Is Latin America an Economic Failure?

FROM NARRATIVES TO DATA

Alejandro Fiorito, José Juan Ruiz, and Ernesto Talvi

Abstract

Latin America is often regarded as an "economic failure," a region prone to crises, with high inflation and other symptoms of macroeconomic instability. But that picture is largely one of the past. Analyzing six areas of macroeconomic management and eight macroeconomic outcomes, this paper shows the substantial improvements the region has achieved in the last three decades. The main challenge for Latin America now is consolidating sustainable and inclusive growth, something that has escaped the region in the 21st century, despite several years of favorable external environment. Even if the convergence to advanced economies seems like an unrealistic goal, improving growth drivers should be first in policymakers' priority list.

Is Latin America an Economic Failure? From Narratives to Data

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Foreword

Latin America faces a global environment that has been delivering multiple shocks and remains highly uncertain—from the pandemic, to rising international conflict, to high inflation and the highest interest rates in the US in over 20 years. Amid these new challenges, it is good to take stock of both what Latin American economies have achieved and what is pending.

This paper showcases the notable advances in macroeconomic management in the region and the resulting consolidation of good macroeconomic outcomes. Enhanced monetary policies, fiscal discipline, and banking regulation and supervision have accompanied and helped stabilize inflation, consolidate fiscal accounts, improve debt profiles, accumulate reserves, and expand financial markets in many countries in the region.

As Latin America is vulnerable to and highly dependent on this external environment, keeping solid macroeconomic fundamentals will limit fragilities and increase resilience. As the authors note, much remains to be done, particularly in reigniting growth by improving its drivers. Substantial gaps in human capital, infrastructure, economic integration, and innovation persist and are associated with the endemic low productivity that hinders growth in the region.

This work acknowledges progress and successes, but also reminds us of the importance of redirecting and focusing efforts to prioritize policies and invest finite human, political, and social capital in the crucial issues that can foster growth in this complex region.

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Executive summary[1]

A widespread notion in European capitals is that Latin America is an economic failure: a highly volatile region, prone to all kind of recurrent crises, and unable to develop and sustain a dynamic of convergence towards the income levels of advanced economies, as the Asian Tigers did.[2] To paraphrase a well-known saying about Brazil, the established perception is that "Latin America is a land of the future and it always will be."[3]

Data shows this view is biased and does not match reality. First, **progress in macroeconomic management over the last 20 years has been very significant and the results are notable**. An entire Latin American generation has grown up in an environment of low and relatively stable inflation, reasonably sound public finances, and regulatory and supervisory frameworks that have led to the strong financial systems the region has today. One striking achievement is the reduction in the frequency of exchange rate, sovereign debt, and financial crises: from an average of four crises per year between the mid-1970s and the early 2000s to less than one a year in the last 20 years. As a result of this greater macroeconomic stability, Latin America went from being a *protagonist*—one third of the world's exchange rate, banking, and debt crises between 1974 and 2003 took place in the region—to just playing a *supporting role*: only one of every six crises have taken place in Latin America since 2003.

Second, income convergence from underdevelopment to development is the exception that proves the rule, as **non-convergence is a widespread phenomenon in most emerging markets and developing economies**. To judge Latin America's long-term performance by comparing it with the highly unlikely convergence processes only achieved by Japan, Taiwan, Korea, Singapore, and Hong Kong in the post-war period is, to say the least, incorrect.

The main challenge that Latin America faces is neither macroeconomic management nor trying to achieve the unlikely goal of convergence but consolidating sustainable and inclusive growth. The region's per capita income has been stagnant for a decade. The prolonged absence of sustained economic growth inevitably results in a situation marked by a distributive competition for resources, which not only fosters social tensions but also diverts valuable sociopolitical resources towards managing these tensions, instead of focusing them on the pursuit of economic growth.

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1   This analysis is part of the Elcano Report 32 "Why Latin America Matters" (in Spanish).
2   South Korea, Hong Kong, Singapore, and Taiwan.
3   The original quote, based on the title Stefan Zweig's book "Brazil: Land of the Future", is attributed to Charles de Gaulle.

1. Macroeconomic management

This section assesses six key aspects of macroeconomic management in Latin America[4] and the progress achieved during the 21st century.

1.1 Exchange rate regimes

The exchange rate crises that hit the economies of the region over and over again are largely a thing of the past, and many countries now have more flexible exchange rate regimes.

Currently, eight out of 24 countries in the region have flexible exchange rates,[5] another ten use soft pegs, and only six have fixed or non-transparently managed rates. This contrasts with 1999, when almost one third of the countries in the region had fixed or non-transparently managed rates (Table 1 and Figure 1).

The prevalence of different exchange rate regimes in Latin America is in line with international trends: the proportion of countries in the region using floating exchange rates, soft pegs or fixed rates is very similar to that of the rest of the world (Table 1).

TABLE 1. Distribution of exchange rate regimes, 2021

	Latin America	Rest of the world
	(Percentage of total countries)	
Flexible	33.3	32.8
Soft peg	41.7	48.0
Other	8.3	5.8
Fixed	16.7	12.0

Notes: The flexible exchange rate category includes floating and free-floating rates, depending on the level of intervention in the foreign exchange market, which in both cases is limited to exceptional situations. Soft peg includes (a) crawl-like models, where the exchange rate fluctuates within a 2 percent band with respect to an identified trend for at least six months; (b) crawling peg, where exchange rate whose parity is fixed with another currency or currencies; and (c) stabilized, where the exchange rate fluctuates within a 2 percent band for at least six months. Other exchange rate regimes are those where the regime does not fit into the other categories and is non-transparent. Fixed exchange rate regimes have a constant parity or directly adopt a foreign currency.
Source: IMF (2022a).

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4   Latin America refers broadly to the whole region, including the Caribbean. Data has been collected for 24 countries that comprise the sample in Figure 1 (Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Paraguay, Peru, Panama, Suriname, Trinidad and Tobago, Uruguay, and Venezuela). Different sub-sections may have different samples depending on data availability, and small Caribbean islands (those with a GDP of less than US$1 billion) and countries with no data such as Cuba are excluded from the sample. Unless otherwise noted, general measures for Latin America indicate simple averages.

5   These countries account for 76 percent of regional GDP.

FIGURE 1. Exchange rate regimes, 2021

Source: IMF (2022a).

1.2 Independence of central banks

The loss of central bank independence during most of the 20th century has been reversed over the past 30 years—now, 13 Latin American countries have independent central banks (Figure 2).[6,7]

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6   These countries account for 79 percent of regional GDP.
7   Jácome and Pienknagura (2022) and Garriga (2016).

FIGURE 2. Central bank independence, 2023[8]

Independent ▉   Not independent ▉

Sources: Jácome and Pienknagura (2022) and central banks.

Central banks began to gain de facto operational independence in the 1990s (Figure 3 and Table 2), a process that was followed by legislation that certified and secured this progress. Monetary policy independence was consolidated, and most countries stopped monetary finance—i.e., using money creation to support fiscal deficits.[9]

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8   De facto independence may not be legislated, but it is recognized and exercised. For example, Argentina, Bolivia, and Venezuela have legislated central bank independence, yet these countries' central banks do not have de facto independence, while Brazil's does not have legislated independence, but is de facto an independent central bank. Ecuador and El Salvador recognize the independence of their central banks, despite neither having an independent currency and therefore limited monetary sovereignty, while Panama does not have a central bank itself and it is the National Bank of Panama that performs some of the central bank functions.

9   Some serious concerns have recently been raised regarding central bank independence in Latin America, which further emphasize the relevance of the progress made (see, for example, Citibank (2022)).

