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IMF Sees Continued Strong Outlook for Western Hemisphere, Growth Remaining Relatively High for Latin America

The past year has been another one of strong economic performance for the Western Hemisphere, notwithstanding somewhat slower growth in the United States in recent quarters, according to the IMF's most recent Regional Economic Outlook: Western Hemisphere. Latin America and the Caribbean grew vigorously in 2006 and, although some easing is expected, this region should continue growing at a relatively high rate in 2007, said Mr. Anoop Singh, Director of the IMF's Western Hemisphere Department, at a press conference presenting the report. "The 2004–06 period is now on record as the most vigorous period of growth for the region in Latin America and the Caribbean since the 1970s, reflecting both stronger policies and the favorable external environment," Mr. Singh said. Poverty indicators have also improved further, he added, although more efforts are needed, as governments everywhere recognize.

Mr. Singh said the main challenges for the region remain raising and sustaining long-term growth, and sharing the benefits more equitably. "To substantially raise living standards over the next two decades, Latin America must grow faster on a sustainable basis," he said. At the same time, policies needed to remain vigilant to ensure that the safety margins built up in recent years—particularly in the fiscal area—do not erode.

The Regional Economic Outlook 's main findings for Latin America and the Caribbean are as follows:

2006 was a year of strong economic performance for Latin America and the Caribbean (LAC). Output grew at an average rate of 5½ percent, almost one percentage point higher than in 2005, and slightly above world growth. With many countries experiencing the strongest growth in several years—about one third of them grew at around 7 percent or higher—unemployment and poverty rates have continued to fall. Inequality has also declined, according to the latest available data, the first such fall in several decades.

Other macroeconomic developments have also been favorable. Inflation continued on a downward path, falling to a regional average of 5 percent, although significant differences remain between countries. For the region as a whole and in many individual countries, primary fiscal balances and external current accounts were at record highs, with average surpluses of 2.8 and 1.7 of GDP, respectively. Public debt ratios have fallen somewhat further, and debt structures have also improved. Many of these improvements were shared by countries experiencing critical political transitions, reflecting the new economic stability of the region. A supportive external environment helped, with low interest rates, high commodity prices, and strong world growth.

Looking forward, average growth in the region is expected to decline moderately, to just under 5 percent in 2007 and about 4¼ percent in 2008. This reflects the lower pace of expansion in some countries that grew at historically high rates in 2006, and less buoyant external conditions. At the same time, inflation may edge up, particularly in countries with high capacity utilization, although it is likely to remain contained for the region as a whole. Reflecting strong domestic demand and continued rapid increases in government spending, external and fiscal surpluses are expected to decline, to roughly half their 2006 levels in terms of GDP. This underlines the need to rein in the growth of government outlays, especially current spending.

The report also takes a close look at the sensitivity of Latin American growth to the external environment, which has been exceptionally benign in recent years. Though much improved balance sheets and policy frameworks have made Latin America more resilient than a decade ago, the region remains sensitive to shocks to world growth, commodity prices, and financing conditions. New analysis shows that the region's rising resilience could accommodate moderate changes in these conditions, although the region is still quite vulnerable to sharply slower world growth combined with much tighter financing, or a big drop in commodity prices. Reducing Latin America's vulnerability further to such shocks requires additional progress in lowering public debt levels, making budgets and exchange rates more flexible, strengthening financial systems, and diversifying the export structure.

Looking to the medium term, the Regional Economic Outlook shows that significant increases in investment and—more importantly—in productivity growth would be needed to raise per capita incomes substantially in Latin America, and illustrates the potential effects of reforms in two key areas (education and labor markets). Based on recent research, the report also addresses the question whether Latin America has now succeeded in breaking with its history of periodic growth reversals. It finds that several critical determinants of sustained growth—including political institutions and trade regimes—have indeed improved significantly in the last decades, and macroeconomic volatility is much lower. Intensified efforts to create more equitable and less divided societies—which will be better positioned to avert sharp growth reversals in the future—would also help. Progress in this area will take time and require fiscal, education, labor, and financial sector reforms. In the meantime, macroeconomic policies will need to remain vigilant, to ensure that the region can grasp the opportunity to entrench and raise growth.