Growth and Stability in Latin America and Asia

"PT (Sir Purushothamdas Thakurdas) Memorial Lecture"

Indian Institute of Banking & Finance

Mumbai, India

Guillermo Ortiz

November 10, 2006

Index

1. Introduction

It is an honor to be here today at the Indian Institute of Banking & Finance in this year PT (Sir Purushothamdas Thakurdas) Memorial Lecture. Sir PT had an active interest in the economic life of India and was a firm believer in the logic and philosophy of free enterprise and the market mechanism to achieve an efficient allocation of resources, but he also understood the role that the State must play to foster growth and development. This is precisely one of the main challenges currently faced by Asia and Latin America.

As we all are aware of, in the last decades the global economy has changed significantly. In particular, technological advances and trade liberalization have played key roles in facilitating global integration, which has produced considerable efficiency gains and benefits for the world economy.

During the period from 2004 to 2006, the world economy will have achieved the highest growth rates since the 1970s, with many regions of the world growing at vigorous rates, most noticeably China and India. For example, India has been experiencing, for more than two decades, extraordinary high growth rates. For 2006, the Indian economy is expected to grow more than 8.0 percent. This is reflecting that India is, without doubt, one of the most dynamic economies in the global scene. In addition, since 2001, export growth in India has averaged more than 22 percent a year and its share of world exports has nearly doubled in the past fifteen years. As a whole, Asia has consistently exhibited the highest world growth rates during the last decades.

This clearly illustrates that in the last years there have been important changes in the geographical locus of global economic activity. In particular, the role of emerging economies in global output and trade has increased significantly. Moreover, these economies are likely to play a more important role in the world economy in the next years.

To illustrate this, Goldman Sachs has analyzed and forecasted the performance of large emerging market economies. In particular, the so-called BRICs (Brazil, Russia, India and China), together with Mexico and Korea, as economies that have the potential to become important in a global scale (Mexico and Korea were originally excluded from the BRICs because they were considered to be already more developed). According to Goldman Sachs projections, by the year 2050, China, India, Brazil and Mexico will be the first, third, fourth and sixth largest economies in US dollar terms, respectively. These projections must be considered with some reserve, since they assume that various elements of policy are put in place in order to promote rapid growth and to converge to developed country income levels.

Among the most important conditions for growth considered in the aforementioned projections are: i) macroeconomic stability (inflation, government deficit, external debt); ii) macroeconomic conditions (investment rates, openness of the economy); iii) technological capabilities (penetration of PCs; phones; internet); iv) human capital (education; life expectancy); and, v) political conditions (political stability; rule of law; corruption).

These issues illustrate that the considerable increase in economic integration and globalization is creating a unique opportunity for emerging economies, as some of them, are already experiencing high growth rates and a significant improvement in the living standards of their population. It is important to emphasize that higher growth contributes significantly to reduce poverty. This takes place in two ways: i) by raising household's income, and ii) by increasing the resources available for poverty-reduction policies. These factors enhance the population's productive capacities and foster growth, creating a "virtuous circle" between economic growth and poverty reduction. This is an area where India has made significant progress in the last years (according to the World Bank, the national poverty headcount ratio that was 36 percent in 1994 was reduced to 29 percent in 2000).

The economic performance of emerging economies varies considerably. In particular, Latin America has lagged with respect to the growth rates observed in Asia. In this regard, one of the key ingredients that help explain the insufficient economic growth observed in Latin America in the last four decades is mainly associated with the severity and frequent financial crises that have afflicted the region. This clearly highlights that one of the most important elements to achieve strong economic growth is macroeconomic and financial stability. In this regard, I will present some of the benefits the Mexican economy has attained by avoiding crisis episodes for more than a decade and by maintaining low inflation.

Nonetheless, this is not enough. There are other elements of utmost importance that are needed to foster strong economic growth. This would be addressed in the final part of my intervention, where I stress the importance of making our economies more flexible and providing an adequate set of incentives. Therefore, emerging economies need to articulate a comprehensive set of policies to create the conditions that can spur economic growth and poverty reduction. Advancing in this agenda will allow our countries to fully profit from globalization and exploit our economies' potential.

2. Growth Performance

Let me now turn to a brief evaluation of the economic performance of Mexico and Latin America. During the last four decades, the region, and Mexico in particular, has exhibited a weak economic performance. While during the 60s and 70s Mexico's per capita GDP figures were similar to those of Chile and Spain, and larger than those of Singapore and Korea, in 2005, Mexico's per capita GDP was significantly lower than the figures for these countries. An interesting comparison arises when considering China. In 1960, Mexico's per capita GDP was almost six times more than that of China; by 2005 that large gap has been reduced considerably, to less than double.