FIGURE 3. 100 years of central bank independence
(Index 0–1; 1= highest level of independence)
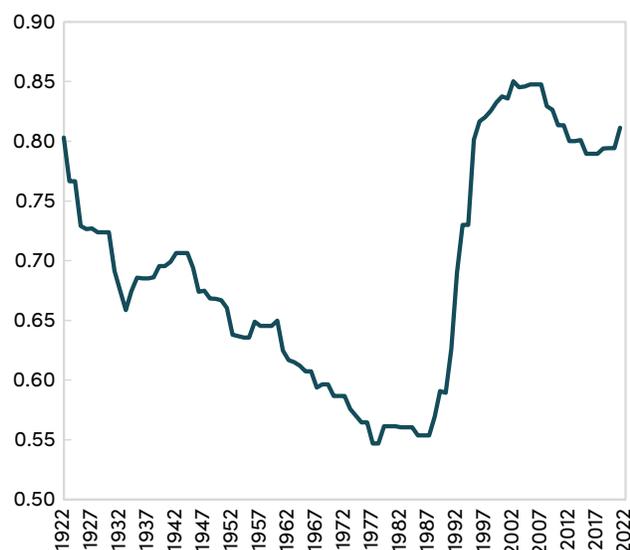
TABLE 2. Independence of central banks by subcomponents
(Average for Latin America, index 0–1)

	Pre-reform (1980–1989)	Post-reform (2021)
Global Index	**0.58**	**0.81**
Board independence	0.39	0.71
Central bank objectives	0.29	0.79
Policymaking	0.71	0.85
Government financing	0.70	0.85

Notes: Board independence is defined by (1) the term of office of the central bank president; (2) the election process to select the central bank president; (3) the term length of the board; (4) the process of electing the board; (5) the presence of the government on the board; and (6) the process of dismissing board members. *Central bank objectives* is defined according to the importance given to price, financial system, and payment system stability within the monetary authority's mandate. *Policymaking* is defined according to the central bank's independence in monetary policy and exchange rate policy. *Government financing* is defined according to (1) the central bank's ability to provide funding advances to the government; (2) its ability to extend credit in secondary market; (3) who are the potential beneficiaries of central bank financing; (4) the maturity of the advanced funding that the central bank can provide; and (5) whether the central bank is allowed to provide credit in the primary market.
Sources: Jácome and Pienknagura (2022) and central banks.

1.3 Inflation targeting

In 1998, only 26 years ago, no country in Latin America had explicit inflation targets, while today at least 11 of them have adopted this kind of scheme, which generally better supports price stability.[10,11]

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10 These countries account for 80 percent of regional GDP.

11 Brazil, Chile, and Colombia adopted explicit inflation targets in 1999, Mexico in 2001, Peru in 2002, Guatemala in 2005, Paraguay in 2011, Dominican Republic in 2012, Uruguay in 2013, Jamaica in 2017, and Costa Rica in 2018, see De Gregorio (2020).

Just two countries use targets for monetary aggregates, while eight use an exchange rate anchor, mainly small and open economies with strong ties to the US (Figure 4).

FIGURE 4. Monetary policy models, 2021

Notes: An *inflation target* regime implies a public announcement of an inflation target and an institutional commitment by the monetary authority to achieve this objective, typically over the medium term. A *monetary aggregate model* means that the monetary authority tries to achieve a growth target of one of its monetary aggregates (M1, or M2, for example). An exchange rate *anchor model* implies that the monetary authority buys and or sells foreign currency to maintain the exchange rate at a predefined level or within a range, using this variable as a nominal anchor and intermediate target for monetary policy. Other models include those in which the country does not have an explicitly set nominal anchor.
Source: IMF (2022a).

1.4 Fiscal rules

Fiscal rules[12] that support public finances' stability began to be implemented in the late 1990s and early 2000s. Brazil was the first country to adopt a number of these measures in 1998, but it was

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12 Fiscal rules impose restrictions on fiscal budget aggregates. They can be national, regional, or supranational, but for Latin America we will be focusing on national standards. See types of fiscal rules in Figure 7.

Chile's structural balance rule, implemented in 2000, that was used as a reference and model around the region.[13],[14] This was due to its institutional structure, its capacity to achieve fiscal surpluses during good economic times, and its countercyclical considerations, which are unusual not only in Latin America but, overall, in emerging countries.[15]

Nowadays, 13 countries use some sort of fiscal rule (Figure 5 and Table 3).[16]

FIGURE 5. Adoption of fiscal rules since 1998

Source: Davoodi et al. (2022).

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13 Brazil incorporated a budget balance policy rule into the constitution in 2000 and adopted a fiscal responsibility law in 2000, Pereira (2016).

14 This policy rule has a structural balance target. Government expenditures are budgeted ex ante based on the revenue that would be raised if the economy were at its potential level and copper and molybdenum prices were at historical averages. The latter, the potential level of GDP and the prices of copper and molybdenum, are determined by independent committees Ffrech Davis (2016), Gallegos Zuñiga (2018) and Davoodi et al. (2022). Some countries like Colombia are moving towards a debt rule instead of a structural balance rule.

15 Talvi and Végh (2000).

16 These countries account for 91 percent of regional GDP.

TABLE 3. Types of fiscal rules

	Total	Expenditure	Balance	Debt
Argentina	1	X	–	–
Brazil	2	X	X	–
Chile	1	–	X	–
Colombia	2	X	X	–
Costa Rica	2	X	X	–
Dominica	2	–	X	X
Ecuador	3	X	X	X
Jamaica	2	–	X	X
Mexico	2	X	X	–
Panama	2	–	X	X
Paraguay	2	X	X	–
Peru	3	X	X	X
Uruguay	2	X	X	–
Countries with no fiscal rules	12	Belize, Bolivia, Dominican Republic, El Salvador, Guatemala, Guyana, Haiti, Honduras, Nicaragua, Suriname, Trinidad and Tobago, and Venezuela.		

Note: There are three types of fiscal rules: expenditure or revenue rules (those that limit the collection or use of the fiscal budget), balance rules (those that set a fiscal balance target), and debt rules (those that set a debt ceiling or growth limits based on certain factors).
Source: Davoodi et al. (2022).

1.5 Public debt management

Public debt management, a key factor in fiscal sustainability, has become more professionalized in the region, especially in the larger Southern Cone and the Andean region countries.[17,18]

Progress has been achieved in all areas of debt management, including institutional and governance models, macroeconomic policy coordination, debt management and sustainability strategies, data availability and risk management, and issuance processes. (Table 4).[19]

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17 Chiara and Prats (2022).
18 The countries of these two subregions account for 62 percent of regional GDP.
19 Debt issuance processes and debt management and sustainability strategies are weak *only* in the Caribbean, and to a lesser extent in Central America. The Southern Cone has room for improvement in its debt issuance processes.

TABLE 4. Quality of public debt management

Subregion	Institutional model and governance	Macro-economic coordination	Strategy and sustainability	Office management and resources	Data and risk management	Issuance process and other activities
Andean region	4–5 (very high)	3–4 (high)	3–4 (high)	4–5 (very high)	4–5 (very high)	3–4 (high)
Southern Cone	4–5 (very high)	4–5 (very high)	4–5 (very high)	4–5 (very high)	3–4 (high)	2–3 (medium)
Central America	3–4 (high)	3–4 (high)	2–3 (medium)	4–5 (very high)	3–4 (high)	2–3 (medium)
Caribbean	3–4 (high)	3–4 (high)	0–1 (very low)	4–5 (very high)	3–4 (high)	0–1 (very low)
Average	3–4 (high)	3–4 (high)	2–3 (medium)	4–5 (very high)	3–4 (high)	2–3 (medium)

Notes: The Andean region includes Bolivia, Colombia, and Peru; the Southern Cone includes Argentina, Brazil, Chile, Paraguay, and Uruguay; Central America includes Belize, Costa Rica, El Salvador, Guatemala, Haiti, Honduras, Mexico, Nicaragua, Panama, and the Dominican Republic; and the Caribbean includes the Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago. The score is obtained from the index as follows:

0–1 (very low)	1–2 (low: NA)	2–3 (medium)	3–4 (high)	4–5 (very high)

Source: Chiara and Prats (2022).

1.6 Banking regulation and supervision

Seven Latin American countries, including the five largest economies (Argentina, Brazil, Chile, Colombia, and Mexico), have adopted or are on track to adopt Basel III standards (Figure 6 and Table 5).[20]

This regulatory framework strengthens the supervision of financial systems, establishes minimum capital and liquidity provision requirements, requires stress tests, and defines countercyclical capital buffers that can be used in case risks materialize.[21]

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20 These countries account for 81 percent of GDP and a large majority of banking assets in the region.

21 For further detail, see BIS (2023) and Bank of Spain (2023). Countercyclical capital buffers are capital requirements that are automatically increased during expansionary phases "to curb the development of systemic imbalances, raise solvency of institutions and thus improve the capacity to absorb this type of risk" and are released during contractionary phases "to help mitigate the negative impact of crises on the credit provisions to the real economy."

FIGURE 6. Implementation of the Basel standards

■ Basel III　■ Basel II　■ Basel I

Source: Fitch (2022).

