WG2. The Impact of the Global Economic Crisis on the Americas
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The Social and Political Consequences of the International Financial Crisis in Latin America

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The latest international financial crises began with the collapse of the mortgage market in the United States in 2007, expanding first to investment markets and subsequently to the real side of the economy. Turmoil in financial markets led to a marked decline in levels of consumption, investment and growth expectations. Although the epicenter of the crisis has been in the advanced industrial economies of North America and Europe, Latin American countries began to feel its adverse effects in 2009. In particular, the effects of the global financial and economic crisis reached Latin America and the Caribbean through three main mechanisms: a decline in the price of commodities and its resulting impact on export revenues, the irregular access to credit markets, and the interruption in foreign capital inflows.

These mechanisms, however, have affected individual countries in the region in different ways and to varying extents. Mexico, Central American and Caribbean countries have been more severely hit, given their close economic links with the United States, which not only include trade in goods and services but also important migration and remittances flows. The economies in Central America and the Caribbean were also severely hit by the collapse in tourism flows. South American countries, on the other hand, have been more affected by the decline in commodity prices and export opportunities, which translated into higher unemployment levels and slower rates of growth. After several years of expansion, 2009 saw many Latin American countries, including Mexico and Brazil, experiencing negative growth. Yet, in contrast to previous episodes of international crisis, Latin American countries experienced a quick rebound from the recent global downturn. Average growth rates, which had fallen to -1.7% in 2009, reached 5.7% in 2010.

Much has been written about the economic causes and consequences of the international financial crisis for emerging economies and developing countries. Less attention has been paid to the social and political implications of these economic shocks. This paper seeks to take a step in this direction by focusing on the Latin American economies. An economic crisis of this magnitude typically generates high levels of uncertainty, weakening consumers' and investors' confidence and increasing social demands on the state. Growing pressures on political actors in a context of limited resources may weaken the legitimacy of institutions in democratic systems. How have Latin American governments responded to the political and social dimensions of the global economic crisis? To what extent and in what ways has the crisis affected the stability of democratic governance in the region?

Socioeconomic and Political Effects of the International Financial Crisis

The macroeconomic effects of external financial shocks tend to be accompanied by important socioeconomic problems. Economic contractions resulting from a fall in exports, for example, lead to falling employment levels and temporary increases in income poverty. Slower growth and unemployment in the export-oriented sector may also have consequences on the distribution of income, deepening the severe problem of inequality in Latin American economies.

The deterioration in socioeconomic variables typically has political consequences, potentially increasing social tensions and deepening political and class cleavages. Despite declining fiscal revenues, governments confront growing social pressures and demands for compensation from those groups that are more severely affected by the crisis. This is particularly problematic in those countries in which the state is weak and constrained in its financial and technical resources. Governments' inability to respond to citizens' demands may result in an erosion of support for democratic institutions. At the same time, the limited availability of resources may lead to increased competition and tension among social groups, which may result in deepening cleavages between capital and labor, and/or urban and rural sectors. Finally, the effects of the crisis may create conflict among different levels of government, as national, state, and local authorities compete for limited fiscal resources.

The crisis may end up having international political consequences as well. If governments in developing countries are unable to confront its economic effects on their own, they may be forced to resort to international financial institutions and other donor governments for external support. In the case of many Latin American governments, this would be seen as a significant step backward, given their emphasis on national autonomy and their rejection of so-called "neoliberal" economic principles.

External Shock	Macroeconomic Effects	Socioeconomic Effects	Potential Political Consequences
Decline in prices of commodities Decline in remittances flows Instability in and limited access to foreign capital markets	Contraction of exports Decline in capital inflows Decline in fiscal revenues Deterioration of the current account Reduction in consumption and investment expenditures Higher interest rates Exchange rate instability	Increase in unemployment rates Reduction in disposable income levels Increase in poverty and inequality Increase in crime and insecurity	Increase in social tensions Growing demands for social compensation Growing politicization regarding tax system Emerging/deepening of class cleavages (capital/labor or urban/rural) Greater state intervention Political instability and electoral changes Decrease in support for democratic institutions