PPP Adjusted Per Capita GDP
(1996 dollars)

	1960	1970	1980	1990	2000	2005	Annual Growth Rate 1960-2005
Ireland	5,207.7	7,275.4	9,978.4	14,133.5	26,379.0	30,803.8	4.0
Singapore	**2,280.3**	**5,318.9**	**11,460.3**	**17,953.5**	**27,905.3**	**29,080.7**	**5.8**
Spain	4,692.8	9,034.3	11,519.8	14,469.2	18,054.6	20,112.1	3.3
Korea, Rep.	**1,570.9**	**2,776.9**	**4,829.5**	**9,958.6**	**15,881.3**	**18,969.1**	**5.7**
Chile	3,818.2	4,805.5	5,418.3	6,151.5	9,920.0	11,314.7	2.4
Mexico	**3,969.8**	**5,513.1**	**7,602.6**	**7,341.8**	**8,766.1**	**8,826.0**	**1.8**
China	684.6	820.1	1,071.9	1,789.8	3,747.0	5,634.4	4.8

Source: Penn World Tables 6.1 and International Monetary Fund.

Mexico's poor economic growth performance during the 1960-2005 period reflects, to a great extent, the impact of the so-called "80s lost decade". Despite a slight rebound of the economy during the 1990s, economic growth in this period has been significantly lower than that achieved from 1960 to 1977, and lower than that attained by other emerging economies.

To broadly illustrate how costly the periods of low economic growth and crises were, some exercises were performed. Specifically, actual per capita GDP in Mexico is compared to the levels that would have been obtained had our economy maintained growth rates similar to those observed prior to the start of the debt overhang process of the late 70s and to the crises derived from an inadequate macroeconomic management.

The first scenario assumes that from 1978, per capita GDP grows at the rate observed on average during the period 1960-1977 (3.02 percent). This result suggests that per capita GDP in 2005 could have been 70 percent more than the current value. In a second scenario, from 1978 to 1985, the per capita GDP is assumed to grow at the rate observed on average during the period 1960-1977 (3.02 percent); and from 1986, at an annual rate of 4.11 percent, which is the average growth rate for the period 1985-2005 in Chile. The result reveals that per capita GDP could have been more than twice the observed figure.

Per Capita GDP in Mexico and Alternative Scenarios
(1996 dollars PPP adjusted)

	1960	2005	Annual Growth Rate 1960-2005
Observed	**3,970**	**8,826**	**1.8**
Scenario 1	**3,970**	**15,156**	**3.0**
Scenario 2	**3,970**	**18,889**	**3.5**

Latin America has performed poorly in terms of economic growth, not only compared with East Asian economies, but with the more recently developed countries of the European Union (European Four) as well.[1] For example, during the period from 1960 to 2005, East Asia's per capita GDP increased on average 5.4 percent per year, while the European Four countries achieved 3.4 percent growth per year; in contrast, during the same period, Latin America's growth rate was only 1.3 percent per year.

PPP Adjusted Per Capita GDP
(1996 Dollars PPP Adjusted; Weighted Regional Average)

	1960	1970	1980	1990	2000	2005	Annual Growth Rate (1960-2005)
Latin America	4,444	5,723	6,970	6,303	7,737	7,921	1.3
European Four	4,476	8,499	11,154	13,785	18,025	20,259	3.4
East Asia	1,670	3,037	5,720	10,106	15,552	17,442	5.4

Source: Penn World Tables 6.1. IMF's IFS from 2000 onwards.

Had Latin America continued to experience growth rates of per capita GDP similar to the average experienced from 1960 to 1977 (2.06 percent), prior to the macroeconomic crisis experienced during the 80s, per capita GDP would have been 11,111 dollars of 1996 (PPP adjusted), instead of 7,921 dollars.

PPP Adjusted Per Capita GDP
(1996 Dollars PPP Adjusted; Weighted Regional Average)

	1960	1970	1980	1990	2000	2005	Annual Growth Rate (1960-2005)
Latin America	4,444	5,723	6,970	6,303	7,737	7,921	1.3
Latin America Scenario	4,444	5,723	6,678	8,186	10,035	11,111	2.1
European Four	4,476	8,499	11,154	13,785	18,025	20,259	3.4
East Asia	1,670	3,037	5,720	10,106	15,552	17,442	5.4

Source: Penn World Tables 6.1. IMF's IFS from 2000 onwards.

It is clear that part of the explanation for the disappointing growth rates, not only in Mexico, but in most of the Latin American region, has been the incidence of economic crises. On this matter, even though some Asian economies have also experienced crises, it is important to remember that, in Latin America, economic crises have been more severe and distressing.

