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FEATURED Q&A

How Can Latin America Become More Productive?



Latin American countries are seeing low levels of productivity, CAF-Development Bank of Latin America said in a recent report. Factory workers in Ciudad Juárez, Mexico, are pictured above. // File Photo: Mexican Government.

Q Low productivity has been the primary culprit for Latin America's limited capacity to transform productive resources into high-quality goods and services, according to a report released last month by CAF-Development Bank of Latin America. What are the reasons behind Latin America's persistently low productivity rates, and what consequences do they have on the region's overall growth? What measures should policymakers and businesses implement to reverse this trend? To what extent do noneconomic factors such as weak rule of law and bureaucracy play a role in the region's stagnant productivity measures, and what can be done to improve countries' business environments in relation to these areas?

A Alicia Bárcena, executive secretary of the U.N. Economic Commission for Latin America and the Caribbean: "Labor productivity in Latin America relative to the United States has been falling since the 1980s and has also trended lower since the end of the 1950s relative to the current members of the European Union, when it was equivalent to 76 percent, falling to just 41 percent in 2015. This decline continued even in the 1990s, when the region embarked on a program of trade opening and privatization that was expected to boost productivity. Falling labor productivity in Latin America in the aftermath of the global economic and financial crisis of 2008-2009 can be partially explained by a decline in gross fixed capital formation, which contracted significantly over the period. This has directly affected the rate of productivity growth, since modern technological innovations are embedded in the most recent additions to the capital stock. The impact

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TODAY'S NEWS

POLITICAL

Colombian Court Orders Release of Former FARC Leader

Colombia's Special Jurisdiction for Peace ordered the release of former rebel leader Seuxis Hernández, better known as Jesús Santrich. The move led the country's attorney general and his deputy to resign in protest.

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ECONOMIC

Ecuador Agrees to Return of USAID

Ecuador's foreign minister and the U.S. Agency for International Development's administrator agreed to the agency's return after a four-year absence.

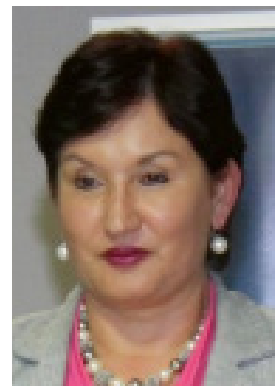
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POLITICAL

Guatemalan Court Blocks Candidacy of Former Attorney General

Guatemala's Constitutional Court blocked the presidential candidacy of former Attorney General Thelma Aldana.

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Aldana // File Photo: Guatemalan Government.

POLITICAL NEWS

Special Colombian Court Orders Release of Ex-Rebel Leader

A special court set up to handle cases of former Colombian rebels on Wednesday ordered the release of former guerrilla leader Seuxis Hernández, better known as Jesús Santrich, and rejected a U.S. request to extradite him, *El Tiempo* reported. In a 3-2 vote, magistrates of the Special Jurisdiction for Peace ordered Hernández's release, citing a lack of evidence against him. Hernández, a former leader of the Revolutionary Armed Forces of Colombia, or FARC, rebels, had been imprisoned since April 2018, and prosecutors in the United States and Colombia have accused him of involvement in the shipping of 10 metric tons of cocaine

“The court is acting like the FARC's accomplice, rather than its judge.”

— Sen. Fernando Araújo

to the United States, *The Wall Street Journal* reported. The magistrates' decision led to the resignation of Colombia's two top prosecutors. Attorney General Néstor Martínez resigned in protest, saying he would not carry out the order to release Hernández and calling the decision “an affront to judicial order.” An hour later, Martínez's deputy, María Riveros, who would have stepped in as attorney general, also quit. Colombian President Iván Duque and the prosecutor's office said the government would appeal the magistrates' order. Political allies of Duque, who campaigned on vows to crack down on alleged war criminals, on Wednesday said the country needs judicial reform. “None of this brings us closer to peace,” said conservative Sen. Fernando Araújo. “The court is acting like the FARC's accomplice, rather than its judge.” However, one of the special court's judges, Jesús Bobadilla, said the order to release Hernández must be followed. “This

court's independence must not be perturbed and therefore these orders must be carried out,” Bobadilla told reporters. Hernández's supporters have denied the charges against the former rebel leader and say the charges against him were orchestrated by opponents of the country's 2016 peace accord with the FARC. A spokesman for the U.S. attorney's office in the Southern District of New York, which filed the extradition request, declined to comment to *The Wall Street Journal*. Upon his release, Hernández would be eligible to fill one of the seats in Congress that was guaranteed to the FARC as part of the peace accord, the newspaper reported.