TABLE 5. Implementation of the Basel standards and minimum capital requirements

	Basel regulatory framework	Minimum capital requirements (percentage of risk-weighted-assets)
Argentina	III	8
Bolivia	I	10
Brazil	II	8
Chile	II*	8
Colombia	I*	9
Costa Rica	II*	10
Ecuador	I	9
El Salvador	I	12
Honduras	I	10
Guatemala	I	10
Jamaica	I	10
Mexico	III	8
Nicaragua	II	10
Panama	II*	8
Paraguay	I	12
Peru	II	10
Dominican Republic	I	10
Uruguay	Hybrid	8

Notes: Countries with an asterisk are in the process of implementing Basel II and/or III. Countries that have implemented or are in the process of implementing this regulatory framework are labeled as Basel III. Uruguay is labeled as Basel II/Hybrid as it has a hybrid model that combines Basel II and III elements but has no plans to fully adopt Basel III.

Source: Fitch (2022).

2. Macroeconomic results

The remarkable progress in macroeconomic and financial management was reflected in the gradual achievement of positive macroeconomic results that consolidated in the 21st century.[22]

This century began with economic turbulence between 1998 and 2003—a period of financial and sovereign debt crises and severe economic collapses, especially in Argentina. This was followed by the commodities boom and strong capital inflows between 2004 and 2013, 10 years of brief economic buoyancy that were abruptly interrupted by the 2008–2009 global financial crisis.

In much less favorable external conditions, the region entered a stagnation period from 2014 to this day, which was worsened by the impact of the pandemic.

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22 Unless otherwise noted, this section uses simple averages to provide estimates for Latin America as a whole. Weighted estimates are noted and use GDP PPP weights.

Within this environment of strong fluctuations in the external conditions, the region made headways in multiple macroeconomic indicators, making these results even more impressive and showing the impact of improved macroeconomic management. This section analyzes progress in eight macroeconomic areas during the 21st century.

2.1 Reduction and convergence of inflation

After numerous countries recorded annual inflation rates above 100 percent during the 1980s and 1990s, inflation in Latin America declined sharply and has converged with global and United States inflation rates (Figure 7).

The pick-up of inflation in the region since mid-2021 took place against the backdrop of rising inflation in the US and the EU. And, although 2022 saw double-digit inflation levels in many countries in the region, it is widely acknowledged that central banks reacted swiftly and decisively, raising interest rates a year before the US Federal Reserve did. As a result, inflation is in the process of easing in many of the region's countries.[23]

FIGURE 7. Weighted annual inflation
(Percent)
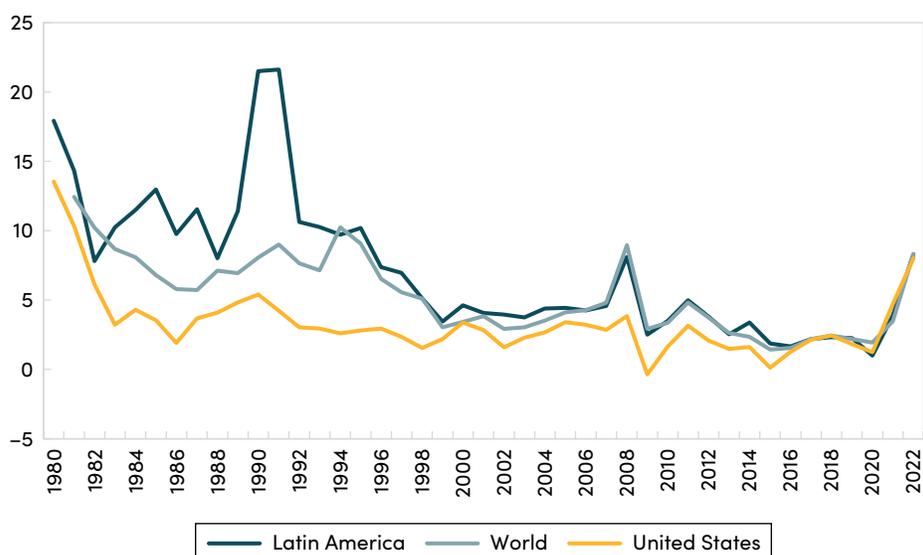
Source: World Bank (2023a).

2.2 Consolidation of fiscal deficits and moderation of public debt

According to IMF projections, and despite huge external shocks, Latin America continued decreasing fiscal imbalances. In fact, it is the only emerging region, together with Europe and East Asia, that is moving towards fiscal consolidation (Figure 8.1).

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23 Latin American Committee on Macroeconomic and Financial Issues (CLAAF) (2022).

The persistent moderation of fiscal deficits has led to the stabilization of public debt at its current levels, interrupting the upward trend that the region had shown in the previous decade (Figure 8.2).[24]
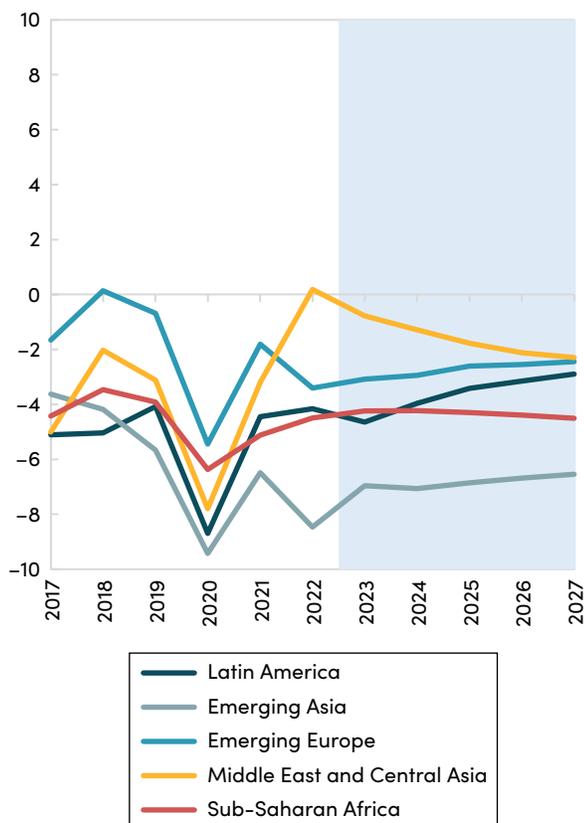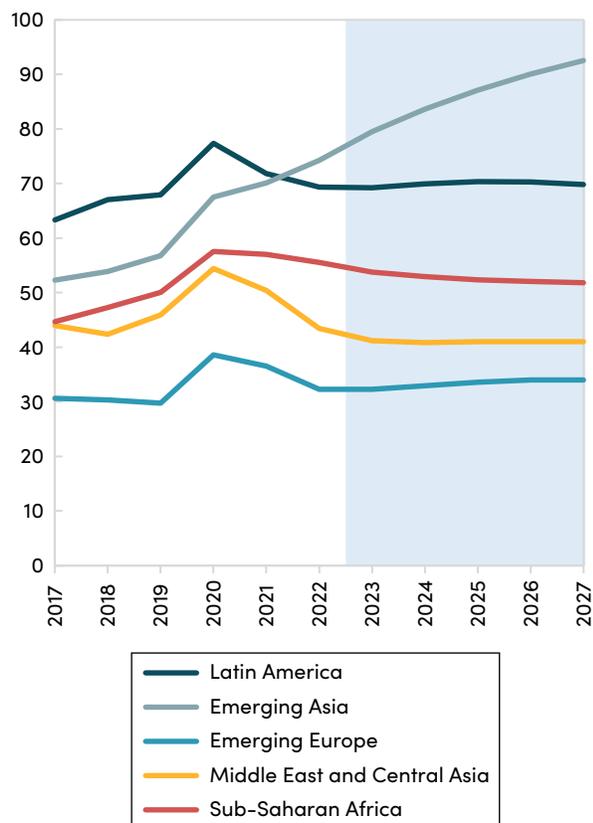
FIGURE 8.1. Fiscal balance
(Percentage of GDP)

FIGURE 8.2. Gross public debt
(Percentage of GDP)

Legend (both figures):
- Latin America
- Emerging Asia
- Emerging Europe
- Middle East and Central Asia
- Sub-Saharan Africa

Notes: Unlike other charts, this one uses the default IMF regions and not those of the World Bank. The main difference is in the grouping of Southeast Asian countries with those of East Asia and the Pacific and Central Asian countries with those of the Middle East rather than with Emerging Europe. This different categorization does not alter the conclusions.
Source: IMF (2022b).

2.3 De-dollarization of public debt

Public debt in foreign currency has declined and continues to show a downward trend, reducing external vulnerabilities.

On average, only 11 percent of the debt issuance in Latin America between 2017 and 2021 was made in foreign currency, well below other emerging regions (Figure 9.1).[25]

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24 Since current levels are still high, it is likely that the region will require a somewhat more ambitious fiscal consolidation than that anticipated in the IMF's projections.