3. Macroeconomic Stability

One of the most important goals of economic policy in Latin America since the 80s has been to achieve and maintain macroeconomic stability. In this front, significant progress has been attained. For the first time since the 60s, Latin America will have several years with less than one digit inflation. This has been the result of a benign global outlook and a clear conviction about the merits of macroeconomic stability as a necessary condition to improve the living standards of society and as a requirement for economic development.

[1] This exercise considers the following classification: Latin America.- Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Jamaica, Mexico, Nicaragua, Peru, Panama, Paraguay, Uruguay, and Venezuela. Eastern Asia.- Korea, Hong Kong, Malaysia, Singapore, Thailand, and Taiwan. European Four.- Greece, Ireland, Portugal, and Spain.

In the last decades, the world has enjoyed a significant reduction of inflation and inflation persistence. Several factors have contributed to the abatement of inflation and to more stable inflation dynamics throughout the world.[2] To mention a few, for example:

- Competition of goods and services in global markets has increased as a result of higher international trade flows.
- Labor supply has also increased worldwide, due mainly to the growing presence of countries like China and India in international markets.
- Significant technological progress in recent years has fostered productivity growth.
- Noticeable improvements in macroeconomic management, particularly, in monetary policy.

Consumer Price Index
(Annual % Change)

	70's	80's	90's	2000-2005	2004	2005
Global	10.9	15.6	15.1	3.7	3.4	3.6
Industrial countries	8.7	6.2	2.8	2.0	2.0	2.3
Developing countries	16.2	36.7	36.0	5.8	5.1	5.1

Source: IMF, International Financial Statistics Database.

In addition to a benign global outlook for inflation, lately, the majority of the economies in both regions, Latin America and Asia, have made significant progress in terms of macroeconomic management. In particular, the following strategic indicators have undergone significant progress: i) fiscal discipline; ii) the abatement of inflation; iii) the reduction of the current account deficit; and, iv) a greater openness to trade.

Fiscal restrain and inflation control have helped to reduce vulnerabilities in both economic regions. The importance of sound fiscal policies cannot be overemphasized, since, among other benefits, it enables monetary policy to abate inflation. In this regard I would highlight that in the last years both India and Mexico have enacted fiscal responsibility laws and have taken important steps to improve their fiscal accounts.

General Government Financial Balance
(% of GDP)

		2000	2001	2002	2003	2004	2005	2006*
Latin America		**-2.6**	**-3.0**	**-3.2**	**-3.3**	**-1.6**	**-1.2**	**-1.2**
	Mexico	-1.3	-0.7	-0.8	-1.1	-1.0	-0.8	-0.3
	Chile	-0.7	-0.5	-1.2	-0.4	2.1	4.6	3.5
Asia		**-3.9**	**-3.9**	**-3.8**	**-3.5**	**-2.8**	**-2.6**	**-2.5**
	India	-9.6	-10.1	-9.7	-9.1	-8.5	-8.1	-7.7
	China	-2.4	-2.3	-2.6	-2.2	-1.3	-1.1	-1.1

*/ Forecast.
Source: Moody's Statistical Handbook; May 2006. IMF.

[2] Cecchetti, Stephen, and Guy Debelle (2004) "Has the Inflation Process Changed?" Working Paper, Bank for International Settlements. Rogoff, Kenneth (2003) "Globalization and Global Disinflation" in Federal Reserve Bank of Kansas City, Monetary Policy and Uncertainty: Adapting to a Changing Economy.

Inflation

(Average Annual Inflation)

	60s	70s	80s	90s	2000-2005	2004	2005	2006*
Latin America	**11.0**	**48.5**	**245.3**	**427.8**	**7.7**	**6.0**	**6.3**	**5.5**
Mexico	2.5	14.7	69.1	20.4	7.4	4.7	4.0	3.5
Chile	26.6	174.6	21.4	11.7	2.8	1.1	3.1	3.5
Asia	**34.2**	**10.6**	**11.7**	**10.2**	**2.6**	**3.8**	**3.0**	**3.3**
India	6.4	7.5	9.1	9.5	4.0	3.9	4.0	5.6
China	…	…	7.5	7.8	1.2	3.9	1.8	1.5

*/ Forecast.

Source: World Bank and WEO, September 2006.

