Latin America and the Caribbean in the World Economy

The region in the decade of the emerging economies
Latin America and the Caribbean in the World Economy is an annual report prepared by the Division of International Trade and Integration of ECLAC. The ECLAC subregional headquarters for the Caribbean, the ECLAC subregional headquarters in Mexico and the Commission’s country office in Washington, D.C. assisted with the preparation of this year’s edition.

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Notes
The following symbols have been used in the tables shown in the Survey:
Three dots (…) indicate that data are not available or are not separately reported.
A dash (-) indicates that the amount is nil or negligible.
A full stop (.) is used to indicate decimals.
The word “dollars” refers to United States dollars unless otherwise specified.

2011-617
CONTENTS

Summary ........................................................................................................................................... 5
A. Crisis and convergence on the international front ....................................................................... 6
B. Relations between the Latin American and Caribbean region and its main non-regional trading partners ............................................................................. 15
C. Securing a better position in the global economy: challenges for the region ......................... 20
Bibliography .................................................................................................................................... 26

Tables
Table 1 Industrialized and developing countries: contribution to global GDP growth, 2008-2011 ................................................................................................... 8
Table 2 Latin America and the Caribbean: external trade, 2009-2011 ...................................... 10
Table 3 Latin America and the Caribbean: share of selected partners in total exports and imports, 2000 and 2010 ................................................................................. 15
Table 4 Latin America and the Caribbean: asymmetries in per capita income and social spending ............................................................................................................... 25

Figures
Figure 1 Latin America and the Caribbean: breakdown of growth in goods trade, 2011 ........................................................................................................................................ 10
Figure 2 Latin America and the Caribbean: trade balance by type of product, average 2009-2010 .................................................................................................................................. 11
Figure 3 World: distribution of exports, 1985 and 2010................................................................. 14
Figure 4 Latin America and the Caribbean: export structure by main destination, average 2008-2010 .................................................................................................................................. 17
Figure 5 Latin America and the Caribbean: share in world exports of goods and services, 1980-2010 .................................................................................................................... 21
Figure 6 Latin America and Asia: productivity of selected ports, 2008-2010 ............................ 24
In mid-2011, conditions deteriorated in the industrialized economies. Early in the year, instability in North Africa combined with other factors to push up fuel prices. Then, in March, the tragedy of the earthquake, tsunami and nuclear disaster in Japan damaged global production chains. Although the impacts of these factors eased in the second semester, concern mounted over the threat of default in Greece, Ireland and Portugal and the repercussions of such an event for larger European economies. In late July, the difficulties in securing congressional approval on the United States public debt ceiling added to the volatility prevailing in financial markets. The downgrading of the United States’ sovereign debt rating for the first time ever and lacklustre economic growth rates in the euro area and the United States added to the uncertainty.

Volatility and uncertainty are again reaching worrying levels. Following the agreement by the United States Congress on the country’s public debt ceiling and the approval by European authorities and the International Monetary Fund (IMF) of a second support package for Greece, the major stock exchanges have been highly volatile and have seen falls reminiscent of past financial crises. Economic stagnation in the euro area, including in its largest economies, France and Germany, is another cause of volatility. International commodity prices are beginning to reflect this uncertainty and volatility and have declined sharply in a short time span, although they remain above their long-term trend, particularly in the case of metals and minerals.

Leading composite indicators show that slower growth in the industrialized countries is starting to act as a drag on the main emerging economies. Data for mid-2011 suggest that the slowdown in the industrialized countries is affecting China and, particularly, Brazil and India. If these trends continue, exports to Europe and the United States should be expected to slow in 2012 and export growth will be compromised in economies whose exports depend heavily on those markets. As growth slows in the emerging economies and the industrialized economies show increasing weakness, international commodity prices are likely to fall, affecting the trade and current account balances of net commodity exporters.

The industrialized economies will experience slack growth for the next few years. The outlook in these economies is for several years of growth below potential, high unemployment rates and latent financial threats amid considerable instability and jittery financial markets. The inability of political leaders to find credible and sustainable solutions to fiscal deficits and high sovereign debt adds another element of uncertainty. The fiscal adjustments needed in Europe and the United States are highly complex and will need a long process of consolidation, which will prove difficult to achieve without broad political support over several administrations.

This scenario limits the political space for agreement on the governance of globalization. Economic turbulence and high unemployment in the industrialized economies may prompt a resurgence of protectionist forces and reduce the margin for new initiatives for responding to the challenges of globalization. The Doha Round of trade talks, for example, has failed to achieve even the minimal agreements which could conclude the Round after 10 years of unsuccessful negotiations. The early announcements by the Group of Twenty (G-20) on reform of the international financial system appear to have disappeared from its agenda. Successive summits on climate change have not been able to tackle the issues with the required speed. Furthermore, the increasing weight of emerging economies in the main variables of the global economy seems to have inspired apprehension and defensiveness on the part of the industrialized economies.
The decade 2011-2020 could still be a boom period for the emerging economies. The engines of the global economy will depend increasingly on growth in the emerging economies and on South-South trade and investment. As emerging economies achieve high and stable growth rates and their population growth slows, their per capita income will rise and move towards convergence with the industrialized economies, particularly for the middle class in these countries.

This trend is not without risks. The announcements of the United States Federal Reserve concerning the possibility of a third package of quantitative easing and a near-zero interest rate for the next two years will heighten dollar liquidity in financial markets, amid continuing weakness in the industrialized economies. This may accentuate the diverging monetary cycles between industrialized and emerging economies, generating additional upward pressure on emerging-economy currencies. In the absence of an effective mechanism for currency coordination among the main economies, some emerging economies will find it difficult to avoid taking trade measures to defend their markets from competitive advantages arising from inefficiencies in the international monetary system.

Given the great uncertainty augured for 2012, the main recommendation for Latin American and Caribbean economies is macroeconomic prudence. Financial volatility is affecting economies with deep financial and stock markets in the region and the slowdown in Europe and the United States will limit export growth and depress commodity prices. Fresh quantitative easing in the United States could worsen currency appreciation in those countries already grappling with large capital inflows. In these circumstances, Latin American and Caribbean economies should strengthen macroeconomic management, pursue sustainable fiscal and external accounts, reinforce macroprudential measures, and steer their policy decisions by the long-term behaviour of main economic variables.

Prudent macroeconomic management must be complemented with more strenuous efforts to further regional cooperation. Deeper commitment to integration and regional cooperation, with extra support for intraregional trade, the consolidation of macroeconomic and social achievements made thus far and progress in forming an enlarged regional market, could help to cushion the impacts should international conditions take another turn for the worse. There is room for more initiatives on trade facilitation and greater cooperation on infrastructure, transport, logistics, custom rules, innovation and technology. Initiatives of this sort would not only open opportunities for exports by small and medium-sized enterprises (SMEs) with a stronger manufacturing content, but also make the region a more attractive partner for trade and foreign direct investment (FDI) (see section C).

