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Latin America on the Brink

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One of the arguments that has run through the Common Market controversy in this country has been the view that any further strengthening of the "rich man's club" in Europe will inevitably damage the trading prospects of the developing countries, and thus retard their growth. In Latin America, in particular, there is widespread apprehension that the evolution of the EEC will not only restrict the market for its temperate foodstuffs (meat and grains) and discriminate against its tropical products (coffee and cocoa), but also divert investment interest from the area. Whether these forebodings prove to be justified or not, the impact of the EEC is likely to be remote and marginal compared with the region's present predicament. For in Latin America the crisis has already arrived.

Since the early 1950s economic development in the continent has become increasingly difficult to maintain, and some of the larger countries, such as Argentina and Chile, have experienced long periods of stagnation. With the exhaustion of the swollen exchange reserves that were a legacy of the war and the halting, and then reversal, of the upward trend in commodity prices, the rapid and easy development of the early postwar years was brought to an end. The pace of the continent's development is set by the volume of exchange resources at its disposal; as its current export receipts levelled out its dependence on foreign investment and aid increased. Fortunately, at this time the world-wide movement towards multilateralism and liberal economic policies worked to the benefit of Latin America. The dismantling of exchange controls in Europe was followed by similar relaxations in Latin America itself. Exchange rate structures were simplified, physical controls on imports abolished and free exchange markets established for the transfer of capital and income. This liberalization, together with the recognition of the economic potential of the region, brought a resurgence of interest by foreign investors. The annual net flow of long-term capital to Latin America rose sharply--from an average annual rate of $587 millions in 1951-55 to one of $1,218 millions in the years 1956-59. In the second half of the 1950s, indeed, Latin America was attracting nearly two-thirds of the total private long-term capital flowing to the developing countries; even allowing for the massive, once-only, investments in the Venezuelan oil industry in 1956 and 1957, the rise in the inflow of foreign capital was impressive. Nevertheless, it was still inadequate to support the pace of development required. For what the region gained on the one hand by its greater capital resources, it lost on the other through lower export receipts brought about by falling commodity prices. Today, the value of Latin American exports is only 9 per cent above the 1955 level and below the 1957 peak; since 1958 total exchange revenue has hovered around $8,500 millions a year. It is estimated that by the end of this year Brazil alone will have suffered an exchange loss of nearly $1,300 millions through coffee prices falling below their 1956 average--which itself was well below the record high prices of 1954.

The growth in population, the increased demands for a higher standard of living by the Latin American peoples and the very process of development itself, with its increasing demand for industrial raw materials and capital equipment, created a propensity to import that it was far beyond the capacity of available resources to finance. Short- and medium-term credits were increasingly resorted to, and supplying countries were persuaded to lengthen their credit terms for all types of equipment, in many cases with only slim chances of payment on due date. Argentina and Brazil were buying as much as 20 per cent of their total imports on deferred payment terms. Thus, in this unplanned and unco-ordinated manner the region's short-term and medium-term indebtedness rose astonishingly: in Argentina official exchange commitments rose to $2,700 millions, with an unknown value of private debt not statistically collated, whilst in Brazil medium- and long-term obligations have soared to more than $3,000 millions. From the beginning of the 1960s, interest and repayment obligations began to assume alarming proportions; both Argentina and Brazil at present face exchange commitments of the order of $400 millions for each of the next three years, or about one-third (or more) of their export income.

Scaring Off the Foreign Investor

Latin American short- and medium-term indebtedness has reached a record level at a time when official exchange reserves are the lowest for the past ten years and when there is little immediate likelihood of export income increasing. Moreover, there are now signs that the capital inflow has begun to falter. The ill-success of IMF-sponsored stabilization plans in the area, continuing inflation and a return to more rigorous exchange controls are signs that the movement towards liberalism and orthodoxy has been reversed. Depreciating currencies, particularly in Argentina and Brazil, and interference with the free financial markets are themselves powerful deterrents to the foreign investor. Moreover, these economic troubles have been accompanied by (and aggravated by) political dissension, military government and a general growth of extremism. Not surprisingly, the foreign investor has been scared off. Net private US investment in Latin America, which totalled $338 millions in 1959, had fallen to $135 millions last year; it is officially estimated that since June 1961, new US investment in the area has been negligible. Britain's private direct investments, excluding oil and insurance companies, rose sharply from $15 million in 1959 to $44 millions last year, but this year, mainly because of unfavourable conditions in Argentina, they are expected to have declined drastically. German private direct investment has so far held up well: in the first six months of this year it reached $40 millions, against an annual average of $55 millions in the previous two years. It is probable, however, that the figures for the second half of this year will show a marked decline, since some two-thirds of German investment in Latin America is concentrated in Brazil, where political tension persists and where the recent passing of restrictive legislation on profit remittances and the interruption of the free workings of the exchange market have done much to discourage new commitments.