25 As noted by the OECD (2022), higher foreign currency funding costs in 2021 drove higher issuance levels in local currencies.

Regarding debt stocks, the most systemically relevant countries in the region have very low foreign currency debt ratios, except Peru and Argentina (Figure 9.2).
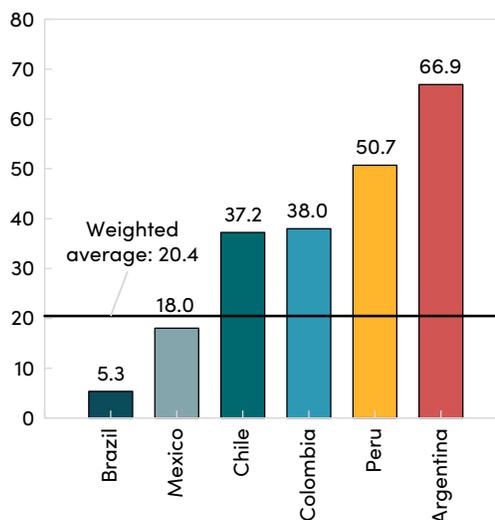
FIGURE 9.1. Public debt issuance in foreign currency by region, 2017–2021
(Percentage of total issuance, average)
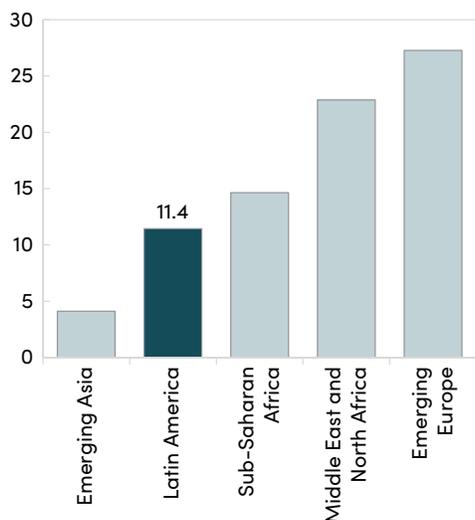
Note: Emerging Asia excludes China, and the categories are slightly different than other charts due OECD data limitations.
Source: OECD (2022).

FIGURE 9.2. Stock of public debt in foreign currency, 2022
(Percentage of total public debt)

Source: IIF (2023).

2.4 Improvement in the external debt maturity profile

The external debt profile has also improved substantially in recent years, preventing the concentration of short-term maturities.

Short-term external debt relative to total external debt has been steadily declining since the early 1980s (Figure 10.1). Today, short-term external debt represents only 11 percent of total external debt, less than half of the levels recorded in the early 1980s, immediately before the debt crisis and the "lost decade" in Latin America.

This has significantly reduced the risks associated with roll-over risk and has placed Latin America as the second emerging region with the lowest percentage of short-term external debt (Figure 10.2).[26]

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26 The OECD (2022) shows how Latin America's debt issuance has increasingly longer maturities. For example, in 2009 the average debt maturity was five years, while in 2019 and 2021 it increased to over seven years.

FIGURE 10.1. Short–term external debt in Latin America
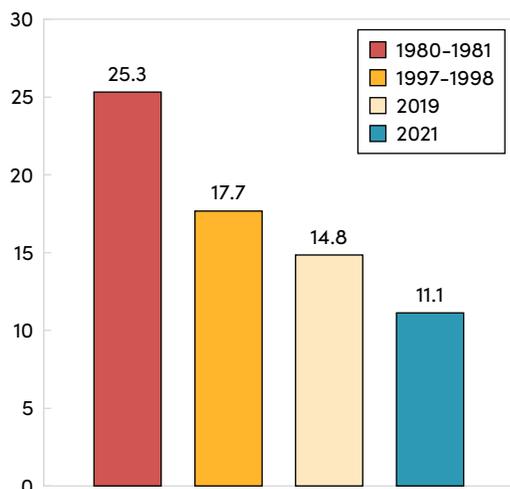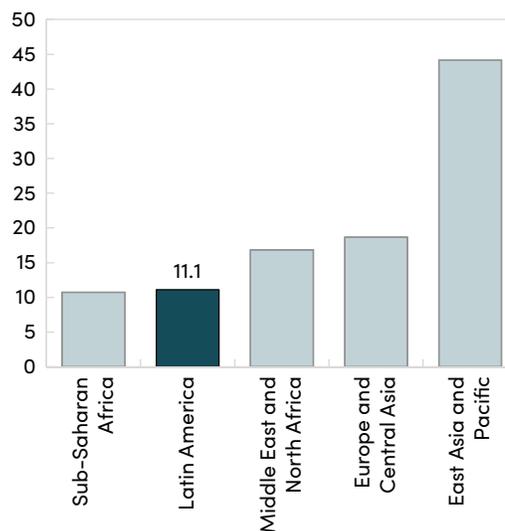*(Percentage of total debt)*

Legend:
- 1980–1981
- 1997–1998
- 2019
- 2021

Values: 25.3, 17.7, 14.8, 11.1

FIGURE 10.2. Short–term external debt by region, 2021
(Percentage of total public debt)

Regions: Sub-Saharan Africa, Latin America (11.1), Middle East and North Africa, Europe and Central Asia, East Asia and Pacific
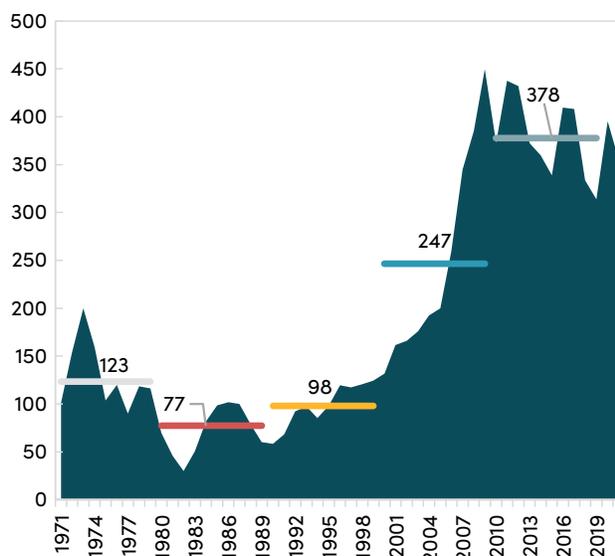
Source: World Bank (2022).

2.5 Historic accumulation of international reserves

Latin America's accumulation of international reserves over the past 20 years has been outstanding. Foreign currency reserves went from 50 percent of short-term external debt in the early 1990s (98 percent on average in the 1990s) to close to 400 percent in the present (Figure 11).

FIGURE 11. International reserves in Latin America
*(Percentage of total debt)*

Values shown: 123, 77, 98, 247, 378

Note: The horizontal lines show the average for the 1970s, 1980s, 1990s, 2000s and 2010s, respectively.
Source: World Bank (2022). See reserves and short-term debt.

Although this trend was observed in all emerging regions, Latin America's performance outshined others'. From being the emerging region with the second-lowest level of reserves compared to short-term external debt in the 1990s, it became the emerging region with the second-highest level of reserves, only behind the Middle East and North Africa, a region whose expansion is explained by the fact that it concentrates a large number of oil-producing countries (Figure 12).

FIGURE 12. International reserves by emerging regions
(Percentage of short–term debt)
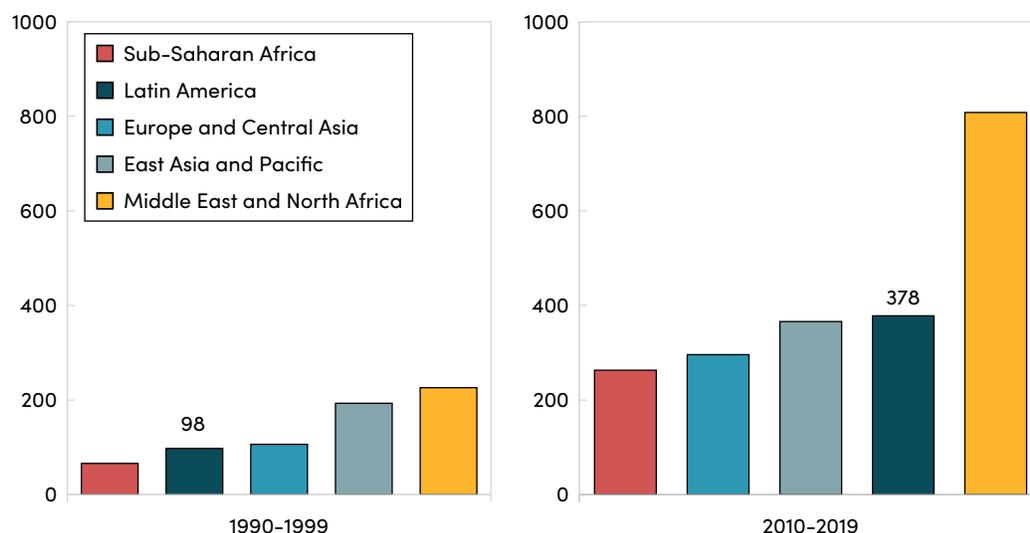
Source: World Bank (2022). See reserves and short-term debt.