A. CRISIS AND CONVERGENCE ON THE INTERNATIONAL FRONT

Three years after the collapse of Lehman Brothers, the global economy has been unable to shake off the legacy of the financial crisis as risk and uncertainty still exact heavy tolls. In the euro area, the sovereign debt crisis and unwieldy fiscal deficits continue to jeopardize the euro, even after the approval of a second rescue package for the Greek economy. In the United States, the budget cuts following congressional approval of the increase of the sovereign debt ceiling could tip the economy into another recession. Private investment remains slack and unemployment high, preventing private consumption from rebounding as strongly as had been expected. Japan is still working through the fallout from the disaster of March 2011 and its impact on the electric power supply, which is hampering the fragile recovery under way in its economy.
The United States economy has weakened more than first thought. Early in 2011, the projected annual growth rate was 3.5%, but revised data for the first two quarters show that the average annualized rate was under 1%, with 0.4% in the first quarter and 1.0% in the second. These GDP data revisions also indicated that the 2009 recession was deeper and longer than had initially been estimated (BEA, 2011).

In the wake of the agreement to raise the sovereign debt ceiling in the United States, serious concerns have arisen over the weakness of the economy. The United States has entered a phase of self-imposed fiscal austerity and is in the process of phasing out the stimulus programmes, while the real economy and private consumption are showing few signs of picking up. The end of the stimulus programmes could shave 1.5 percentage points off the growth rate for 2012 and it is difficult to see how this gap could be made up, given that the crisis and the predominant views in Congress have drastically reduced the manoeuvring room for fiscal policy. It appears that economic policy continues to be misdirected towards reducing the fiscal deficit rather than boosting employment and growth (Krugman, 2011).

Nevertheless, the United States is in a less fragile situation than Europe. United States Treasury bills continue to be a safe haven in the context of the crisis in industrialized economies, as illustrated by the fact that even the highly unusual downgrading of United States sovereign debt did not prevent a further drop in the medium-term yields of these papers. Banks in the United States are not as compromised as those in Europe, having improved their solvency indicators and risk exposure. Businesses in the United States have made large profits and have built up cash reserves by postponing investment decisions. By contrast, the Greek and Portuguese economies are still mired in recession while accumulating debt at rates which make repayment well nigh impossible. Many European banks are highly exposed to the economies in crisis, and the slowness of the European institutions in responding to the situation adds further uncertainty. Moreover, the euro area economies showed flat growth in the second quarter of 2011 and the outlook appears grim.

Neither the perception that Greece is liable to default nor the threat of contagion spreading to larger European economies has dissipated after the second support package for the Greek economy. Two weeks after the package was approved, Spain’s and Italy’s risk premiums soared close to the levels which had prompted bailouts for Ireland, Greece and Portugal.1 Worse still, the measures’ ineffectiveness is exacerbated by their slowness, inasmuch as they still have to be approved by a number of European parliaments, which is unlikely to happen before October.

The time has arrived for innovative formulas for deepening European integration. It seems unlikely that Europe can overcome the current crisis without strengthening its mechanisms of regional solidarity and cooperation. The key discussion is whether the way out of the crisis is through more or less integration. If the current policies remain unchanged, the euro could well enter a severe crisis which would have serious implications for integration itself. Sooner rather than later, the recovery of growth will be contingent on massive debt purchases by the European Central Bank or the issue of European debt to replace national liabilities, together with credible commitments to fiscal consolidation.

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1 The steep stock market falls in Europe and the United States following the agreement to increase the sovereign debt ceiling in the United States led the European Central Bank (ECB) to depart from its previous stance and buy bonds from countries under heavy pressure, including Italy and Spain, which helped to lower risk premiums.
The European and United States economies will bear the legacy of hefty public debt left by the crisis for many years to come. The crisis produced a deterioration in these economies’ fiscal accounts worse than any seen before. The public debt stock in the industrialized economies climbed from 77% of GDP in 2007 to 104% in 2010. According to projections, even if fiscal policy is gradually tightened, the debt-to-GDP ratio could rise to 126% by 2020 (Deutsche Bank, 2011). Without tougher fiscal measures, this ratio could rise as high as 150% (134% in the case of the United States).

Fiscal and public debt challenges threaten the industrialized economies with the possibility of a “lost decade”. Given the magnitude of the challenges, the adoption of technically sound measures will need to be underpinned by firm political consensus allowing the adoption of painful decisions which will take several years to implement. Political leaders are on the horns of a double dilemma: they are caught, first, between medium-term needs and day-to-day electoral pressures and, second between the overall impacts of their decisions and their effects on the next election. The amounts needed for fiscal consolidation and public debt reduction are so large as to cast serious doubt over any recovery in growth in the next three years or more. Given also the fiscal pressures that financing future pensions for an ageing population will exert on the industrialized economies, it is no exaggeration to suggest that the industrialized economies could be entering a lost decade.

After regaining pre-crisis levels of GDP and trade, the main emerging economies began to show signs of a slowdown around mid-2011. Several of these economies were growing above their potential in 2011, running the risk of overheating. The recovery in this group of economies began in China then spread to India, Indonesia and the rest of the Asia-Pacific region, and from there to the rest of the emerging economies. High growth rates in emerging Asia are rooted in stronger domestic demand and a dynamic trade performance. In Latin America and the Caribbean, the monetary and fiscal stimulus measures that supported the post-crisis recovery gave way to an upturn in private consumption and investment, together with an increase in exports. Export growth has also been boosted by favourable terms of trade, particularly for mineral products. As a result, for the last few years emerging and developing countries have accounted for around three quarters of global economic growth (see table 1).

<table>
<thead>
<tr>
<th>Countries and groupings</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrialized countries</td>
<td>0.12</td>
<td>-1.79</td>
<td>1.55</td>
<td>1.22</td>
</tr>
<tr>
<td>United States</td>
<td>0.00</td>
<td>-0.53</td>
<td>0.56</td>
<td>0.53</td>
</tr>
<tr>
<td>European Union</td>
<td>0.15</td>
<td>-0.87</td>
<td>0.36</td>
<td>0.35</td>
</tr>
<tr>
<td>Japan</td>
<td>-0.07</td>
<td>-0.37</td>
<td>0.23</td>
<td>0.08</td>
</tr>
<tr>
<td>Others</td>
<td>0.04</td>
<td>-0.02</td>
<td>0.40</td>
<td>0.25</td>
</tr>
<tr>
<td>Developing countries</td>
<td>2.74</td>
<td>1.27</td>
<td>3.46</td>
<td>3.18</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
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<td>0.07</td>
<td>0.12</td>
<td>0.14</td>
</tr>
<tr>
<td>Latin America and the Caribbean</td>
<td>0.37</td>
<td>-0.15</td>
<td>0.52</td>
<td>0.40</td>
</tr>
<tr>
<td>Developing Asia</td>
<td>1.64</td>
<td>1.66</td>
<td>2.29</td>
<td>2.10</td>
</tr>
<tr>
<td>China</td>
<td>1.13</td>
<td>1.19</td>
<td>1.40</td>
<td>1.37</td>
</tr>
<tr>
<td>Middle East and North Africa</td>
<td>0.25</td>
<td>0.09</td>
<td>0.19</td>
<td>0.20</td>
</tr>
<tr>
<td>Central and Eastern Europe</td>
<td>0.11</td>
<td>-0.12</td>
<td>0.15</td>
<td>0.12</td>
</tr>
<tr>
<td>World</td>
<td>2.87</td>
<td>-0.52</td>
<td>5.01</td>
<td>4.40</td>
</tr>
</tbody>
</table>

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of data from the International Monetary Fund (IMF).
The rise of China and the rest of the South is associated with the geographical fragmentation of global production and the spread of global value chains. Global value chains are a key feature of today’s organization of international trade, in which the exchange of finished goods among nations is gradually losing ground to trade in intermediate goods, along with increased specialization in tasks or phases of production. The distribution of value added within value chains reveals their inherent governance structure, in which control is often exerted by one or a few firms, both in terms of suppliers (upstream) and sellers (downstream). Even though value chains have developed mainly in China and the rest of East Asia, they are spreading to other geographical regions. In Latin America and the Caribbean, the increasing importance of trans-Latins reflects this trend.