To better understand the progress achieved in terms of macroeconomic management, it is important to consider some of the challenges that Asia and Latin America faced after the 90s crises. In particular, many Latin American economies migrated to an inflation targeting framework with a freely floating exchange rate regime. In contrast, several Asian economies adopted a mixture of exchange rate regimes and diverse monetary policy frameworks with an important group using the exchange rate as a nominal anchor. It is not easy to identify with precision what factors explained the differences in monetary policy arrangements; nonetheless, a brief revision of the prevalent economic conditions at that time may be helpful to understand some of the monetary and exchange rate choices in both regions. Among the most relevant are: i) the characteristics and severity of their crises; ii) the relative size of the external sector; iii) the trade patterns; iv) the region's inflationary history; and, v) financial markets development.

Let me highlight that during the last years prudent fiscal and monetary policies in Latin America have contributed significantly to macroeconomic stability. The inflation targeting framework, along with a freely floating exchange rate, seems to be benefiting the Latin American economies that have adopted them at least in two aspects: by anchoring inflation expectations and by reducing inflation persistence.

In the case of Mexico, after decades of high and volatile inflation, headline inflation has been at one digit levels for the last six years, and, in 2006, inflation has been around the 3 percent target. These results reflect that Mexico's inflation targeting framework has been effective in strengthening the role of monetary policy as the nominal anchor of the economy.

The adoption of a floating exchange rate regime and the attainment of low and stable inflation have fostered a better performance of the Mexican economy. Among the benefits of stabilization are: i) building credibility on monetary policy, in particular by reducing the exchange rate pass-through; ii) reducing the vulnerability of the economy by the re-composition of capital flows; iii) achieving stable paths for key economic variables; and, iv) developing domestic financial markets.

As credibility on monetary policy has increased and firms perceive that exchange rate fluctuations are not persistent and, unlike in the past, they do not tend to lead to higher inflation, the process of price determination is now based more on inflation expectations than on observed exchange rate fluctuations. Moreover, as the nominal exchange rate has become an adjustment variable when facing several shocks, inflation persistence has diminished. Currently, an increase in the exchange rate causes a lower revision in inflation expectations, as compared with the past. That is, nowadays, a depreciation of the exchange rate is perceived more as an adjustment in relative prices than as a source of inflationary pressures. In consequence, it does not lead to a generalized process of price revision as significant as in the past.

All of the above have rendered significant benefits for all economic agents; in particular:

1. The Federal Government has been able to manage public debt in a predictable and sustainable manner. This has been reflected in an extension of the average maturity and duration of government domestic securities. In this regard, a few weeks ago the Federal Government issued for the first time a 30-year bond in pesos.
2. Up to a few years ago, the private sector relied on external markets to obtain long-term financing. Currently, such financing can also be obtained in the domestic market in pesos.
3. Greater credit availability, which has allowed households to reach broader and more stable consumption patterns (total consumer credit increased from 1.8 percent of GDP in 2000 to 4.8 percent at the end of 2005).
4. Credit bureaus have information of more than 38 million individuals with over 77 million credits in their database.
5. Higher share of sales via automobile financing (while in 2000 the share of sales via automobile financing was 30 percent, in 2005 it reached 60 percent).
6. Higher number of families with access to mortgage lending (from 1998 to 2005, 3.2 million mortgage loans were granted).

The aforementioned illustrates how macroeconomic stability has conveyed significant benefits for all economic agents (the Federal Government, firms and households). It has also contributed to reduce the economy's vulnerability. As a result, Mexico is in a much better position, as compared with previous episodes, to face adverse shocks.

As the abovementioned benefits extend and consolidate within Mexico's population, Mexicans commitment to secure an environment of macroeconomic stability will be strengthened. Nonetheless, stability is a necessary but not the only condition to attain sustained growth. Progress towards a greater stability of the Mexican economy has had a significant impact on aggregate demand, allowing consumption and investment to expand and become more stable throughout the years. However, the current challenge is to implement structural changes destined to increase the flexibility of the economy's productive structure and, hence, to raise its potential growth. This leads me to the next topic I would like to address: the key drivers of competitiveness, and how Latin America compares to other regions in this regard, particularly Asia.

4. Competitiveness

Certainly, macroeconomic stability and the recent favorable global conditions have benefited most of the Latin American countries. However, the region still has to undertake diverse structural reforms to improve its competitiveness and, therefore, achieve higher growth rates as those experienced by several Asian economies.

4.1. Growth and competitiveness

Undeniably, competitiveness is a rather complex concept, difficult to define with precision. Nonetheless, competitiveness seems to be related with the economic conditions that determine productivity growth in those sectors where an economy has comparative advantages. Therefore, it is clearly related with two factors: i) an economy's ability to fully exploit its comparative advantages, by efficiently allocating its resources; and, ii) the country's capacity to increase its productivity growth, in those economic activities in which a comparative advantage prevails.

