

Lat.Am. & Caribbean

GDF 2003 Summary



Global themes

- Global growth is projected to accelerate steadily from 1.7% in 2002 to 2.3% in 2003 and 3.2% in 2004. Importantly, this view incorporates the effect of a relatively quick military conflict in Iraq. While very much a recovery, the expansion now underway is quite subdued by historic standards, especially given the sizeable stimulus from policy.
- The past few years has seen a fundamental shift in the pattern of private sector financing for developing countries, away from debt flows to equity-related FDI flows. The drop in debt finance has been partly driven by lower demand on the part of many developing countries seeking to lessen their vulnerability to swings in volatile debt finance, as well as a reduced supply of debt from banks and bondholders. The rise in FDI reflects greater optimism about globalization, the spread of FDI in services and heavy privatization.
- While this rotation from debt to equity should continue, the signs are that the low point in the current private debt cycle came in 2002Q3, and that net debt flows to developing countries are likely to turn positive again in 2003 for the first time in three years. While most likely, the overall buoyancy of FDI flows should not be taken for granted, however. Flows are already off their peak; privatization-related revenues have fallen sharply; and FDI in telecom and other areas of infrastructure has slumped. Moreover, rates of return on both FDI and in the corporate sectors of developing countries have generally fallen in recent years.
- Workers remittances have become an increasingly important component of global development finance, having risen to \$80 billion in 2002. They have some very attractive financial features. They are more stable than private debt flows and are less concentrated in the major middle-income countries than FDI flows.
- Aid flows to developing countries probably rose in 2002 and will continue to do so in 2003 and beyond, in line with the commitments made at the Monterrey Conference in March 2002. Emergency financial support (e.g. IMF) is likely to fall in 2003, on the presumption that no new major debt crises are in the offing. In between, official non-concessional lending (which includes the IBRD) is generally quite weak. Note that net IBRD lending was -\$4.1 billion in 2002 and is on track for an even larger decline in 2003.

Regional themes

- The broad-based decline in debt flows, which was first evident in East Asia and the Russian Federation, became focused on Latin America in 2002. This largely accounts for the severity of the downturn in the region in 2002, where output fell 0.9 percent (there was a modest rise of 0.8 percent in the region, excluding the large 11 percent decline in Argentine GDP).
- Led by the recovery in Argentina, growth in the region is expected to accelerate by the most of any region in 2003. That said, growth will still be only 1.7 percent. It is then forecast to accelerate gradually towards 4 percent by 2004-05.

- As the region most heavily dependent on market-based debt financing, it suffered the most dramatic drop in debt flows in 2001-02. *Gross* market-based financial flows fell by \$31 billion in 2002, or by 40 percent. The decline was severe even after excluding Argentina: a drop of \$26 billion, or 38 percent. *Net* debt repayments from the region continued despite Argentina's default. The region repaid a net amount of \$9 billion in external debt to private creditors in 2002, similar to 2001. Note that the region also saw a drop in net debt inflows from official creditors. Notably, the region repaid the IBRD \$0.3 billion in 2002.
- Latin America and Caribbean also suffered the severest decline in FDI among all regions, falling to \$42 billion in 2002 from \$69 billion in 2001, with the decline evident across all countries. FDI flows to Brazil—still the main FDI destination in the region and the second largest in the developing world—fell to an estimated \$17 billion, significantly below the \$30 billion annual average seen during 1999-2000.
- The reduced supply of capital to the region forced a remarkably rapid change in the region's current account position, brought about partly by currency depreciations. The region's trade balance shifted from balance in 2001 to a surplus of \$25 billion in 2002. The current account deficit narrowed by about \$35 billion, to \$16 billion.
- Latin America and the Caribbean is the region with the largest receipts of workers' remittances. In 2002, the region received \$25 billion in such remittances, up almost 50 percent from 1999. Mexico ranks second (\$10 billion in 2001) in the list of the top recipient countries of workers' remittances. Other countries (Brazil, Colombia, Dominican Republic, Ecuador and El Salvador) are also among the top recipients. Relative to GDP, remittances are largest in Central America.

Other key regional points to note

- In parallel with the rotation from debt to equity, international banks in recent years have shifted away from cross-border lending and towards greater participation in the local banking market. However, the losses suffered by foreign banks during the Argentine crisis of 2001 may lead banks to reconsider this shift, especially in Latin America.
- One of the factors accounting for the decline in FDI in 2002 was the lack of any "mega-deals", such as the Citibank-Banamex transaction in 2001.
- Latin American bond markets are in a period of transformation. There is a welcome shift towards funding in local currency markets over borrowing in foreign currencies. In some cases (Chile, Colombia and Mexico), there has also been considerable success in lengthening the maturity of this domestic debt. In Brazil, however, the domestic debt is excessively short duration, and this contributed to the problems experienced in 2002.
- The report focuses on the merits and demerits of the recent proposals for improving the framework for restructuring bond debt. The Collective Action Clause approach has recently enjoyed a boost from Mexico's first issue of such a bond.
- Some Latin American companies have become important globally. Box 4.4 highlights the role of Cemex, the Mexican cement company, in promoting South-South FDI.