International trade contributed much to recovery following the economic and financial crisis of 2008 and 2009. International trade and open markets prevented the crisis from worsening and swiftly transmitted the recovery in final demand. The significant contribution of international trade to GDP growth is explained in part by several effects that temporarily increased the trade elasticity of output. Also, the international trading system was able to contain the protectionist outbursts prompted by the worst international crisis in 80 years. The agreements brokered by G-20 from 2008 onwards also help to ensure this outcome.

South-South trade, led by China and the rest of emerging Asia, is the main engine of world trade growth. Exports from developing and emerging countries grew 17% by volume in 2010, compared to 13% for the industrialized economies and a global average of 15%. Within this group, China showed the highest rate of trade recovery, since its exports jumped by 28% in volume terms in an impressive reversal of the 10% drop registered in 2009 and almost doubling the rate of global trade growth for that year. Imports by developing and emerging countries grew 18% by volume in 2010, compared to 11% for the industrialized economies. As a result, the developing and emerging economies had regained pre-crisis import and export values by late 2010. These groups of countries accounted for almost 60% of the growth in global export values between 2005 and 2008 and in 2010, and represented a smaller share of the drop in world trade in 2009. The industrialized countries are thus benefiting from dynamic external demand from developing and emerging economies while their own domestic demand remains weak.

The value of goods exports from the Latin American and Caribbean region is projected to rise 27% in 2011. Prices will contribute most —18 percentage points— of this rise, whereas volumes will contribute 9 percentage points (see table 2 and figure 1). This breakdown of 2011 export growth is similar to the pattern for 2010. The 2011 projection is based on an assumption of second-semester growth in external demand for the region’s products similar to that seen in the first semester, and on stable commodity prices for the remainder of the year.

The value of imports by Latin America and the Caribbean is projected to rise 22% overall, but more sharply in the case of fuels (46%). Slower growth in imports than in exports may result in a regional trade surplus of around US$ 80 billion at year-end, in particular with the United States and, to a lesser extent, with the European Union. The region overall will widen its trade deficit with China and the rest of Asia, but with a differentiated subregional pattern since South America will register a surplus and the rest of the region, a deficit.
Table 2  
LATIN AMERICA AND THE CARIBBEAN: EXTERNAL TRADE, 2009-2011  
(Annual growth rates in percentages)

<table>
<thead>
<tr>
<th>Region/country</th>
<th>Exports</th>
<th></th>
<th></th>
<th>Imports</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Latin America and the Caribbean</td>
<td>-22.6</td>
<td>26.7</td>
<td>27.0</td>
<td>-25.0</td>
<td>29.5</td>
<td>23.0</td>
</tr>
<tr>
<td>Latin America (19)</td>
<td>-21.9</td>
<td>27.0</td>
<td>27.0</td>
<td>-24.9</td>
<td>30.4</td>
<td>23.0</td>
</tr>
<tr>
<td>Southern Common Market (MERCOSUR)</td>
<td>-21.9</td>
<td>29.8</td>
<td>30.0</td>
<td>-27.3</td>
<td>42.2</td>
<td>27.0</td>
</tr>
<tr>
<td>Andean countries</td>
<td>-27.7</td>
<td>20.7</td>
<td>32.0</td>
<td>-20.9</td>
<td>19.9</td>
<td>29.0</td>
</tr>
<tr>
<td>Central American Common Market</td>
<td>-11.6</td>
<td>15.2</td>
<td>29.0</td>
<td>-24.3</td>
<td>19.0</td>
<td>24.0</td>
</tr>
<tr>
<td>Other countries</td>
<td>-19.9</td>
<td>28.9</td>
<td>21.0</td>
<td>-25.0</td>
<td>28.8</td>
<td>19.0</td>
</tr>
<tr>
<td>Chile</td>
<td>-18.5</td>
<td>31.5</td>
<td>20.0</td>
<td>-30.9</td>
<td>38.3</td>
<td>24.0</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>-18.7</td>
<td>20.3</td>
<td>25.0</td>
<td>-23.1</td>
<td>24.4</td>
<td>22.0</td>
</tr>
<tr>
<td>Mexico</td>
<td>-21.2</td>
<td>30.0</td>
<td>21.0</td>
<td>-24.1</td>
<td>28.5</td>
<td>17.0</td>
</tr>
<tr>
<td>Panama</td>
<td>7.8</td>
<td>1.8</td>
<td>20.0</td>
<td>-10.9</td>
<td>20.3</td>
<td>28.0</td>
</tr>
<tr>
<td>Caribbean Community (CARICOM)</td>
<td>-43.4</td>
<td>10.8</td>
<td>28.0</td>
<td>-25.5</td>
<td>3.5</td>
<td>18.0</td>
</tr>
</tbody>
</table>

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.  
a  Projections.

Figure 1  
LATIN AMERICA AND THE CARIBBEAN: BREAKDOWN OF GROWTH IN GOODS TRADE, 2011  
(Rates of variation in percentages)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official monthly data.  
a  Projections.  
b  Includes the Central American Common Market and Panama.
Commodity prices have been booming since early 2009, benefiting net commodity exporters. These prices began to rise more sharply in the second half of 2010 and came to exceed pre-crisis levels for many products. By contrast, prices for manufactured goods have increased only slightly in the past few years. The commodity price boom is driven chiefly by demand factors, both real demand from emerging economies and speculation in a context of low financial returns in industrialized economies. In the case of agricultural products, higher prices in 2010 were also attributable to poor climate conditions in producer countries.

The commodity price boom was interrupted in mid-2011, as uncertainty mounted amid the sovereign debt problems of Europe and the United States and the stagnation of their economies. Sharp volatility on main stock exchanges and the dollar’s loss in value against gold, the Swiss franc and the yen also contributed to the commodity price drop. It is too soon to draw firm conclusions about the trajectory of commodity prices, but their volatility is evident. Accordingly, global mechanisms are needed to soften both price shocks and their transmission to domestic economies through saving of temporary inflows, structural fiscal rules and other measures that facilitate public expenditure planning on the basis of medium-term revenues.

The effect of higher commodity prices is highly positive for most South American countries but negative for most countries in Central America and the Caribbean. The largest benefits accrue to South America, particularly Paraguay and Uruguay in the case of food and beverages, Chile, Peru and Plurinational State of Bolivia in the case of metals and minerals; and Bolivarian Republic of Venezuela, Colombia, Ecuador and, here again, Plurinational State of Bolivia in the case of energy products. In contrast, higher commodity prices hurt terms of trade for most Central American and Caribbean countries. The Caribbean countries are even more vulnerable than those of Central America, because they run a trade deficit in food and beverages, metals and minerals, and energy products, whereas the trade deficit of the Central American countries is concentrated in this last category (see figure 2).

