paris, New York or London. However, the positive side is that artistic activity has become very widespread: lots of artists, lots of galleries, lots of collectors, lots of museums. In short, there's an interest now that didn't exist half a century ago, so what has happened is good.

How much did other painters of the region influence you at the start of your career?

Back in my time, most of what you saw was Mexican muralist art. Even in Medellín there was an exponent of that genre, Pedro Nel Gómez. But in general, there was little interest in looking beyond our borders, and there wasn't enough information. One of the reasons is that in the Colombia of the fifties, there were no galleries or museums where you could view original works. I only began learning about the topic of art when I arrived in Europe at the age of 19. I remember that the first original I saw from a well-known

painter was a Zurbarán at the entrance to the Montjuïc Museum in Barcelona, right after I got off the boat that had brought me there. Before then, I'd only seen poor copies and poor reproductions in books, other than having seen local Colombian painting. That was a real epiphany for me.

What happened to you no longer happens to young painters in any Latin American country today. . . .

Without a doubt. Today we have a lot more information in every sense of the word, thanks to television, the Internet or even higher-quality books. However, beyond simply enjoying this access, painters in the region need to have a voice that embodies their own flavor, their personality. If you see a Spanish or German painting, you know it was created in those countries because it displays certain unique characteristics that are the essence of those nations.

But there is now a concept of Latin American art, wouldn't you say?

Yes. Quite a few things have happened to bring this about, like auctions in New York that have generated attention and interest in Latin American

art. In the past, making a living as a painter was nearly impossible, and getting your foot in the door was very difficult. I know this because I was the first Colombian painter to exhibit internationally, and it was quite complicated.

Are there more artists now than before in the region, or are they simply better known?

There are many more artists today, more now than ever. The only problem is that specialized auctions have created a type of Latin American ghetto, which is a bad thing because they pigeonhole all the region's painters into one group when they should be including them among painters from everywhere else in the world.

Is there a sense of belonging to a group?

That has changed a lot. In the past, there were groups that shared a common philosophy, regardless of their nationality, which gave them a reason to come together, as was the case with the Surrealists and the Impressionists. Nowadays, it's so individualized that I don't think it has any impact. I don't see schools any more.

What is your reaction when you exhibit in the region?

When I exhibit in Latin America, I feel very pleased, and I see people identifying quite a lot with my work. That's very satisfying for me.

What is the current outlook?

My problem is that I have very specific ideas when it comes to art, and these ideas don't always correspond with what I see nowadays in the region.

What would you like to see, moving forward?

Art can evolve in mysterious and surprising ways. When abstract art first appeared, many people thought that we'd continue in the same direction. Then came hyperrealism, which is the exact opposite. That's just how art is. So, you never know. There are people working in obscurity whom we don't know about. The true artist will eventually stage a coup d'état, so I'm sure that there are those who are secretly planning one. It could very well be started by a Latin American. There could be true artists there, those who don't follow current fashion but who do things their way, differently.

What do you tell young people when they ask for your advice?

I don't give advice because I'm not a fortune teller of any sort. The only thing I tell them is that in art, it's very important to study what the masters have done. It's not just about painting, about knowing your craft, but about realizing that the most important part of it is ideas, beliefs and philosophy.

And with regard to nationality?

You either have roots or you don't. If you're Latin American, you have a special sensibility for pre-Columbian art, for example. But you might also be interested in popular or colonial art or in the reality of the region. However, you still need a connection to the country of your birth.

And you have one. . . .

Obviously, of course I do. Identifying with the place you come from is very important, because it makes your paintings more than just beautiful—it gives your work depth and moves people in a special way. For art to be universal, it has to start by being parochial or local. Greek art is from Greece, just as Egyptian art is from Egypt and Spanish art is from Spain. This should be true for us as well.

(Continued from page 253)

ences could be explained by the average length and quality of education, income levels, government support of certain cultural activities, and the production systems of various cultural industries with strong financing capabilities thanks to their sizeable markets (Andrés Bello Convention, 2003).

The economic cycle is also, without a doubt, highly influential. The evidence suggests that if internal demand decreases, demand for cultural activities will drop by a similar amount. In other words, the cultural sector is cyclical in nature. When purchasing power falls from one period to the next, cultural goods and services are excluded to a greater extent than goods and services from the family shopping basket. In many middle-class households affected by the crisis, the consumption of “non-basic” goods and services tends to decrease. Thus, trips to the movie theater become less frequent, people buy fewer books, magazines, newspapers and records (or the demand for them grows in the informal market), pay television subscription services go unpaid, fewer concerts are given and theater audiences become smaller. People continue to watch free-access television and listen to the radio; however,

advertising, the source of income for these activities, decreases: in times of crisis, companies typically cut advertising expenses. Other economic factors such as unemployment and high debt also affect the demand for these goods (Andrés Bello Convention, 2003).

This analysis is especially relevant in light of the current global economic downturn that began in late 2008 and has had clear repercussions for Latin America and the Caribbean. However, despite the magnitude of the crisis, the outlook for the medium term is that the region’s cultural sector should see above-average growth rates as the industry continues to mature and play an increasing role in international markets.

From a demand point of view, the growing appetite for Latin American cultural phenomena suggests the presence of an expanding market. However, what is perhaps most striking is the subject of supply, as a rising number of artists with a diverse variety of specialties are making their work known to the wider world, benefiting from an appreciable reduction in the costs of entry into certain disciplines. In film and music, for example, the cheaper cost of technology has made it possible to



Starting from the ground up, crews in Brazil restore a historic neighborhood in an IDB-financed program that also trained artisans and provided education on cultural heritage.

create high-quality productions without a great deal of resources. Likewise, the development of the Internet has made it possible for artists to disseminate work and share experiences with other artists in different parts of the world.

Factors such as these are creating a greater space for culture, even amid a scenario of consolidation of the assets of entertainment companies. On a medium scale, there are publishing houses, independent record producers, bookstores, software firms, and film producers, some of which cover market niches that allow them to stay afloat. For example, in the case of audiovisual production, medium-sized enterprises produce genres such as documentaries or narratives that do not necessarily enjoy mass appeal. University radio stations play alternative and classical pieces that are far removed from the latest hits, while local TV and radio stations are building closer relationships with communities. Therefore, on the level of medium-sized

firms, an opportunity exists to create room for a range of content and cultural processes that differ from offerings aimed at mass markets (López and Amaya, 2004).

Lastly, there is, of course, the crucial issue of talent, dedication and the capacity to create, all of which Latin America and the Caribbean seem to have in an inexhaustible supply. As Gabriel García Márquez said in March, 2007, upon being honored for his achievements by the Fourth Congress of the Spanish Language (Congreso de la Lengua Española, or CILE) in 2007 (CILE, 2007):

I don't know at what point it all happened; I only know that from the time I was 17, I've done nothing else but wake up early every day and sit before a keyboard to fill a blank page or a computer screen with the sole mission of writing a story not yet told by anyone and making the life of some new reader happier.

Interview with Juan Luis Guerra



Considered by some to be the greatest Dominican musician of all time, Juan Luis Guerra is a well-known figure

throughout the hemisphere. Educated at the Santo Domingo Conservatory and the Berklee College of Music in Boston, this arranger, singer, composer and producer is equally at ease in genres such as ballads, *bachata*, *merengue*, and jazz. In this interview, Guerra explains how his identity is reflected in everything he does.

Would you say that your awareness of being not only a Dominican voice, but a Caribbean and Latin American voice as well, has grown throughout your career?

It certainly has. The songs are partly a reflection of the society in which we live. I often ask and question the realities of our people, their dreams and their hopes. However, it's not just the song that is responsible for the solution, but the person hearing it.

Do you feel that the music you and some of your other colleagues make has helped erase borders in the region?

Music is a unique language. All of us understand it, in one form or another, and it's the perfect link to bring us together and resolve our differences. Juanes, Alejandro (Sanz), Ricky (Martin) and many others are tangible proof of that.

Do you believe in the existence of a Latin American culture?

Certainly, and it is vast, defined and lovely. We reflect our own identity in everything we do.

Do you see difficulties in preserving the region's culture?

We are in charge of preserving it, taking care of it and transmitting it to future generations. If we do that, then we have nothing to worry about.

Allowing yourself to dream for a moment, what would you like to see happen in Latin America in the coming years?

I'd like to dream of a Latin America where education and health play a prominent role, where judges and authorities honor God and judge impartially, understanding that when the punishment for a crime isn't enforced immediately, the hearts of the people become filled with reasons to do what is wrong.

In what ways do you believe the IDB can help build this dream?

I think the IDB can help in many ways, since its main goal is reducing poverty in Latin America and the Caribbean and fostering the development of our peoples with loans and aid for the most needy. With vision, integrity and commitment, we can achieve anything we set our minds to.

Box 10.1 The Work of the IDB in the Field of Culture

The Inter-American Development Bank has done a great deal of work in promoting the cultural values of Latin America. In addition to the existence of the IDB Cultural Center, created in 1992 for the purpose of contributing to social development and fostering a better image for the IDB's member countries in the United States, the Cultural Development Program established in 1994, and the acquisitions made on behalf of the Art Collection, the program that the organization is promoting in the region is an important one.

Perhaps what is most significant is the design and financing of protection and development programs for urban cultural heritage, an initiative that has benefited various historic centers that have been added to the World Heritage List by UNESCO. Beneficiary properties include the historic districts of Cuzco, Peru, and Panama City, Panama. In some cases, the rehabilitation of archeological sites has been furthered as part of tourism-related projects. Technical assistance has also been provided for interpreting the unique cultural characteristics of certain communities, as is the case with the Mundo Maya Organization.

To complement these programs, the Bank has supported initiatives that strengthen social cohesion and generate economic benefits. These include concerts offered by the Youth Symphony Orchestra of Venezuela and support for the protection of intellectual property in regard to handicrafts created by indigenous communities.

The Inter-American Culture and Development Foundation (ICDF) was established in 2005 through a Bank-led initiative as a non-profit

organization with the goal of driving cultural development in Latin America and the Caribbean, with a commitment to helping cultural organizations become more competitive and reaffirming culture as an instrument of change. The foundation has defined five strategic work areas: cultural industries and tourism, community and regional museums, intangible and tangible cultural heritage, social and cultural entrepreneurship, information culture and technologies, and communication for development.

The ICDF's objective is to promote sustainable methods for reducing poverty, improving quality of life and achieving greater social equity in the region, as demonstrated through its projects. These include the GeoAmericas Portal, which identifies and promotes the cultural, historical and environmental heritage of the hemisphere through georeferencing, compiling text, images and video, and making these available to the public via the Internet; the organization Museos Comunitarios.org, which promotes the development, implementation and proper functioning of community museums in Latin America and the Caribbean by disseminating practical information tools that guide communities, native populations, cultural administrators and organizations in developing sustainable projects; and the Lake Titicaca Museums, charged with the mission of preserving the lake's cultural heritage. Also worth mentioning is the technical and financial support provided by the Lima Museum of Art (MALI) for the purpose of promoting educational and cultural programs for children and young adults in Peru and exhibiting an art collection of great importance to the history of the country.

Interview with Alicia Ritchie



Alicia Ritchie, a Cuban-born United States citizen, is the manager of the Andean Group Country Department and has

worked at the IDB for two decades.

During her career at the Bank, she has been involved in multiple areas, including housing, urban development, social protection and microfinance. She holds a master's degree in international relations from the Johns Hopkins University School of Advanced International Studies (SAIS) and a bachelor's degree in political science from Newton College of the Sacred Heart in Newton, Massachusetts.

Why is cultural development important, and why has the IDB approved programs of this nature?

The Bank recognized early on that culture is closely related to social and economic development. Cultural expressions such as music, architecture, theater, literature or film help create a sense of common identity and belonging, thus supporting inclusion and social development. The cultural industry, which includes tourism, sports and publishing, is also a high-growth, global economic sector that generates a significant amount of income and supports other production sectors.

How has the Bank supported culture?

The Bank has supported culture through projects financed with non-reimbursable resources and investment loans in areas such as restoring historic sites and supporting centers for art and music. It has also sponsored art and film competitions with the goal of linking artistic expression with some aspect of socioeconomic development in Latin America. For example, it has promoted culture by financing the Youth Orchestra System in Venezuela and the Culture Factories program in São Paulo, Brazil. Both projects have

been quite successful, and both of them support sociocultural growth through artistic and cultural activities, thus contributing to the region's social development and facilitating the insertion of children and young participants into the community. These programs, of course, have artistic objectives—the Venezuelan Youth Orchestra, for example, has a recognized reputation throughout the world. But they also offer social prevention in focusing their interventions on segments of the population that are at social risk.

What other activities has the Bank encouraged?

Another type of initiative has centered on supporting the preservation of the region's cultural heritage, including historic centers and archeological sites. In the last 10 years, the Bank has invested around US\$700 million in restoring downtown urban areas. With symbolic programs like the restoration of the historic city center of Quito and the Old Town of Panama City, activities in Cartagena de Indias and Cali, Colombia, or the Monumenta program in Brazil spearheaded by the Brazilian government, the Bank not only supports historical and cultural heritage,

but also invests in improving the urban environment through comprehensive action in public services and public-private partnerships to ensure the sustainability of investments and social projects in the communities involved. Two of the Bank's major contributions to these types of projects have been its facilitation of the dialogue between various institutions and groups involved in cultural heritage, and promoting the exchange of experiences between countries.

Where do you see this issue going in the future, and what should be the Bank's role?

We've learned a lot from the Bank's past experience that should be used in future projects. For example, the IDB is helping to replicate the success of Venezuela's Youth Orchestra System in several other countries in region. We're also working on new focus areas for revitalizing and preserving heritage sites, increasing the community's involvement and the central role of the private sector in these efforts and supporting the critical role played by the public sector in developing regulations, policies and coordination that attract and complement private investment.

There's also plenty of room for working together on developing the cultural industry, because it includes centers for entertainment, education and information, design, print media and manufactured products, in addition to heritage preservation and tourism, which the Bank can also support in the future. Without a doubt, Latin American countries and cities will continue to seek the Bank's support in this important area of cultural and socioeconomic development.

Interview with Ángeles Mastretta



Ángeles Mastretta is one of the best-known writers in the region. Born in Puebla, Mexico, she has authored such novels as

Mujeres de ojos grandes (Women with Big Eyes), *El cielo de los leones (Lion Sky)*, and *Mal de amores (Lovesick)*, for which she won the Rómulo Gallegos Award in 1996. Her most famous work is *Arráncame la vida (Tear This Heart Out)*, translated into more than 20 languages and made into a very successful movie in 2008.

Over the course of your career as a writer, how has the culture of Latin America and the Caribbean evolved?

It is impossible to answer this question. As impossible as an “all-hours miracle, a dolour with no source,” as the poet Jaime Sabines would say.

Do you have the perception that there are more women writers today? Do they have a distinct voice, or do you think that the issue of gender is not so important?

My perception is just that, a perception. I don't know if more women are writing these days, but it is obvious that many more women are publishing their work. Surrendering to the reader, without reserve or fear, whatever they imagine, witness, suffer or enjoy. What they invent, what they are burning to tell.

Is there a distinct voice? Is gender important or not?

Since I am a writer and not a theorizer, I can say that I answer these two questions every day of my life. For a while, it seemed to me that it was reverse discrimination to say

that literature written by women was different, that it contained something uncommon and urgent. I believed, in all honesty, that literature was gender-neutral, that like medicine, biology or arithmetic, you either know it or you don't, you can write or you can't. I still believe it, actually, but I also know that I find things in the stories and the intent of certain books that tell me that they could only have been written by women. However, once again, this is a question whose answer could fill a book.

Do you feel that the region's borders have disappeared thanks to the texts that you and your colleagues write?

Yes, I think that language and books transcend borders. But this is not a recent phenomenon. Great writers have been doing it for a long time. Amado Nervo and Rubén Darío, for example. Not to mention Gabo (García Márquez), Borges, Cortázar and Fuentes. However, we still have a long way to go. As with Latin American cinema, we need to hear each other more. Know more about each other, like each other more.

Do you think that there is a Latin American culture, or is it simply a sum of national and/or regional cultures?

I believe there are both.

Do you see any dangers in preserving the region's culture?

No. I think that we preserve the best parts. They aren't lost, even if they get absorbed. You have to take a look at what Day of the Dead has turned into in Mexico. Halloween pumpkins have been added to the famous and celebrated altars to the dead, and it's the migrant workers, not just the wealthy traveling for pleasure, who are bringing pumpkins back with them.

What opportunities do you see?