It is important to highlight that the concept of comparative advantage is not static. If a country engages in brisk innovation and technological change in one sector it is likely to develop a comparative advantage. A good example of this is India's vigorous development in the Information Technology industry (IT). India has been able to exploit its comparative advantage on technically adept English-speaking talent in an era of broadband communications and globalization. In this case, the combination of adequate public policies and private investments have allowed "business process outsourcing" in India (IT outsourcing) to generate revenues of nearly 5 percent of GDP and gain a dominant position in an industry that still has significant untapped potential.

A country can be more competitive if, for example, it assigns resources efficiently in terms of its comparative advantages; it invests in human, physical and technological capital; and, if it maintains a framework that fosters innovation and the adoption of new technologies. Also, comparative advantages and efficiency gains are better attained when the economy is more open to trade. In this regard, Asian economies have increased significantly their intra-regional interdependence. As an example, consider that 40 percent of East Asian exports are channeled to China and other East Asian economies, while only 12.9 percent of Latin American exports are directed to the region.

On a more structural basis, a fundamental element to boost competitiveness and development depends on the incentives structure faced by society. In relation to the incentives linked to economic activity, competitiveness seems to rely on the following: i) markets that operate under competitive conditions; ii) flexibility in the allocation of resources; and, iii) an institutional framework that leads to the alignment of economic agent's incentives with those activities that yield higher social returns.

Actually, there is a close relationship between competitiveness and economic competition. In fact, empirical evidence from research studies done by Banco de Mexico suggests that, in those sectors with a higher market concentration, which implies less competition, lower productivity growth is observed. This finding is consistent with similar studies done for other developed countries. Considering the aforementioned, and taking into account the international experience, the component that emerges as a main driver of productivity growth is the incentive structure or, in other words, the "rules of the game" that can make markets operate properly and transparently.

4.2. Fostering Competitiveness

We can think of three kinds of basic determinants, which, as discussed above, play an important role in encouraging competitiveness, and thus, economic growth:

i. **Immediate**: savings and investment rates.
ii. **Structural**: infrastructure in networks and human capital.
iii. **Institutional**: a framework that aligns economic agent's incentives with activities that yield higher social returns.

Next, I will briefly comment on how these aspects have evolved in our regions.

4.2.1. Savings and Investment

Latin America saves and invests substantially less than Asia and the European Four. By 1960, Asia had saved and invested lower proportions of its GDP than Latin America. However, in the following 40 years, Latin America diminished substantially its saving efforts. In contrast, as a consequence of important domestic savings efforts, Asian countries increased their investment rates significantly. Most of these efforts are related to forced saving schemes; an example are the so-called "provident funds" of Singapore and other countries.[3] However, savings and investment may be endogenously determined, along with growth, as a function of deeper determinants, which will be addressed in the following section.

[3] The Central Provident Fund (CPF) is a comprehensive social security savings plan. Employers make monthly contributions to the CPF which are channeled into three accounts: i) Ordinary Account - the savings can be used to buy a home, pay for CPF insurance, investment and education; ii) Special Account - for old age, contingency purposes and investment in retirement-related financial products; and, iii) Medisave Account - the savings can be used for hospitalization expenses and approved medical insurance. Source: Central Provident Fund Board, Singapore Government.

Domestic Savings
(% of GDP)

	60s	70s	80s	90s	2000-2004
Latin America	**20.9**	**22.7**	**23.2**	**19.9**	**20.9**
Chile	17.4	16.8	19.0	25.9	25.6
Mexico	16.8	21.3	25.7	21.3	19.7
Asia	**19.3**	**25.2**	**29.0**	**34.0**	**33.7**
China	24.1	30.5	34.7	39.5	38.1
India	14.0	17.3	20.0	22.3	24.7

Gross Fixed Capital Formation
(% of GDP)

	60s	70s	80s	90s	2000-2004
Latin America	**18.4**	**21.8**	**20.3**	**19.6**	**18.9**
Chile	17.5	17.7	17.2	24.3	21.0
Mexico	17.4	20.3	20.2	19.0	19.8
Asia	**15.0**	**23.2**	**26.1**	**30.9**	**29.7**
China	…	27.0	28.9	32.0	35.5
India	14.0	15.8	20.2	22.4	24.1

Source: Penn World Tables 6.1 and International Monetary Fund.

4.2.2. Infrastructure and Human Capital

a) Infrastructure

The structural reforms in Latin America have been insufficient to restore many of the relative deficiencies that this region exhibits with respect to other faster growing regions. For example, Latin America has important lags in the creation of basic infrastructure, as compared with Asia. Moreover, during the last four decades, most of Asia's investment expenditures' composition was directed to projects with very high social returns, allowing important increases in the stock of basic infrastructure. For instance: i) paved roads; ii) electric generation capacity; iii) telephone lines; iv) railroads; and, v) drinking water facilities.