**Figure 2**

**LATIN AMERICA AND THE CARIBBEAN: TRADE BALANCE BY TYPE OF PRODUCT, AVERAGE 2009-2010**

*(Percentages of GDP)*

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**Source**: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Commodity Trade Database (COMTRADE).

a Data for 2009 only.

b Data for 2010 only, using mirror statistics for minerals and metals.
Disequilibria between the current accounts of the major economies and those of their trading partners are growing again, largely as a result of real-exchange-rate trends. In the United States, the dollar has been depreciating more or less steadily since late 2001. China’s real effective exchange rate has been appreciating since 2006, but not quickly enough to rebalance its current account.

After almost 10 years of negotiations, the Doha Round of the World Trade Organization (WTO) has reached a critical point. For most of this time the greatest disagreements have concerned agriculture, but recently differences have centred on the liberalization of trade in manufactures in the main emerging economies (particularly Brazil, China and India). Discussions on the future of the Doha Round will likely dominate the Eighth Ministerial Conference of the World Trade Organization, which will take place on 15-17 December 2011. It will be difficult to complete the Round in 2012, as several large member countries (including France, India and the United States) are due to hold elections that year.

Growth rates can diverge only so far between emerging and industrialized countries. Until now, emerging countries have withstood the impacts of the 2008-2009 crisis better than the industrialized countries, recovered more swiftly and maintained higher growth rates —bearing out to some extent the theory of decoupling between the two groups of economies. However, the stock market turmoil during the first half of August 2011 has already hurt commodity prices and if the economic slowdown persists in Europe and the United States, exports to these economies will inevitably suffer. In other words, even a slackening in economic growth in the industrialized countries will cloud the growth outlook of emerging markets. An even more pessimistic scenario in the rich economies would have larger consequences, in all likelihood forcing governments to implement new stimulus programmes to safeguard employment and economic growth as in 2009. This, of course, would depend on these countries having the policy space for such measures. For all these reasons, macroeconomic prudence and a close watching brief on the international economic situation head the economic policy agenda of emerging economies.

The consequences of the subprime mortgage crisis —the largest and deepest since the Great Depression— are still being felt four years after it broke out, yet the drive for reforms has dissipated. The declarations made by G-20 leaders at their Washington Summit on Financial Markets and the World Economy, held in Washington D.C. on 14-15 November 2008, called for major reforms to the international financial system and regulatory practices. As stimulus packages and the containment of protectionist measures diminished the likelihood of a global depression, however, the appetite for reforms and international cooperation also waned. Recent meetings of G-20 have been dominated by national interests, not a collective effort to reform the system and policies that allowed the crisis to happen.

More global cooperation is needed to avoid a new international economic crisis. Several themes should be on this agenda. In the economic sphere, agreements must be reached in the short term on the regulations governing sovereign debt, on the functioning of sovereign debt rating agencies, on measures to resolve the European crisis, and on mechanisms that could dampen the volatility of commodity prices. Key issues for the medium term include financial early warning mechanisms, the need to resolve excessive current account disequilibria to avoid emerging economies having to bear the brunt of adjustment through currency appreciations disconnected from productivity gains and, lastly, regulations requiring banks to hold provisions proportional to the risk of their operations.

Emerging markets need to have a stronger voice within global cooperation efforts. All the matters discussed here impinge increasingly upon the growth prospects of emerging economies although they refer to forces that have taken shape basically in the industrialized world. It is therefore only logical that the emerging economies, which underpin most of global economic growth today, should have something to say about the origins and trajectories of these disequilibria and their effect on the
globalization process. A fresh round of quantitative easing in the United States and the repurchase by the European Central Bank of European countries’ bonds would give rise to abundant international liquidity, which could worsen the current difficulties for emerging economies. To avoid these potential growth constraints, emerging economies should improve their coordination within G-20, with well thought-out diagnosis and proposals. The three Latin American members of G-20 should also seek closer coordination with the rest of Latin America and the Caribbean, inasmuch as their voice in G-20 would undoubtedly be strengthened if they represented concerted regional views on the aforementioned international issues.

The recent global financial and economic crisis and the different growth paths followed by emerging and industrialized economies thereafter has accelerated convergence in per capita income both the two groupings. Steady expansion in emerging economies, led by China, compared with flat growth in industrialized countries, has brought forward productive, technological and industrial convergence between the two. Thus, in mid-crisis, emerging economies improved their position in the world economy. Increasing trade links between developing countries helped these economies to decouple to some extent from the adverse cycle in which the most developed OCED economies were caught up.

The Latin American and Caribbean region managed to reduce its per capita income gap relative to the industrialized countries during the boom in world growth between 2003 and 2008 and in the two years post-crisis. In contrast to the two previous decades, from 2004 to 2010 the region’s income gap with respect to the advanced economies narrowed. China and the newly industrialized Asian countries (Hong Kong Special Administrative Region of China, Republic of Korea, Singapore and Taiwan Province of China) have achieved constant per capita income convergence for several decades. Stagnation in the advanced economies in 2010 and 2011 and rapid, steady growth in most emerging economies have hastened the reduction of global per capita income gaps.

Since the recent crisis, the emerging countries have gained a larger share in the main variables of the world economy. First, the contribution of emerging economies to global GDP growth increased from a third in 2000 to three quarters in 2007 and almost 100% in 2008 and 2009. Projections indicate that by 2016, emerging economies will account for three quarters of total growth in world GDP. China is the single largest driver of growth both among the emerging countries and globally.

Regarding the participation of the South in world consumption, the Asia-Pacific region is likely to represent two thirds of the world’s middle class by 2030. China’s middle class is already the world’s second largest in absolute terms, after the United States. Rapid expansion of the middle class in China and India could compensate for some of the stagnation expected in middle class growth in the United States and Europe.

Trade has grown much faster for the emerging economies than the industrialized countries in the past few decades. South-South trade has been particularly dynamic: having accounted for only 6% of world trade in 1985, growth in this trade gathered pace during the past decade, taking its share in world trade from 14% to 24%. During that time, South-North trade expanded from 12% to 21% and the share of North-North trade dropped significantly (see figure 3). The crisis reduced exports from the South in 2009 but does not seem to have affected long-term trends. If South-South trade continues to increase more rapidly than other trade combinations, its share in global trade will exceed that of North-North trade by about 2018. The rapid growth in South-South trade mostly reflects increased trade between Asian developing countries, with China as the centerpiece. Almost 85% of South-South trade is among Asian emerging economies or between these and other regions in the South.
The South has gained more ground as a recipient of global FDI than it has as an originator of this type of investment. Between 1970 and 2007, the South’s share in global FDI inflows rose from a fourth to a third. The financial crisis may have further increased the weight of emerging countries in FDI inflows by some way: in 2010 the South represented over half of world FDI inflows for the first time. Developing and transition countries are gaining share of global outflows of FDI, as well, of which they represented 22% in 2010.

The current variable-speed global economy is fraught with uncertainties. The economies of the United States, Japan and the European Union are stagnant and are facing severe fiscal difficulties and have virtually depleted their monetary policy space. The emerging countries could find their good prospects tarnished if the industrialized countries fail to resolve these difficulties. Economies which have a major trade link with the United States —including Mexico and the Central American and Caribbean countries— could find their exports to that market slackening if growth there continues to slow during the second semester of 2011 and into 2012. Industries with significant exports to the European Union may also be affected unless they redirect trade towards more dynamic markets.