I see the Internet as the newest and most obvious opportunity. I use it, and I enjoy it. I have a blog on *El País* (from Madrid), and every day I realize how alike we Spanish speakers are in our emotions and concerns. And how it's possible to get to know one another and like each other in cyberspace and among multitudes.

Giving yourself permission to dream, what would you like to see in Latin America in the years to come?

Equality and certainty. To live in our countries without fear and without shame. Without feeling insulted, without this nightmare of imagining, sometimes correctly, but a thousand times incorrectly, that we could be the victims of crime, kidnapping or disgrace. It's like banging our heads against the clouds, the mountains and the sea.

Interview with Ricky Martin



Few artists of the Americas are as clear an example of bicultural heritage as Ricky Martin. Although he began his professional career

at an early age in Puerto Rico, it was his career as a solo artist that allowed him to conquer the English-speaking market, opening doors for other Latin American singers along the way. Less well known are his humanitarian efforts and his work in fighting child trafficking, an issue he addresses in this interview.

What is your general opinion of the state of culture in Latin America and the Caribbean?

The region is known for having its own very rich and, at the same time, very diverse identity. This fusion has given rise to a wealth of cultural expression that reflects our history.

Would you say that the hemisphere is more multicultural now than in the past? What examples would you highlight?

I think so. Influences from cultures as distant as the Middle East, Asia, Africa and Europe have continued to strengthen our own culture. We're noticing it in all of our artistic expressions, from music to literature, painting, theater, dance and film.

A new relationship between culture and philanthropy has emerged. How would you explain it?

Both music and philanthropy are bridges of hope. They are cultural phenomena that seek to unite us in

working for social progress—in our case, protecting children.

What would you like to see in Latin American culture, and how can the IDB help achieve it?

I'd like to see Latin American children have the right to be registered at birth. That's the purpose behind the "I Love America" campaign that we're promoting with the help of the IDB. At the same time, we'd like to keep working to stop child trafficking, which is in our view the most vicious crime in the world. In 2006, with the help of the Bank and the International Organization for Migration, we launched "Call and Live," the first regional campaign against human trafficking, with excellent results. We've educated millions of people about an issue that was once taboo. We've saved lives and generated hundreds of prevention calls as well as hundreds of investigations. In the future, new countries will continue to come on board.

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¹ Conversation between Juanes and Ricardo Ávila, September 2008.



A path toward the future. High atop the Andes, a topographer plots a new road that will allow isolated communities to participate more actively in the life of the nation. One of the Bank's fundamental goals has been to connect peoples and countries, breaking down barriers to trade, promoting access to social services and the exchange of technologies and new ideas. In the coming years, the Bank will support the initiatives of its member nations to expand their economic reforms, distribute the benefits of development and strengthen democratic institutions.

XI The IDB: A Half-Century of Results¹

It has been a half-century since the Inter-American Development Bank (IDB) was turned from an aspiration into a reality. Since then, the organization has established itself as a regional financial institution known for its excellence, with a broad, evolving portfolio that reflects the profound political and economic changes taking place in the region.

As such, the IDB initially focused on major projects aimed at closing the enormous gap in basic infrastructure and promoting social progress, but it adapted these programs as time went on, all the while playing an ongoing role in the sweeping structural transformations taking hold across the hemisphere. This was the case, for instance, when Latin American and Caribbean nations adopted policies that promoted, among other things, the lowering of trade barriers, institutional reforms and the involvement of the private sector in activities that were previously off limits. The Bank complemented these moves with new plans

and programs, proving once again that it was able to respond to the region's evolving needs without abandoning its focus on solving the region's critical issues.

This was confirmed once again in late 2008 with the onset of the global financial crisis, which resulted in shrinking lines of credit to the region. In response, the IDB quickly implemented short-, medium- and long-term plans of action aimed at guaranteeing liquidity and maintaining programs for improving competitiveness and growth opportunities.

A BIT OF HISTORY

Developments like these seemed unthinkable 120 years ago. The First International Conference of American States was held in October 1889 in Washington, D.C., and was attended by delegates from 18 countries. The event, which took place at the request of the United States, featured an ambitious, nearly seven-month-long agenda that

was finalized in the form of various agreements in April 1890. One of these called for the creation of an International American Bank with offices or agencies in the nations represented at the conference.

The issue reappeared sporadically at subsequent meetings. Finally, at the Seventh Conference held in Montevideo in late 1933, there was explicit talk of an Inter-American Bank that would function as a “Central Continental Bank, a regulator of credit and currency.” However, further action had to wait until 1940 when, as part of the Inter-American Financial and Economic Advisory Committee, a convention was drafted proclaiming the creation of the Bank and establishing its functions in greater detail. Once approved, the convention was signed by nine of the region’s countries.

These aspirations were vigorously proposed once again at the Bogota Conference, which in 1948 saw the creation of the Organization of American States (OAS). There, initiatives were presented that centered on the need to establish a financial institution to promote the region’s economic and social development. Consequently, the Inter-American Economic and Social

Council (IAECOSOC) of the OAS was asked to study these proposals. In 1950, the Council resolved that “under the current circumstances, it does not appear feasible or advisable to create institutions of this nature.” In response to this position, a specialized inter-American economic conference within the framework of IAECOSOC was held at the Quitadinha Hotel in the Petropolis district overlooking Rio de Janeiro from November 22 to December 2, 1954.

Prior to this meeting, the countries had submitted a preliminary report to the Executive Secretariat of the Economic Commission for Latin America and the Caribbean (ECLAC), which would later serve as the basis for a Preparatory Meeting presided over by Chilean senator Eduardo Frei Montalva, with Carlos Lleras Restrepo from Colombia as its speaker, and attended by Evaristo Araiza of Mexico, Rodrigo Fació of Costa Rica, Francisco García Olano of Argentina, and Cleantho de Paiva Leite of Brazil.

Based on their previous work, the countries of Latin America articulated their most comprehensive vision yet on their pursued objectives and mechanisms for creating a regional finan-

cial organization. The proposal from the Chilean delegation, a group that included the General Manager of the Central Bank of Chile, Felipe Herrera, was especially significant. According to the Chilean plan, resources for the new institution would consist primarily of contributions from the countries of Latin America. These nations would transfer nearly US\$3.5 billion from their international reserves with the assurance that the funds could be “reasonably and prudently mobilized.”

In an atmosphere overshadowed by a certain degree of skepticism, at the end of the meeting a commission was formed of representatives from the central banks of several Latin American countries for the purpose of submitting a project to the OAS on the creation of a regional financial institution. The team met in Santiago in 1955 to draft a set of by-laws that was sent to IAECOSOC to conduct the necessary governmental inquiries, but the process was not successful.

In 1958, due to growing regional turmoil, the plan began to change course. The correspondence between the President of Brazil, Juscelino Kubitschek, and the President of the United States, Dwight Eisenhower,

played a particularly influential role, as it laid the groundwork for the so-called “Pan-American Operation” proposed by Kubitschek and led to the establishment of the “Committee of 21” by IAECOSOC, a “specialized commission in charge of negotiating and drafting the articles of incorporation of an Inter-American financial institution.”

From January to April 1959, this Special Advisory Commission worked, largely on the basis of the ideas proposed at the Quitadinha, to draft the “Agreement Establishing the Inter-American Development Bank” at OAS headquarters. The final document containing the text of the Agreement was ratified by all the delegates on April 8, 1959. It established the Bank’s authorized ordinary capital at US\$850 million and an additional Fund for Special Operations (FSO) of US\$150 million. Its purpose would be to “contribute to the acceleration of the process of economic development of the member countries, individually and collectively.”

The new institution would have the following functions:

- i) to promote the investment of public and private capital for development purposes;



Improving living conditions by supplying clean water and sanitation services has been one of the IDB's top priorities from the beginning.

ii) to utilize its own capital, funds raised by it in financial markets, and other available resources for financing the development of the member countries, giving priority to those loans and guarantees that will contribute most effectively to their economic growth;

iii) to encourage private investment in projects, enterprises, and activities contributing to economic development and to supplement private investment when private capital is not available on reasonable terms and conditions;

iv) to cooperate with the member countries to orient their development policies toward a better utilization of their resources, in a manner consistent with the objectives of making their economies more complementary and of fostering the orderly growth of their foreign trade; and

v) to provide technical assistance for the preparation, financing, and implementation of development plans and projects, including the study of priorities and the formulation of specific project proposals.

The Secretary General of the OAS, through IAECOSOC, was then asked to keep the Agreement open for ratification until December 31, 1959, and to call the first Meeting of the Board of Governors of the Bank. The ratifications took place between October 14 and December 30. Once the necessary number of votes had been obtained, the Agreement took effect, giving life to the Inter-American Development Bank. The 20 founding members of the IDB were Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, the United States, Uruguay and Venezuela.

Meanwhile, a Preparatory Commission working at the OAS between September 1959 and February 1960 defined the structure and functions of the institution. The Board of Governors of the new entity met for the first time in February 1960 in San Salvador and unanimously elected Felipe Herrera as president of the Bank. Thus, the IDB officially began operating on October 1, 1960, and approved its first loan in February 1961.

DEFINING INTERNAL MANAGEMENT

By separating the Bank's ordinary capital (OC) from its additional, "soft" resources, the organization successfully addressed what was perhaps the greatest uncertainty in conversations about the creation of the IDB: how great the voting power of member countries within the institution would be in proportion to their share of the OC. Once it was agreed that the Latin American nations could contribute more than 50 percent of the OC, as a voting bloc they were more powerful than the United States, the primary individual shareholder.

Although the IDB has had checks and balances in place since its inception to facilitate consensus-building and mediate the differing interests of the member countries in specific operations with conflicting aspects, the legal and political principle that the voting power of the member countries is equivalent to their contribution to the OC has been preserved, even as extra-regional countries began joining the Bank during the 1970s. Within this context, Latin American countries retained majority decision-making power in the institution's governing bodies.

Another original feature of the new entity, which had been proposed in various documents prior to its incorporation, was its authorization to receive and administer soft resources, the access to which was nearly unprecedented among the first international financial organizations. These resources were aimed at making credit operations and technical assistance possible under concessional terms for relatively less developed countries or areas or for low-income segments of society.

Such terms included reduced interest rates, longer grace and amortization periods and the option of repayment in local currency. For these operations, resources were needed at costs so low that they could not be obtained in international markets. Incorporating these resources into the financial structure of the institution posed a challenge, leading the parties to the Agreement to create the FSO. The FSO's soft resources were greatly bolstered when the United States placed the Social Progress Trust Fund under the control of the IDB as part of the Alliance for Progress.

Given the need to safeguard the IDB's international financial credibility, incorporating soft resources into its financial structure could potentially



In 1961, the first president of the IDB, Felipe Herrera, and the President of the United States, John F. Kennedy, signed an agreement creating the Social Progress Trust Fund, to be administered by the IDB.

have created a problem in terms of the solidity of the Bank's backing in obtaining funds on the market. The issue was resolved by establishing a clear distinction between cases and conditions where OC resources could be used and where soft funds could come into play. Additionally, in some cases OC resources could serve as backing for obtaining funds on the market, but soft funds would not play such a role. However, this separation of resources did not lead to the division of their administration into two parallel units, as proposed in some negotiation phases regarding the Agreement. Instead, their administration was assigned to a single, unified structure for the entire IDB. This allowed the Bank to maintain unity between its operational policies and its financial management and administration policies without damaging its solvency in international capital markets.

During the formation phase of the institution, the location of the Bank's headquarters was also a source of debate. One group of countries favored locating the IDB in the United States to facilitate the Bank's links to its primary source of resources, while others preferred sites in Latin

America for the purpose of reinforcing its regional character. To that end, an official proposal was submitted to make the city of Caracas the Bank's headquarters, which had already been suggested by Venezuela in 1954 during Felipe Herrera's tour through several countries to raise support for the project to be presented by Chile at the Quitadinha. Only after intense negotiations did the members settle on Washington, D.C., as the Bank's headquarters.

According to the Agreement, all powers related to directing the Bank would be assigned to the Board of Governors, composed of a governor and a deputy governor from each member country and appointed by each country. Their functions included admitting and suspending members in accordance with the Agreement's provisions, designating the president of the Bank, setting the amount of the OC and the FSO as well as determining each country's contribution to these funds, approving the Bank's financial statements, and revising the Agreement. Some proposals brought forth during previous negotiations included the power to establish the Bank's operational policies, something that was ultimately not incorporated into the Agreement due to its implied inclusion

in the functions of the Board of Governors as the holder of all governing powers for the institution. In fact, all decisions regarding the Bank's financial and operational policies discussed and proposed by the Board of Executive Directors were submitted to the Board of Governors for consideration. The Board was to hold a meeting once a year in the capital of one its member countries, but from very early on it implemented the practice of calling extraordinary meetings.

Responsibility for conducting the Bank's day-to-day operations fell to the Board of Executive Directors, the president, and an executive vice president, who, in practice, was from the United States. The Board of Executive Directors would function permanently at the Bank's headquarters. It was composed of seven directors, six of whom were elected by designated groups of Latin American countries and the remaining one by the United States, all of them for a three-year term. Special attention was given to the composition of the group to ensure that relatively less developed countries would have access to voting power.

The president led the meetings of the Board of Executive Directors and

acted as the head of administration, the structure of which was flexibly responsive from the very beginning to the demands posed by the volume and direction of the Bank's operations. The Bank was initially established with several divisions, but was soon re-organized into six departments, a structure that was maintained even as the number of departments grew. The initial six departments were operations, financial, technical, legal, administrative and secretarial.

As a reflection of its increasingly close relationship with its member countries, the Bank opened representative offices throughout the region. In less than a year, the institution was able to implement the central aspects of its organization. It had succeeded in reconciling its multilateral character with its regional roots and established the transparent and constructive coexistence of its majority partner and its borrower countries, facilitating the fluid formulation of its policies and sound operational performance. A contributing factor was the Bank's flexibility in adapting its management activities to new challenges, a trait it possessed from the start.



More and better education for Latin American boys and girls: an area where much has been achieved and where great challenges still lie ahead.

THE FIRST DECADE

The bank was created with US\$1 billion in resources, of which US\$850 million was allocated to authorized OC and US\$150 million to the FSO. Of the OC, US\$400 million came from contributions payable over a period of three years, the balance corresponding to subscribed callable capital that could be used as backing for accessing financial markets. Contributions from the United States to the OC were to be made in United States dollars, while those from borrower countries would be made in both United States dollars and local currencies. By the end of 1970, the IDB had approved financing totaling more than US\$4.1 billion. This volume would have been impossible without vigorous financial support from all of the Bank's member countries, particularly the United States.

Under the presidency of Felipe Herrera, the OC received three increases. The first was approved in 1964 for the amount of US\$1.3 billion, of which US\$75 million was payable in cash; the second came in 1968 for US\$1.005 billion, none of which was in cash; and the third was authorized in 1970 for US\$2 billion, including US\$400 million

in cash. Authorized OC would thus grow to US\$5.155 billion, bringing the institution's total resources to US\$8.98 billion.

The FSO was established to handle loan requests requiring concessional terms. In the first decade of the Bank's existence, these operations held special qualitative importance for relatively less developed countries. At its Annual Meeting held in Panama in 1964, the Board of Governors decided that future increases in soft resources would take place via the FSO, with the goal of simplifying the financial and operational structure of the IDB. The Bank authorized significant increases to its FSO: US\$73 million in 1964, US\$900 million after the meeting in Panama, and US\$1.2 billion in 1967. In 1970, an expansion of FSO resources was approved in the amount of US\$1.5 billion, to be contributed between 1971 and 1973. In 1970, Felipe Herrera recognized the region's more highly developed countries for their willingness to allow their FSO contributions in local currency to be used for loans to other countries, particularly relatively less developed ones.

In September 1960, in the midst of the Bank's organization, the United States entrusted the entity with the management of the Social Progress Trust Fund (SPTF), which originally held

US\$394 million and grew to US\$525 million in February 1964. The SPTF's resources were channeled toward financing Alliance for Progress-backed programs in rural development, urban housing and sanitation, and advanced education. The Bank ensured that these investments would become a part of broader development and reform plans in beneficiary countries requiring significant mobilization of local resources.

The Bank's capacity to generate additional resources beyond the contributions paid by its member countries, particularly for its OC, was a reflection of its robust financial health, its positive operational performance and the excellent quality of its portfolio. As a result of these factors, its marketable securities received the highest rating in international markets. This rating in turn allowed it to obtain resources under favorable terms through bond issues and direct loans.