Ironically, this falling off in private investment has coincided with the Alliance for Progress, the regional programme launched by President Kennedy last year to provide the basis of a "decade of development." It had been a long-standing grievance of Latin Americans that while the US Government has poured out reconstruction funds to Europe and financial assistance to the politically risky areas of the world, Latin America had been virtually ignored. Up to the end of June 1961, Latin America had received from the US Government $4,887 millions in economic aid, or only 8 per cent of the total made available over the 16-year period. With the advent of Fidel Castro, the needs of Latin America in US eyes were changed almost overnight. At the Punta del Este conference in August 1961, the Administration agreed that a minimum of external resources amounting to $20,000 millions should be made available for Latin America in the next ten years. Of this sum, about one-half was to be provided by the Government and the remainder in equal proportions by private US investors, the international organizations and Europe and Japan. The figure of $20,000 millions over a ten-year period was about twice the value of foreign capital resources received by Latin America in the 1950s, and represented an increase of about one-third on the rate of inflow in the period 1956-59. Even so, taking into account the stagnation in the region's export income and the increasing demands on exchange availabilities, the scale of the US Government's undertaking (about 2 per cent of US defence expenditure) did not impress the Latin Americans as being over-generous. The Alliance has got off to a disappointingly slow start: only five republics have so far succeeded in drawing up acceptable overall development plans, some of the social reforms advocated in the Punta del Este declaration are bitterly resented by the ruling groups in the republics and much of the aid under the first year of the Alliance has been of a familiar stop-gap kind, such as temporary balance-of-payment loans, surplus food dumping and budget financing. Of the $1,000 millions actually allocated by the US Government in the first year of the Alliance, only one-quarter is believed to have been disbursed. The total flow of external resources moving to Latin America in the first year of the Alliance has been optimistically estimated in Washington at $2,500 millions, but it is probable that this gross figure includes some double counting. Rather than representing a genuine increase in the region's exchange resources it partly reflects the rephasing of short and medium-term liabilities that European and US creditors have been forced to undertake and leaves out of account the substantial outward movement of funds from Latin America for servicing and amortization. Latin America's own development bank, moreover, seems unlikely to be able to make a decisive contribution to the region's capital requirements. Loans authorized by the Inter-American Development Bank in its first full year's operation amounted to $178 millions, which committed about 40 per cent of its dollar resources (actual disbursements, however, were only $6 millions). The Bank is faced, therefore, with an early curtailment of its lending operations, though it will continue to play an important rôle in the administration of the Social Progress Fund under the Alliance.

Stabilizing the Coffee Price

But while the development aid programme for the region has still to get off the ground, some progress has been made in underpinning the export revenues of some of the primary producers. In particular, coffee producers have succeeded in persuading importing countries to participate in the new long-term World Coffee Agreement. The coffee trade, though it has been surpassed as the region's principal exchange earner in recent years by oil exports, is of concern to no less than 13 Latin American republics, and provides 18 per cent of the area's export earnings. For Brazil and Colombia coffee accounts for 60 and 75 per cent respectively of total exports. Coffee prices today are little more than a third of their postwar peak.

The new agreement is largely an extension of the principles of the previous international coffee agreements initiated by Latin American producers in 1957, and subsequently widened to cover some 95 per cent of world production. It is, however, the first to include both producers and importers. Its lack of definition is attributable to the compromises that were necessary to reconcile the divergent interests of 57 member countries. In fact, Latin American aspirations are far from being satisfied by the agreement, which contains only a vague assurance that prices should not fall below their 1962 levels. Most of the obligations remain on the producing countries, who will be responsible for withdrawing from the market supplies of coffee in excess of their export quotas established under the agreement and for adjusting production to consumption. Importers, however, have agreed to examine the possibility of reducing barriers impeding the expansion of coffee consumption; the introduction of a certificate of origin for coffee, along with other measures, will ensure that coffee traded under the agreement will not fall below 95 per cent of the world coffee trade. The agreement makes no provisions for the financing of surplus coffee stocks or for meeting the costs of adjusting production, which are to be borne by the producer countries themselves. Latin Americans have welcomed the participation of the richer industrialized countries in the agreement, largely because they believe that from these small beginnings a comprehensive world-wide stabilization scheme will be evolved.

Nevertheless, although the new agreement may succeed in finally stabilizing coffee prices and be followed by similar schemes for other commodities, these arrangements can neither improve international prices nor ensure that the world demand for primary commodities expands fast enough to provide the rising volume of exchange resources required. Latin America, therefore, faces the prospect of continuing balance-of-payments deficits for many years to come. And in the short run there is probably very little that it can do itself to avert the danger. The Latin American Free Trade Association, with its aim to enlarging the market for industrial products within the area, is a promising venture, but is as yet too weak to inspire the confidence of the foreign investor and seems unlikely to call forth the interest desired. The problem can be solved only by assistance from the industrial countries--in the form of long-term capital and aid funds. Short-term credits will not meet the situation. The mass of short-term debt that has brought Latin America to the brink of insolvency was itself built up haphazardly as the result of export drives of the industrial countries. Current commitments have reached such proportions that only a thoroughgoing funding would provide real relief in the next decade. And such a funding, like the continuing programme of long-term assistance that should accompany it, would inevitably be inspired more by political considerations than by economic.