Table 1: Macroeconomic, Socioeconomic and Political Effects of External Shocks
Source: Author's work based on OAS (2009)

a) Unemployment levels

The labor market is one of the main transmission mechanisms between economic contraction and household incomes and poverty levels. Falling demand for labor results in increasing unemployment, declining real wages, and a worsening of working conditions. The latest financial crisis had a negative but relatively moderate effect on the evolution of labor markets in Latin America. In fact, it reversed albeit temporarily, the significant progress achieved in previous years. Between 2004 and 2008, unemployment in Latin America had fallen from 11% to 7.4% (ILO, 2011). In the first half of 2009, unemployment increased more than 1%. However, both economic activity and employment levels experienced a rapid rebound in 2010. Income per capita rose by 4.8% while unemployment levels fell back to around 7.7% in 2010.

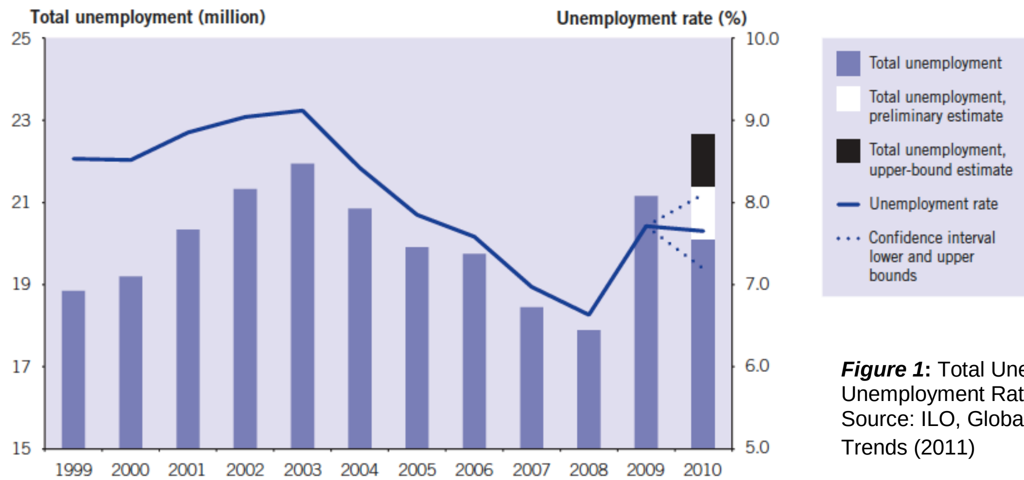

Figure 1: Total Unemployment and Unemployment Rate, 1999-2010
Source: ILO, Global Unemployment Trends (2011)

Yet, there are important differences across countries and among different types of workers. Wage earning workers in Brazil and Chile and all kinds of workers in Mexico seem to be the most severely hit by the crisis (Freije and Murrugarra, 2009). Indeed, total unemployment seems to have increased by less than 2 percentage points in the other four largest Latin American economies, namely Argentina, Brazil, Colombia, and Peru (Ferreira and Schady, 2009). Evidence indicates that the decline in real wages in the manufacturing sector was also moderate for 2008-2009.

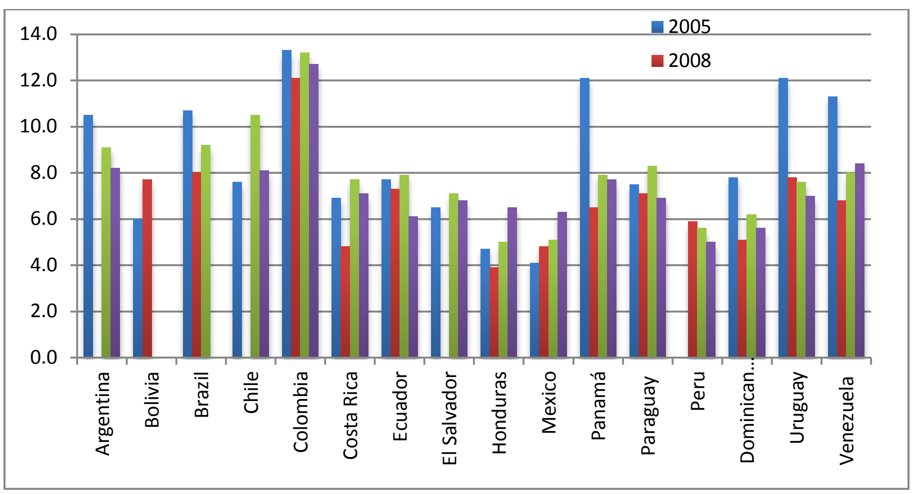

Figure 2: Unemployment Rates, 2005-2010
Source: Prepared by author based on data from ECLAC (2011)