During its first decade of operation, the Bank received additional financial support from several non-member developed nations through loans, parallel financing, and the sale of shares in special loans and funds under its management, the largest of which was created by Canada. A significant por-

tion of money accumulated from loans was obtained between 1968 and 1970. All of these contributions were important precedents for the incorporation of extra-regional countries into the Bank, which took place the following decade.

At the start of the IDB's operation, it was thought that the majority of its debt would be placed in United States markets, but by the end of the first decade, the statistics showed that resources originating in the United States comprised 48 percent of all acquired funds, while 33 percent of resources came from Austria, Belgium, Germany, Italy, Japan, the Netherlands, South Africa, Sweden, Switzerland and the United Kingdom, and 19 percent came from short-term bonds purchased by the region's central banks. Because the Bank was obtaining a substantial part of its resources from international banking and securities markets and was therefore subject to the prevailing interest rates in those markets, the average interest rate for OC loans during its first decade was 8 percent per annum. The interest rates at which the Bank had to obtain its resources and the demands and restrictions imposed on the Bank's operations by the relatively high cost of interest were issues

under constant analysis by the Board of Executive Directors and the Board of Governors.

The IDB adopted special policies aimed at encouraging internal savings and investments, incorporating measures into its loans to strengthen the financial situation of executive organisms or to encourage the revision of fee structures for its services. It also supported national development institutions; industrial, agricultural and mining banks; credit, marketing and housing cooperatives; and other financial institutions receiving credit and technical assistance.

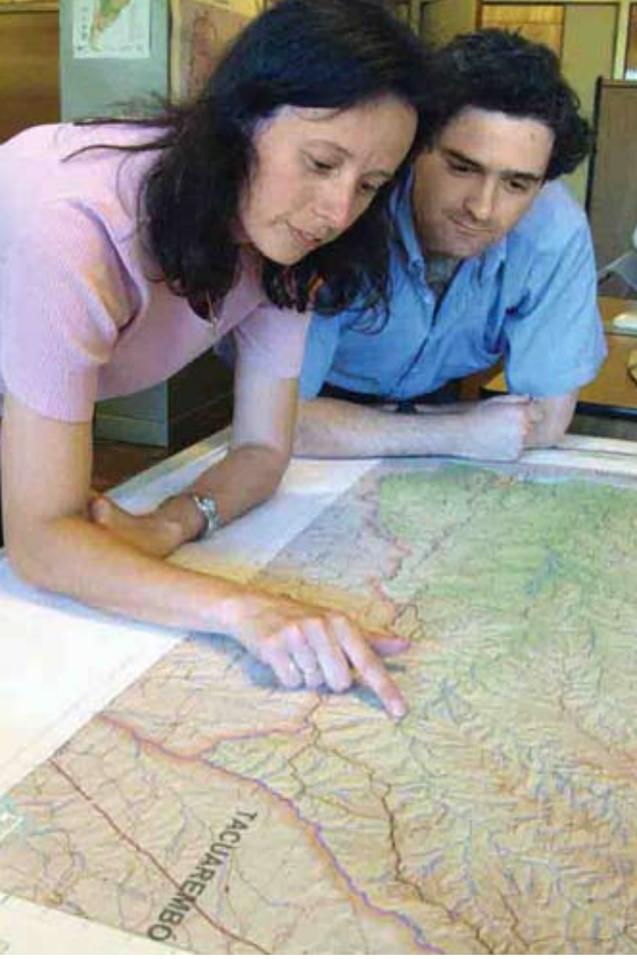
For Latin America as a whole, the Bank approved financing of more than US\$15 per capita during its first decade. For the relatively less developed countries of Central America, the Caribbean and South America, per capita financing was almost twice as high. Financing terms for less developed or more vulnerable countries or areas, granted largely as soft resources, were much more favorable in terms of interest rates, amortization and grace periods and requirements for local matching funds.

As a result of the Bank's lending activities, at the end of its first decade

its portfolio consisted of more than US\$4.102 billion in authorized loans for over 600 programs and projects with a total cost of over US\$11.4 billion. Of this total, 38 percent was authorized with OC funds, 49 percent from the FSO, 12 percent from the SPTF and 1 percent from funds managed by the Bank on behalf of non-member countries such as Canada, the United Kingdom, Sweden and the Vatican. Thus, concessional loans came to account for more than 60 percent of all IDB operations.

Cumulative disbursements during this period exceeded US\$2.15 billion, or more than 50 percent of all approved loans. By the end of the decade, as a result of its expanded technical and operational capabilities as well as the impact of its technical assistance and pre-investment activities, the Bank had approximately US\$1.8 billion in potential operations under consideration, demonstrating the growing ability of its borrower countries to develop investment programs and projects.

By the end of the period, the Bank's portfolio showed that 45 percent of committed resources had been channeled toward productive activities: agriculture, which benefited from



Uruguay expanded its geographic database with everything from maps to computers for the purpose of planning and managing infrastructure as part of a project financed by a donation from the IDB.

\$1.103 billion in loans, or 27 percent of the portfolio, and industry (including export financing), mining and tourism, which together received US\$717 million or 18 percent of the portfolio. Physical infrastructure, i.e., projects in transportation, ports, telecommunications and electrical power, received loans reaching US\$1.204 billion or 29 percent of the portfolio. Urban development received US\$373 million, equivalent to 9 percent of the portfolio, while sanitation received US\$476 million, or 12 percent of the portfolio. Education benefited from US\$146 million (4 percent), while health care got US\$11 million. Finally, US\$49 million was allocated to pre-investment activities, equivalent to 1 percent of the portfolio.

INTERNATIONALIZATION

The start of the 1970s coincided with the retirement of Felipe Herrera as president of the Bank and the arrival of Antonio Ortiz Mena as the new head of the organization. The transition was accompanied by profound changes in the world economic order as a result of the unexpected rise in oil prices in 1973 and the subsequent imbalances that were generated. Although many

Latin American nations had just experienced high growth rates, they could not escape the impact of the global recession, nor were they immune to the temptation to accept cheap, abundant loans. For example, contributions from official bilateral or multilateral sources to foreign investment in the region fell from an average of 60 percent at the start of the 1960s to less than 15 percent by the end of the 1970s.

The debt crisis of 1982 brought with it skyrocketing inflation, budget crunches and a decline in social indicators. At the same time, Latin America recovered its democratic lifestyle, along with a “de-ideologization” of economic policies that paved the way for widespread reforms at the end of the 1980s and in the 1990s. By the end of the century, the region would recover its stability thanks to fiscal reforms and orthodox monetary policies with independent central banks. This period also saw increased efficiency as a result of accelerated, unilateral economic liberalization and the resumption of export expansion. Privatizations, an overhaul of the regulatory system and government decentralization were also set in motion.

In addition to market liberalization, there was a fresh attempt to modernize integration mechanisms and free trade associations.

However, before delving into an analysis of the impact of these circumstances on the IDB's activities, it is necessary to take a look at its membership. Initially, in accordance with its incorporation agreement, only countries belonging to the OAS could be members of the Bank. Thus, when European colonial territories in the Caribbean gained their independence and these new nations were incorporated into the OAS, they became eligible for membership in the Bank, as in the case of Trinidad and Tobago in 1967 and Barbados and Jamaica in 1969. The process continued with Guyana in 1976 and the Bahamas in 1977. Suriname joined the group in 1980, and Belize came on board in 1992. Canada's entry in 1972 as a full-fledged member was also a significant development, although its close ties to the IDB had been firmly established for almost 10 years.

This change in the original rules culminated in the mid-1970s with the addition of Japan, Israel and several European nations as IDB partners.

Acceptance by the borrower countries of a substantial reduction in their relative share in the Bank's capital for the purpose of creating room for the entry of new members was crucial. Their incorporation as full-fledged members and not as associate members would therefore represent an important change in the original capital structure, in which borrower and non-borrower shareholders would own approximately equal parts. The concept of a bank in which ownership is split almost evenly among countries that receive and those that contribute resources had been proposed in the 1970s and was formally adopted 20 years later as part of the agreements of the Bank's Eighth General Increase in the Resources, negotiated in Guadalajara in 1994.

One of the major milestones of the negotiations on the incorporation of extra-regional countries was achieved in December 1974 in Spain, when 12 nations signed the Madrid Declaration establishing the basis for their entry into the IDB. The mechanisms for political decision-making and the legal formalities allowing them to sign the agreements and contribute the required resources to the Bank varied from country to country. Therefore, they



Japan signs documents to enter the IDB as part of a group of countries from outside the region, thus adding the global dimension that has characterized the institution since 1976.

could not join the bank simultaneously. The first group of nine countries (Belgium, Denmark, Germany, Israel, Japan, Spain, Switzerland, the United Kingdom and Yugoslavia) joined the Bank in 1976. Another six countries (Austria, Finland, France, Italy, the Netherlands and Sweden) followed in 1977. The process was finalized with the incorporation of Portugal in 1980 and Norway in 1986. Korea would later join the IDB in 2006, followed by China in 2009.

During the deliberations on the entry of extra-regional countries, it was necessary to come to a consensus on what their relative share in the Bank's OC would be, as no models or precedents existed to define this particularly important policy aspect. Interestingly, in the Bank's initial conversations with Japan, it was agreed that this Asian nation would be the principal shareholder among the Bank's extra-regional member nations, albeit marginally. Japan's special role would be reaffirmed 20 years later in the agreements pertaining to the Eighth Increase.

Another interesting aspect of the negotiations had to do with the incorporation of Eastern European coun-

tries, whose ties to the Soviet Union had been loosening in anticipation of the post-Cold War reality. Contact was made and negotiations were conducted with several countries, resulting in the entry of Yugoslavia, followed by Croatia and Slovenia in 1993. Besides Japan, the only non-European country to join the Bank initially was Israel. This country brought with it a wealth of valuable technical experience, particularly in agriculture and the management of water resources—technologies that are highly relevant to many Latin American countries.

EXPANDED OPERATIONS

Despite the dramatic institutional changes brought on by the incorporation of new countries as members of the Bank, the Ortiz Mena years were marked by strong programmatic and operational continuity from the Bank's initial phase of activity. The IDB's actions were primarily characterized by its capacity for response and innovation in meeting new demands and needs.

Quantitatively, the Bank became an increasingly important actor in the region's external financing activities.

During the presidency of Ortiz Mena, total authorized resources, which had totaled nearly US\$9 billion after the 1970 increase, grew by US\$32.81 billion (the OC by US\$28.806 billion and the FSO by US\$4.005 billion). In 1975 the Board of Governors approved a fourth increase amounting to US\$5.806 billion in authorized capital for the 1976–78 period, including resources from new Bank members. There was a fifth increase of US\$8 billion followed by a sixth increase of US\$15 billion in subsequent years. Of these total resources, only US\$1.703 billion was payable in cash, while the US\$675 million in cash received for the sixth increase represented merely 4.5 percent of the total amount pledged. Of these three increases, US\$1.552 billion, US\$1.75 billion and US\$703 million, respectively, were allocated to the FSO.

The proportion of operations approved with funds from the OC, complemented by intra-regional capital, grew in relation to the Bank's previous period, reaching 70 percent of the total portfolio between 1971 and 1987. Meanwhile, as a reflection of the availability of soft funds, the proportion of the FSO fell to 24 percent of

the portfolio. Funds from the OC and the FSO were also used to finance technical cooperation operations, which, in the case of the FSO, included those of a non-reimbursable nature. Funds contributed to the portfolio by other sources during the period amounted to 4 percent. Due to the insufficient availability of FSO funds, in 1983 the Intermediate Financing Facility (IFF) was created to defray a portion of the costs of interest on OC loans to benefit less developed countries.

The annual volume of Bank-approved loans grew notably over the 17 years of Ortiz Mena's presidency, ultimately exceeding US\$3 billion per year starting in 1983. During that period, accumulated loans grew to US\$32.606 billion. The physical infrastructure sector received US\$13.207 billion, equivalent to 41 percent of the total; the productive sector received US\$13.18 billion, or 40 percent of the total; and the social sectors received US\$5.718 billion, or 18 percent of the total. Within the infrastructure sector, the largest amounts went to energy, with US\$8.88 billion, followed by loans for transportation with US\$3.974 billion and loans for communications with US\$353 million.



Throughout the years, the Bank has stood firm in its efforts to promote work and improve quality of life for lower-income populations.

EVOLUTION AND GROWTH

When Antonio Ortiz Mena retired as president of the IDB to assume new responsibilities in Mexico, the IDB found itself at a crossroads, as the foreign debt crisis had shaken some of its foundations and core premises for action. Negotiations among the Governors to expand the Bank's resources were stretched out over two years of meetings, proving that coming to a full consensus that would satisfy all the Bank's members would be difficult. Two opposing views were debated, one espousing a "small" Bank that would continue along its traditional line of action without a significant increase in resources, and another arguing for a "large" Bank that would receive a substantial increase and modify its policies and line of action. It was in this context that the Board of Governors appointed Enrique Iglesias as the Bank's new president in February 1988.

The Governors finally overcame their differences, accepting the concept of a large organization, at their Annual Meeting in Amsterdam in 1989, where they agreed to increase the Bank's resources on the basis of a new mechanism through which loan

approvals would be postponed for analysis by one or more executive directors and would be submitted at the end of the discussion period to the Board of Executive Directors for approval using current mechanisms. New organizational guidelines were also enacted whereby policy adjustment loan analyses would be conducted by a specialized department, with their approval conditioned on World Bank co-financing for a period of two years. During this time, the Bank acquired experience in processing these operations, and as a result of its sound financial management, the condition was allowed to expire.

The Seventh General Increase in Resources, approved in 1989 in the amount of US\$26.5 billion and slated for allocation to the OC from 1990 to 1993, took effect on January 17, 1990. FSO resources increased by US\$200 million. The primary objective of the increase was to strengthen the Bank's backing of borrower countries in their efforts to re-establish growth and macroeconomic equilibrium, battle inflation, solve the foreign debt crisis, correct global and sectoral economic distortions, expand employment and improve social conditions.

(Continued on page 284)

Interview with Daniel Zelikow



Daniel Zelikow, a U.S. citizen, has been the executive vice president of the IDB since 2007. Prior to joining the Bank, he was the managing director of

the Government Institutions Group of JP-Morgan Securities Inc., which he joined in 1999 after holding senior positions in the United States Department of the Treasury. As deputy assistant secretary of the Treasury Department, he was responsible for financial policy towards the Americas, Asia and Africa. A summa cum laude graduate of Dartmouth College, Zelikow holds a doctorate in economics from Oxford University. He has been an active contributor and advisor to nonprofit institutions as well as to ad hoc committees established by multilateral agencies and think tanks.

How do you view the evolution of the IDB and its recent changes?

The IDB is an essential player in the region, but—like other multilateral development institutions—for a while it was using an outmoded operating model that made it less relevant and put its long-term future at risk. At the same time, there were administrative procedures that definitely had to be updated to make the institution more efficient. Moreover, it was evident that the region was at a turning point that called for a clear definition of priorities and of the best way to achieve effective development.

Can you be more specific?

The model had to be changed based on the region's success. Many countries have applied solid economic policies and successful structural reforms that have allowed them to grow more quickly and gain access to international capital markets. In addition, the development of domestic capital markets paved the way for local funding sources to finance development. Therefore, the Bank's main product—long-term loans in United States dollars—became less and less necessary for some of our borrowers. Although the current financial

crisis underscores the need for the Bank to maintain its financial strength, in the long run the underlying realities will become apparent and we will have to adapt to them. This means that we must offer more financial products that set standards in the market, loans in local currency and products that help our shareholders control their financial and economic risks.

What can be said about the IDB's technical expertise?

Obviously, the IDB doesn't have a monopoly on knowledge with respect to development in our region. More and more frequently, governments are using their own experts who are just as good as or even better than ours and who have access to networks where they can obtain other sources of expertise. Therefore, we've had to think about the areas where we stand out and focus our efforts on the issues that may be important over the next 20 years, such as creating more effective ways to promote the social and economic inclusion of the poor, building better infrastructure in the region, developing sustainable energy sources or adapting to climate change. What sets us apart is that we can combine knowledge and expert

advice with the loans we grant, but we mustn't limit ourselves to that. In other words, we should be in a position to offer expert advice alone if money is not required, and financing by itself if our clients' plans are already fully developed.

Would you like to add something else?

Our client base was too small and we couldn't achieve the maximum impact. There were basically 16 sovereign governments and three of them absorbed 65 percent of our financing. As any financial manager knows, that is a dangerously concentrated client base. For that reason we recognized that we needed a larger scope if we were to have a positive effect in the region, and we set out to develop a broader clientele that included sub-national governments and private companies, while always keeping in mind appropriate risk management guidelines, of course.