Guatemalan Court Blocks Aldana's Presidential Bid

Guatemala's Constitutional Court on Wednesday blocked the candidacy of former Attorney General Thelma Aldana in the upcoming June 16 presidential election, *Prensa Libre* reported. Judges voted 6-1 to uphold a previous decision by the Supreme Court and the electoral tribunal, which Aldana had appealed, and which ruled Aldana was ineligible for office for not having a required certification confirming that all of her public accounts were settled. “It has become clear that the fight against corruption and criminal structures in our country has a very high cost for those who, like me, decide to do so,” Aldana wrote on Twitter, adding that with the court's announcement, Guatemala was being “pushed toward the edge of the precipice.” Aldana served as the country's attorney general from 2014 to 2018, leading investigations of high-level officials including now-jailed former President Otto Pérez Molina and his vice president. Aldana has said the case against her is retaliation by current President Jimmy Morales and others for her work to combat corruption, *The Wall Street Journal* reported. A spokesman for Morales has denied the president sought to block Aldana's candidacy. Aldana fled to El Salvador in March after Supreme Court Judge Víctor Manuel Cruz issued a warrant for her arrest on accusations of embezzlement and

NEWS BRIEFS

Venezuelan Government, Opposition Send Envoys to Talks in Norway

Venezuela's government and the opposition have set envoys to launch talks in Norway to discuss ways to end the country's political crisis, the *Associated Press* reported Wednesday. The power struggle between the two sides has left the country paralyzed. The opposition has accused President Nicolás Maduro of using previous talks to buy time.

U.S. ‘Close’ to Deal With Mexico, Canada on Tariffs: Treasury Secretary

The United States is “close” to a deal with Mexico and Canada regarding steel and aluminum tariffs it imposed on them nearly a year ago, U.S. Treasury Secretary Steven Mnuchin said Wednesday during a Senate subcommittee hearing, *Politico* reported. Canada and Mexico, along with some U.S. legislators, have called for the complete removal of tariffs without the imposition of new restrictions, such as quotas. Mexico's undersecretary for North America, Jesús Seade, on Wednesday told reporters the deal could include a tracking system that prevents other countries from bypassing tariffs by shipping the metals through Mexico.

Brazilian Students, Teachers Protest Education Budget Cuts

Tens of thousands of students and teachers marched in cities across Brazil on Wednesday in nationwide protests against President Jair Bolsonaro and his administration's plans to slash the budget for education, the *Financial Times* reported. The government has announced a 30 percent cut to the funding of federal universities and a plan to shift financial support away from the humanities and toward areas such as medicine, veterinary care and engineering.

tax fraud. She denied wrongdoing, saying the charges were politically motivated to prevent her from running. Cruz is currently under investigation for allegedly accepting bribes to issue the detention order, prosecutors said last week, the Associated Press reported.

ECONOMIC NEWS

Ecuador Agrees to Return of USAID as Relations Warm

Ecuador's government on Wednesday agreed to the return of the U.S. Agency for International Development, which had been expelled from the country four years ago during the administration of then-President Rafael Correa, the Associated Press reported. USAID Administrator Mark Green and Ecuadorean Foreign Minister José Valencia signed the agreement in Ecuador. USAID is offering Ecuador \$30 million to help address the Venezuelan migration crisis.

BUSINESS NEWS

Embraer Posts \$42.5 Million Loss for First Quarter

Brazilian aircraft manufacturer Embraer on Wednesday posted a \$42.5 million loss for the first quarter of this year, its fifth consecutive quarter of losses, as revenue dropped amid fewer plane deliveries and heavy spending ahead of a deal with Boeing, Reuters reported. Overall revenue fell 14.1 percent in the January-March period, and revenue in Embraer's commercial aviation segment dropped by 26 percent to \$281 million. The company delivered 11 commercial jets in the quarter, three fewer than a year earlier. The results were "weaker than expected," analysts at Brazilian bank BTG Pactual said in a note to clients.

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of this trend is compounded by the fact that the region's productive structure remains concentrated in activities whose competitiveness depends on natural resources and/or low wages, rather than on innovation and new technologies and capabilities. The leading sectors of the region's economy have weak linkages with the rest of the production structure, giving rise to a heterogeneous structure in which the difference in productivity levels in small- and medium-size firms (which provide most employment) and large firms is much higher than in developed economies. Weak productivity can also be explained in how Latin America invests in human capital. Despite gains in access to primary and secondary education in the region, serious concerns about quality remain. Investment in education is key for boosting labor productivity growth. The region also invests little in innovation: R&D expenditures are below 1 percent of GDP, with a notable exception being Brazil. This weighs heavily on productivity levels, limiting the incorporation of new technology in the productive structure. Limited investment in R&D also has the concomitant effect of reducing demand for a highly trained labor force that can make use of these innovations. Finally, the region's pervasive inequality has deleterious impacts on production system efficiency, leading to loss of opportunities, incentives and resources for learning and innovation."