The high level of reserves, together with the improved debt maturity profile (lower short-term debt), makes it possible to mitigate sudden interruptions in access to international capital markets, which, in the past, was a major crisis trigger for the region.

2.6 Credit risk improvements

Progress in macroeconomic management, stable inflation, fiscal consolidation, an improved debt maturity profile, high reserves level, and dollarization rates which, with the exceptions of Argentina and Peru, are below 50 percent, resulted in a generalized reduction in default risk as measured by the EMBI (Emerging Markets Bond Index) spreads.[27]

Although the Latin American EMBI spread as a whole is around 60 basis points over the global EMBI, the average spread of the main debt issuers in the region (Brazil, Chile, Colombia, Mexico, and Peru) is consistently (circa 100 basis points) below global EMBI (Figure 13).

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27 Emerging market bond index spreads (*Emerging Markets Bonds Index*, EMBI).

FIGURE 13. EMBI spread in Latin America and the Caribbean
(Basis points)

Legend: Latin America — Global — Average for Brazil, Chile, Colombia, Mexico and Peru
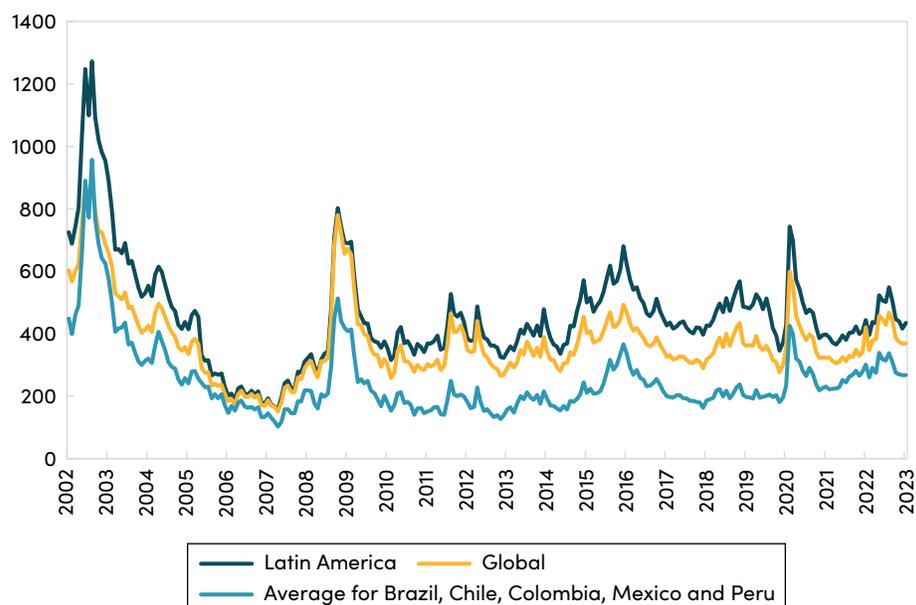
Source: J.P. Morgan (2023).

2.7 Expansion of banking systems and high levels of capitalization

In the last 20 years, domestic credit to the private sector in Latin America has risen from a modest 20 percent of GDP to 55 percent (Figure 14). Some countries, such as Brazil and Chile, have approached similar levels to those of Europe and Central Asia or East Asia and the Pacific.

FIGURE 14. Credit to the private sector in Latin America
(Percentage of GDP)
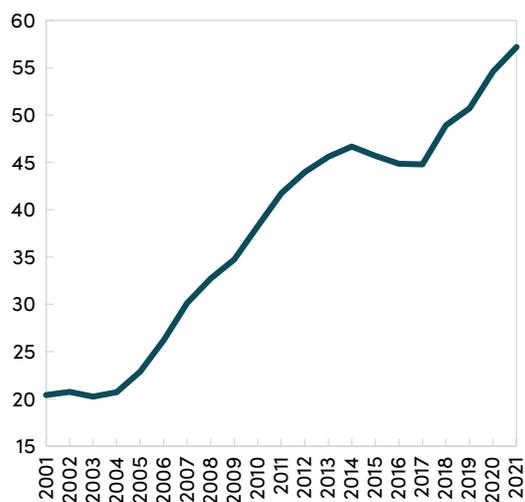
Source: World Bank (2023b).

This expansion of banking systems in the region took place in parallel with improved regulation and supervision and a significant increase in capitalization levels. All countries that adopted Basel III standards have capitalization levels well above the recommended minimum of eight percent of capital to risk-weighted assets (Figure 15.1) and in line with other emerging regions (Figure 15.2).

FIGURE 15.1. Capitalization levels, 2023
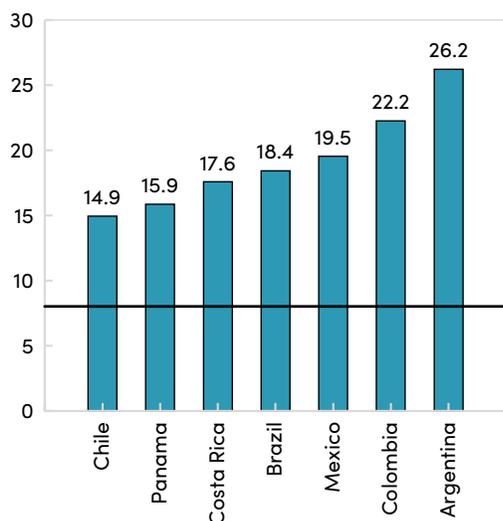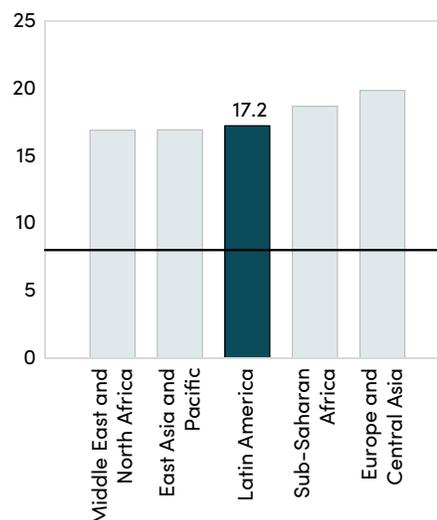*(Percentage of risk weighted assets)*

FIGURE 15.2. Capitalization levels in Basel III countries, 2023
(Percentage of risk weighted assets)

Note: East Asia and Pacific exclude China and countries in the process of adopting Basel III. The horizontal line represents the recommended minimum of 8 percent.
Source: IMF (2022b).

2.8 Lower crisis frequency

Between 1974 and 2003, a period which had four phases: two expansionary (1984–1981 and 1991–1997) and two contractionary (1982–1989 and 1998–2003), Latin America experienced a large number of currency, banking, and sovereign debt crises: a total of 108, or an average of about four crises per year. The region's crises accounted for nearly one third of the world's exchange rate, banking, and debt crises during this period and 42 percent of those crises in emerging and developing markets. Even more strikingly, Latin America had 73 percent of the total triple crises (when all three of these types of crises coincide in the same year or occur in consecutive years) during this period.

This trend has substantially moderated since 2004. While the incidence of these types of crises has decreased worldwide, the total crises in Latin America dropped from 108 to 12 between 2004 and 2018 and the average number of crises per year decreased four-fold from almost four to less than one.

During this same period, Latin America accounted for only 16 percent of global crises (one in six), and one in three of those that happened in emerging countries. The region did not experience any triple crises between 2004 and 2018 (Table 6).