There were some internal changes.

We are thoroughly studying the policies and procedures to see what

can be done so that this organization can serve its clients better. There is the feeling at the Bank that we have to modernize our own culture. We are really the region's Bank, and the relationships and the affinity we have with our shareholders gives us very unique access and insider knowledge. However, two-thirds of our employees work in Washington. Therefore, an important part of rejuvenating our presence in Latin America and the Caribbean is to have a greater physical presence in the countries themselves.

What has been achieved?

The Bank is doing well in these aspects. We have cut loan approval times in half, and disbursements under our regular programs reached unprecedented levels last year and the year before. Loans to sub-national governments and to the private sector currently make up a significant portion of our portfolio. We offer products in local currency, and we're launching an initiative to provide specialized expert advice. We were able to increase our on-site employees by 26 percent in the

space of a year and have updated our risk evaluation process and our procedures. We are beginning to improve our independent programs for developing knowledge and skills, as I have already mentioned. The bottom line is that in the long term, the Bank won't be able to provide significant help in the region by just lending money.

In your opinion, what is the Bank's function in the face of the current international crisis?

It is clear to me that the Bank continues to play an important anti-cyclical role in the region's public and private sectors, especially in times like these. We must have sufficient financial headroom to be able to play this role, but at the same time we must not lose sight of the fact that we are, above all, a development institution. And this anti-cyclical intervention must also favor development in public as well as private sector projects. When we think about the way we approve loans in times of crisis, we have to be just as judicious as we are during times of prosperity, if not more so.

(Continued from page 281)

During this period, the Bank was re-organized in an attempt to modernize and adapt its departmental functions by creating new units and merging others. New divisions were created, including divisions to manage sector-focused policies and loans; macroeconomic policies for dialogue with borrower countries; environmental protection; education and health; microenterprises; co-financing and export promotion; and regional cooperation.

The Bank took on the administration of the Multilateral Investment Fund (MIF), officially established on January 11, 1993, with an initial contribution by its member countries of US\$1.2 billion, later expanded to US\$1.3 billion. The MIF, conceived as part of the Initiative for the Americas, has since its inception supported innovative mechanisms for improving the environment for private investment, workforce training, and the development of small businesses.

At the end of the Seventh Increase period, the Bank's portfolio of activities showed highly satisfactory results. Authorized loans between 1990 and 1993 totaled US\$21.1 billion, more than four times higher than at the time of the Sixth Increase. Loans granted in

1992 and 1993 reached a remarkable US\$6 billion, an unprecedented figure at that time. These authorized amounts allowed the Bank to reclaim its status in 1991 as the primary official source of external financing for the region's development, particularly for countries with smaller economies and lower income, a position it had lost in previous years as a result of the reduced availability of resources.

Nevertheless, by 1994, the IDB was facing new and greater challenges. The economic progress made by many countries in the region since the start of the decade was not enough to stop the social gap from widening due to increased unemployment, the unequal distribution of income, and the expansion of the informal economy. All of this signified the need to review the Bank's priorities once again and adapt its modes of action in a way that would improve its contribution to the region's development during the second half of the decade and in the transition to the new millennium.

The principal elements embodying the strategic guidelines of the Bank's action plan during the Eighth Increase period included such aspects as productive modernization, strengthening



The construction of schools in Haiti was financed by a long-term, low-interest loan as part of an IDB concessionary program for less developed countries.

the central role of the private sector, social reform, financial reform, modernizing the government, strengthening civil society and a citizenry dedicated to economic and social development, and democracy.

In April 1994 in Guadalajara, Mexico, the Eighth General Increase in Resources was approved by the Board of Governors in the amount of US\$40 billion, increasing the OC to US\$101 billion. The Governors authorized an increase of US\$1 billion for the FSO, thus bringing its resources to over US\$10 billion. This increase was the largest in the Bank's history and the largest amount ever authorized to a regional multilateral development institution. The agreement was ratified on July 31, 1995, along with a cash contribution of US\$1 billion and US\$30 billion in callable capital for the OC, the subscriptions for which would be issued in six installments between 1995 and 2000.

The Governors also agreed to modify the voting power of the countries. The participation rate of extra-regional nations more than doubled, rising from 7.132 percent to 15.996 percent. The United States' share fell from 34.627 to 30 percent, while Canada's share

dropped from 4.374 to 4 percent. The Latin American and Caribbean countries decreased their participation from 53.867 to 50.004 percent. Another change in the Bank's representative composition was ushered in by the addition of two seats on the Board of Executive Directors, one for extra-regional countries and the other for borrowers.

BUILDING ON REFORMS

The 1990s were an extraordinary period of reform in Latin America and the Caribbean, when the role of government was redefined and a clear trend toward political and administrative decentralization in the region's countries began to emerge. The region's growing openness to foreign investment flows and the private sector's increasing involvement in areas that were previously off limits were also evident. Nevertheless, these changes were accompanied by rising volatility as a result of international circumstances.

These events had a clear impact on the Bank's role. In response to new trade-related and geopolitical realities, the IDB opened an office in Tokyo in 1995. In the same year, the Bank's Board of Executive Directors approved

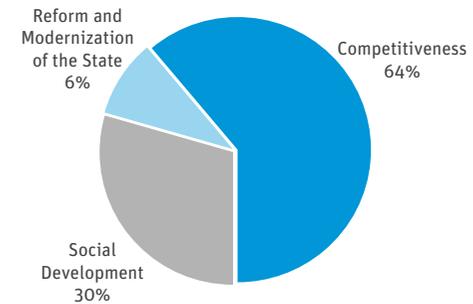
the offer of guarantees without the need for government-issued counter-guarantees.

Along with these new developments came a clear emphasis on lending programs. For example, in 1997, most of the Bank's lending portfolio was concentrated on initiatives for reducing poverty, social sector reforms and government modernization programs (see Figures 11.1 and 11.2, showing Bank loans by sector between 1961 and 2008, and in 2008).

An essential milestone was achieved in 1999 when the more economically developed countries agreed to convert the equivalent of US\$2.4 billion of their home currency resources in the FSO into foreign currencies for the benefit of less developed nations. At nearly the same time, a plan valued at US\$9 billion above the normal credit limit was approved for a period of one year to help confront internal financial emergencies. These efforts would result in US\$4.57 billion in approved loans for the purpose of offsetting global financial volatility.

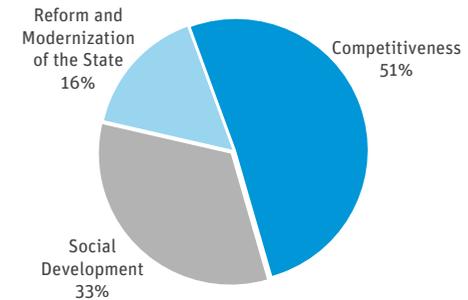
With the dawn of the new century, the IDB continued to place a priority on government reform and modernization efforts. At the same time, new flex-

Figure 11.1 Lending by Sector, 2008



Source: IDB (2009).

Figure 11.2 Lending by Sector, 1961–2008



Source: IDB (2009).

ible credit instruments were approved, including loans for innovations, multi-stage loans, sector-focused mechanisms, and tools for project preparation and execution. The development of new mechanisms and programs for financing occurred at a time when the economies of Latin America and the Caribbean were beginning to experience a remarkable boom comparable to the one that took place in the 1960s. Thanks to factors such as these, the balance sheet was quite encouraging by the time Enrique V. Iglesias took the helm of the institution. Between 1988 and 2005, the Bank's lending activities grew to US\$100.694 billion, distributed across 20 different issue areas. Of this total, 23 percent was concentrated in the area of government reform and modernization, followed by social investment (19 percent), transportation (9 percent), energy (8 percent), sanitation (6 percent) and urban development and housing (6 percent).

This sum was achieved as a direct result of capital increases that expanded the Bank's lending capacity to some US\$8 billion a year. This was complemented in 1999 by a capital increase of US\$500 million approved by the member countries of the Inter-American

Investment Corporation (IIC), thus expanding the Bank's capacity to facilitate loans to the region's small and medium-sized enterprises (SMEs). Also, in recognition of the MIF's success, in 2005 its donors agreed to replenish its resources with US\$502 million in new contributions.

In addition to expanding, its lending capacity, during Iglesias's term the IDB greatly developed its academic research capacity. Avant-garde work by specialists in the Office of the Chief Economist, in collaboration with a vast network of research centers across the region, shed light on an entire range of development aspects, from the impact of non-economic factors such as demographics and the quality of public institutions to issues such as access to credit for companies and families, the vulnerability of financial systems in times of crisis, the creation of formal employment, regional economic integration, and the keys to competitiveness.

The IDB also confirmed its ability to call together global players by leading numerous meetings of organized advisory groups to coordinate contributions from the international community in support of various countries in the

region. The largest and most complex of these was the Consultative Group for the Reconstruction and Transformation of Central America, launched in 1998 after Hurricane Mitch, a devastating storm that resulted in the loss of more than 10,000 lives and some US\$6 billion in economic losses in the countries of the Central American isthmus. Thanks to the combined efforts of governments, multilateral institutions and civil society, nearly US\$9 billion was pledged in the form of humanitarian aid, donations, concessional loans and debt relief for the region.

At the same time, the Bank reaffirmed the leadership position it had assumed since its inception in supporting social programs. In addition to traditional areas such as health care, education and housing, the IDB was a pioneer in supporting innovative initiatives that would later spread throughout the region and serve as inspiring models for other parts of the world. One example was the Favela-Bairro Project, an initiative born in Rio de Janeiro to improve quality of life in marginal neighborhoods through investments in infrastructure, public services and social programs. Another emblematic IDB-supported initiative

was PROGRESA/Oportunidades, a conditional cash transfer program in Mexico.

Despite the achievements of his long term in office, upon his departure from the IDB, Iglesias confessed his frustration over the region's meager economic growth, which had diminished the possibility of significantly reducing poverty and closing the gaps that have made Latin America the world's most inequitable region. Paradoxically, when Iglesias passed the torch to his successor, Luis Alberto Moreno of Colombia, Latin American economies began a clear rally from the "lost half-decade" that followed the Asian and Russian financial crises in 1997 and 1998 and was exacerbated by the terrorist attacks of September 11, 2001.

A MORE AGILE BANK

Despite this recovery, which would last until the outbreak of the global financial crisis in 2008, there was a downward trend in the demand for multilateral financing, particularly from medium-income countries with broad access to international financial markets and their own growing inter-



In a pioneering IDB project, the municipal government of Rio de Janeiro joined forces with non-governmental organizations and residents of the city's favelas to improve living conditions there.

nal capital markets. These countries, who were once major clients of the IDB, the World Bank and the International Monetary Fund (IMF), were now less in need and had even less desire for the traditional long-term loans offered by multilateral institutions in Washington.

Upon assuming the presidency of the IDB in 2005, Moreno made it clear to the institution's staff that the Bank's major challenge would be to become "more agile, more innovative and more efficient" in supporting member countries. The IDB needed to concentrate on areas where it could have maximum impact in terms of development, decentralize its operations in order to be closer to its clients, and create a culture of results.

Under the Moreno administration, the IDB sought to expand its client base, simplify its procedures for preparing financial operations, and realign its organizational structure. The first objective was a response to the new realities of the region; as a result of the decentralization processes carried out by many countries, the responsibility for a great number of basic services now lay in the hands of states, provinces and municipalities instead of national

governments, and these sub-national governments were in need of the Bank's services. The second objective sought to reduce the Bank's preparation time for projects, with the goal of placing greater emphasis on risk control during execution and on obtaining results. Finally, the Bank's realignment was intended to pave the way for a new matrix structure and the Bank's increased presence in borrower countries.

Box 11.1 A New Organizational Chart

The Bank's realignment led to the creation of four vice presidents who oversee all the IDB departments and report to the executive vice president, who is responsible for the day-to-day administration of the Bank. The Vice President for Countries manages the Bank's relationships with the borrower countries and supervises the 26 IDB representatives across the region. The Vice President for Sectors and Knowledge is in charge of experts in different areas of specialization. The Vice President for Private Sector and Non-Sovereign Guaranteed Operations supervises the activities of the Department of Structured and Corporate Finance, the IIC and the MIF, the three programs related to the private sector. The Vice President for Finance and Administration organizes and manages the IDB's resources and provides the support services needed for an efficient operation.



Upon being elected president of the IDB in 2005, Luis Alberto Moreno declared that the Bank's main challenge was to become "more agile, more innovative and more efficient."

The Bank's renewed focus on key sectors for regional development has led to an emphasis on infrastructure, energy, water and sanitation. In the case of the latter two sectors, two specialized programs have been launched: the Sustainable Energy and Climate Change Initiative (SECCI) and the Water and Sanitation Initiative. SECCI has distinguished itself through its promotion of renewable energies and energy efficiency in the region. The Water and Sanitation Initiative, which spearheads programs for improving basic services in cities and rural communities throughout the region, attracted the interest of the Spanish government, which in 2008 granted the IDB control of a €300 million fund for financing these types of projects in the region.

Another recent initiative responds to the need to seek alternative business models for bringing the benefits of economic development closer to the masses, that is, low-income segments that lack opportunities for creating their own wealth. The Opportunities for the Majority Initiative supports projects with corporations, non-governmental organizations (NGOs) and communities to create jobs and offer quality products and services to people at the

bottom of the socioeconomic pyramid.

In addition to the region's continued economic recovery, the organizational changes that were implemented from 2006 to 2008 spurred an expansion in the IDB Group's operations. Funds approved by the Bank, the IIC and the MIF rose from approximately US\$7 billion in 2006 to US\$9.6 billion in 2007 and a record-breaking US\$11.6 billion in 2008.

In turn, the volume of financing aimed at the private sector grew as a result of a series of decisions made by the Board of Governors in 2005 and 2006, including increased limits for non-sovereign guaranteed loans and the expansion of eligible sectors for these types of operations. Originally, these loans and guarantees could not exceed US\$75 million and could only be granted for infrastructure, energy and capital market projects. The new ceiling was fixed at US\$200 million (in exceptional cases, up to US\$400 million) and eligible sectors were expanded to include manufacturing, agroindustry, mining, tourism and other services.

The Governors also authorized non-sovereign guaranteed loans to sub-national entities and state-run or mixed enterprises. In 2006, the Board of Executive Directors permanently established

the Regional Trade Finance Facilitation Program, launched as a pilot concept the year before to facilitate loans for export and import operations.

Thanks to these reforms, the volume of non-sovereign guaranteed operations, primarily concentrated in private firms, grew from US\$683 million in 2005 to US\$2.9 billion in 2008, when such symbolic operations were approved as the US\$400 million loan for expanding the Panama Canal.

Another important topic on the IDB's agenda in recent years has been debt relief. Although the IDB had not participated in the Gleneagles Agreement, under which developed countries decided to cancel a large portion of the debt owed by Heavily Indebted Poor Countries (HIPC) to the IMF, the World Bank and the African Development Bank, the Board of Governors agreed at the end of 2006 to extend similar benefits to five member countries receiving debt relief under the HIPC Initiative: Bolivia, Guyana, Haiti, Honduras and Nicaragua.

The decision went into effect the following year at the Annual Meeting held in Guatemala City, where a decision was announced to cancel US\$3.4 billion of these countries' debts, with

the added benefit of forgiving some US\$1 billion in interest on these loans. Bolivia, Guyana, Honduras and Nicaragua, which had already completed the process of the HIPC Initiative, immediately enjoyed the benefits of the cancellation. Haiti, which had not yet reached the Initiative's so-called "completion point," was expected to receive them shortly thereafter.

The cancellation of such a significant portion of their debt created a historic opportunity for favored nations to devote more resources to high-priority social programs. Nevertheless, in contrast to the Bretton Woods institutions and their African counterpart, the IDB received no commitment to increase FSO resources. Under the agreement, the member countries of the IDB agreed to analyze its concessional loan program before 2013. They also accepted the creation of a Donation Fund, of which Haiti has been the primary beneficiary.

Another important milestone in the last five years was the addition of two new extra-regional members to the Bank: the Republic of Korea in 2005 and the People's Republic of China in 2009. These Asian nations, already growing trade partners of Latin America, acquired the IDB shares that had become

available after the dissolution of the Yugoslav Republic. Both Seoul and Beijing offered significant resource contributions to funds and programs managed by the IDB, the IIC and the MIF.

