Perilous Journey

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If Argentina's economy appears to be in the pink, the same cannot be said of the Casa Rosada (Pink Palace) which is the presidential seat near the River Plate in the middle of Buenos Aires. Only one of the palace's four exterior walls remains pink and it is said that a shortage of funds is to blame. The once-elegant statues positioned on the palace roof are covered with clumps of moss and grass and at a recent press conference a large piece of plasterwork fell in the palace's main conference room. Closer inspection of the economy will also reveal defects, despite economic growth last year of 8.7% (which was the second highest in the world after China) and inflation remaining below 4%. Some buoyant analysts are comparing this reversal of fortunes with the country's halcyon period between 1890-1914 when Argentina had the world's sixth largest economy. But the Land of Sorrow (Latin Letters, Dec/Jan 2003, Issue 132) is also the Land of Borrow where the largest sovereign default in history occurred after the government ceased regular payments on its domestic and external debt obligations (over USD12 billion). Businesses looking for financing are having a hard time because banks are not offering credit; they remain in limbo, wondering whether the government will compensate them fully for the devaluation débàcle in January 2002. The same goes for securing foreign lending until Argentina resolves its public debt. Finding money to paint walls at Casa Rosada is the least of President Nestor Kirchner's worries.

In Brazil, President Luiz Inàcio Lula da Silva's economic policies during his first year in office have been praised. The Sao Paulo stock exchange more than doubled in US dollar terms (the country's sovereign bond market has seen the highest return of any emerging market in 2003) and exports have increased from USD58 billion in 2001 to an expected USD82 billion this year. Unlike Argentina, banks are aggressively increasing their lending portfolios but rates remain high (perhaps the highest of any major economy in the world) because they reflect Brazil's debt burden. At the end of the President's first year in office Brazil's net debt reached 58.3%of GDP (versus 55.5% in 2002). Besides fiscal reform, however, Brazil has to make a special effort to tackle judicial reform. Unlike most other Latin American countries which have made positive improvements to their judicial systems during the last two decades, Brazil has fallen behind. The return to democracy in the 1980s that spurred controversial economic reforms also placed the judiciary in the middle of Brazil's affairs but, unlike the executive branch of government, the judiciary found it hard to adapt. It has remained rigid in its procedures and practices, becoming even more entrenched in its ways, and a survey of Brazilian businessmen has suggested that GDP growth is 20% less than it might be because of an ossified judiciary. The Supreme Court's 11 judges, for example, dealt with 164,000 cases in 2003 whereas its counterpart in the United States had less than 100 cases to hear. The President's intention to streamline the judiciary will require all the tactical skills he is said to possess.

Chile is also enjoying economic vibrancy, but is not, unlike Argentina and Brazil, suffering from debilitating public debt. It has an enviable credit rating because of a consistent economic policy and prudent fiscal management. Interest rates and inflation are heading towards historic lows and even unemployment at 7.4% is at its lowest level in five years. Social policies (labour laws and health reforms, for example) have been criticised, but President Ricardo Lagos says that 17 years of military rule has taken its toll and that more time is needed to remedy the social issues. Meanwhile, as I write, the country's mineral exports are robust and a construction industry boom means that Santiago, the country's capital, is experiencing an ever-changing skyline. The strong demand for copper - mainly from China - has seen prices close to a 10-year high but exporters, on the other hand, are complaining about the increased value of the Chilean peso (at the end of April the US dollar had depreciated against the peso by 20% since the beginning of 2003). The exchange rate appreciation might eventually have an adverse impact on GDP growth but so might external (and uncontrollable) forces.

Argentina, Brazil and Chile walk on a tightrope trying to keep their economic balance and, so far, there has been a safety net of low US dollar rates and Chinese demand. But how secure is the safety net? When US dollar rates rise, perhaps investors will exit Latin America for safer havens (when this happened on previous occasions, it resulted in the Latin debt crisis in the early 1980s followed by the 1994 Mexican financial fiasco). If the rampant Chinese economy slows rapidly, rather than gradually, so will the demand for iron ore, soya and copper. An absence of investor funds and a drop in commodity prices will make that journey across the tightrope even more perilous.

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