Table A.4 Latin America and the Caribbean outlook in summary, 1981–2003

Real economy (percent change, unless stated)	1981-90	1991-00	1997	1998	1999	2000	2001	2002e	2003f
Real GDP growth	1.1	3.3	5.2	2.0	0.2	3.5	0.3	-0.9	1.7
Private consumption per capita	-1.0	2.3	3.2	-0.2	-1.6	2.1	-0.9	-3.4	0.3
GDP per capita	-0.9	1.6	3.4	0.4	-1.4	1.9	-1.3	-2.4	0.3
Population	2.0	1.7	1.6	1.6	1.6	1.6	1.6	1.5	1.4
Gross domestic investment/GDP ^a	20.1	19.9	21.1	21.3	19.7	19.6	19.1	17.7	17.0
Inflation ^b	17.3	11.9	8.2	6.7	4.2	7.2	6.8	4.6	4.2
Central government budget balance/GDP	-9.1	-3.3	-3.0	-4.0	-3.0	-2.2	-1.8	-2.6	-2.8
Export market growth ^c	4.4	11.3	12.7	7.7	5.0	12.0	-1.2	0.3	6.8
Export volume ^d	5.4	8.6	9.8	7.9	6.3	10.4	0.7	4.0	8.6
Terms of trade/GDP ^e	0.9	0.2	0.4	-0.2	0.2	0.7	-0.3	0.0	-0.4
Current account/GDP	-1.5	-2.8	-3.3	-4.5	-3.2	-2.4	-2.9	-1.0	-1.2
Workers remittances (billions of dollars)	—	—	13.6	14.8	16.9	19.2	22.6	25.0	—
Memorandum items									
GDP growth: Latin America and the Caribbean excluding Argentina	1.6	3.1	4.6	1.7	0.9	4.3	1.1	0.8	1.6
Central America	1.0	4.4	4.7	5.2	4.4	2.9	0.4	1.8	2.8
Caribbean	2.0	4.0	4.8	5.2	5.9	5.9	3.1	2.9	3.9
External Financing and Debt (billions of dollars unless stated)									
	1995	1996	1997	1998	1999	2000	2001	2002e	2003f
Net inward FDI	30.5	44.4	66.1	73.4	87.8	75.8	69.3	42.0	38.0
Net inward portfolio equity flows	4.8	12.2	13.3	-2.1	-3.6	-0.4	2.3	1.0	2.0
Net inward debt flows	61.3	36.0	24.3	37.9	12.3	-1.1	11.4	3.5	0.0
From public sources	22.0	-10.7	-8.6	10.9	1.6	-11.1	20.2	12.6	6.0
From private sources	39.3	46.8	32.9	27.0	10.7	10.0	-8.7	-9.1	-6.0
Gross market-based capital inflows	42.8	84.9	120.6	84.5	75.3	89.9	75.8	45.3	44.0
Total external debt	650	671	702	774	795	783	765	—	—
Medium- and long-term	522	550	575	656	685	677	669	—	—
Short-term	128	121	127	119	109	106	96	—	—
Owed by public-sector borrowers	435	433	413	436	442	433	443	—	—
Owed by private-sector borrowers	215	238	289	338	353	350	322	—	—
Owed to public-sector creditors	217	194	176	180	183	170	181	—	—
Owed to private-sector creditors	432	477	526	594	612	613	584	—	—
Gross foreign exchange reserves	125.1	153.1	166.7	157.5	150.0	152.9	155.9	151.9	161.9

— Not available.

Note: e = estimate, f = forecast.

a. Fixed investment, measured in real terms.

b. Local currency GDP deflator, median.

c. Weighted average growth of import demand in export markets.

d. Goods and non-factor services.

e. Change in terms of trade, measured as a percentage of GDP.

Table A.25 External financing: Latin America and the Caribbean, 1997–2003
(billions of dollars)

	1997	1998	1999	2000	2001	2002e	2003f
Current account balance	-66.3	-89.5	-55.7	-47.2	-54.1	-16.3	-19.5
as a percentage of GDP	-3.3	-4.5	-3.2	-2.4	-2.9	-1.0	-1.2
Financed by:							
Net equity flows	79.4	71.3	84.2	75.4	71.6	43.0	40.0
Net FDI inflows	66.1	73.4	87.8	75.8	69.3	42.0	38.0
Net portfolio equity inflows	13.3	-2.1	-3.6	-0.4	2.3	1.0	2.0
Net debt flows	24.3	37.9	12.3	-1.1	11.4	3.5	0.0
Official creditors	-8.6	10.9	1.6	-11.1	20.2	12.6	6.0
World Bank	0.8	2.4	2.1	2.0	1.3	-0.3	—
IMF	-3.9	2.5	-0.9	-10.7	15.6	12.3	—
Others	-5.4	6.0	0.4	-2.4	3.3	0.7	—
Private creditors	32.9	27.0	10.7	10.0	-8.7	-9.1	-6.0
Net medium- and long-term debt flows	41.6	54.4	18.6	12.6	0.5	-5.6	—
Bonds	11.0	17.3	19.1	5.3	3.5	4.5	—
Banks	31.4	39.3	-1.4	8.3	-1.4	-8.3	—
Others	-0.9	-2.3	1.0	-0.9	-1.6	-1.8	—
Net short-term debt flows	-8.6	-27.4	-7.9	-2.6	-9.2	-3.5	—
Balancing item ^a	-23.8	-28.8	-48.2	-24.2	-25.9	-34.3	-10.5
Change in reserves (- = increase)	-13.5	9.2	7.5	-2.9	-2.9	4.0	-10.0
Memo items:							
Bilateral aid grants (ex. technical cooperation grants)	2.8	3.3	3.0	2.5	3.2	3.2	3.0
Net private flows (debt + equity)	112.3	98.3	94.9	85.4	62.8	33.9	34.0
Net official flows (aid + debt)	-5.8	14.2	4.5	-8.6	23.4	15.8	9.0
Workers' remittances	13.6	14.8	16.9	19.2	22.6	25.0	—

— Not available.

Note: e = estimate; f = forecast.

a. Combination of errors and omissions and net acquisition of foreign assets (including FDI) by developing countries.