b) Poverty Reduction

The Latin American region had made significant progress in terms of poverty reduction in the years leading up to the crisis. Between 2002 and 2007, the number of people living in poverty fell by almost 10 percentage points. In this context, the crisis had only a moderate effect, decreasing the rate of poverty reduction (See Table 2). The percentage of people living in poverty fell only slightly, from 33.2% in 2008 to 33% in 2009. The declining trend continued in 2010, with poverty level falling to 31.4% and extreme poverty falling almost 1 percentage point relative to 2009 (ECLAC, 2011).

Year	Poverty level (%)
1980	40.5
1986	43.3

1990	48.4
1994	45.8
1997	43.5
1999	43.8
2002	43.9
2005	39.7
2006	36.2
2007	34.0
2008	33.2
2009	33.0
2010	31.4

Table 2: Poverty levels in Latin America, 1980-2010*
Source: ECLAC (2011)
*Percentage of people living under the national poverty line. Average for 18 countries in the region plus Haiti.

The available data also shows that there are important differences across countries. Five out of twelve countries considered in Table 2 (Peru, Ecuador, Argentina, Uruguay, and Colombia) experienced significant reductions (between -1.4 and -3.5) in poverty rates in 2010. Only Honduras and Mexico exhibited significant increases in poverty levels, of 1.7 and 1.5 percentage points, respectively (ECLAC, 2011).

c) Inequality

Some effects of economic crises may work to deepen inequality. First, less qualified workers, and self-employed workers tend to be more vulnerable to shifts in the economic cycle. Many of these are employed in the construction sector, which was particularly hit by the crisis. Second, the increase in the price of foodstuffs also has a distributional impact, harming primarily the poor. Nevertheless, the positive trend observed in the past decade was not significantly altered by the international financial crisis. Up to 2008, the gini coefficient fell at a rate of 1% per year in more than 10 Latin American countries. The data for 2010, moreover, shows that inequality did not increase substantially in any of the 11 countries for which information is available. In three countries, Mexico, Venezuela and Uruguay, indeed, the gini coefficient fell by 2%, while in two others (El Salvador and Peru), it decreased by 1% (ECLAC, 2011).

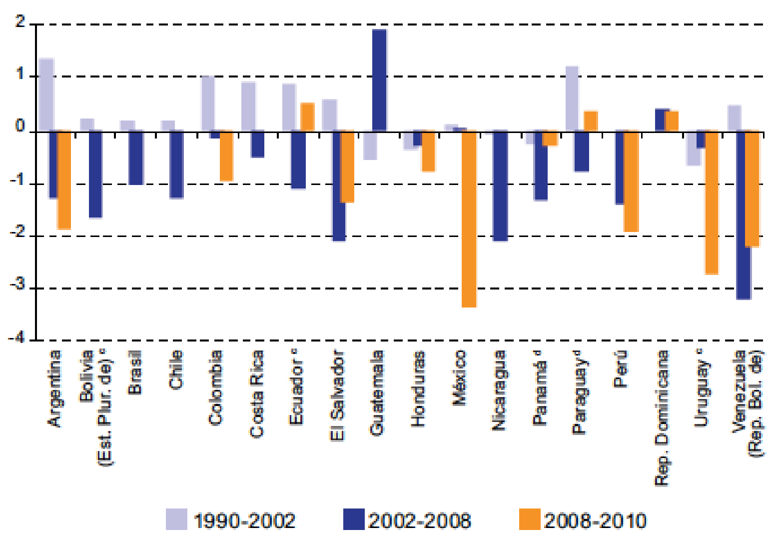

Figure 3: Evolution in Gini Coefficient, Latin America
Source: ECLAC (2011)

Some analysts have claimed that the crisis may also have adverse effects in terms of gender inequality. Indeed, economic crises tend to have a stronger impact on the most vulnerable groups in society, namely, women, children, and minority groups. These social groups have traditionally been particularly vulnerable in Latin America. Labor market conditions for women are usually more precarious and less stable than for their male counterparts, which make them more vulnerable to the fall in demand and wages experienced in a crisis.