The world economy still faces major risks that could lead to an increase in protectionist measures. These risks include the persistence of global disequilibria between countries running deficits and those running surpluses; high levels of unemployment in the industrialized economies; the deep-reaching fiscal consolidation process under way in Europe, particularly in Greece, Ireland, Portugal and Spain; and food price volatility. The large capital flows entering emerging economies may fuel pressures to increase protection, as the local currency appreciation they induce benefits imports relative to locally produced goods and services.
B. RELATIONS BETWEEN THE LATIN AMERICAN AND CARIBBEAN REGION AND ITS MAIN NON-REGIONAL TRADING PARTNERS

Asia has become a much more important trading partner for Latin America and the Caribbean over the past decade, while the United States has lost share in the region’s trade and the portion going to the European Union has stood still. The United States is still the region’s largest trading partner, but its share has declined significantly. Exports to the region’s second largest trading partner, the European Union, rose slightly during the past decade, while imports from the bloc remained constant (see table 3).

<table>
<thead>
<tr>
<th>Table 3</th>
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<td>LATIN AMERICA AND THE CARIBBEAN: SHARE OF SELECTED PARTNERS IN TOTAL EXPORTS AND IMPORTS, 2000 AND 2010 (Percentages)</td>
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<td>50.4</td>
<td>29.1</td>
<td>14.2</td>
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**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Commodity Trade Database (COMTRADE); official information from the countries and International Monetary Fund (IMF), Direction of Trade Statistics database (DOTS).

*a* Includes Australia, Brunei Darussalam, Cambodia, China, Philippines, India, Indonesia, Japan, Lao People’s Democratic Republic, Malaysia, Myanmar, New Zealand, Republic of Korea, Singapore, Thailand and Viet Nam.

The surge in trade between the Latin American and Caribbean region and Asia-Pacific largely reflects the dynamic trade relationship with China. In the first half of the last decade, China displaced Japan as the region’s largest trade partner in Asia-Pacific. Trade with China exceeded US$ 100 billion for the first time in 2007 and reached US$ 187 billion in 2010, and accounts for half the region’s total trade with the Asia-Pacific region. China’s significance as a destination market varies from one country to another within Latin America and the Caribbean, however. China has become a key market for (in decreasing order of importance) Cuba, Chile, Brazil, Peru, Argentina and Bolivarian Republic of Venezuela. By contrast, it represents less than 3% of total exports for Paraguay, Ecuador, Mexico, Central America (except Costa Rica) and most of the Caribbean countries. India, despite its rapid growth in the past two decades, represents only 6.4% of the region’s total exports and 3.4% of imports to Asia-Pacific, ranking below the Republic of Korea as a trading partner for Latin America and the Caribbean. Asia-Pacific is a more significant trading partner for imports into the region than for its exports, which has led to a growing trade deficit for the region, particularly for Mexico and Central America.

In 2005-2010, the Latin American and Caribbean region was the fastest-growing trading partner for China and the second fastest for Japan. China’s exports to and imports from Latin America and the Caribbean expanded nearly twice as fast as its total exports and imports in that period. As a result, the region’s share in China’s trade gradually rose from a very low base to nearly 6% in 2010 for both exports and imports. During the same period, Japan’s exports to Latin America and the Caribbean outgrew those to any other destination market and its imports from the region were surpassed only by those from the Community of Independent States (CIS).
The Latin American and Caribbean region is also an increasingly important trading partner for the United States. During the past two decades, the United States’ trade with the region has increased more rapidly than with its other partners, with the notable exception of China. In 2010, Latin America and the Caribbean became the largest buyer of United States goods exports, accounting for 23% of the total. That year, 19% of total United States goods imports were sourced from the region, which positioned it similarly to China in the United States import ranking. Bilateral trade between Latin America and the Caribbean and the United States is concentrated in few countries, with Mexico representing more than two thirds of the region’s exports to and half of its imports from that market. The Andean countries are the region’s second largest supplier of exports to the United States market and, together with the Southern Common Market (MERCOSUR), represent a quarter of the value exported to that country from the region in 2010. In the case of imports into the region, the order is reversed: MERCOSUR is the second largest importer from the United States, followed by the Andean countries.

Contrasting with the region’s importance as a trading partner for the United States, China, and Japan, it represents only a fraction of the European Union’s international trade. The share of the Latin American and Caribbean region in the total trade of the European Union has hovered at around 3% for the past three decades. Although the European Union remains the region’s second largest trading partner, it could lose this position to China towards 2015. Latin American and Caribbean trade with the European Union is concentrated in a few countries, with MERCOSUR representing almost half of the total. The five MERCOSUR countries and Mexico together represent 61% of the region’s total exports to the European Union and 69% of its total imports from that bloc.

The Latin American and Caribbean region’s intraregional exports and those to the United States show a larger proportion of manufactures not based on natural resources than those to Asia-Pacific and the European Union. Notably, however, exports to the United States in this category chiefly reflect the large proportion of Mexico’s manufacturing exports in the region’s total exports to the United States. At the other extreme, primary products and natural-resource-based manufactures account for almost 90% of the region’s exports to Asia-Pacific (see figure 4).

Although during the past decade the Latin American and Caribbean region has considerably increased the range of products it exports to all destination markets, no market outside the region comes close to matching the intraregional market in terms of the number of exported products. By 2010, the intraregional market was receiving the largest range of export products, followed by the United States, the European Union and —at a considerable distance— the Asian markets. On average, in 2008 and 2009, the number of products exported within the region itself exceeded those exported to China by a factor of 10, and those exported to the rest of Asia by a factor of 4. This confirms the growing importance of the intraregional market as a destination for manufacturing exports and as a vehicle for the development of regional value chains.

The current priorities of United States trade policy do not include a strategic vision for Latin America and the Caribbean. The region is barely mentioned in the trade policy agenda the President of the United States presented to Congress in March 2011, and then only in reference to the administration of existing agreements, the President’s intention to seek congressional approval for the agreements negotiated with Colombia and Panama, and his interest in expanding and diversifying economic relations with Brazil. There have been no significant developments in terms of trade talks between the United States and Latin America and the Caribbean since 2007. The sole exception came in 2010 with negotiations to broaden the Trans-Pacific Strategic Economic Partnership (also known as the Trans-Pacific Partnership, or TPP). Chile and Peru participate in this initiative, but its main focus is
clearly the Asia-Pacific region. This is in contrast to the dynamic negotiating activity between many Latin American and Caribbean countries and European and Asian partners.

Figure 4

LATIN AMERICA AND THE CARIBBEAN: EXPORT STRUCTURE BY MAIN DESTINATION, AVERAGE 2008-2010
(Percentages of the total)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of United Nations Commodity Trade Database (COMTRADE).

In this context, ECLAC has proposed a new hemispheric alliance between the United States and Latin American and Caribbean region to tackle common challenges and seek closer integration with the global economy. The main points of this agenda include:

- The reinstatement of the Plurinational State of Bolivia as eligible for the benefits of the Andean Trade Promotion and Drug Eradication Act (ATPDEA).
- The renewal in 2011 of ATPDEA and the Generalized System of Preferences (GSP) for a sufficient period to provide the region’s countries with a stable system.
- Congressional approval in 2011 of free trade agreements with Colombia and Panama.2
- A definitive settlement to the dispute over admittance of Mexican trucks into the United States.

2 This approval was still pending in August 2011.
• Cumulation of origin to be allowed among the different free trade agreements between the United States and countries in the region, in order to promote a more integrated production structure and help to develop regional value chains.