The creation of Asian infrastructure was partly the result of explicit policies. In contrast, Latin America is still behind in terms of the basic infrastructure needed to fully reap the benefits from trade and to attract higher levels of foreign direct investment. In the latest global competitiveness report, this becomes more evident as Latin America presents lower rankings in all infrastructure indicators (port, railroad, air, and overall infrastructure). As for overall infrastructure quality, Latin America has a grade of 2.8 (7 being the maximum grade), while Asia ranks higher with a grade of 3.5. In this regard, India ranks 2.9, slightly above the Latin American average, while Mexico ranks 3.5.

General Infrastructure Quality				
	Overall*	Port	Railroad	Air
Asia	**3.5**	**3.8**	**3.9**	**4.4**
China	3.2	3.6	3.6	4.0
India	2.9	3.1	4.2	4.5
Latin America	**2.8**	**2.6**	**1.8**	**3.9**
Mexico	*3.5*	*3.3*	*2.2*	*4.9*

Source: The Global Competitiveness Report 2005-2006, WEF.
Note: For Asia and Latin America, a weighted average is considered.
Index based on a survey: General infrastructure in your country is 1= poorly developed and inefficient, 7= among the best in the world.

A distinctive and standard guide for infrastructure development is paved road statistics. In this respect, Asia is better off, since the percent of paved roads in the region has increased from 61.5 during the 90s to 73.1 during the 2000-2003 period. A similar scenario is observed for India. In contrast, Latin America has deteriorated rather than improved: the percentage of paved roads has decreased from 20.1 to 16.5 during the 90s and the period 2000-2003, respectively.[4]

Paved Roads (% Total)		
	1990-1999	2000-2003
Asia	**61.5**	**73.1**
Korea	76.3	76.7
China	-	78.9
India	54.4	63.0
Latin America	**20.1**	**16.5**
Mexico	33.1	33.5

Source: World Development Indicators, World Bank

As for electricity production, things are not quite different for Latin America. Asia has reverted significantly the pattern that prevailed from the 70s to the 90s. During the 2000-2003 period, electricity production in Asia grew at an average annual rate of 14.4 percent, while in Latin America it did so by 1.8 percent. During the 70s, the scenario was quite the opposite, with Latin America recording an average growth rate of electricity production equal to 11.6 percent, while Asia's electricity production grew by 0.2 percent, on average. In line with the observed trends in the region, India increased its average rate, from 0.7 percent during the 70s to 4.1 percent during the 2000-2003 period. This is a key indicator of the dynamism of economic activity.

Electricity Production (kWh) Average Annual Growth				
	1970-1979	1980-1989	1990-1999	2000-2003
Asia	**0.2%**	**0.6%**	**1.7%**	**14.4%**
China	1.2%	0.1%	0.4%	12.1%
India	0.7%	1.6%	1.2%	4.1%
Latin America	**11.6%**	**5.8%**	**4.3%**	**1.8%**
Mexico	9.1%	6.5%	5.1%	2.3%

Source: World Development Indicators, World Bank.

[4]An appalling fact is that in 1960 Korea had less than half of paved road density than Mexico. Currently, Korea has five times more. Source: World Bank.

Regarding fixed line and mobile phone subscribers, Asia has exhibited higher growth rates than Latin America. During the period 1975-2004, the number of subscribers in Asia grew at an average annual rate of 14.8 percent, while in Latin America this indicator did so by 10.3 percent.[5] Despite the better performance of Asia, Latin America still has a higher density of subscribers.

Fixed line and mobile phone subscribers (per 1,000 people)

	1975-1979	80s	90s	2000-2004	Average Annual Growth 1975-2004
Asia	**11.2**	**26.0**	**90.9**	**331.8**	**14.8**
China	2.0	3.1	42.9	335.8	21.3
India	2.7	4.1	14.0	55.8	13.1
Latin America	**35.7**	**52.9**	**117.3**	**402.8**	**10.3**
Mexico	33.3	48.6	107.2	410.2	10.9

Source: World Development Indicators, World Bank.

Access to improved water has grown at higher rates in Asia than in Latin America. During the period 1990-2004, the percent of population with improved water sources increased at an average annual rate of 1.8 percent, while in Latin America it did so by 1.3 percent. However, it must be noted that Latin America has a slightly higher penetration of improved water sources than Asia, with 79.3 percent of its population having access in 2004. Asia's penetration was 74 percent during that year.