THE CRISIS: CHALLENGE AND RESPONSE

China joined the Bank at a time when the global financial crisis was expanding. Latin America and the Caribbean, after six years of prosperity, would no longer be immune to the effects of this situation. At the Annual Meeting held in Miami in 2008, the IDB's Research Department presented a study exposing the region's dependence on favorable external factors, such as the rise in prices for raw materials that was benefiting large exporters of hydrocarbons and cereal grains and harming small countries dependent on oil and food imports. That same year, a shortage of basic consumer products caused massive disturbances in several cities. In response, the IDB created a US\$500 million fund to help borrower countries handle food emergencies. This would be the first in a series of actions designed to help the region preserve its

achievements in economic growth and poverty reduction.

The collapse of the mortgage industry in the United States impacted financial systems around the world, causing liquidity to dry up and restricting access to credit. The IDB responded to the situation by establishing a US\$6 billion line of credit to help borrower countries handle temporary emergencies in their financial systems. In early 2009, the Board of Executive Directors approved the expansion of the Regional Trade Finance Facilitation Program, raising its ceiling from US\$400 million to US\$1 billion.

In light of the region's slowing growth, which was expected to fall to around 1 percent in 2009, the IDB offered to accelerate loan approvals for projects in the pipeline, with the goal of ensuring greater availability of financial resources for the region. Nevertheless, the magnitude of the needs of borrower countries would clearly exceed the current lending capacity of the world's multilateral institutions. One of the first leaders to draw public attention to this issue was Michelle Bachelet, the president of Chile, who called upon the IDB's partners to increase its capacity to help borrower countries survive the crisis of



A non-sovereign guaranteed loan from the IDB for financing the expansion of the Panama Canal helped attract other sources of financing for this enormous project.

the new millennium. This launched a debate, coinciding with the 50th anniversary of the Bank, on the future of an institution that is key to the development of Latin America and the Caribbean.

All of this has been framed, of course, by a half-century of achievements. Behind the US\$169.073 billion approved by the IDB in loans and guarantees between 1961 and 2008, which have allowed the development of projects valued at US\$377.177 billion (Tables 11.1 and 11.2), lie the efforts of thousands of men and women who have worked toward the highest ideals inside as well as outside the institution. These figures will surely be eclipsed by other operations in the years and decades to come. But then, as now and in the past, the objective will remain the same: to make Latin America and the Caribbean a better place for all, a region where opportunities blossom, equality is firmly established, and peace and progress reign.

Table 11.1 Yearly (2008) and Cumulative (1961–2008) Lending Information^{a,b}
(Millions of U.S. dollars)

Country	Loans and Guarantees Approved ^a					Disbursements			
	Total Cost of Projects	Total Amount	Ordinary Capital ^b	Funds for Special Operations	Funds in Administration	Total Amount	Ordinary Capital ^b	Funds for Special Operations	Funds in Administration
Argentina	52,100.0	27,014.8	26,320.8	644.9	49.1	22,380.2	21,686.2	644.9	49.1
Bahamas	696.7	495.4	493.4	—	2.0	353.0	351.0	—	2.0
Barbados	830.9	452.4	392.4	41.0	19.0	368.4	308.4	41.0	19.0
Belize	199.7	136.7	136.7	—	—	110.6	110.6	—	—
Bolivia	6,357.1	3,945.2	1,432.5	2,441.1	71.6	3,441.4	1,326.7	2,043.1	71.6
Brazil	99,928.0	34,478.7	32,791.1	1,555.6	132.0	29,658.1	27,970.4	1,555.7	132.0
Chile	14,966.4	6,517.3	6,268.6	205.2	43.5	5,781.0	5,532.3	205.2	43.5
Colombia	27,460.7	14,904.4	14,074.8	765.9	63.7	14,381.3	13,551.7	765.9	63.7
Costa Rica	5,607.7	3,880.5	3,381.1	361.5	137.9	2,535.6	2,036.9	361.5	137.2
Dominican Republic	4,233.7	3,142.4	2,307.1	747.9	87.4	2,737.2	1,901.9	747.9	87.4
Ecuador	9,263.9	5,142.2	4,066.9	981.6	93.7	4,700.1	3,628.8	981.6	89.7
El Salvador	5,420.6	3,710.1	2,764.3	796.6	149.2	3,283.7	2,341.4	796.6	145.7
Guatemala	4,990.1	3,459.5	3,073.5	675.5	70.5	2,829.0	2,084.3	675.5	69.2
Guyana	1,339.1	1,136.5	159.6	970.0	6.9	907.5	130.2	770.4	6.9
Haiti	1,774.4	1,290.2	—	1,283.9	6.3	1,012.6	—	1,006.3	6.3
Honduras	4,824.7	3,078.5	743.3	2,266.9	68.3	2,605.3	596.7	1,947.0	61.6
Jamaica	2,580.3	2,060.2	1,690.2	171.1	198.9	1,907.9	1,537.9	171.1	198.9
Mexico	53,149.7	22,183.4	21,565.2	559.0	59.2	20,117.3	19,499.1	559.0	59.2
Nicaragua	3,935.0	2,653.7	379.2	2,206.8	67.7	2,286.4	301.5	1,921.0	63.9
Panama	11,168.7	3,251.6	2,916.1	293.4	42.1	2,272.6	1,938.1	293.4	41.1
Paraguay	3,228.5	2,415.5	1,764.2	639.4	11.9	1,965.0	1,332.2	620.9	11.9
Peru	19,437.6	9,079.4	8,421.8	436.6	221.0	8,218.1	7,560.5	436.6	221.0
Suriname	303.5	189.4	183.0	6.4	—	95.9	93.9	2.0	—
Trinidad and Tobago	1,711.7	1,151.4	1,095.6	30.6	25.2	1,027.4	971.6	30.6	25.2
Uruguay	6,173.0	4,787.0	4,640.9	104.3	41.8	4,149.0	4,002.9	104.3	41.8
Venezuela	16,351.2	5,119.3	4,945.1	101.4	72.8	4,512.1	4,337.8	101.4	72.9
Regional	19,144.3	3,415.3	3,168.9	232.8	13.6	2,824.3	2,579.2	231.5	13.6
Total	\$377,177.3	\$169,265.1	\$148,991.1	\$18,519.4	\$1,755.3	\$146,461.0	\$127,712.2	\$17,014.4	\$1,734.4

Source: IDB (2009).

^aAfter cancellations and exchange adjustments. Totals may not add up due to rounding.

^bDetail includes non-sovereign guaranteed loans, net of participations.

Table 11.2 Distribution of Loans and Guarantees by Sector of Activity
(Millions of U.S. dollars)

Sector	1961–2008	%
Competitiveness	87,351.5	51.6
Energy	23,032.6	13.6
Transportation and Communication	20,990.0	12.4
Agriculture and Fisheries	15,014.2	8.9
Industry, Mining and Tourism	13,563.9	8.0
Multisector Credit and Preinvestment	4,913.4	2.9
Capital Markets	3,077.9	1.8
Productive Infrastructure	2,739.8	1.6
Science and Technology	2,081.9	1.2
Trade Financing	1,937.8	1.1
Social Development	55,676.7	32.9
Social Investment	20,971.7	12.4
Water and Sanitation	11,164.7	6.6
Urban Development	9,019.5	5.3
Education	6,777.7	4.0
Environment	3,835.9	2.3
Health	3,401.8	2.0
Microenterprise	505.4	0.3
Reform and Modernization of the State	26,237.6	15.5
Reform and Public Sector Support	11,820.2	7.0
Financial Sector Reform	7,966.9	4.7
Fiscal Reform	4,521.1	2.7
Decentralization Policies	1,122.7	0.7
Modernization and Administration of Justice	434.2	0.3
Planning and State Reform	158.6	0.1
Parliamentary Modernization	85.7	0.1
Trade Policies Support	50.7	0.0
E-Government	47.7	0.0
Civil Society	22.0	0.0
Total	169,073.1	100

Source: IDB (2009).



Box 11.2 Felipe Herrera Lane, One of the Founders and First President of the IDB (1960–1970)

Felipe Herrera Lane was born in Chile on June 17, 1922. A lawyer and economist, he held high-ranking positions early on in his professional life. Between 1947 and 1958 he was a professor of political economy at the University of Chile. In 1953 he was named Chile's Minister of Finance and became the General Manager of the Central Bank of Chile that same year. In 1958 he became the executive director of the IMF for Argentina, Bolivia, Chile, Ecuador, Paraguay, and Uruguay. Two years later he was named president of the IDB. He was re-elected for two five-year terms in 1964 and 1969 until he resigned in October 1970. He began his retirement in early 1971.

In the period surrounding the creation of the IDB, the region was bubbling with ideas related to the possibility of development and overcoming the poverty that engulfed Latin America. This was manifested in proposals like Juscelino Kubitschek's Pan-American Operation of 1958. The Act of Bogota of September 13, 1960, also proposed measures for the acceleration of social and economic development. Such measures were further developed in the Declaration and Charter of Punta del Este, which laid out the blueprint for launching the Alliance for Progress in August 1961, when the IDB was already operational.

Many of the great objectives set out at Punta del Este would be pursued by the region over the rest of that decade and would also serve to guide IDB proposals such as promoting economic growth; financing social reforms in health care, education and housing to improve the living conditions of lower-income segments of the population; spearheading agricultural and tax reforms; facilitating the redistribution of income; promoting democracy; accelerating integration and free trade among the region's countries; and modernizing the communications infrastructure.

From the start of his term at the IDB, Felipe Herrera had to face the unprecedented challenges of building an institution of the IDB's magnitude in the tenuous economic, political and social situation the region was facing at that time and the increasing polarization of the world into two opposing camps, reflected in the tensions emerging among the member countries and their foreign policies. In the interest of fulfilling the IDB's mission, the first president proposed not only to convert the newly formed Bank into a financial backer of the projects necessary for the economic development of its member countries, but also to transform the Bank into a "bank of ideas" that would provide its members with new concepts and technologies and offer solutions to their problems and needs. This focus paved the way for the emergence of an entire generation of Latin American managers and economists who would play a crucial role in setting the course of the region's economic and social development.

Enrique V. Iglesias describes in detail the work that began with the inception of the IDB:

In the history of the Inter-American Development Bank one can make out a first generation that came up with the foundational vision for the institution, defined its objectives and laid the groundwork for its operational organization. We may call them the Bank's "founding fathers." The second generation belongs to those who have endeavored to make the dreams and aspirations of their predecessors come true. We may call this generation the "builders of the IDB." Felipe Herrera is included among these men, as he enjoys the rare virtue of being one of the Bank's most notable founders as well as the primary architect of the institution during the first 11 years of its existence, a critical phase when the basic features of the IDB's personality were taking shape: "being a bank, it is also more than a bank," as stated by Herrera in his February 1960 inaugural address in San Salvador upon being elected president of the organization.

Even when we accept that on the long road toward the Bank's creation and during the phases of growth and institutional consolidation, there have been favorable historic circumstances, we cannot fail to recognize that men gifted with great sensitivity and a strong will and motivation to take advantage of the opportunities that arise are needed in order to read the signs of the time quickly and correctly. Felipe Herrera knew how to respond successfully to those challenges, as was unmistakably revealed not only by the conception, birth and maturation of our Bank as it became a major, if not the main, financial and international technical assistance agency for development in Latin America, but also by his contribution to strengthening an experience that was fully multilateral, with the active joint participation of all the member countries in the promotion of shared interests with regard to development of the region.

During the Bank's construction phase, Herrera presided over the initial meetings of the Board of Executive Directors; participated in the first Board of Governors meeting held in El Salvador in 1960; interpreted and implemented the basic documents that created the Bank; guided the approval of the first loans, for example, the 1961 drinking water and sanitation project for Arequipa, Peru, and the first technical cooperation projects, such as the one aimed at strengthening the Bolivian mining sector; managed the first three increases in resources; designed the issuance of the first IDB bond;

promoted the creation of the Institute for the Integration of Latin America and the Caribbean (INTAL) in 1965; and promoted the first bi-national loans. In addition, during Herrera's term the first English-speaking countries of the Caribbean joined the Bank: Trinidad and Tobago in 1967 and Jamaica and Barbados in 1969.

This vast and multi-faceted work of the Bank is clearly reflected in his own words, written on the Bank's 10th anniversary for a roundtable discussion at Punta del Este, Uruguay, on the IDB's first decade:

In its first 10 years of existence, the Bank was characterized by continuously expanding the frontiers of international lending to new methods and new sectors. The availability of soft funds allowed the IDB to strike an unprecedented balance between economic investments and projects of a social content. The IDB was the first institution to promote modernization in higher education, the first multinational agency to finance housing projects, and the first external financing entity to formulate a comprehensive urban development policy. In quantitative terms, the Bank's work with regard to environmental remediation has been quite impressive. The IDB played a leadership role in financing agricultural development and continues to play this role by maintaining a presence in sectors such as agroindustry, fishing and forestry. The Bank's work has also been on the cutting edge with regard to integration, the financing of exports, and participating in multinational projects and zones.

The innovative mission of the IDB has not only been expressed through its operations but has also frequently led it to play a direct role in developing the ideas that have flourished throughout the last 10 years in Latin America. The Bank was a vital contributor to the intellectual work that laid the foundation for regional economic integration, to the search for a more balanced economic and social development, to the development of planning methods by its member countries, and to the assimilation of the concepts and institutions that have facilitated the process of mobilization of our internal resources.

Felipe Herrera passed away in September 1996. He is remembered as one of the founders of the IDB and as the Bank's great leader from its inception through the first 11 years of its existence. He is also remembered as an admirable human being, a dedicated intellectual and visionary, and one of the great pioneers of Latin American development.



Box 11.3 Antonio Ortiz Mena, Second President of the IDB (1971–1988)

Born in Mexico on April 16, 1907, Antonio Ortiz Mena was a lawyer by profession as well as an economist and politician. At the end of a successful stint as director of the Mexican Social Security Institute (IMSS) from 1952 to 1958, he served as Mexico's finance minister for 12 years until 1970 when he ran for president of the country. He was appointed president of the IDB in 1971 and was re-elected three times. At the end of 1987 he resigned, handing over the reins the following year.

During his tenure at the helm of the Bank, Ortiz Mena faced enormous challenges and lived through some sweeping global changes that had a great economic, political and social impact on the region. At the beginning of Ortiz Mena's presidency, the region was experiencing significant growth, good export performance and ample international liquidity. However, this reality was chronically plagued by macroeconomic instability and by many of the problems that had been diagnosed in the Charter of Punta del Este.

In 1973, two years after Ortiz Mena took office, the first global energy crisis arose. This crisis, which re-emerged in 1979, seriously affected the region's economies, obligating them to increase their indebtedness in order to maintain their growth and stability. This situation set the stage for the debt crisis and the so-called "lost decade" of the eighties.

Ortiz Mena had to confront these situations while keeping the institution focused on concrete proposals and actions to deal with the new realities. He authored countless papers and presentations for different forums, in which he analyzed the region's realities with great clarity and wisdom, proposed solutions to resolve the crisis that was tearing at the region, and suggested the direction the Bank should take to support its member countries and mitigate their problems.

In evaluating the reality of the region's situation in the mid-eighties, he stated:

As you know, the main objective of our Bank, which has just completed 25 years of operations, is precisely to help promote balanced social and economic development in Latin America. We feel that this objective was achieved during the sixties and the beginning of the seventies. Growth rates reached and exceeded 6 percent annually in real terms and made progress possible in a wide range of economic and social sectors. During those two decades, Latin America's GDP tripled and per capita income doubled. The region's greatest achievements lie in serving basic human needs; infrastructure grew, and external financial commitments were met on time.

However, the recession of the eighties brought economic growth to a standstill. This was accompanied by a reversal in the terms of trade for our region and a basic change in the pattern of international financial flows. In this environment, the development of Latin America came to a virtual halt, living standards reverted to the levels of the previous decade, and the region's countries were unable to pay off their rapidly growing foreign debt. For Latin America, the crisis of the recent past has not only been a problem of international financial liquidity but, in a broader sense, it has been a development crisis as well.

From the beginning of his mandate, Ortiz Mena believed that it was crucial for the Bank to diversify access to funding sources and incorporate the experiences of other realities into the institution to provide it with new knowledge and technologies. The Madrid Declaration of 1974 permitted extra-regional countries to join the IDB. This process occurred mainly from 1976 to 1977 and was preceded by Canada's entry in 1972. Such factors led to the first bond issue in the Japanese market in the seventies. In 1981, the Board of Governors met for the first time in a country outside the region: Spain. Subsequently, in 1987, Ortiz Mena reached an agreement with the Export-Import Bank of Japan on the groundwork for initiating parallel project financing, and the first bond issue in European currency took place two years later.

