

The nineties: Latin America and the Washington Consensus

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1. Introduction.

This paper focus on the evolution of the Latin American countries in the nineties, and comment the roll that the reforms inspired by the so-called "Washington Consensus" had in the performance of the economy in these countries.

Firstly, we will make a commentary on the previous model of imports substitution and its successor, the call First Washington Consensus (FWC). Then, we will see the differences that characterize to the Second Washington Consensus.

Thirdly, we will make an analysis of the performance of Latin American Countries in the Nineties, with respect to the macroeconomic indicators and the growth: movements of capitals, the international trade, the macroeconomic performance, the direct foreign investment, the GIP, etc.

Finally, we will finish making some commentaries.

2. Economic models in Latin America.

Since the finish of World War II, two noticeably different economic models reigned in Latin America.

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First, the *model of import substitution*, took place until the Seventies, when gradually it went leaving after the crisis of petroleum and the later crisis of the external debt at the beginning of the eighties.

This model was characterized by the intervention of the State, with public companies in certain strategic sectors, noticeable protectionism with high tariffs, the search of the autarky, the regulation, and the little opening to the flows of capitals¹.

The model that replaced it, known as *Washington Consensus* (FWC), begins to be applied in the countries of the Southern Cone (Argentina, Chile and Uruguay). It was based on the unilateral opening of the economy, free movements of capitals, the reduction of the State, the deregulation, the privatization of public companies, the search of direct foreign investment and external indebtedness as a way of finance the commercial deficits, etc².

This model was executed with vigor in the nineties, and after the Mexican crisis of 1994-1995 (known as “the tequila effect”), it had his first critics, which gave rise to the so-called Second Washington Consensus (SWC), that focus on the quality of the institutions, and maintain the previous recommendations of the First Washington Consensus³.

3. Latin America in the nineties.

In the Latin American countries the ideas of the First Washington Consensus were applied without exceptions during the Nineties. Thus, Mexico with their entrance to the NAFTA, Argentina and its Convertibility

¹ See BIRDSALL, N. y LOZADA, C. *Shocks externos en economías vulnerables: una reconsideración de Prebisch*, and BOUZAS, R. y FFRENCH-DAVIS, R., *La globalización y la gobernabilidad de los países en desarrollo*, published in CEPAL, *Cincuenta años. Reflexiones sobre América Latina y el Caribe*, Santiago, 1998.

² The phrase that summarize the model was: “*Let's the market do the job*”.

³ On the models, the reforms and the critics, see FANELLI, J. M. y POPOV, V., *On the philosophical, political and methodological underpinnings of Reforms*, First Draft, 2003.

Plan, Brazil and the Real Plan, etc. all the countries applied with different intensity and some particularities the economic recommendations to reach the promised development and growth.

If we analyze the economic indicators, we will be able to have a general concept on the performance of this model of growth⁴.

a) International Trade:

From the middle of the seventies, tariff protectionism was left gradually by the Latin American countries. So, the exports and the imports began to grow quickly (and the fiscal deficit too). Thus, the region began to be integrated to the international trade more and more, exporting raw materials, commodities, and some goods elaborated from the raw materials (with little added value); and importing capital goods and intermediates goods, and some goods for consumption in times of fluency of capitals.

While the exports grew to a rate of the 2.6 and imports to one of the 7.8 in the decade of the seventies, in the nineties they respectively did it to 9.0 and 14.0 %, which shows the degree of opening reached after several years of application of the new model (the FWC), and the bigger fiscal deficit and its correspondent external debt.

b) Movements of capital:

With the financial liberalization, the movements of capitals became a decisive factor for the macroeconomic stability and the growth in Latin America. The capital flows allow to import external saving to finance investment or national consumption, delaying adjustments in the trade balance. Also, however, they allow that the national saving could be send abroad, with serious consequences on the macroeconomic balance (which is strongly related to the growth).

⁴ About the macroeconomic indicators, see FANELLI, J. M., *Macroeconomic regimes, growht and the International Agenda in Latin America*, LATN, FLACSO, Buenos Aires, 2000.

So, there were in Latin America recurrent financial crises, exits of massive capitals, investments with volatile risk, etc.

c) The GIP and volatility:

The rate of growth of the GIP was very fluctuating during this period, because the growth strongly is related to volatility in the income by exports and to the availability of capitals in the world market.

Thus, in the decade of 1970 Latin America grew to an annual average of 5.6%, whereas in the eighties it did it to the 1.7%, and in the nineties to an annual average of 2.7%. We can noticed a strong stagnation in the decade of 1980, period of shortage of capital flows to developing countries, due to the crises of the external debt and the rise of the interest rates in the United States.

d) Consumption and investment:

The same volatility of the GIP caused the volatility of the consumption and the investment in Latin America, that depend on the international prices of the exports of the region and the cycles of the world economy (capital flows, interest rates, etc.).

The investment had a coefficient of variation of 7.1% in Argentina, and 3.5% in Mexico, for example, while the standard one in developed countries does not reach 2,5%. The consumption, on the other hand, varied 2.4% in Argentina, and 2.3% in Chile, whereas in developed countries it does not reach 0,7%.

4. Final Considerations.

After this brief analysis, we can observe that *the performance of Latin America because of the application of the reforms inspired by the*

Consensus of Washington has been mediocre: the GIP does not grow consistently (neither do it strongly), it has been strong shocks due to extra-regional factors, the countries have had strong deficits in their respective commercial balances, and the external debt of the region has increased considerably.

In order to finalize, we can remark that:

- macroeconomic volatility affects the growth, therefore the countries of the region (that are “policy taking”, not “policy making”) must implement anti-cyclical policies and suitable institutions to anticipate the shocks which they are exposed to⁵.
- With the same objective, the reform of the domestic financial architecture (DFA) must be systematic and consistent with international the financial architecture (IFA)⁶.
- A prudent fiscal policy is not sufficient, and neither elevated rates of internal saving nor capital controls can isolate the economy of financial panic. It is necessary to consolidate the financial sector in the long term, and make other institutional reforms (income distribution, tax system, external debt, etc.)⁷.
- It is necessary to promote a more dynamic and diversified insertion in the world trade, so as to increase the incorporation of technology and to spread to productivity in the society⁸.

⁵ OCAMPO, J. A., *Counter-cyclical policies in the developing world*, published in TEUNISSEN, J. J. (Editor), *New Challenges of crisis prevention*, FONDAD, 2001.

⁶ FANELLI, J. M. y MEDHORA, R., *The Emerging International Financial Architecture and its implications for Domestic Financial Architecture*, Federal Reserve Bank of Atlanta, 2001.

⁷ See BIRDSALL, N. y LOZADA, C. *Shocks externos en...* (*op. cit.*).

⁸ See BOUZAS, R. y FFRENCH-DAVIS, R., *La globalización y...* (*op. cit.*).