Improved Water Sources
(% of population with access)

	1990	2004	Average Annual Rate 1990-2004
Asia	**58.2**	**74**	**1.8**
China	70	77	0.7
India	70	86	1.5
Latin America	**66.5**	**79.3**	**1.3**
Mexico	82	97	1.2

Source: World Development Indicators, World Bank.

Summing up, Asia and Latin America's infrastructure development is still insufficient; however, in general, Asia has been advancing in this front at a faster pace than Latin America.

b) Human Capital

Many theoretical growth models and empirical evidence have shown that the accumulation of human capital is a crucial factor to promote sustained growth

[5] Mexico compares unfavorably in relation to China and India, as it has grown at an average rate of 10 percent, compared to 21.3 percent and 13.1 percent of China and India, respectively. Source: World Bank.

and to allow countries to move up in the value chain. The economic success of both regions in the future clearly rests on the progress attained in this front.

Regarding average schooling among the population over 25 years old, Latin America went from 3.4 years in 1960 to 6.1 years in 2000, while Asia went from 1.8 to 6.0 years in the same period. This illustrates that efforts to improve education have been stronger in Asia than in Latin America. Within both regions, there are clear examples of countries that have been very successful in this front: in particular, in 2000, the average schooling in East Asia was 8.2 years, while in Chile it was 7.9 years.

Regarding higher education, the percent of population over 25 years of age that has completed a higher education degree shows modest increases in both regions. In Latin America, it went from 1.3 percent in 1960 to 7.9 percent in 2000, while for Asia figures went from 0.7 percent to 4.5 percent in the same period. Again, East Asia and Chile had a significant progress in this front, reaching 13.2 percent and 10.7 percent in 2000, respectively.

Average Schooling
(Population over 25 years)

	1960	1965	1970	1980	1990	2000
Latin America	**3.4**	**3.4**	**3.8**	**4.2**	**5.1**	**6.1**
Mexico	2.4	2.5	3.3	4.0	5.9	6.7
Chile	5.0	4.8	5.5	6.0	7.1	7.9
Asia	**1.8**	**2.1**	**2.6**	**3.8**	**5.1**	**6.0**
Asia Excl. China & India	**2.5**	**3.1**	**3.8**	**5.0**	**6.3**	**7.8**
East Asia	**3.3**	**-**	**4.1**	**5.2**	**7.0**	**8.2**
India	1.5	1.5	1.9	2.7	3.7	4.8
China	n.d.	n.d.	n.d.	3.6	5.2	5.7

Source: Barro-Lee, 2000.

Highest Schooling Degree: Complete Higher Education
(% of population over 25 years)

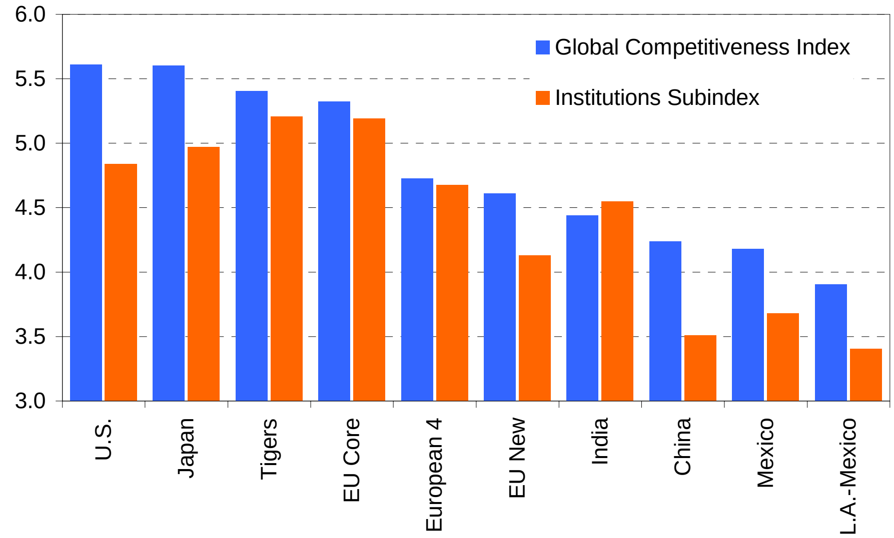
	1960	1965	1970	1980	1990	2000
Latin America	**1.3**	**1.6**	**1.8**	**3.7**	**5.9**	**7.9**
Mexico	0.8	1.0	1.5	3.2	5.4	6.6
Chile	1.4	1.7	2.6	4.9	8.4	10.7
Asia	**0.7**	**0.9**	**1.3**	**2.1**	**3.2**	**4.5**
Asia Excl. China & India	**1.6**	**2.2**	**2.8**	**4.2**	**5.8**	**10.2**
East Asia	**1.3**	**-**	**2.4**	**4.1**	**7.7**	**13.2**
India	0.0	0.1	0.8	1.7	2.9	3.3
China	0.9	0.9	0.8	0.9	1.7	2.3

Source: Barro-Lee, 2000.