Selected Fiscal and Social Policy Responses to the Crisis

Overall, therefore, the socioeconomic effects of the crisis have been moderate for most of Latin America. To what extent has this been the result of the ways in which governments responded to the crisis? While it is difficult to attribute direct causality, several countries in the region implemented a series of fiscal and social emergency measures to counter the adverse effects of the crisis. First, the main economies in Latin America introduced fiscal stimulus packages, consisting of additional expenditures aimed at sustaining aggregate demand. In addition, several governments implemented emergency social measures to protect the incomes of the poor, including direct support to labor demand, subsidies, and unemployment insurance. Some governments have also launched public works in infrastructure to compensate at least partly for the slowdown in the construction sector. Even before the crisis, for example, Brazil introduced the Growth Acceleration Program (PAC), which represented 2.6% of GDP.

There are considerable differences in the design, scope and cost of the programs implemented by each country. Some governments decided to expand existing anti-poverty programs, such as the Bolsa Familia in Brazil and Familias en Accion in Colombia. Others, like Chile, improved and expanded the coverage of unemployment insurance schemes that had been introduced in response to previous crises. Uruguay also introduced a series of reforms along these lines. In February 2009, the government relaxed requirements for claiming benefits for all workers and increased the minimum and maximum subsidies. Pension and retirement programs were also reformed in both countries.

Country	Total Fiscal Stimulus Package	Social Measures
Argentina	\$4.4 billion 1.27% of GDP	1) Subsidy of 10% of labor cost for 12 months, extendable by further 12 months 2) Promotion of worker formalization (through incentives) 3) Plan to create 100,000 jobs
Brazil	\$8.67 billion 0.5% of GDP	1) Increase in Bolsa Familia transfer amount 2) Expansion of Social Program Bolsa Familia to an additional 1.3 million families 3) Extension of unemployment insurance for fired workers from December 2008
Chile	\$4bn 2.2% of GDP	1) Employment subsidy for low-wage young workers and additional cash transfers to low income households. 2) Extension of unemployment solidarity fund to provide access to all unemployed workers.
Colombia	n/a	1) Increase in government investment in public works 2) Increase in number of families by Familias en Accion by 1.5 million 3) 42% expansion in social programs
Mexico	\$13.3bn 1.49% of GDP	1) The temporary employment program at the federal level was expanded by 40% over what had been planned, bringing it up to US\$ 160 million in 2009. 2) US\$ 140 million earmarked under the Employment Preservation Program for protecting employment in vulnerable businesses. 3) Support to unemployed urban workers (US\$110 per month) for a period of four to six months through the Urban Temporary Employment Program.
Peru	US\$4 billion, 3.2% of GDP	1) Special retraining program to support the reintegration of workers who lose their jobs. 2) Additional resources invested in maintaining and equipment for education and health institutions, and social program budgets.
Bolivia	n/a	1) Minimum wage 2) Training and re-training of unemployed workers 3) Unemployment insurance

Table 3: Fiscal and Social Measures
Source: Ferreira and Schady (2009)

Political Implications

In the past two decades, several democratically elected presidents in Latin America were unable to complete their mandates in the context of severe economic crises. Indeed, seven out of fifteen cases of early exit between 1985 and 2004, left office after confronting adverse economic conditions, including high inflation (and in some cases, hyperinflation), fiscal deficits, currency devaluation, and turmoil in the banking system. In the past half decade, the relatively strong economic performance in many countries in the region contributed to increasing political stability and support for democracy.

However, the recent financial crisis and its socioeconomic effects introduced new challenges to Latin American political actors. The crisis has exacerbated ongoing trends, such as the persisting high levels of insecurity and violent crime, political polarization, and mistrust of political institutions. According to data from the Latin American Political Opinion survey (LAPOP), the "victimization rate" measuring the exposure of Latin American citizens to violent crime, increased from 33% in 2008 to 38% in 2009 (Latinobarometro, 2010). The victimization rate, however, fell to 31% in 2010. Survey data also indicates that perceptions of severity of crime have also been on the rise. The proportion of respondents that considered crime to be the most serious problem in their country increased from 17% in 2008 to 19% in 2009, reaching 27% in 2010.