The availability of resources, given the conditions that the region was facing, was a great concern. Between 1976 and 1978, there were two capital increases, followed by a third in 1983, thereby broadening the base required to meet the ever-increasing urgent needs of the region. This increased the availability of resources from Ordinary Capital (OC) and the Fund for Special Operations (FSO) that were earmarked for relatively less developed countries, and the Intermediate Financing Facility was created to reduce the Bank's financing costs for certain member countries.

The Bank's achievements during Ortiz Mena's mandate were enormous. Lending and technical cooperation programs grew considerably. There was more financing for infrastructure, including large bi-national projects such as Salto Grande as the first, followed by Yacyreta. The first loans in the areas of health care, tourism and fiscal reform were signed, and the Bank began to grant the first complementary loans. In addition, the Small Projects Program and the Industrial Recovery Program were established. The Environmental Protection Policy was adopted at the end

of the seventies, giving rise to the creation of the Environment Committee in 1983. Four years later the Bank granted the first loan aimed exclusively at the environmental sector. The charter of the Inter-American Investment Corporation (IIC) went into effect in 1986, although the institution began its operations some time later, and in 1987 the Bank adopted the policy of promoting the role of women in development.

In reference to the enormous task undertaken by Antonio Ortiz Mena during his mandate, Enrique V. Iglesias said:

His contribution began during his years as a governor of the Bank and Mexico's finance minister, with his assistance in shaping the Bank's policies. Later on, as president of the Bank, he exercised extraordinary and outstanding leadership which led to the expansion, consolidation and reaffirmation of the Bank's regional and multi-lateral character, helping to make it the most important and most innovative source of external funding and technical cooperation for economic and social development in Latin America and the Caribbean.

Antonio Ortiz Mena died in March 2007, just short of his 100th birthday. He is remembered throughout the region for the courage and wisdom he displayed in handling the enormous challenges he faced during his presidency. He was also known as a broadly cultured man with a universal education that ranged from philosophy to history, music and art, and was highly regarded for the impressive analytical abilities that he demonstrated, in particular, when dealing with the economic issues for which he felt a special predilection. He left a mark on the Bank that has lasted through the generations, all of whom have flourished under what was his constant concern: the well-being of the Bank's staff. He is remembered in his native Mexico as having stabilized development there from 1958 to 1970.

Interview with Enrique V. Iglesias



Enrique V. Iglesias, born in Asturias, Spain, in 1930, became a Uruguayan citizen after immigrating to Uruguay with his parents in 1934. In 1953,

he graduated from Uruguay's Universidad de la República in economics and business administration. Before his appointment as president of the IDB, Iglesias was president of the Central Bank of Uruguay (1966–1968), executive secretary of ECLAC (1972–1985), and Uruguay's minister of foreign relations (1985–1988). He has also been secretary general of the Ibero-American Secretariat since 2005. In 1991 Iglesias received a Ph.D. in law from Canada's Carleton University, and in 2008 he received honorary doctorates from the Universidad Europea de Madrid and the Universidad Andrés Bello.

You assumed the IDB's presidency at a very special crossroads in its history. How would you describe it?

When I arrived in 1988, a serious rift among the principal shareholders—the United States, the Bank's largest shareholder, and the four major regional members (Argentina, Brazil, Mexico and Venezuela)—had cast a shadow over the Bank's Board of Executive Directors, whose members supported the positions of their respective governments. This estrangement had implications for the Bank's role in the region's development, its internal operations and its operating procedures, and prevented the institution from reaching agreements regarding the necessary replenishment of resources. Naturally, the situation greatly hindered the cooperative dialogue between the Board and administration—key to the organization's success—and also unfortunately tainted the internal climate and the public's opinion toward the Bank.

At the same time, the Bank's situation in the region was very complex. Why?

We were in the midst of what ECLAC called the “lost decade,” with the dramatic intensification of the external debt problem, and the deterioration and

disappearance of many institutions created in the sixties and seventies, such as development banks and planning agencies. Moreover, people were questioning previous development models and, in particular, the role of government, which was stigmatized by its inefficiency and corruption. Anti-statism at all levels was already evident in the structural adjustment policies implemented at the World Bank as part of what began to be defined as the Washington Consensus, a reform package that emerged during the nineties. It represented a return to economic orthodoxy. The paralysis caused by the cooling of relations among its principal shareholders meant the Bank did not participate in developing new types of economic policies, based on Bretton Woods, that became essential to the region in finding solutions to the serious external debt problem that dominated the entire “lost decade.”

Under these two circumstances, what goals were set?

First, to achieve a basic understanding among the shareholders. This would require a constructive working relationship between the Board of Executive Directors and the administration and a stronger internal culture of working

together. Second, to increase the Bank's capital, which was achieved at the historic 1989 Board of Governors meeting in Amsterdam. The Bank regained the support of all its member governments, and its capital increased from US\$34 billion to US\$60 billion. Third, to present the Bank as an important stakeholder in the region's economic and financial recovery. This was achieved through participation in the development of policies supporting the reforms that marked a good part of the nineties. At first, the Governors conditioned our participation in structural credits on World Bank co-financing. After two years, we were authorized to act alone, coordinating joint ventures, but we were still directly responsible for our own credit decisions.

In 1991 the Bank again became the main source of multilateral funding in the region. What did this mean?

We positioned ourselves as the principal source of development funding, which has persisted through the nineties and beyond, reaffirming the Bank's pre-eminent role as the Bank of and for Latin America and the Caribbean, thus fulfilling the dream cherished by Felipe Herrera and Antonio Ortiz Mena.

While this was happening, there was a significant expansion of the programs that were funded. Why?

Modern times and new economic philosophies required new types of loans and cooperation. As I mentioned previously, we created structural support loans to finance reforms. In addition, the Enterprise of the Americas Initiative was launched in the nineties, enabling us to create the Multilateral Investment Fund (MIF), designed to maximize the reforms' impact on renewed governments and on job markets, thus expanding our support of job training. The fund gave preferential treatment to professional development, but we insisted on including small businesses and microenterprises and on taking macroeconomic development incentives into account, giving us a basic instrument for supporting grassroots economic and social development. We also set up the Inter-American Investment Corporation (IIC) to look after small businesses, and today it is a thriving operation. Direct loans to the private sector, which had been a big part of our portfolio when the Bank was created, would be re-introduced as well. The use of technical cooperation on a national and regional level provided many opportunities

for development, greatly enhancing institutional strengthening and project effectiveness.

In light of its past, what do you think about the IDB's role in the present and future and the challenges the institution is facing?

The Bank is faced with a great opportunity as well as a great challenge. The worldwide crisis will affect us in different ways and with differing degrees of intensity. While Latin America is better equipped to deal with it than it has ever been before, we will not emerge unscathed. Therefore, with respect to policies, it is essential to be able to count on a dynamic Bank, a solid financial partner that can open up golden opportunities in support of the region's countries, a Bank that is, as the IDB has always been, the friend of its Latin American and Caribbean partners. One of the biggest challenges facing the institution will be to convince its shareholders of the importance of providing more funding to the Bank through another capital increase. We must all support the current president in this endeavor: governments, directors and officers. I see this as a clear and urgent reality.



Presidents Enrique V. Iglesias and Luis Alberto Moreno mark the IDB's 50th anniversary in a ceremony held at Bank headquarters.

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¹ The present chapter is mostly and textually based on the book *More Than a Bank: Inter-American Development Bank, 40 Years*, edited by Carlos Brezina, a former Bank official (IDB, 1999). The history of the creation of the IDB was drawn partly from a book by Xavier Comas, another Bank official, while the description of the events of the current decade relied on the book *Al servicio de algo más que un Banco: Enrique V. Iglesias, Presidente del BID (1988-2005)* [(*At the Service of Something More Than a Bank: Enrique V. Iglesias, President of the IDB (1988-2005)*)] (IDB, 2006). For the box notes on Presidents Felipe Herrera and Antonio Ortiz Mena, text from their respective recollections of their time at the Bank was used. The portion of this chapter that corresponds to the period between 1998 and 2008 was based on a work by Peter Bate, another Bank official.



A global challenge. The financial crisis, which began as an isolated problem in the mortgage industry, quickly spread and became a worldwide economic crisis.

XII Latin America and the Caribbean in the Current International Crisis

In January, 2009, when the International Monetary Fund (IMF) announced an update to its economic projections for the new year, dozens of analysts expressed their surprise at the move. After all, it was the third time in four months that the multilateral agency was forced to revise its calculations, something that had never occurred before in its history. However, the reasons behind the event were as extraordinary as the event itself. According to the organization (IMF, 2009), advanced economies would grow by merely 0.5 percent, the lowest rate since the end of the Second World War (Figure 12.1).

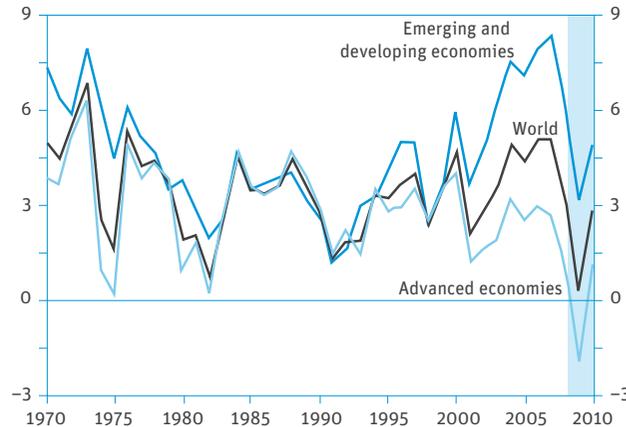
Beyond this simple calculation, though, it was the speed at which the entire world's production activity was expected to deteriorate that was the most striking of all. None of this seemed possible in late 2007, when the United States and several European countries began having problems with their respective real estate

markets after years of booming prices and construction activity. However, rapid drops in the values of hundreds of thousands of homes uncovered a deeper problem, one rooted in the development of various financial instruments backed by subprime mortgages that were recycled numerous times and acquired by entities that were often different from the one that had issued the original loan, located in the world's wealthiest nations.

Thus, as the months wore on, what appeared at first glance to be a downturn in the construction sector quickly spilled over to the world of finance. With increasing speed, banks, brokerage firms and investment funds began suffering million-dollar losses that forced the governments of the most developed economies to act. The initial response came in the form of case-by-case assistance, including incentives for various entities to be absorbed by others. Nevertheless, in certain situations, government authorities decided to allow companies

Figure 12.1 Global and Regional Economic Growth, 1970-2010

(Percent change)



Source: IMF (2009).

to disappear that, in their view, did not deserve to be rescued.

Although their goal of a generalized rescue operation inherently ignored the principles of success and failure inherent to the private sector, governments quickly discovered that the lack of certainty about which entities were solid and which ones were not had in fact paralyzed the global financial sector. As a result, the policy of reducing interest rates adopted by the world's major economies had a limited effect,

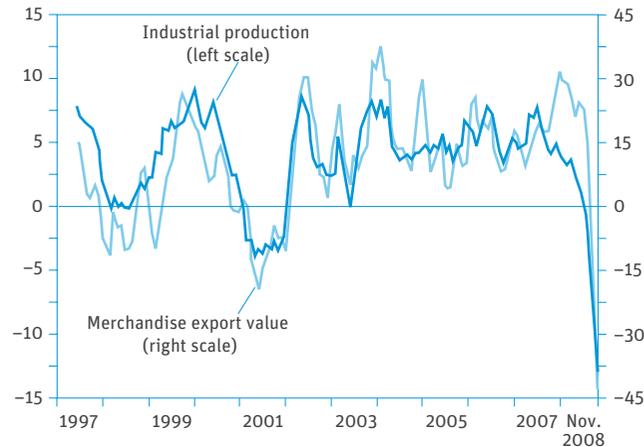
with the flow of credit abruptly drying up, affecting companies and consumers and clearly impacting the real estate sector.

Concurrently, prices for basic products, many of which had exceeded their historic peaks during the first half of 2008, began dropping rapidly. This phenomenon affected not only fuels, but also food and industrial consumables. As a result, the rapid rise in inflation rates reported by many of the world's economies during that period showed at least a partial reversal during the second half of 2008.

These circumstances began to affect the expectations of buyers of a wide variety of products, causing them to proceed with caution. The automotive industry took a particularly strong hit in comparison to many others, registering double-digit losses in sales due to the reluctance of buyers to incur significant expenses. Lower demand in turn led to layoffs, reflecting similar events in the construction and finance sectors (Figure 12.2). Thus, unemployment rates increased considerably, confirming that the cycle of global economic expansion that began in 2002 had been replaced by a vicious circle of layoffs, dropping sales, and recession.

Figure 12.2 Growth in Industrial Production and Merchandise Trade, 1997-2008

(Annualized three-month percent change)



Source: IMF (2009).

The response from the most powerful governments focused on two strategies. The first involved injecting resources into the financial sector and expanding mechanisms for guaranteeing liquidity, complemented by the full or partial nationalization of dozens of credit institutions. The second was the approval of stimulus plans consisting of lowering taxes and increasing spending in key economic sectors such as infrastructure or industry. These mechanisms generated a considerable expansion of

national deficits, under the assumption that the increased shortfall would be eliminated during the recovery period.

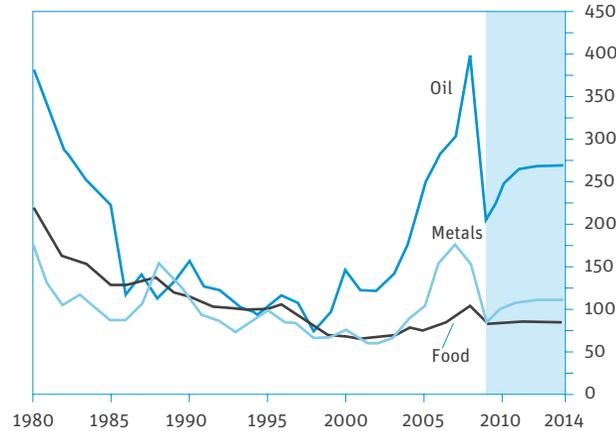
WINDS OF CHANGE

At first, the impact of the crisis was not particularly worrisome for Latin America and the Caribbean. After all, the region had just experienced a boom period, with an average growth rate of five percent between 2003 and 2008. This expansion was accompanied by the accumulation of international reserves, improved taxation systems and a reduction in indebtedness, which seemed to have shielded many economies (ECLAC, 2008). As if this were not enough, the local financial sector managed to escape the problems that were afflicting other regions, making the situation complex but manageable.

However, by the start of 2009, it became clear that a drubbing was inevitable. For example, the IMF reduced its growth forecast for the region to 1.1 percent (IMF, 2009), while ECLAC predicted increases in unemployment as well as poverty and marginalization indices.

In addition, an internal document from the Inter-American Development

Figure 12.3 Real Commodity Prices, 1980-2014
(1995 = 100)



Source: IMF (2009).

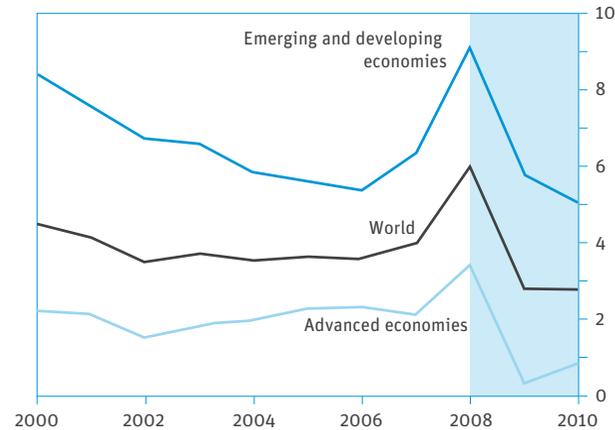
Bank (IDB) determined that the crisis could spread to people throughout the region, resulting in lower income for families due to a rise in unemployment, lower public resources for social programs, a drop in revenue from overseas transfers, and an increase in the price of imported goods due to the depreciation of various currencies (Duryea et al., 2008).