A Jaana Remes, member of the Advisor board and partner at the McKinsey Global Institute: "While reform initiatives and the short-lived rise in commodity prices lifted millions out of poverty, Latin America continues to experience sluggish growth and unequal distribution of the gains of that growth. Our new McKinsey Global Institute [report](#) highlights a 'missing middle' of firms and consumers that will need to be filled if Latin American economies are to regain their erstwhile dynamism and restore inclusive

growth in the region. Among firms, it finds a missing cohort of vibrant midsize companies that could bring dynamism and investment to expand the number of productive and well-paying jobs in Latin America, much as these firms do in many high-performing emerging regions. Large and midsize companies with more than \$50 million in revenue are less prevalent for the size of the Latin American economy as compared with peers elsewhere. The second missing middle is a cohort of upwardly mobile consumers with rising disposable income. Despite poverty reduction efforts, more than 150 million people in the region have not reached a comfortable middle-class existence. They remain unable to afford goods and services that go beyond basic needs and may not have access to credit. Productive, well-paid jobs have been too scarce to meet the needs of the expanding labor force. These missing consumers are a drag on the economy, as they limit demand and growth of markets for domestic firms. Filling in these missing middles may not solve all of Latin America's economic challenges, but it will go a long way to boost productivity and broad-based prosperity."

A Welby Leaman, senior director of global government affairs for the Americas at Walmart: "One lesson from the CAF report is that informality, corruption and weak rule of law in Latin America sap the productivity of businesses and workers that operate within the informal sector. Yet that harm does not stop at the border between the informal and formal sectors. High-compliance-standard businesses and workers, too, could generate more productivity gains for Latin American economies were it not for the disincentive of informality, corruption and weak rule of law. Walmart's 'Despensa Familiar' grocery format in the Northern Triangle is well-designed to expand formality and raise 'total factor productivity' in underserved Class C and D communities by combining the right

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mix of local agricultural sourcing, formal careers, capital and customer surplus. But in retail and other sectors, local sourcing networks fray and investment lags if weak rule of law and misunderstandings about how to strengthen it cause avoidable distrust between buyers and suppliers and between the public and private sectors. Gear-slipping is common in rule-of-law efforts that rely on just one or two of Douglass North's three institution-building components: legal norms, informal cultural norms and enforcement. We can be more productive at strengthening rule of law if we better combine these three 'factors' and increase hours worked on this challenge by recognizing a leadership role for the private sector. In short, we can raise productivity in Latin America in part by more productively working across sectors to strengthen rule of law."

A **Matteo Grazzi, senior specialist in the Competitiveness, Technology and Innovation Division at the Inter-American Development Bank:** "The low productivity of LAC economies has been acknowledged as the main reason of the disappointing long-run economic performance of the region. This is the result of multiple factors, but a key element is the scarce effort of the region in terms of innovation and dynamic entrepreneurship. In fact, most LAC countries underinvest in science, technology and innovation (STI). For example, LAC average R&D intensity as percentage of GDP (a generally accepted indicator of innovation effort) is only around 0.7 percent, compared to more than 4 percent in benchmarking countries such as South Korea and Israel. This is due not only to insufficient public investment, but also, and especially, to the scant participation of the private sector in this effort. On average, in LAC firms' R&D

intensity (expressed as a percentage of sales) is below 0.4 percent, considerably lower than 1.61 percent in Europe and 1.89 percent in OECD countries. This situation is the result of macroeconomic and regulatory factors, but also of the specific strategies and decisions of individual LAC firms. A recent IDB **book** presents the results of recent original microeconomic evidence relating to LAC countries, confirming that innovation is a key engine of productivity growth, but that its impact depends on the specific charac-

“**Most LAC countries underinvest in science, technology and innovation.**”

– Matteo Grazzi

teristics of the firm and on the availability of additional complementary assets, such as access and use of digital technologies, access to finance and external markets, and on-the-job training. This implies that a sound institutional and regulatory framework is a necessary condition for allowing productivity gains, but that, once these barriers are reduced, firms will respond to the same framework in different ways, depending on their characteristics. Then, once the basic framework is put in place, the achievement of further efficiency improvements within firms will require detailed microeconomic policies that address the internal factors that hinder firm-level innovation, technological upgrading, improvements in management and organization, development of technical human capital and entry into export markets."

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