TABLE 6. Exchange rate, banking, and sovereign debt crises

	1974–2003	2004–2018
Total crises	384	75
crises per year	13.2	5.4
double crises[(a)]	38	5
triple crises[(b)]	11	1
Emerging markets and developing economies crises (total)[(c)]	255	45
crises per year	8.8	3.2
double crises[(a)]	38	3
triple crises[(b)]	11	1
percentage of total global crises	66.4	60.0
Crises in Latin America	108	12
crises per year	3.7	0.9
double crises[(a)]	6	1
triple crises[(b)]	8	0
percentage of total global crises	28.1	16.0
percentage of total emerging markets and developing economies crises	42.4	26.7

Notes: Crises defined by their start dates and include systemic banking crises, currency crises, and sovereign debt crises. (a) double crises occur when two of the three crisis types happen in the same year or in consecutive years and (b) triple crises when all three crisis types occur in the same year or consecutive years, (c) Excluding Latin America.
Source: Laeven and Valencia (2018).

3. Convergence and development[28]

3.1 Convergence in emerging economies

Since the late 1990s, emerging markets' GDP per capita has increased thanks to a remarkable economic convergence that has no precedent in the post-World War II era. Figure 16 illustrates the per capita income, adjusted for purchasing power parity (PPP), of emerging economies compared to that of the United States.

While the relative average income level of emerging economies remains low compared to the United States (below 20 percent), it has almost doubled since the late 1990s. If this rapid convergence path is maintained, the relative income of the average citizen in emerging economies would converge with that of the average American citizen in approximately three generations.

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28 Based on Talvi (2016).

FIGURE 16. Convergence in emerging economies
(Percentage of US GDP per capita, PPP in constant 2021 dollars)
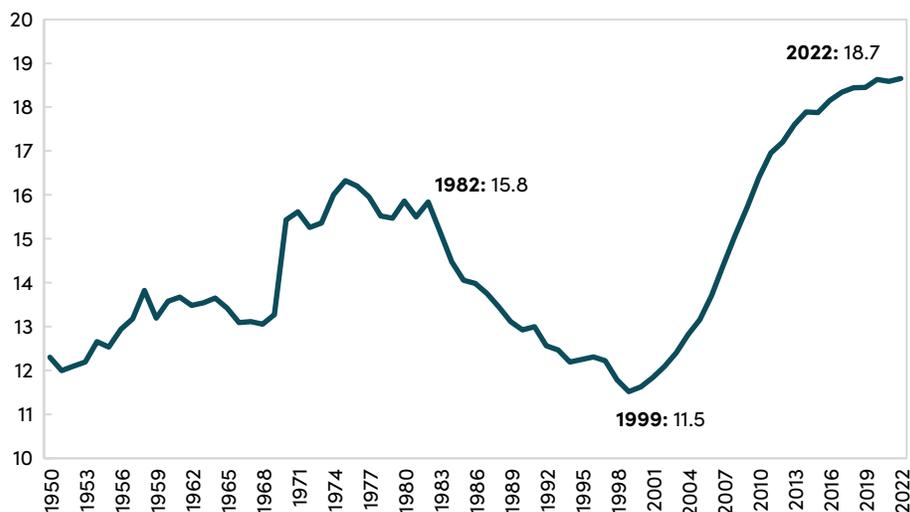
Note: Weighted by PPP GDP, as are all charts in this section unless otherwise noted.
*Source:* Conference Board (2023).

This, of course, had a profound impact on the wellbeing of millions of citizens in emerging economies. More than 700 million people were lifted out of poverty and extreme poverty, leading to the emergence of the middle class, which grew by 150 million people annually. But there are more nuances to this story.

If we exclude China and India from the sample of emerging economies, Figure 16 becomes panel A in Figure 17, where a similar convergence began to emerge in the late 1990s. However, this brief period of convergence was far from significant—relative income remained well below previous peaks—and it occurred after a sharper period of divergence that started in the mid-1970s following the oil crisis. Convergence stalled and regressed from 2013 onward. This pattern of relative income is characteristic in all regions except for Emerging Asia (panels A–F). Latin America, sub-Saharan Africa, the Middle East and North Africa, and Emerging Europe exhibit a similar pattern to that of panel A, albeit with different scales. Emerging Asia is the only region that has sustained a process of convergence. China and India have engaged in an exponential convergence since the late 1990s (panels G–H), while the rest of Emerging Asia has experienced a continuous, though slower, period of convergence since the mid-1960s, affected by the late 1990s financial crisis.

FIGURE 17. Convergence in emerging economies, by region
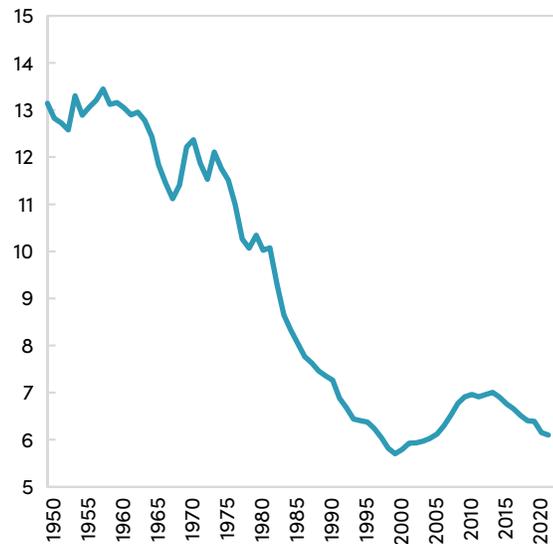*(Percentage of US GDP per capita, PPP in constant 2021 dollars)*

**Panel A: Emerging economies
(Excluding China and India)**
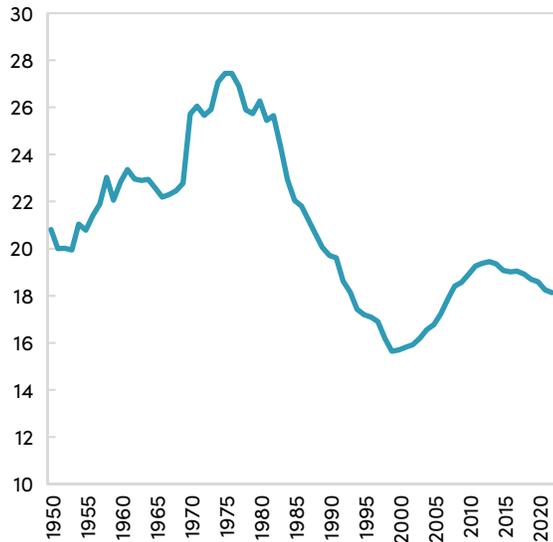
Panel B: Latin America