4.2.3. Institutional Framework

According to The World Economic Forum Index, the quality of institutions in Latin America performs poorly compared to other regions. This a result of poorly defined property rights, inefficient government operations, unstable business environments, perceived favoritism in government decision making, insufficiently independent judiciary and security costs associated with high levels of crime and corruption, which makes it difficult to compete effectively. India's performance is considerably better according to this Index.

Global Competitiveness Index and Institutions Subindex; WEF 2006
(Average Score)



Moreover, Asian countries have experienced a much more important improvement in their Human Development Index than their Latin American counterparts.[6] The index increased 39 percent from 1975 to 2003 in Asia, while it grew only 15.8 percent in Latin America during the same period. It is noticeable the performance of India in this front, with an increase of 46.1 percent. These results can be interpreted as a reflection that macroeconomic stability and sustained economic growth are echoed in improving society's welfare.

Human Development Index
Growth Rate 1975-2003

Asia		**39.3%**
	China	43.8%
	India	46.1%
Latin America		**15.8%**
	Mexico	18.1%

Source: Human Development Report 2005.

Last, Asia scores higher than Latin America in the Growth Competitiveness Index: during the period 2005-2006, Asia ranked 41 (score of 4.42) while Latin America ranked 62 (score of 3.81). Despite the differences between India and Mexico, both countries have a similar score.

[6] The Human Development Index (HDI) is a composite index that measures average achievement in three basic dimensions of human development—a long and healthy life, knowledge, and a decent standard of living. Source: UNDP.

Growth Competitiveness Index 2005-2006

	Rank	Score
Asia	**41**	**4.42**
China	49	4.07
India	50	4.04
Latin America	**62**	**3.81**
Mexico	55	3.92

Source: The Global Competitiveness Report 2005-2006, WEF.
Index from 1 to 7, where 7 is more competitive and 1 is less competitive.

Summing up, it is clear that both Asia and Latin America still have a long way to improve some of the factors that determine their competitiveness. Nonetheless, in recent years, Asia has advanced more significantly than Latin America. Therefore, our region has to move forward in the adoption of policies and reforms needed to improve the economic performance of our economies.

5. Final Remarks

In the last years, the global economy has undergone a significant expansion, with low inflation rates, benign financial conditions, and a considerable increase in international trade. This environment has entailed both benefits and challenges for our regions.

In particular, the growing participation of several Asian economies in international markets as a supplier, with comparative advantage in labor intensive manufacturing processes, has led to a relative reduction in manufacturing goods' prices and to an increase in the prices of different commodities (energy, metals, food, etc.). Such circumstances entail a major challenge for manufacturing activities, especially for manufacturing export economies like Mexico. Also, the significant increase in commodity prices has benefited the Latin American region and has contributed to a significant improvement of its external accounts. As a result, Latin American economies have reduced their vulnerabilities to external shocks.

Nonetheless, Latin America and its society have not been able to fully benefit from the present external conditions albeit the sound and successful macroeconomic policies that now exist in most of the countries. Several aspects are still hampering economic performance, mainly due to the existence of inadequate regulatory frameworks and a biased incentives mechanism, which prevail due to the lack of structural reforms aimed at enhancing the competitiveness of the economies in the region.

In order to revert this situation and to learn from the flourishing experiences that you, our Asian counterparts had, Latin America needs to address some of the factors that are hindering its economic performance. This means to:

1. Attain a pro-competitive orientation of the economy, which includes openness to international goods and capital flows.
2. Implement public policies oriented towards correcting market failures and promoting investment in socially productive activities.

3. Foster a flexible allocation of resources.
4. Develop an institutional framework with incentives towards innovation and efficient production, which will clearly lead to better conditions for growth than a framework that promotes rent-seeking activities and non-competitive market structures.

Apart from several Asian countries, a clear-cut example within the Latin American region that reflects the potential benefits that can be obtained if a meaningful and committed reform agenda is undertaken is Chile. This country achieved high growth rates since the 80s, predominantly, as a consequence of the deep structural reforms it carried out and the considerable improvements in its institutional and incentives frameworks.

I am convinced that with the right set of policies, emerging economies, both in Asia and Latin America, will have a unique opportunity to reach and maintain high growth rates. This will be the most effective way to reduce poverty and raise the living standards of our populations.