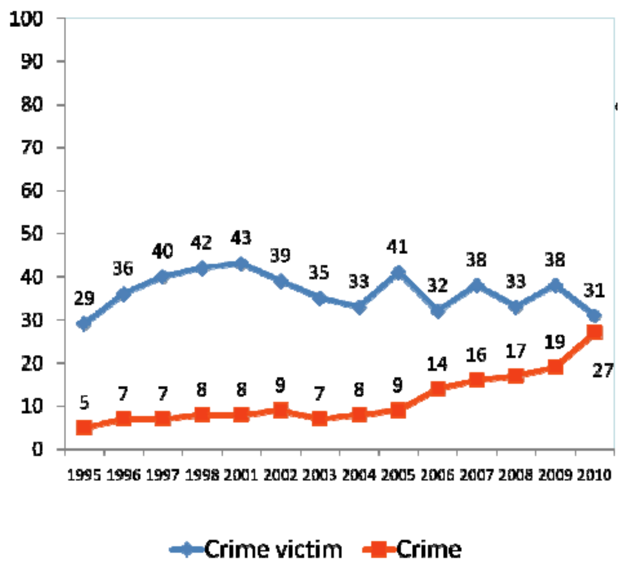

Figure 4: Victimization Rate and Perceptions of Crime as a Problem
Source: Lagos (2010). Crime refers to the percentage of respondents that chose "crime" in response to the question: "In your opinion, which is the most important problem in the country?" Crime victim measures the proportion of respondents that answered yes to the question "Have you been or relative assaulted, attacked, or victim of a crime in the last twelve months?"

Moreover, survey data indicates that, interestingly, since 2008, a greater proportion of Latin American citizens considered violent crime to be a more serious issue than unemployment. This difference has increased significantly for 2010, with 27% of respondents considering crime to be the most serious problem confronted by their country and only 19% choosing unemployment as their main concern.

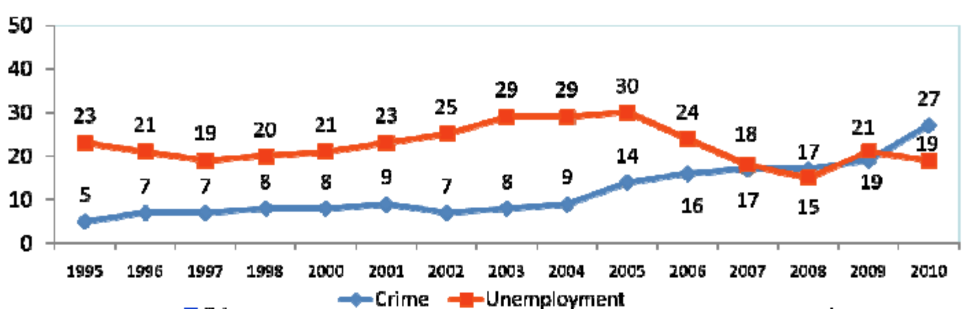

Figure 5: Perceptions of Main Problem in Latin American Countries
Source: Lagos (2010).

The crisis seems not to have had a significant effect on overall levels of support for democracy, which actually increased from 57% in 2008 to 59% in 2009 and to 61%in 2010. Disaggregated data, however, suggests there are some variations across countries. In Ecuador, Colombia, and Paraguay, for example, support for democracy actually fell between 2008 and 2009. In 2010, a number of Central American countries, such as El Salvador, Honduras, Cost Rica and Dominica Republic, experienced small decreases in satisfaction with democracy.