• Adherence of interested countries in the region to TPP negotiations, aiming for a balance between results in traditional areas and on new issues (intellectual property rights, investment, services, labour and environmental standards, and regulatory coherence), as well as other issues of interest to the developing countries party to the talks (antidumping, market access for agricultural products, migration and so forth).

Latin America and the Caribbean and the European Union have sought to inject renewed vigour into their relations in recent years. In a context of low growth and great uncertainty in the European Union, the region has become an increasingly attractive market for European exporters and investors. Accordingly, the European Union concluded negotiations in 2010 for an association agreement with Central American countries (including Panama) and a trade agreement with Colombia and Peru. Also in 2010, negotiations were resumed on an association agreement between the European Union and MERCOSUR. Including the agreements already in place with Chile, Mexico and the Caribbean Forum of African, Caribbean and Pacific States (CARIFORUM), by 2012 or 2013 the European Union could have preferential agreements with 30 countries in the region. This points to the need to promote cumulation of origin between all these agreements, along the lines of the European Union’s practice regarding its agreements with the Mediterranean countries. This would boost the integration of production and the development of regional and interregional value chains.

In addition to free trade, the association agreements negotiated between the European Union and the region include the pillars of cooperation and of political dialogue. As such, these agreements are fundamental for promoting a virtuous relationship between political consensus-building, economic and trade development, and social cohesion, and they represent a more comprehensive view of development than agreements confined solely to trade. Another important difference between the agreements the region has negotiated with the European Union and those negotiated with other partners is that the first include as explicit goals negotiations between regions and the achievement of substantial advances in integration in all the Latin American and Caribbean subregional groupings.

Latin America and the Caribbean and the European Union also have strong investment ties. In the first decade of the 2000s, the share of the region —including financial centres— in FDI flows from the European Union exceeded that of Asia, as the European Union became the main source of FDI in the region. In the wake of the many economic reforms implemented since the 1990s, FDI flows into the region expanded strongly, especially from firms in European countries, which took advantage of privatization in banking, telecommunications and other services. FDI from the United States also increased, but at a slower pace. This produced a shift in the composition by origin of cumulative flows and the European Union became the largest source of FDI in the last decade, with 43% of total flows.

Great potential exists for cooperation between the region and the European Union in such areas as green technology and corporate social responsibility. The European Union is a global leader in environmental protection, in efforts to combat climate change and in corporate social responsibility, all of which contribute to broader and more inclusive development. The European Union contributed between 30% and 38% of all patents issued globally between 2004 and 2006 in environmental technology categories. European Union institutions have been promoting systematic inclusion of the concept of corporate social responsibility in corporate strategies for over a decade. From this perspective, strengthening corporate ties between the region and Europe should advance the goals of achieving growth
with greater equality and developing a less carbon-intensive competitive advantage, which should steer public policies in Latin America and the Caribbean in the next few years.

In the past few years integration in Asia-Pacific has evolved from a de facto situation towards a more formal structure. The Association of South-East Asian Nations (ASEAN) has positioned itself at the heart of this de jure integration process through various trade liberalization initiatives with other Asian countries. As a result of the many trade agreements existing in the Asia-Pacific region, nearly half of all intra-Asian trade is now covered by some form of preferential tariff treatment. At the same time and for many reasons (particularly efforts to secure better market access), Australia, China, Japan, India, Republic of Korea and Singapore, among others in the Asia-Pacific region, have signed free trade agreements and established strategic partnerships with Latin America.

The ongoing removal of barriers to trade among Asian countries could divert trade at the expense of Latin America and the Caribbean. China, India, Japan and the Republic of Korea, among other Asian economies, maintain high tariffs on key sectors for Latin American and Caribbean exporters, including agriculture, textiles, clothing, and some machinery sectors. The lowering or elimination of these tariffs in the context of treaties between ASEAN members and the four counties mentioned above, as well a new agreement in the form of ASEAN+3, therefore favours ASEAN countries at the expense of Latin America and the Caribbean. The resulting trade diversion could be significant unless the region actively pursues policies to secure bilateral or subregional trade agreements that would even out market access conditions in the main Asian markets.

As a result, trans-Pacific trade agreements are increasing rapidly in number. The most active countries in the region in this regard have been Chile and Peru, the two for which the Asia-Pacific region represents the greatest share of total exports. Costa Rica has recently followed suit and has signed free trade agreements with China and Singapore. Colombia is currently negotiating an agreement with the Republic of Korea. These initiatives reflect efforts by the Latin American countries to structure their relations with Asia-Pacific over a longer horizon, but do not yet amount to any sort of shared strategic framework.

In the case of China, an issue that must be carefully addressed is the sensitivities triggered by its industrial exports. Concerns in this regard have emerged in Argentina, Brazil and Mexico, as a result of loss of market share within the region and the threat of displacement in third markets. Here, a coordinated, medium-term approach may be needed between Chinese and Latin American producers with a view to find building on complementarities and cooperation opportunities. Otherwise trade conflicts are likely to grow and prompt new accusations of dumping behaviour and fresh non-tariff barriers.

Although processed mineral products still represent 80% of its total imports from Latin America and the Caribbean, Asia is starting to import new products from the region. Though some of these products belong to the category of primary products, they are not commodities inasmuch as they can, to an extent, be differentiated by quality. As long as household incomes continue to rise in Asia, and its consumption patterns gradually approach those of the West, Asian demand for these products could expand significantly in the near future, presenting growing opportunities for Latin America and the Caribbean. In addition, the competition that the region faces in the Asia-Pacific markets, including the competition from Asian economies themselves, could open opportunities for interesting commercial, productive, and technological alliances. These could include joint investment and strategic alliances in commercial and technological areas that would enable better response to Asian and Chinese demand, with benefits for both regions.
Given that Asia-Pacific is the most dynamic region of the world economy, the Latin American and Caribbean countries must redouble their efforts to forge a new trans-Pacific relationship. China, specifically, is emerging from the global crisis with a strengthened productive, technological and financial base, and with tighter ties to the Asia-Pacific economies. Recent estimates suggest that by 2016 China’s GDP, measured in terms of purchasing power parity, will surpass that of the United States, making China the world’s largest economy. Accordingly, and given ongoing uncertainty over the economic future of Europe and the United States, Latin America and the Caribbean should strive to identify and seize the opportunities offered by greater integration with the Asia-Pacific countries. These efforts will be more fruitful if the region adopts a coordinated approach, such that trade and investment initiatives may benefit from existing synergies, economies of scale and combined political will, thereby opening the door to more ambitious goals.

Economic and trade conditions are highly favourable for pursuing a new relationship between the two regions. The good outlook for growth in both regions represents a unique opportunity to cement the foundation of a new phase in their trade and investment relations. To bring this about, progress must be made in: (i) diversifying the region’s exports to Asia-Pacific; (ii) creating new interregional trade alliances; (iii) increasing the volume of mutual investment flows, emphasizing infrastructure in Latin America and the Caribbean and the introduction of the region’s products into Asian value chains; (iv) substantially increasing cooperation efforts in innovation, technology and human capital; and (v) establishing high-level forums for dialogue between the region’s governments and their counterparts in Asia-Pacific.

