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World Bank: Recession Has Hurt Poor in Latin America Disproportionately

by LADB Staff
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Economic stagnation and the decline in average living standards throughout Latin America have raised questions about the impact on the poor. In a recent research paper, World Bank economist Guy Pfeffermann has attempted to answer the following questions: Have the poor been forced to bear a disproportionate share of the burden? What has been happening to their wages, employment, and access to social services? What are the best ways of easing their hardships?

Pfeffermann reviewed papers prepared by Bank missions to five Latin American countries - Argentina, Brazil, Chile, Costa Rica and Mexico accounting for 260 million of the 400 million people in the region. He also reviewed data for other countries in the region. His results can be summarized as follows: the depression wreaked economic havoc on the poor - havoc unlikely to reverse even with an early revival of rapid economic growth. Between World War II and 1980 Latin America was one of the fastest growing regions in the world. Regional growth was assisted by a buoyant world economy, reasonably strong demand for primary commodities (75% of its exports), and low real interest rates.

The distribution of income remained highly skewed in all but a few countries of the region, but the poorest two-fifths of the population saw living standards rise at roughly the same rate as the whole of the population. Life expectancy at birth rose to 64 years, not far short of the average for middle income Europe. The vast majority of children began attending school. The second oil shock of 1980 turned the tide of progress with a global recession, a collapse of commodity prices, and skyrocketing interest rates. The demand for oil fell, and later so did prices, seriously affecting oil exporters in the region. Interest payments became a huge drain on export earnings and savings.

After 1982 the region began transferring 25% to 30% of its exports of goods and services to creditor nations. The result of all this was a sharp drop in output. Per capita GDP in Latin America and the Caribbean declined by 11% between 1981 and 1983. Per capita consumption fell even more steeply, owing to heavy debt servicing and deteriorating terms of trade. There was some recovery after 1983, but only Brazil, Colombia and Panama have regained pre-crisis levels of per capita GDP.

The capital outflow had a disastrous impact on new investment. For the region as a whole, gross investment fell by one-third between 1981 and 1984. In Argentina, it declined from an average of 20% of GDP in 1971-1981 to 12.6% in 1985. Investment net of depreciation was lower still. The reality behind these numbers is a progressive deterioration of capital every kind roads, schools, hospitals, factories, sewer systems. If unchecked, this deterioration, not always immediately visible, can have grave long-term consequences. None of these statistics, however, can capture the psychological impact of the depression.

Earlier, even the poorest families had hope of a better futuree, hope now fading in many Latin American countries. The numbers on employment, though unreliable for many countries, show...
that depression led to rising unemployment almost everywhere. Argentina was the only country where unemployment remained relatively low (4.5% in Buenos Aires and 6% in other cities.) The unemployment rate in Brazil went up from a low of 2.3% in 1978 to 7.1% in 1984. It fell in the next two years as the economy revived.

There was a similar cycle in Costa Rica. Chile had the worst unemployment rate in the region, rising from 10% in 1980 to 19.6% in 1981 before declining to 13% in the last quarter of 1985. Unemployment among the poorest two-fifths of the population was almost twice the national rate. The government established make-work programs to alleviate poverty, and these programs employed 13% of the labor force at their peak in 1983. Without them the unemployment rate would have been far higher.

In Mexico, open unemployment went up from 2.7 million in 1981 to 4.6 million in 1984. Since 1982 the formal sector has not created a single job (in net terms) while teenagers are entering the labor market at the rate of 700,000 a year. The depression also changed the structure of employment in the region. Urban jobs (especially in construction) suffered most, while agricultural employment revived. Inducing these changes were sharp devaluations and a relaxation of agricultural price controls. (The share of agriculture in GDP rose, as did the terms of trade for farmers). In the early 1980s, real wages fell steeply in most countries of the region, but later retraced some of their losses in some countries. A big jump in food prices meant that real wages fell especially fast for the poorest rural laborers and some of the urban poor who devote most of their income to food.

In Brazil rural laborers' earnings peaked in 1980 and then fell by a third through 1985. Such laborers account for 40% of rural households and 15% of all households. In Chile full wage indexation set a floor to wage settlements and helps explain why real wages (in the formal sector at any rate) rose between 1979 and 1982. Very high unemployment was one outcome. Indexation was then abandoned and real wages declined 13% in the next two years.

Blue collar workers suffered more than white collar ones. Costa Rica was a special case, where foreign aid came to the rescue. Real wages fell 40% between 1979 and 1982, but massive infusions of assistance from the United States and other donors helped incomes to recover subsequently. Mexico had a traumatic time, with real wages falling 28% between 1981 and 1983, followed by a further slight drop in 1984. The decline was the greatest (31%) for agricultural workers. (See: Guy P. Pfeffermann, "Poverty in Latin America: The Impact of Depression," World Bank Publication, 1987; and, "Public Expenditure in Latin America," World Bank Discussion Paper No. 5, 1987. For a different view on this topic in the Mexican case, see Peter Gregory, The Myth of Market Failure: Employment and the Labor Market in Mexico (Baltimore: Johns Hopkins University Press, 1986.)

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