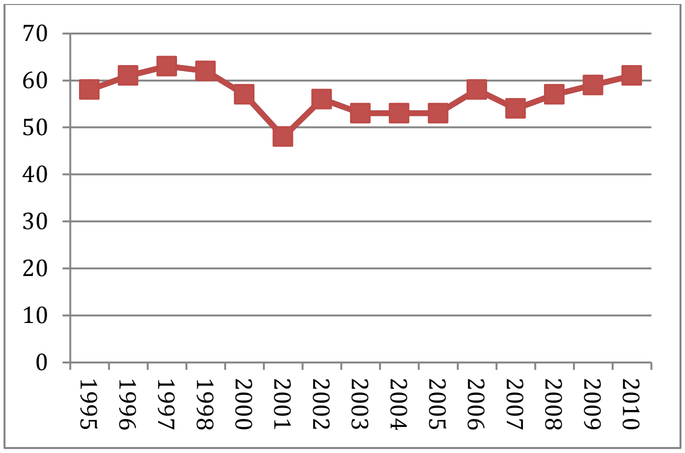

Figure 6: Support for Democracy
Source: Prepared by Author based on data from Latinobarometro (2010). Proportion of respondents that 'Strongly Agree' or 'Agree" with the following statement Do you strongly agree, agree, disagree or strongly disagree with the following statements? Democracy may have problems, but it is the best system of government

As discussed above, the uncertainty brought about by an economic crisis typically leads to increasing demands for social protection, which if left unmet, may result in growing discontent and political tension. Given the fiscal constraints faced by many (if not all) countries in the region, social compensation was a challenge. However, and contrary to what we would have expected, LAPOP survey data indicates that support for Latin American governments was not affected during the 2008-2009 financial crisis. Government approval figures in fact increased from 52% in 2008 to 60% in 2009, falling slightly to 56% in 2010.

Again, there are variations across countries, with the approval rate ranging from 30% in Peru to 85% in Brazil (for 2010). Peru indeed experienced high levels of social unrest in 2011, as indigenous groups in the southeast of the country mobilized against mining activities in the region. A group of 3,000 members of the Aymara indigenous community blocked for more than three weeks the road between the city of Puno and the border with Bolivia. Honduras has also recently experienced political unrest. In June 2009, President Manuel Zelaya was ousted from office and replaced by Roberto Micheletti, in what most states and organizations in the international community considered to be a de fact coup. While it is difficult to establish direct causality, one could speculate that the economic problems brought about by the external crisis could have contributed to these examples of political turmoil.

This brings us to the last point, which refers to the impact of economic crises on government survival. Political scientists have long emphasized the importance of economic performance in explaining electoral support and, in particular, the prospects for incumbents and their parties. An economic recession close to election time is expected to result in a change in governing parties, decreasing the chances for reelection for the incumbent. In Europe, indeed, the crisis seems to have resulted in important political changes, with right-wing parties strengthening considerably and obtaining electoral success in several countries, including Spain, Great Britain, Austria, Belgium and Switzerland. In France, on the other hand, discontent with the state of the economy resulted in a victory of the opposition candidate, the socialist Francois Hollande in the 2012 elections.

In Latin America, presidential elections were held in fifteen countries since 2009. In more than half of these (eight cases), the incumbent's party remained in government, while in the other seven, there were changes in the governing party. While in some countries, like in Peru, there was a shift toward the left, in others (e.g. Chile and Mexico) there was a strengthening of conservative parties. The evidence is thus not very conclusive and does not seem to indicate a clear pattern of association between the international financial crisis and electoral outcomes in Latin America.

Country	Date of Elections	Elected President	Change in party
Argentina	October 2011	Cristina Fernandez de Kirchner	No
Bolivia	December 2010	Evo Morales	No
Brazil	October 2010	Dilma Rousseff	No
Chile	December 2009	Sebastian Pinera	Yes
Colombia	May 2010	Juan Manuel Santos	No
Costa Rica	February 2010	Laura Chinchilla Miranda	No
Dominican Republic	May 2012	Danilo Medina	No
Ecuador	April 2009	Rafael Correa	No
El Salvador	March 2009	Mauricio Funes	Yes
Guatemala	September 2011	Otto Perez Molina	Yes
Honduras	January 2010	Porfirio Lobo Sosa	Yes
Mexico	June 2012	Enrique Peña Nieto	Yes
Panama	May 2009	Ricardo Martinelli	Yes
Peru	April 2011	Ollanta Humala	Yes
Uruguay	October 2009	Jose Mujica	No

Table 4: Presidential Elections in Latin America, 2009-2012

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