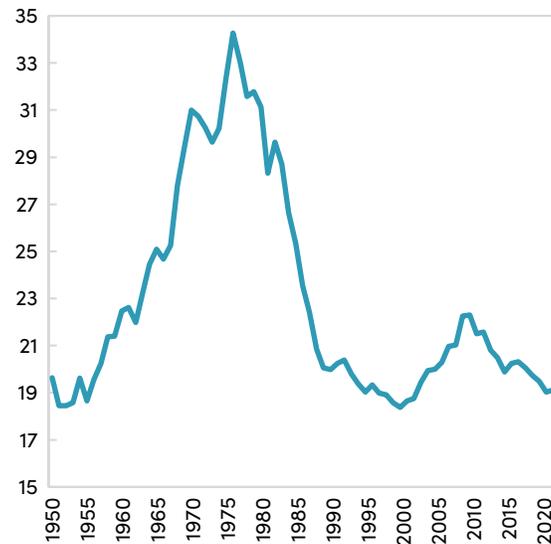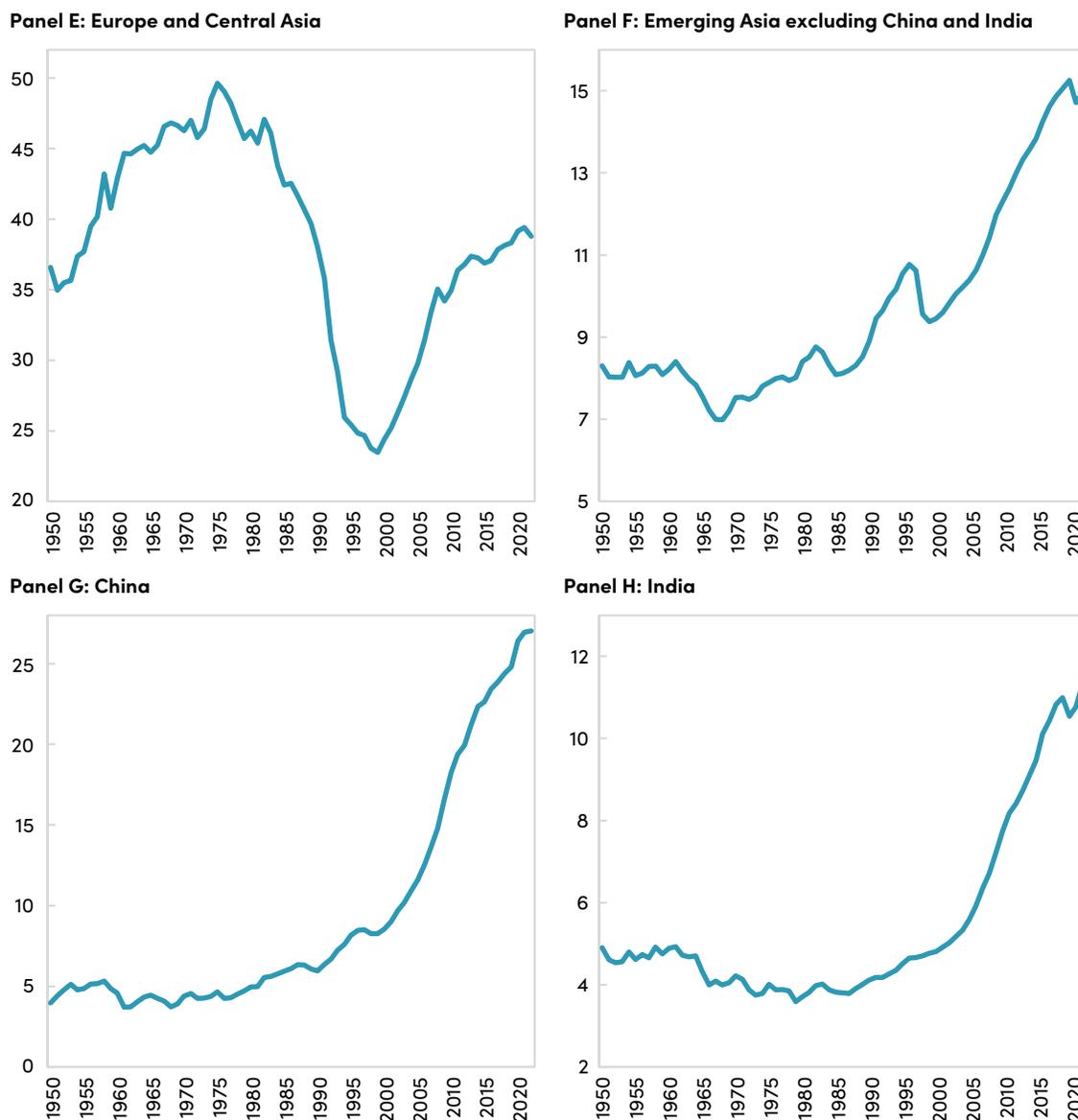**Panel C: Sub-Saharan Africa**

Panel D: Middle East and North Africa

FIGURE 17. (Continued)

Panel E: Europe and Central Asia

Panel F: Emerging Asia excluding China and India

Panel G: China

Panel H: India

Note: Results for Latin America are consistent when excluding outliers like Argentina and Venezuela, albeit the starting GDP per capita level is lower.
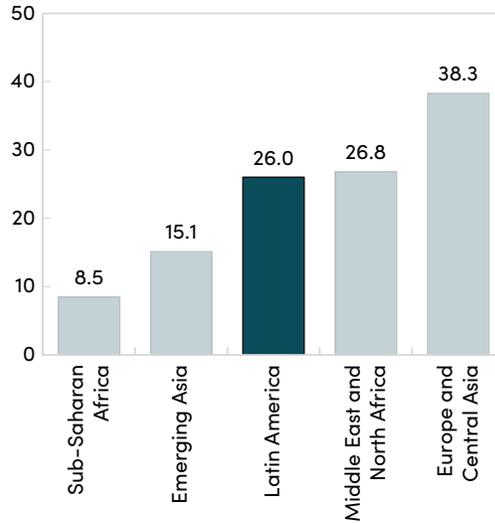*Source:* Conference Board (2023).

The exponential convergence is almost exclusive to China and India. Since China and India represent 37 percent of the world's population and 43 percent of the population of emerging economies, this is of course an event of enormous proportions. However, it does not suffice to tell the entire story of emerging economies as a group.

The Latin American tale is much different. Despite the remarkable growth in China and India's relative GDP per capita, and to a much lesser extent in emerging Asia, in 2019, before the pandemic, Latin America's relative GDP per capita was higher than that of China, India, and Emerging Asia.

It ranked among the highest in emerging regions, trailing only behind Emerging Europe and the oil-rich region of the Middle East and North Africa (Figure 18).

FIGURE 18. Convergence in emerging economies, 2019
(Percentage of US GDP per capita, PPP in constant 2021 dollars)

Source: Conference Board (2023).

When incorporating other development indicators, like those captured by the Human Development Index, Latin America rises to the second position amongst best-performing emerging markets, trailing only behind Emerging Europe. Both are the only emerging regions included in the high human development category (Figure 19).

FIGURE 19. Human Development Index, 2021
(Index from 0 to 1)
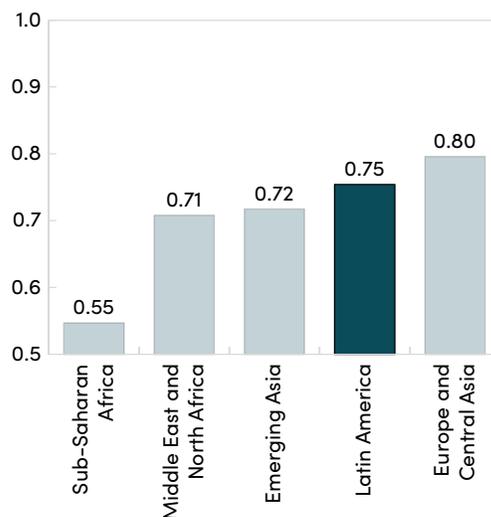
Source: United Nations (2023).

3.2 Asian miracles' growth and convergence

To more precisely define convergence, we need to establish a start and an endpoint. For the purposes of this report, convergence is defined as a process in which a country's per capita income begins at a level equal to or lower than one third of US per capita income at any time since 1950 and reaches a level equal to or greater than two thirds of US per capita income.[29]

According to this definition, the development miracles that have achieved convergence with US per capita income levels since 1950 comprise only 3 percent of the emerging countries as per the current classification in the International Monetary Fund's World Economic Outlook. Only five economies achieved this feat: Japan, South Korea, Taiwan, Hong Kong, and Singapore. They initiated the convergence process from levels ranging between 10 percent and 29 percent of US per capita income (South Korea and Hong Kong, respectively) and took between 16 and 44 years to converge (Singapore and South Korea, respectively) to reach the goal. Average per capita income growth rates varied from a minimum of 6.1 percent annually in Hong Kong to a maximum of 8.5 percent annually in Japan during the convergence period (Table 7).

TABLE 7. Growth and convergence during the Asian miracle

	Year when convergence began	Year when convergence was achieved	Years it took to converge	Relative income in the year convergence began (as percentage of US income)	Relative income in 2022 (as percentage of US income)	Annual GDP per capita growth during convergence (in percent)
Hong Kong	1967	1987	20	29	93	6.1
Japan	1950	1970	20	21	65	8.5
Singapore	1965	1981	16	25	164	8.1
South Korea	1966	2010	44	10	70	6.3
Taiwan	1967	2006	39	14	91	6.1

Source: Talvi (2016).

Convergence towards the levels of per capita income of wealthy countries is an extraordinarily rare occurrence. Labeling Latin America—or any other emerging region—an economic failure when comparing it to a virtually impossible benchmark is, at the very least, using an inaccurate metric to define success.

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29 One third and two thirds of US per capita income represent the mean minus one standard deviation and the mean plus one standard deviation of the per capita income distribution of all the countries in our sample compared to the US in 2021, respectively. In its income categories, the World Bank employs a different, much less stringent, definition of high-income countries. The World Bank's threshold for defining a high-income country is a gross national income per capita of 13,589 US dollars, which is equivalent to 20 percent of the gross national income per capita of the US.

3.3 The growth challenge

Looking ahead, the challenge for Latin America does not lie in macroeconomic management. As previously analyzed, the region has made significant progress in numerous dimensions of macroeconomic management, which yielded high returns.

Regarding convergence towards the per capita income levels of rich countries, it is more of an aspiration than a realistic economic policy target. Only a handful of Asian economies have achieved this.

