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The Coming Turmoil in Latin America

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OP-ED
OCTOBER 8, 2015 *ATLANTIC*

SUMMARY Many people across Latin America may soon discover that their recent economic advances are not as permanent as they think.

Latin America has gone from a period of prosperity to a period of peril. Between 2004 and 2013, the region experienced extraordinary economic growth and social progress. Demand—mostly from Asia—for the commodities that constitute the region's main exports increased sharply, pushing up both the prices of those exports and the volumes traded. Revenues from this trade, in turn, stimulated regional economies and helped fill governments' coffers. This unprecedented demand coincided with a period of very low interest rates, abundant credit, and surging foreign investment flows into Latin America.

Recently, however, China's economic sluggishness and weak global economic growth have brought down commodity prices, foreign investment has slackened, and monetary policies have become less expansionary. This year, economic growth in Latin America is expected to be lower than in the previous year for the fifth consecutive year. Between 2010 and 2015 the economies of the region are likely to grow at only 40 percent of their growth rate between 2003 and 2010.

Sudden, painful transitions from economic prosperity to slowdown and even meltdown are nothing new in Latin America. The opposite, in fact: Between 1970 and 1998, Latin America experienced an economic crisis every two years. From 1979 to 1998, Peru had such a crisis nearly every year. Indeed, Latin America is one of the most economically volatile regions in the world. Regional indicators such as GDP growth, exchange rates, and fiscal deficits are roughly two to three times more volatile than those of industrialized countries. In terms of monetary policy and inflation rates, Latin America has more variability than any other region.

But the current period—characterized by low or no growth (or, as in the case of Brazil, deep recession), currency devaluations, rising unemployment, public-spending cuts, and falling incomes—has several new dimensions. One is that the economic boom that just passed benefitted the region's poorest citizens more broadly than past periods of growth did, according to José Juan Ruiz, the chief economist at the Inter-American Development Bank (IDB). This resulted not only in poverty reduction, but also, for the first time ever, in significant declines in Latin America's notoriously high rates of economic inequality. Governments in the region used their windfalls to spend more money than ever before on direct subsidies to the poor, and on health, education, housing, and social programs targeted at low-income populations. Not only did governments spend more on the poor, but they did so more efficiently. According to IDB estimates, between 2005 and 2012 public spending on social policies increased at double the rate of economic growth in the region. Social spending went from being 14 percent of the regional economy to an unprecedented 19 percent.

Thanks to this enhanced social spending, during the boom years the percent of people living in poverty in the region dropped from 34 percent to 21 percent, and the biggest middle class in Latin American history took shape. Currently, one-third of Latin Americans belong to the middle class (in 1990, that figure was 17 percent). Today, for the first time, members of this middle class outnumber those living in poverty.

It's a welcome reality, but also one that poses threats: Some percentage of the people belonging to this new, broader but still fragile middle class are at risk of falling back into the poverty they escaped not long ago. The consequences of the busts that followed Latin America's booms used to be borne primarily by the poor. That's no longer the case.

Relative to poorer citizens, members of the middle class often feel more politically empowered and connected; their expectations of government rise in tandem with their economic status, and they are in a better position to organize and demand that those expectations be met. This organization often comes in the form of anti-government street protests, which have grown frequent from Mexico to Argentina. Compounding poor economic conditions in the region is a slew of corruption scandals that have engulfed the highest levels of government, including the administrations of Enrique Peña Nieto in Mexico, Dilma Rousseff in Brazil, Ollanta Humala in Peru, Michelle Bachelet in Chile, Juan Orlando Hernández in Honduras, and the recently resigned and jailed Otto Pérez Molina in Guatemala. A larger, politically awoken middle class has far less tolerance for corruption these days, particularly as the deteriorating economy threatens to sabotage their newly attained standard of living, and they have access to new technologies that facilitate the spread of information and lower the costs of political coordination. These dynamics may produce positive outcomes like removing politicians and parties that have been in power for far too long, but they could also result in corrosive social conflict, government paralysis, and political instability.

The aspirations of this new middle class are lofty and revolutionary. According to surveys by Latinobarómetro, 45 percent of Latin Americans consider themselves members of the middle class and twice as many as 15 years ago say they are satisfied with their living conditions. Surprisingly, only 20 percent of those who identify as middle class feel their progress is due to the economic growth of their country, while 32 percent believe their success is due to their own hard work. But perhaps the most shocking statistic is that 50 percent of Latin Americans think that the improvement in their living conditions is permanent.

Unfortunately, many may soon discover that their economic advances are not as permanent as they think, and that their hard work is not enough to maintain the improved standards of living they attained when the region was prospering.

That is why perilous years lie ahead for Latin America.

This article was originally published in the *Atlantic*.

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