In terms of regional growth, there were various reasons behind the reduced projections. The first was the impact of the plunge in raw material prices (Figure 12.3), a particularly

thorny phenomenon for a region focused on exporting basic or unfinished goods. Second, there was the downturn in the global goods trade, estimated by the IMF at 2.8 percent by 2009. The third element was the drop in tourism revenue and the foreseeable stagnation of workers' remittances, calculated by the IDB at US\$67.5 billion in 2008. A fourth factor is tied to the influx of foreign direct investment (FDI) and credit resources provided by international private banks. As during other periods of financial difficulty, nervousness over emerging markets generates a mass exodus of funds in search of options offering the least possible risk, regardless of whether the original recipient countries were doing things right. Lastly, there has been a decreased internal dynamic associated with the deterioration of corporate and consumer expectations, an aspect magnified through the lens of the pessimism spread by globalization and telecommunications.

In response, the region's governments announced plans aimed at stopping economic deceleration (ECLAC, 2009), including public spending programs focused on developing infrastructure and supporting vulnerable sectors of the population,

Figure 12.4 Inflation, 2000-10
(Percent)



Source: IMF (2009).

depending on the fiscal wiggle room of each economy. Concurrently, the region's central banks responded with measures for increasing liquidity and lowering interest rates amid low inflation (Figure 12.4). Also, the region received clear support from multilateral agencies which reached out to the region by helping countries in need and keeping open lines of credit for foreign trade.

The effectiveness of these measures will remain uncertain for some time. But despite the magnitude of

the crisis, a wide variety of analyses show that the region's medium-term and long-term perspectives are positive (Table 12.1). In other words, calculations indicate that the region's countries will return to a path of growth similar to that of the current decade, even faster, in fact, than other areas of the world. One of the reasons is that the structural strengths of the region's economies, which had nothing to do with the current debacle, should allow them to stay afloat, hopefully in more tranquil and promising waters than the current ones.

PERSPECTIVES FROM EXPERTS IN THE REGION

Andrés Velasco Brañes,
Finance Minister of Chile

Over the past 50 years the IDB has accompanied our countries on each step of this long journey to economic and social development. It has watched us put to rest old paradigms and create new ones. It has given us advice, some of which we have heeded and some of which we have ignored. At the end of each decade we have faced an increasingly broader array of tests, a horizon of increasingly complex challenges.

Table 12.1 Global and Regional Economic Growth, 2007-10
(Percent change)

	2007	2008	Projections	
			2009	2010
World output^a	5.2	3.4	0.5	3.0
Advanced economies	2.7	1.0	-2.0	1.1
United States	2.0	1.1	-1.6	1.6
Euro zone	2.6	1.0	-2.0	0.2
Germany	2.5	1.3	-2.5	0.1
France	2.2	0.8	-1.9	0.7
Italy	1.5	-0.6	-2.1	-0.1
Spain	3.7	1.2	-1.7	-0.1
Japan	2.4	-0.3	-2.6	0.6
United Kingdom	3.0	0.7	-2.8	0.2
Canada	2.7	0.6	-1.2	1.6
Other advanced economies	4.6	1.9	-2.4	2.2
Newly industrialized Asian economies	5.6	2.1	-3.9	3.1
Emerging and developing economies	8.3	6.3	3.3	5.0
Africa	6.2	5.2	3.4	4.9
Sub-Saharan Africa	6.9	5.4	3.5	5.0
Latin America	5.7	4.6	1.1	3.0
Brazil	5.7	5.8	1.8	3.5
Mexico	3.2	1.8	-0.3	2.1
Commonwealth of Independent States	8.6	6.0	-0.4	2.2
Russia	8.1	6.2	-0.7	1.3
Excluding Russia	9.7	5.4	0.3	4.4
Central and Eastern Europe	5.4	3.2	-0.4	2.5
Middle East	6.4	6.1	3.9	4.7
Developing Asia	10.6	7.8	5.5	6.9
China	13.0	9.0	6.7	8.0
India	9.3	7.3	5.1	6.5
ASEAN-5	6.3	5.4	2.7	4.1

Source: IMF (2009).

^a Quarterly estimates and projections account for 90 percent of global weighting for purchasing power parity.

Despite the enormous diversity of our region, the aspirations of our countries and the challenges we face unite us. We continue to be strongly affected by the vicissitudes of the world economy, although to a lesser degree now than before. Social disparities continue to be overwhelming and are exacerbated during periods of crisis.

The results achieved during the IDB's 50-year history have been mixed. However, it would be unfair to blame the Bank for our omissions. In the first and final analysis, those are the exclusive responsibility of our governments and of the policies that we have decided to promote.

Today, after a long period of prosperity, the region's countries find themselves once again in a recessionary cycle. A recession is defined by a decrease in the average income of the economy. We must remember that previous recessions have been particularly difficult for us because they were usually accompanied by a scarcity of foreign financing and the inevitable pinch that this generates. The impact is felt the most intensely by the most vulnerable segment of the population. These weakest sectors must live

with the long-term consequences of economic crises, such as the effect on the nutritional development of children and on their participation in the education system—factors that compromise an investment in the future.

Nevertheless, the region has learned to mitigate some of these effects. We have improved our fiscal policies, learned to save in times of prosperity in order to sustain government spending in difficult times. We have made progress in building social protection networks like conditional transfer programs and in the development of unemployment insurance programs and the provision of health care services.

Although the results have been mixed and we are once again facing a crisis, there is an element that allows us to look to the future with greater optimism. From our experiences we have learned that choosing pragmatic policies and implementing them consistently is superior to any school of thought or dogma. Today, conservatism and progressivism make sense only to the extent that they complement our final objectives: to eliminate poverty and create a society of opportunities.

The 50th anniversary celebrations of the IDB are beginning amid a pro-

found international crisis. Much has been written on this topic and even more will be written in the months to come. In many countries, the numbers are getting worse every day, and there seem to be no easy answers.

To resolve this crisis and get the region back on the development track without becoming pessimistic and paralyzed, we must start by asking ourselves: what have we learned over the last few years?

- We have learned—and to a large extent, we have achieved the desired results—to take advantage of the good times to establish sound economic policies and more efficient social policies.
- We have learned to invest in macroeconomic policies that ensure stability. Our desire to achieve low and stable inflation rates and reduce the region's indebtedness and interest rates, as well as our efforts to open up our economies to international markets and adopt flexible foreign exchange policies, are just some of the measures that will enable us to take on this new challenge with more and better tools.

- We have made enormous progress in education coverage.

However, boom times never last forever. This is perhaps the first lesson that we had trouble understanding in time. So we have to ask ourselves: where were our biggest deficits?

- It has been difficult to use our enormous supply of natural resources to generate new engines of development.
- We suffer from a huge innovation deficit that restricts our productivity and competitiveness.
- We still have not been able to educate all our children to the standard that the modern world demands.
- Although we have made significant progress in poverty reduction, the levels that remain are still unacceptable. Inequality in income distribution is still an embarrassment to the region.
- In many respects, we continue to be, as Neruda said, “a dark continent searching for clarity.”

In the final analysis, the main piece of unfinished business on the agenda is to build a society that provides equal opportunities for all of the hemisphere’s inhabitants.

The progress achieved over the last few years is not inconsequential, but neither is it sufficient.

Today the challenge is even more complex. We need different strategies for countries that face different challenges. At the same time, certain deficits that are common to all the region’s countries persist. IDB support will continue to be essential in tackling these issues.

The current crisis reinforces the fact that we live in an interconnected world. Therefore, we must vastly improve our integration networks in order to successfully navigate this scenario. This involves making a long-term investment in infrastructure. We cannot keep relying on a local mentality to face challenges we can only overcome by acting as a region.

In order to ensure sustained growth, we must learn to construct a new equilibrium that allows us to achieve levels of economic growth intelligently without mortgaging the future of our children and grandchildren. Our growing energy requirements must be compatible with the need to mitigate climate change and protect our extraordinary natural resources.

Lastly, although our systems of government are democratic, more participatory and transparent, our public institutions still have huge shortcomings when it comes to their ability to design and implement public policy efficiently and effectively. To overcome these deficiencies, we must work toward such goals as modernizing our governments, making key improvements in public management and the allocation of funds, and placing an even greater emphasis on strengthening our fiscal policies.

We will continue to depend on the IDB, our partner and ally, as we deal with this unfinished business. The Bank's ability to harvest and transmit best practices will be essential in order to make headway with respect to our objectives and be better prepared for the next crisis.

In 1971, Felipe Herrera stated (IDB, 1971):

The future will bring its own problems and challenges, but I am sure that the Bank will be able to deal with them successfully because it has incorporated the thinking of that unforgettable public servant Dag Hammarskjöld into its own philoso-

phy: "Never look down to test the ground before taking your next step: only he who keeps his eye fixed on the far horizon will find his right road."

This advice could not be timelier. The IDB must help us keep our eyes on the road ahead. To do so, we need a financially solid Bank, one that gives perceptive advice, pays humble heed to its partners, and is able to respond quickly. Realignment has made significant progress possible, but we need to strengthen further the Bank's financial and technical capacities. The magnitude of the unresolved issues is huge and we need the Bank's committed support. In some cases, this will mean financial backing through loans or concessionary terms; in other cases, it will mean front-line technical assistance. Both products will require the strengthening of the IDB through recapitalization.

It is fitting for the 50th Annual Meeting of the Bank to be held in Colombia, in the land of Gabriel García Márquez. There, we can reaffirm the commitment made by the IDB's founders to build an institution together to help us meet the enormous challenges we face so that we may give those who live in Latin America and Caribbean a more decent life.

In Márquez's words, we have been and will continue to be committed to "a new and sweeping utopia of life, where no one will be able to decide for others how they die, where love will prove true and happiness be possible, and where the races condemned to one hundred years of solitude will have, at last and forever, a second opportunity on earth" (García Márquez, 1982).

We know that in building this utopia, the IDB will remain at our side until it becomes a reality.

Agustín Carstens, Finance Minister of Mexico

The international financial crisis that began in the mortgage industry of the United States has become a global economic crisis.

Toward the end of last year, the effects of contagion became evident. Decreased consumption in the United States and the rest of the world led to a sharp contraction in industrial production and in world economic growth, resulting in the worst recession in decades for the world's developed countries and in a significant slowdown elsewhere around the globe.

This crisis has affected all the countries of the region to a greater or lesser

extent and has reduced our prospects for economic growth. It has had a negative impact on the most tangible variables: exchange rates, employment, consumption, credit and investment.

The uncertainty and the crisis of confidence in international markets have weakened our economies and our currencies. This has sparked new inflationary pressures at a time when it seemed that the rate of inflation would be adjusted downward in line with the drop in prices for raw materials.

This is the scenario we are facing this year as we celebrate the IDB's 50th anniversary. We are forced to reflect on the future of the Bank and the strategy we must use to make sure the institution remains relevant to the region's development. In particular, we must define the Bank's role in helping us face the difficult situation we are experiencing. Now more than ever, in these times of uncertainty and financial instability, we must be able to count on the support of a strong Bank, with guaranteed access to credit and backing for the economic recovery programs that our countries require.

Unlike previous crises, this one occurred after many years of implementing sound macroeconomic policies

and making progress with structural reforms. Mexico currently enjoys a stable macroeconomic environment: we maintain a high level of international reserves, we have a free-floating exchange rate, we follow a sound budgetary policy, we have created an infrastructure support trust, and we have four stabilization funds built with petroleum profits. In addition, we are promoting an open trade policy and greater economic competition in our markets, and have managed to strengthen our financial sector through the application of best regulatory practices.

Today, for the first time in recent history, we are in a position to implement a series of anti-cyclical measures to deal with the crisis and offset its negative effects on the economy, mainly on investment flows, lines of credit, exports, remittances and tourism. Our current challenge is to keep up our guard and not be tempted to apply protectionist measures that distort markets even more. On the contrary, now is the time to move forward in establishing regulatory frameworks that reassure investors and promote greater productivity and competition.

Nevertheless, we need to do more in Mexico in particular, and in Latin

America and the Caribbean in general, to counteract the effects of the crisis without jeopardizing the stability that has taken us so much time and effort to build. The region's governments and the IDB must work together to mitigate the effects on our families through the strengthening of job protection and social programs. We must make further progress on these issues, which are areas where the Bank has demonstrated that it has the appropriate experience and human resources.

Countries such as Mexico and Brazil, which have social support programs of proven efficiency, should consider expanding and enhancing them with the Bank's support. Countries that are still without conditional transfer programs should look at introducing them as soon as possible with the Bank's assistance, and thus continuing to add value to the IDB's participation in the region's development.

The current adverse conditions in international financial markets require a decisive and committed response from governments and the private sector. The challenges generated by this crisis are forcing our financial sector to play a more active role as a catalyst of economic growth.

It is important to highlight the role of development banks in implementing anti-cyclical strategies in our countries at this time through the impetus of direct credit and guarantees for the industrial and service sectors, for investment and infrastructure projects, and to decrease the perception of risk attached to private financial institutions. Only by guaranteeing access to available private sector financing, particularly during these times of extreme volatility and uncertainty in international markets, can we succeed in supporting our region's job markets.

The Bank can also contribute to the strengthening of our development banks. Throughout history, many of our countries have experienced difficulties with restructuring and recapitalizing public financial institutions. We must continue to support their efforts while promoting corporate governance policies that are in line with best international practices. Our development banks must set an example of efficiency while helping to partially neutralize the effects of the crisis.

The implementation of anti-cyclical economic policies is essential at this time. However, it is also true that we must use this crisis to increase our

economic growth potential, which has been limited for many years due to a lack of competitiveness, a lack of competition, and too much regulation in domestic markets.

We can no longer postpone the dialogue with all sectors of society on the structural reforms required to make the region's countries more competitive and to strengthen the rule of law. In this way, once the crisis has been overcome, we will be in a better position to recover lost jobs and achieve more rapid and sustained growth.

Through the years, the Bank has gained a great deal of useful experience on how to increase the growth potential of the region's countries. Now it must assume a leadership role in the region and act as a catalyst to promote the implementation of the above-mentioned reforms. Today's globalized world forces us to take on the challenge of promoting competitiveness and laying the groundwork for sustainable growth and a better future for our countries.

To carry out these tasks, our region will require a Bank that is bigger and better equipped in terms of financial and human resources. The

realignment process that was begun in 2007 played a major role in strengthening the Bank in top-priority areas. But this was just the first step. Now, we must move beyond those areas and lay the foundation for the Bank we want to have over the next 50 years.

The institution has received eight capital increases since its inception. The recapitalization that took place 15 years ago increased the Bank's callable capital by US\$40 billion, bringing it to the current total of approximately US\$100 billion. This decision, which was visionary at the time, enabled the Bank to increase its loan portfolio from US\$5 billion per year to US\$7 billion, thus allowing it to adequately meet the funding requirements of its borrower countries for more than a decade.

However, as the region continued to develop, the IDB's relative role in terms of funding was reduced. The Bank had to re-evaluate its strategic framework and was more selective in the operations it supported, trying to ensure the highest possible added value and the maximum impact on development. This fostered the creation of areas of specialization and the introduction of new financing programs

and sectors. Innovative tools have been designed to meet the demand of sub-national governments and the private sector, and recently, a matrix structure has been adopted to enable the Bank to incorporate greater value and experience into its operations.

This year, when most of our economies will experience a period of stagnation or even recession, we must be able to count on a strong Bank capable of meeting the funding needs of the region's countries. Last year, total approved operations amounted to US\$11.5 billion, representing an increase of over 30 percent compared to the previous year and double the authorized limit for 2007. To maintain this rate of growth and be able to meet the requirements of our countries, we must begin to talk about the Bank's future. We can no longer put off discussing another capital increase at the IDB if we want it to continue to be our development partner in the future. Now, more than ever, we have to be creative and propose schemes that allow us to increase our lending capacity and make better use of our capital, even if this involves a change in shareholder participation that is better adapted to the size of our economies.

**Danilo Astori, Former Minister of
Economy and Finance, Uruguay**

The Inter-American Development Bank is turning 50, and this anniversary finds it firmly entrenched as an indispensable part of the inter-American reality and, in particular, of the history of Latin America. It would be very difficult to attempt an analysis and an interpretation of the development of our societies over the last five decades without including this essential participant.

The first few years of the 21st century have seen significant changes in the region's economic history. Of particular note is the tremendous increase in global demand originating in Asia, especially in China and India, whose economies, which grew at very high rates, became true elements of world stabilization and regulation. In the early years the region reported poor results with respect to output, which grew at just under 0.2 percent per capita between 2000 and 2004, but this rate shot up to 4 percent between 2005 and 2008. Under these circumstances, the production and export of food and raw materials, as well as their prices, reached historic levels.