After a decade where per capita income has been stagnant, Latin America's challenge is to reignite growth (Figure 20). The prolonged absence of growth inevitably leads to a distributive competition for limited resources—which fuels social tensions and diverts valuable resources that, instead of being concentrated on achieving growth objectives, are used to neutralize these tensions.

FIGURE 20. GDP per capita in Latin America
(2015 constant PPP dollars)
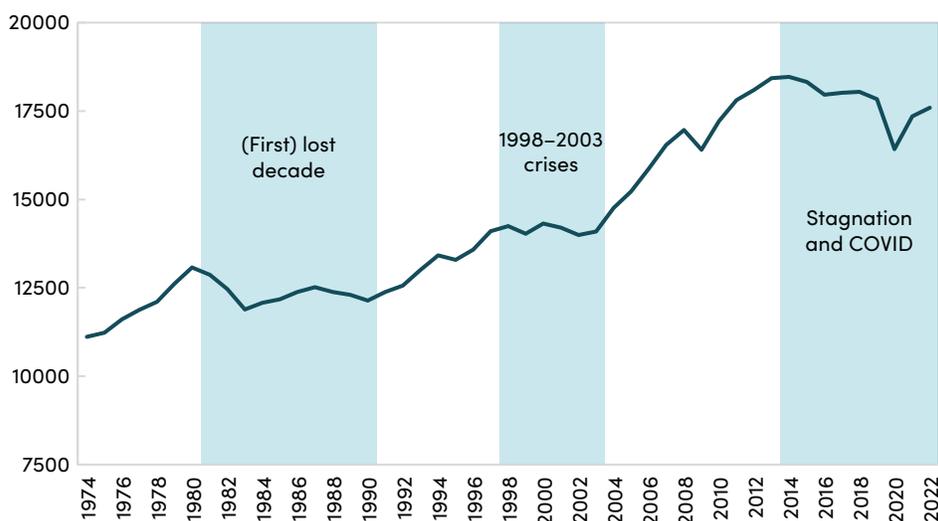
Note: The blue areas indicate periods of economic crisis or stagnation.
Source: World Bank (2023).

Since the mid-1970s, the region only managed to grow at a high rate during periods of extremely favorable external conditions, characterized by high prices of the commodities that Latin America produces and exports and significant influx of foreign capital that boosted growth.[30] When the external context became unfavorable, there were periods of significant declines in growth and stagnation. Due to the lack of significant progress in terms of growth drivers, the region's outcomes have been mediocre since the early 1980s.

30 See Izquierdo, Romero and Talvi (2007).

3.4 The golden decade: 2004 to 2013

To illustrate the previous point, we analyze the "golden decade" when, driven by what has come to be known as the commodities boom, Latin America's growth rates exceeded five percent annually. During this period, the region experienced a turning point after 25 years of relative income decline (Figure 17, panel B). This raised expectations that Latin America would finally embark on the path of convergence. However, this was not the case, and warning signs were evident.

This decade of extremely high growth rates was not accompanied by similar advancements in key growth determinants, factors that have shown to have a positive effect on growth: trade integration, physical and technological infrastructure, human capital, innovation, and the quality of public services.[31]

In stark contrast to the favorable evolution of relative income during the golden decade, Latin America failed to make progress in improving growth drivers compared to advanced economies. The overall growth drivers index—the simple average of five sub-indices—remained unchanged during the golden decade (Figure 21).

FIGURE 21. Evolution of relative income and growth drivers in Latin America
(Index 2004=100, percentage of US GDP per capita, and percentage of advanced countries indices)
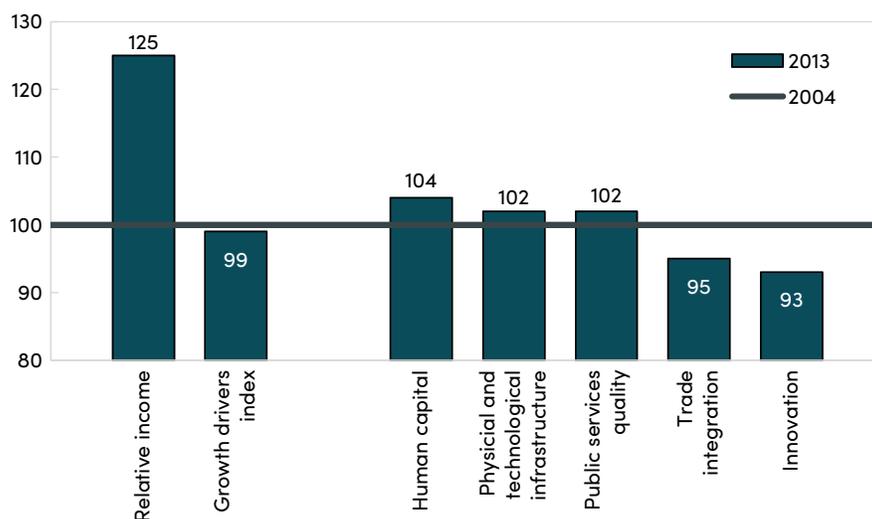

Source: Talvi (2016).

Something similar occurred with export sophistication, which the Harvard Growth Lab uses as an indicator to predict future growth. During the golden decade, the region also failed to make significant advancements in the sophistication of its export matrix (Figure 22).

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31 See Barro (1991). For a comprehensive review of cross-country growth regressions, refer to Durlauf and Quah (1999) and Durlauf, Johnson, and Temple (2005).

FIGURE 22. Evolution of relative income and export sophistication in Latin America
*(Index: 2004=100; percentage of US GDP per capita and percentage
of export sophistication in advanced economies)*
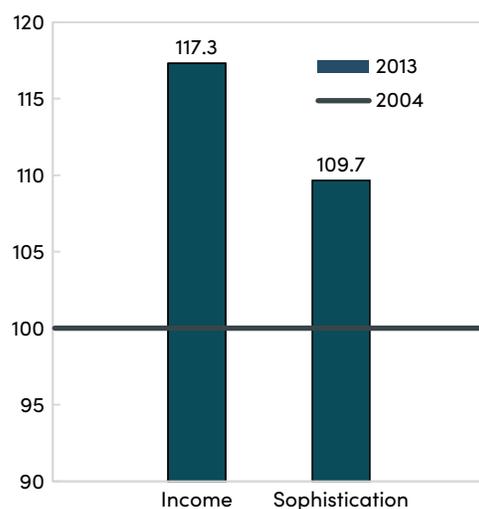
Note: Relative income numbers differ from the previous chart due to different sources.
Sources: Harvard (2023) and Conference Board (2023).

4. Looking forward

In order to achieve sustained growth, Latin America needs to redouble efforts to deepen integration with the global and intraregional economy, which will enhance human capital, the pace of innovation, the quality of public services, and, finally, modernize physical and technological infrastructure. All of these improvements are necessary to revitalize growth and finally reduce the region's excessive reliance and dependence on favorable external factors.

Despite these substantial-sounding challenges, there are plenty of reasons for optimism—Latin America has laid solid foundations to drive growth.

First, democracy has consolidated throughout most of the region, and an entire generation has grown up seeing elections as the only legitimate means of choosing a government. In terms of democratic development, Latin America ranks at the top among emerging regions.

Second, a significant group of key countries in Latin America has achieved remarkable macroeconomic outcomes. A whole generation has already grown up with low and relatively stable inflation, reasonably sound public finances, and less frequent crises. Furthermore, banking system regulation and supervision have significantly improved in recent years, and Latin America now has robust financial systems.

Third, the region could be close to achieving deeper economic integration with the European Union. As shown in the section on opportunities in the new context of the Elcano report "Why Latin America Matters," many Latin American countries already have free trade agreements (FTAs) with the EU and, if the EU-Mercosur Association Agreement is ultimately ratified, the EU would have FTAs with countries representing 94 percent of the region's GDP.

If these countries were able to connect their existing bilateral trade agreements with the EU—by harmonizing standards, rules of origin, and customs procedures, for example—an immense economic space could emerge: a partnership between the EU and Latin America would encompass 1.1 billion people with a total GDP exceeding 22 trillion dollars, similar to the US economy and surpassing that of China.

If such a partnership were to materialize, there could be enormous mutual benefits. The economies of the EU and Latin America complement each other. Latin America possesses abundant energy and mineral resources: sun, wind, water, and fertile land, while the EU can provide the region with the capital, technology, and knowledge needed to enhance the complexity of Latin America's export matrix. If this agreement comes to fruition, Latin America's development path could resemble that of Spain and Portugal more than the Asian miracles. In Spain and Portugal, democratization came first, followed by economic integration (with the EU), and, finally, inclusive and sustainable development.