C. SECURING A BETTER POSITION IN THE GLOBAL ECONOMY: CHALLENGES FOR THE REGION

The profound transformations taking place in the world economy present the region with the challenge of rethinking its international position and its global alliances. The weak recovery and great uncertainty prevailing in the United States and Europe, which will probably persist for some years, are contributing to the growing share of the developing economies in the different economic variables. At the same time, production, trade and investment are increasingly structured around regional and global value chains. Faced with these changes, the Latin American and Caribbean region has sought closer links with other emerging regions, particularly Asia.

In the coming decades, the quality of the region’s international economic position will be strongly determined by its links with other developing economies. The main channel for these linkages today is trade between the region and other developing countries (South-South trade). Another, increasingly important channel is investment, both the attraction of FDI and other capital from Asia and investments made by companies from the region —in particular the large internationalized corporations known as “Trans-Latins”— in Asia and other developing regions. Moreover, ample space exists to develop alliances between firms from the region and those in other emerging regions through a variety of production modalities (including franchising, licensing, manufacturing contracts and services subcontracting) which are playing growing roles in the context of global value chains.

The Latin American and Caribbean region has important assets for conquering a higher-quality role in the international economy. First, the region has absorbed important macroeconomic policy lessons, the benefits of which were made clear by the recent global financial crisis. The region’s production, employment and social indicators were not left unscathed by the impacts of the crisis but they held up better than during previous episodes of smaller magnitude. Second, improvements in the region’s
social indicators and the expansion of its middle class in recent years have upped the strategic value of the Latin American and Caribbean market. This larger consumer market makes the region more attractive as a trade and investment partner.

The region’s abundant endowment of natural resources constitutes another strategic asset. Latin America and the Caribbean is a major agricultural producer, particularly in soybean (accounting for almost half of the world’s production), beef (of which it produces almost a third) and dairy (almost a quarter). A similar situation prevails in the mining sector: Latin America and the Caribbean generates over 45% of the world’s copper production and over 20% of molybdenum, zinc and tin. In energy, the region accounts for 30% of global biofuel production. Latin America and the Caribbean also boasts the largest fresh water reserves—a third of the world’s total. Lastly, a third of the world’s potential crop land lies in the region. These factors are all strategic advantages, since the world’s population is projected to grow to 9 billion by 2050, with the resulting nutritional needs.

Despite its assets, the region has been unable to significantly increase its share in world exports of goods and services in the past three decades. Between 1980 and 2010, the share of Latin America and the Caribbean in world merchandise exports rose only marginally, from 5.1% to 5.7%. To a large extent, this flat growth was determined by the slackening of Mexico’s exports, while the rest of the region increased its share. Over the same period, the region’s share in world services exports fell from 4.5% to 3.4% (see figure 5), with an especially weak performance in the “Other commercial services” category—the fastest-growing at the global level in the past decade and the most closely linked to knowledge-intensive activities. In short, against a backdrop of a growing participation by developing economies in world exports, the region’s performance has resembled more of a stagnation.

Figure 5
LATIN AMERICA AND THE CARIBBEAN: SHARE IN WORLD EXPORTS OF GOODS AND SERVICES, 1980-2010
(Percentages)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of World Trade Organization (WTO).
Although there are important differences between the export orientations of each subregion, they share the problems of insufficient value added and inadequate incorporation of knowledge and technology. The South American countries have become increasingly specialized in the export of natural resources, in both primary and processed forms. This pattern has been reinforced by strong demand from Asia, particularly China. The Central American countries and Mexico have specialized in manufacturing industries intensive in assembly activities, and the Caribbean countries in certain services niches. The common denominator among these three patterns is specialization based on static comparative advantages such as abundant unskilled labour and natural resources, and the lack of value added and knowledge embodied in both final products and productive processes.

The emergence of global value chains and the growing importance of innovation in world production and trade make it imperative for the region to take new steps in terms of its international participation. The market opening and trade liberalization processes that have taken place since the 1980s have provided a necessary yet insufficient condition for sustained economic growth through trade expansion. In the current international economic environment the region must go further and make parallel progress on three related fronts: (i) from trade opening and export orientation to strategies for the internationalization of its firms; (ii) from interindustrial participation in international trade to integration into global value chains (or in specific niches of high-technology products or specialized services, especially in the case of small countries); and (iii) from a competitiveness model based on national efforts alone to one in which public-private alliances and regional cooperation are a growing component.

This last point represents a two-pronged challenge. On the one hand, a strategic vision must articulate policies dealing with export promotion and diversification, innovation and technology dissemination, attraction of FDI and skills development. On the other, public-private alliances must be promoted to support both the setting of objectives on a mutually agreed basis and concerted work to accomplish them. This would enable the region to emulate—with the necessary adaptations to different national situations—the experiences of several countries in Europe, Asia and Oceania that have positioned themselves successfully in the world economy.

In the new international setting, the region must take advantage of its growing links with other developing regions and enhance its competitiveness by strengthening regional integration. Here, the concept of open regionalism put forward by ECLAC almost two decades ago is still relevant (ECLAC, 1994). Open regionalism is aimed at developing regional strengths to better meet global challenges. It complements integration into the main world markets with the stimulus provided by intraregional trade and, in so doing, it favours intra-industry trade, export diversification and a stronger presence of SMEs in export flows. The larger scale provided by an integrated regional market would not only boost intraregional trade but would also help to attract FDI and pave the way for the creation and expansion of more trans-Latin firms. Moreover, the regional framework would provide enabling conditions for still incipient regional production chains and would help to spread and leverage innovation processes. Equity in the region would also benefit from greater internationalization of SMEs and the creation of employment in activities that embed more value added and knowledge than those that produce most of the region’s exports to extraregional markets today.

To these traditional arguments in favour of integration is added the fact that in today’s globalized economy competitiveness increasingly incorporates regional elements. Regional or subregional coordination is essential to achieve objectives such as an adequate transport, energy and telecommunications infrastructure, since coordinated action among governments yields better results than isolated national efforts. These objectives are crucial to boosting the countries’ international
competitiveness, particularly given the needs in terms of infrastructure, logistics, customs facilities, and so forth stemming from trade with “mega markets” such as the United States, the European Union and (increasingly) Asia.

**Compared to other regions, intraregional trade in Latin America continues to be limited in relation to its total exports, and is intensive in final goods.** Over the past two decades, intraregional exports have never exceeded 20% of the total exports by Latin America and the Caribbean, a much lower figure than the 46% for East Asia and the Pacific. Intraregional trade in Latin America and the Caribbean has a strong manufacturing component, but continues to be dominated by finished goods. By contrast, the steep rise in Asia’s intraregional trade has been closely linked to the growing geographical fragmentation of production in value chains, and has therefore been characterized by strong growth in trade in parts and components in the sectors of machinery, transport equipment and electronics.

The small proportion of intraregional trade in total Latin American and Caribbean exports is partly a result of the natural-resource-oriented export pattern of many of its economies, but it also has to do with the lack of an integrated economic space. In particular, non-tariff barriers persist which, often being opaque and rather discretionally applied, can dampen trade even more than tariffs. The development of value chains in the region is limited not only by remaining obstacles to trade in goods and limitations on cumulation of origin, but also by the uneven treatment of regulatory issues, such investment, services, competition policy and technical standards. The experiences of East Asia and Central and Eastern Europe seem to bear out the idea that value chains require a certain minimum level of regulatory harmonization among participating countries in order to function.