Two other factors that have accompanied the above-mentioned process are worthy of note. The first is that the implementation of more consistent and sounder economic policies helped many of the region's countries combat past weaknesses while they were able to achieve greater sustainability of the results in fiscal terms and with respect to public debt management, price stabilization and changes in output and exports. Thus, the negative effects of years of huge inequalities were left behind from an economic and social perspective. The second is that the region has benefited from the availability of relatively easy credit at favorable interest rates. This factor, together with the more stable conditions generated by the sounder economic policies that have been implemented over the past few years, led to an attractive environment for foreign direct investment. Significant investment flowed into the region, not only for the purpose of developing our natural resources and expanding our infrastructure, but also to take advantage of the growth in domestic consumer markets that was making a big splash during that period, particularly in the region's larger countries.

Thanks to these factors, and in particular to sounder and more credible monetary policies in a flexible exchange rate environment, net external funding requirements fell. This generated a positive balance of trade, whether because of surpluses or a reduction in negative trade balances, and the region's countries became less dependent on foreign financing. Consequently, more resources were available to meet social needs that had been ignored for a long time.

However, because of the unique characteristics and economic, social and political processes of each country in the region, these new conditions were not present everywhere to the same degree. Different internal conditions also led to different public policy decisions which were reflected in unequal states of preparedness for possible reversals of the economic cycle. In other words, the region's countries demonstrated different abilities to implement anti-cyclical policies.

This situation is extremely important today, given the circumstances of 2008 that triggered a financial crisis that has been unprecedented in the last few decades and caused a chain reaction in the areas of production and

global trade. It is not yet possible to determine the duration and severity of the impact with precision. There is still a great deal of uncertainty that is expected to continue at least until the end of the first half of 2009. Therefore, one could argue that this is not the right time to reflect on the future of Latin America and the IDB's role in the region. At the same time, one can also say that the reversal of the favorable conditions enjoyed by the region's economies over the last few years provides a stimulus for the diagnosis of unresolved challenges and for a dialogue about the possible consequences of the new world situation. It also provides an opportunity to talk about the contributions the Bank can make in order to mitigate and overcome the effects of the crisis.

It is important to point out not only the main challenges facing Latin America in the future, but also its undeniable potential. The region's countries are, to a large extent, net exporters of food and raw materials, including energy resources. In addition, Latin America possesses a very significant proportion of the world's fresh water resources and is in a position to make decisive contributions to the

preservation of the environment. It is very difficult to imagine a world that is attempting to improve the essential living conditions of the population, and is struggling to combat poverty and indigence, without the strategic involvement of Latin America, given its natural conditions.

Latin America must be able to adequately and efficiently supply the demands of the rest of the world in areas where the region possesses superior resources. At the same time, in addition to improving its productive base, it must use this base to begin a process of industrial diversification that includes technology and innovation, as well as a significant expansion of the services sector, which is closely associated with such diversification.

It will be impossible to meet these objectives without sound and sustainable economic policies such as those that have emerged in several countries of the region over the past few years. In this regard, we have a long way to go in improving the design and practical application of anti-cyclical policies, as well as associating these policies with activities in the social arena aimed at combating poverty and indigence. At the same time, we must

work to provide more equitable access to the benefits of growth in a region that suffers from the most inequitable distribution of income in the world.

Progress with respect to regional integration in Latin America is necessary in order to make better use of the region's potential and ensure that effective advancements are made in the social sphere. There are still enormous deficiencies to overcome in this area. Some of them are basic, such as the difficulty of gaining access to wider markets as defined by agreements between countries, the lack of coordination of the economic policies of the Bank's member countries, and the lack of basic common infrastructure, especially in energy and transportation. Also worth mentioning are the serious weakness of institutions at a supra-national level and the region's limited ability to reach agreements with other world blocs.

With respect to the Bank's role in this context, we must begin by recognizing the institution's main asset: its credibility and the trust that is placed in it by the region's countries regardless of who is at the helm in each country. The Bank has earned this distinction legitimately, primarily

because of its staying power at critical times. In addition, this condition creates an atmosphere of interaction and cooperation among borrowing and non-borrowing shareholders. These partners represent significant potential resources in a possible future scenario characterized by energy and water shortages and placing a much higher priority on the availability of food and the protection of the environment.

It is important to reflect on the appropriate size of the Bank within the framework of a debate that is already raging between those who foresee a decline in the involvement of multilateral funding agencies over the long term in middle-income countries, and those who do not share this view. Even if the Bank's presence were to decrease in favor of more frequent use of private funding by the region's countries, the process of accommodation in order to achieve this end, although it won't last forever, will certainly be lengthy.

The Bank is called upon to play a decisive role in achieving greater financial self-sufficiency for Latin American countries, particularly for those that are the weakest economi-

cally speaking. The effectiveness of its work in this regard will depend on maintaining a flow of resources that, although it may be reduced as a proportion of output, will increase in real terms.

For these reasons, a discussion about the size of the Bank is very important. While we are aware that the Bank will become weaker if it does not reach an appropriate size that is consistent with its responsibilities, it must be pointed out that under the present circumstances recapitalization will be necessary, keeping in mind that many financial institutions in the developed world have received and continue to receive capital infusions. We should remember that since the Bank's inception, regional GDP has increased 40 times over in current prices and seven times over in constant prices. In addition, since the last capital infusion in 1994, output doubled in current prices and grew by 50 percent in real terms.

We know that the path we will be taking in the future will not be linear but will depend on the different situations and specific conditions in each country. These situations will require made-to-measure responses; therefore,

the automatic application of generic solutions will not work. Even so, the Bank must not stop offering traditional financial products, but will also have to provide new instruments to those middle-income countries that ask for them, such as hedging, insurance, guarantees, loans in local currencies, and a greater range of payment terms.

Simultaneously, and in addition to maintaining a strong financial presence in the region, the Bank must improve its analytical capacity in order to enhance the quality of its dialogue and interaction with the region's countries. It must also strengthen its ability to differentiate between sound and unsound policies within the framework of the economic and social development objectives to which the people of Latin America aspire and to which they have a right.

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The future of the region. Education is the key to faster growth, the ability to compete in a globalized world, and winning the battle against inequality.

EPILOGUE

A Conversation with Luis Alberto Moreno, President of the IDB

The Bank's 50th anniversary celebration is taking place amid a complex global scenario. . . .

Yes, indeed. But this half-century mark for the IDB is also a good opportunity to put the situation into perspective and remember that this is not the first time that the countries of Latin America and the Caribbean have faced a major crisis. Also, despite the impact that the sharp economic downturn will have on the region, the region's countries are, without a doubt, in a much better position to handle it effectively this time around. Our past challenges have left us with greater experience and some harsh lessons learned, as well as the conviction that the sun will rise again, no matter how dark the horizon might be.

Why do you believe the region is stronger?

Just looking at the numbers—for example, the figures on our interna-

tional reserves or foreign debt—is enough to conclude that we are less vulnerable now than in the past. There's also greater fiscal space, which allows us to adopt anti-cyclical programs for lessening the impact from the outside. And then there are stronger local institutions. To cite one concrete example, thanks to better banking supervision, the Latin American financial sector has been able to avoid the pitfalls experienced by other regions.

But this doesn't mean that the region will come out of this crisis unscathed. . . .

Of course not. From 2003 to 2008 the region had one of its best growth periods since the creation of the IDB. As a result, nearly 40 million people escaped poverty and there was notable progress on social indicators. Now we're in an era of relative stagnation, but if we do things right, we'll be able

to handle this deluge of bad news without retreating, as was sadly the case during other periods. Some economies are more vulnerable than others, but we have enough resources to support them and prevent the return of the “lost decade.”

What does this support consist of?

In the immediate term, it consists of a US\$6 billion aid package introduced last October to support nations with liquidity problems. From a more structural standpoint, we’re looking to expand our lending capacity from what it has been in recent years. We’re aware that the volume of resources available to the region is lower now, and we have to make up for that difference. We’re also offering our technical consulting capabilities to countries that might need it.

Is the IDB prepared to face this challenge?

Without a doubt. I feel very proud of the ability of our people to react quickly to the situation. I believe this will be the true test of whether our realignment efforts over the past few years have paid off and whether the Bank now has stronger, more flexible

procedures in place to respond when needed.

After several years leading the Bank, how do you feel about the institution?

It’s an organization that the region can be proud of. Looking back, we find that it has always stuck to its core principles, but at the same time it has known how to change along with Latin America and the Caribbean as the region changes. I think my predecessors did a great job, not just in fulfilling their mandate to work toward developing and building “much more than a bank,” but also in bringing together a team of top-notch officials with the ability to deliver results and a vision. I know that sounds nice, and even rhetorical, but when you see the effects of the IDB’s programs on the region, you realize just how much this institution can impact people’s lives.

What would you say has been the greatest success of Latin America and the Caribbean over the past 50 years?

Without a doubt, it’s the region’s progress on social issues, which has allowed life expectancy and other indicators to rise to levels approaching those of the wealthiest nations, as shown by

the United Nations Human Development Index. A good part of the reason why this has occurred is the region's commitment to democracy, which has allowed it to adopt programs aimed at the common good that were developed through public processes.

And what is the region's biggest failure?

It continues to be the world's most inequitable region. However, as we've seen in some countries, the situation is reversible, and the widespread application of successful formulas should be one of our objectives in the years to come. In every case, we're seeing the need to open doors so that opportunities are universal and not restricted to just a few people.

What's the most visible change in the region?

That of the population. Not only have demographic rates fallen overall, but the vast majority of people are now living in urban areas. This situation creates great opportunities as well as challenges in development. That's why a significant part of our recent efforts have been aimed at working with sub-national govern-

ments, which has had an impact on our programs along the way. Half a century ago, the challenge was to provide drinking water or electricity. Today, mass transit and the environment are part of our agenda.

And what's the most visible change in the world?

Globalization, which has broadened horizons and brought lower trade barriers as well as the technology revolution. A more concrete example is the emergence of China, whose trade with Latin America and the Caribbean grew 13 times over from 1995 to 2007, reaching US\$110 billion. This is one of the reasons why we're very pleased to have China on board as one of the Bank's non-regional shareholders.

What are some positive surprises?

The speed at which integration flourished when barriers to trade and the movement of people were lowered. It may sound trite, but in Latin America and the Caribbean, close ties are no longer the work of governments, but of people. This affects everything from tourism to investments, including the exchange of goods and

services. What we're seeing here is a practically irreversible change.

What would you have liked to see?

Greater progress in education, which is the key to growing more quickly, competing in a globalized world and battling inequality. It's not that the region hasn't done anything in this area, but other regions have advanced more rapidly. As such, we've been left behind. Also, international surveys show that the gap between our students and those of emerging Asian economies, for example, is very wide. That's why it's essential not only to work harder, but also to work smarter. I also would have liked to see greater efforts in infrastructure, particularly with regard to roadways and ports as well as logistics management. These barriers keep us from developing adequately and must be torn down. Now, in light of the global crisis, greater efforts have become crucial on this front.

Do you view the private sector's takeover of traditional state monopolies and other services as a positive thing?

Absolutely, although we can't overlook the mistakes that were made due to poorly designed processes. In

general, what we've seen is that the quality of services has improved and that governments that adopted this privatization plan have doubled their returns, because not only did they exit areas where they were incurring great losses, but they are now receiving more tax revenue. They also have increasingly satisfied customers who are benefiting from better service coverage and higher quality. That said, the plan is sustainable only if you have adequate public regulation that places a priority on technical criteria and long-term decisions. We must also remember that the participation of the private sector does not mean that public investment should be reduced, since the former does not substitute for the latter but rather complements it.

Why is the IDB now working with the private sector and not just the public sector?

It's an inevitable reality, due to the fact that more than 90 percent of the region's overall economic activity depends on private activity. Of course, this involves establishing programs at all levels. Not only are we helping to finance large projects, but we're also reaching small and medium-

sized enterprises and individuals. Our achievements in microfinance are very important, as we've helped millions of families broaden their horizons. To paraphrase the motto of one of our programs, it's about "creating opportunities for the majority."

Looking ahead, what's in store for Latin America and the Caribbean?

First, we'll have to deal with the crisis, which, no matter how long it lasts, will eventually come to an end. At that point, I believe the region will be in an excellent position to take advantage of the coming cycle of new expansion, thanks to its abundant resources and the fact that it will have suffered less damage than other regions. However, for that to occur, we need appropriate policies, without wavering or taking steps backward to apply solutions that didn't work before and won't work now.

And what's in store over the longer term?

We've got to concentrate on our challenges. First, we've got to make a greater investment in human capital in Latin America and the Caribbean, which is not only a social imperative

but a strategic decision to promote development in the region. In other words, if basic literacy isn't made one of the pillars of personal development, it certainly can't serve as one for the development of a country. Second, we must make a greater investment in science and technology, which today represents less than one percent of the region's GDP. In a world of change, we need to be innovative. Third, we must keep in mind that the demand for energy, food, water and clean air is threatening sustainable growth and development in Latin America and the Caribbean. That's why we must be able to work in the area of clean, renewable technologies, taking advantage of our abundant natural resources as well as advancements in technology and knowledge.

All of this will take place against the backdrop of climate change. . . .

Yes, indeed. Although it's a global problem and the region has relatively low greenhouse gas emissions, we will pay for the excesses of others. The situation requires us to grow in a responsible manner and be better prepared to mitigate the disasters that we're already experiencing in coastal as well

as inland areas, which will probably become more extreme over time.

Will the IDB be prepared when these and other challenges arrive?

Of course. The Bank has shown its ability to change, which must be one of its permanent features. It's not about denying the past, but about being unafraid of change. But while this is happening, the institution must continue to manage its finances adequately by allocating risk properly and providing high-level technical advice. The expansion of programs will likely entail a greater need for resources, a decision that will be on the minds of our partners when the time comes or the situation demands it. However, the last 50 years have allowed us to look optimistically toward the future, in the sense that responsibility will always be our top priority in managing the affairs of this institution.

Are things better now in your view?

Of course, but from a realistic standpoint. Many of the problems we're facing today will continue to exist in Latin America and the Caribbean for decades to come. However, the region has learned from its failures, which

have sometimes been painful, and it knows that it can come out ahead, as proven by the unique, unflagging and unbreakable optimism of its people.

The IDB aspires to be a key instrument in this objective, working every day toward inter-American development.

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The IDB Office of External Relations was responsible for the original concept and general direction and focus of the subject matter. The overall coordination of the project and the establishment of guidelines were handled by Juan Notaro, Fernando Fernández and Carlos Ferdinand, with unwavering support from Germán Quintana and María Claudia Gómez. Executive Directors Alejandro Foxley Tapia (Chile), Cecilia Ramos Ávila (Mexico), and Marcelo Bisogno (Uruguay) provided some particularly valuable guidance.

The majority of the text was written by Colombian journalist and editor Ricardo Ávila, the book's main author and editorial coordinator, relying on dozens of Bank studies and publications produced throughout the years. Economist María del Pilar Sandoval contributed greatly to reviewing the chapters and adding sources, figures and tables. Laura Lubi León lent her assistance by conducting interviews and obtaining photographs.

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Although science has unlocked the secrets of the human genome, the causes of social and economic development remain stubbornly enigmatic.

Why do some countries adopt new technologies more readily than others? Why does income inequality persist in some regions—even in the face of rapid economic growth? Why do some societies welcome the challenges of globalization while others attempt to turn back the tide?

Honoring the Past, Building the Future examines these and many related questions through the experience of Latin America and the Caribbean. In an accessible, journalistic style, author Ricardo Ávila explores a tumultuous half-century in which the region went from backwater to breadbasket, from dictatorship to democracy, and from economic basket case to emerging power.

It is a story of heroic advances in health care and basic education, but also of weak institutions, lagging competitiveness and crippling debt. It is a chronicle of wealth built on seemingly unlimited natural resources, and of a dawning awareness that agriculture, minerals and oil are not enough.

The story is told through the compelling voices of Nobel-winning scientists such as Mexico's Mario Molina, pathbreaking politicians such as former Chilean President Ricardo Lagos, and dozens of renowned economists, academics and leaders of civil society and the private sector.

Drawing on these testimonies and on an extensive body of published research, *Honoring the Past, Building the Future* exposes the deep contradictions that continue to define Latin America and the Caribbean. It also shows how the theory and practice of development—as seen through the actions of the Inter-American Development Bank—have evolved to meet new challenges.

Through a candid assessment of the development formulas and policy fads of the last 50 years, *Honoring the Past, Building the Future* ultimately shows that progress in Latin America is occurring in unexpected and sometimes contradictory ways. And it argues that regional development institutions such as the IDB, by partnering with innovative governments, communities, civil society groups and companies that are still striving for a better future, will remain effective agents for change in the 21st century.