**Taking better advantage of the considerable potential offered by the regional market will require action on at least six fronts.** First, there is room for greater convergence among the different components of the region’s economic integration architecture. Given the size of the economies concerned, the main missing link to complete the network of preferential trade relationships within the region is between Mexico and MERCOSUR. Within this context, the negotiations on a strategic integration agreement between Brazil and Mexico which were announced in late 2010 could infuse momentum into the entire Latin American economic integration process. Nevertheless, at the time of writing the negotiations had yet to start. Other initiatives are also under way to advance convergence between countries and integration schemes. Progress is being made, for example, in talks between Mexico and the Central American countries on merging the existing three free trade agreements between them into a single accord. Another noteworthy development is the creation, in April 2011, of the Pacific Alliance, which is intended to establish a deep integration area between Chile, Colombia, Mexico and Peru.

**South American countries should re-engage with the economic and trade convergence agenda, as is already happening in Mesoamerica.** A very useful first step would be to allow cumulation of origin among the countries of the region. With the exception of the three economic complementarity agreements between MERCOSUR and the Andean countries, most agreements negotiated in the framework of the Latin American Integration Association (LAIA) do not include cumulation of origin. This reduces the potential for developing regional and subregional value chains and hence for achieving greater productive integration. A second step would be to preserve as much as possible of the tariff and other commitments between the members of the Andean Community and the Bolivarian Republic of Venezuela, with whom Ecuador and the Plurinational State of Bolivia have already concluded bilateral agreements to that effect.
Second, the region needs to invest heavily in trade facilitation, as it lags behind the world leaders in terms of the costs associated with foreign trade. This is partly a result of the region’s large infrastructure deficit, which will take large investments over several years to close (see the next point). Nevertheless, significant efficiency gains can be reaped over shorter time frames and at a lower cost by rationalizing customs and other procedures that affect merchandise trade at national borders. Although such reforms are primarily the domain of individual governments, coordination of national efforts at the regional or subregional level can create useful synergies, as evidenced by subregional cooperation experiences in trade facilitation in Central America.

Third, it is necessary to enhance regional and subregional cooperation to reduce the infrastructure gap in Latin America and the Caribbean. Infrastructure in the region falls short of the average for South-East Asia in all of the countries, and short of the broader world average in most of them, which stymies efforts to improve their integration into the world economy. This lag is exemplified by the region’s ports, most of which underperform in relation to more efficient ports in Asia (see figure 6). ECLAC (2011) has estimated that the region would need to devote an annual investment of around 5.2% of GDP to infrastructure between 2006 and 2020 simply to meet the needs arising from its projected economic growth. Regional and subregional cooperation can create synergies between national efforts in this area. Cross-border development conduits, including bi-oceanic corridors, help to reduce the transport time and costs associated with foreign trade, both within and outside the region. They also contribute to more harmonious territorial development between countries and between regions within countries. The Initiative for Regional Infrastructure Integration in South America (IIRSA) and the Mesoamerica Project are notable examples of such schemes.

**Figure 6**

**LATIN AMERICA AND ASIA: PRODUCTIVITY OF SELECTED PORTS, 2008-2010**

* (Containers per ship hour)

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Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information from the ports.

\(^{a}\) Refers to the average for two terminals (BACTSSA and Exolgan, S.A.).
The region could gain greater benefits from Aid for Trade to overcome its shortcomings in physical infrastructure and trade facilitation. The Latin American and Caribbean region receives a relatively small share (9% in 2009) of total Aid-for-Trade flows. This is partly because most of the countries in the region are classified in the middle-income category. Nevertheless, Latin America and the Caribbean could still secure a larger share of such flows if the countries were to define priorities and identify and present relevant projects that could unlock fresh resources. In this context, priority should be given to attracting grants for projects such as IIRSA and the Mesoamerica Project, which involve several countries and have a clear trade facilitation component.

Fourth, social factors—and their complementarity with the economic and trade agenda—must be afforded greater prominence in regional cooperation efforts. Great inequality both within and between countries is unfortunately a hallmark of Latin American and Caribbean. This is manifested in large disparities in indicators such as per capita GDP and social spending (see table 4). The integration modalities promoted must therefore contribute to reducing these stark asymmetries of development, as a necessary condition for the sustainability and legitimacy of the broader integration process.

<table>
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<th>Table 4</th>
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<td>1995</td>
<td>46</td>
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<tr>
<td>2000</td>
<td>51</td>
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<tr>
<td>2005</td>
<td>103</td>
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<tr>
<td>2008*</td>
<td>104</td>
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Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

a Figures were calculated on the basis of the available information that was closest to 2008 (in some cases it corresponds to 2006 or 2007).

All integration schemes should adopt systems of asymmetric benefits in favour of relatively less developed economies. This principle has long been expounded in the proposals of ECLAC regarding open regionalism. In particular, structural funds aimed primarily at those economies must be strengthened, building on the positive experience of the Structural Convergence Fund (FOCEM) of MERCOSUR and similar initiatives in other subregional schemes. It is also important to make the markets of the larger integration partners more open to exports from the relatively less developed members and to redouble efforts to integrate firms from these countries into subregional value chains.

Fifth, the region must increase regional cooperation on innovation and competitiveness. The Latin American and Caribbean region lags significantly in the area of international competitiveness, as shown consistently in international indices. For example, only two countries in the region (Chile and
Barbados) rank among the top 50 in the Global Competitive Index (GCI), which is compiled annually by the World Economic Forum. The Global Innovation Index (GII) 2011, which is prepared by the French business school INSEAD together with other institutions, including the World Intellectual Property Organization (WIPO), captures data on 125 countries to reflect a broad view of innovation. Of the 20 Latin American countries included in GII, only Chile, Costa Rica and Brazil rank in the top 50 (at positions 30, 45 and 47, respectively).

Given the limited individual capacity of many countries in the region to substantially boost their investment in research and development (R&D), it is imperative to pool national efforts and adopt a concerted approach. This could be accomplished, for example, by integrating national technological centres into multinational research efforts on common topics, thereby creating synergies and a regional critical mass of human and financial resources. At the national level, this approach also requires: (i) greater coordination among the different public agencies working on competitiveness issues; and (ii) the formation of public-private partnerships to share information and define objectives of common interest. These general guidelines can lead to concrete actions such as the creation of a regional cooperation fund for innovation, which would finance programmes or actions defined jointly by the countries in the region.

Sixth, the link with Asia-Pacific could be tapped to deepen regional integration. During 2011, the Chinese authorities have repeatedly expressed a willingness to cooperate in promoting the diversification of Latin American and Caribbean exports to that country. Another key challenge for regional integration is the facilitation of investments from China and the rest of Asia through a single regional window. Such investments, especially if they were made in infrastructure, energy, transport and logistics, would not only help to strengthen trade links with Asia-Pacific, but would also create positive externalities for the region’s internal integration process.

The region should, in the near term, prepare a document setting forth lines of action for forming closer strategic ties with China. China took the first step in this direction in November 2008, when it issued a policy paper on Latin America and the Caribbean. The coordination needed to prepare a response to China’s document could pave the way for the holding of a first Summit of Heads of State of China and Latin America and the Caribbean in the coming years. A meeting of this sort would provide the opportunity to agree upon a shared agenda of trade and investment projects. The recently created Community of Latin American and Caribbean States (CELAC) could build this issue into its agenda of work.

Bibliography