

Latin American Crises and Social Costs: What Lessons for Asia?

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The following article was published in the International Herald Tribune on May 29, 1998:

East Asia's financial crisis is almost a year old. The social dimensions of the crisis are still unfolding, dramatically in Indonesia, quietly in the lives of many individuals in Korea, Thailand, the Philippines and Malaysia, through job losses, service cutbacks and lower incomes. Economic crises have been relatively rare in the region, with the Philippines the major exception. By contrast, in the last fifteen years, Latin America experienced two major crises, both starting with Mexico, and both with substantial social costs. In the 1980s Mexico's debt crisis spread throughout Latin America on the back of terms of trade shocks and weak public finances; the period became known as the "lost decade". In 1995, Mexico's liquidity crisis, whose root lay in excessive private lending spread only to Argentina. What can East Asia learn from the experience of Latin America?

The two Latin American crisis hit households hard. In the 1980s real wages in Argentina and Mexico fell by close to forty percent and poverty doubled and rose by a third, respectively. In Chile, real wages contracted by about 15 percent and open unemployment shot up by 9 percentage points within a year. In Brazil, real wages fell by 11 percent and poverty rose by between 10 and 20 percent. Although social indicators such as infant mortality rates and average years of schooling continued to improve, they did so at a slower pace, and there were widespread cutbacks in social spending. In the 1995-96 episode, real wages in Mexico fell by over 30 percent. In Argentina unemployment increased by 6 percentage points and remained at around 18 percent for over two years and poverty rose by more than fifty percent. In many countries in both episodes, income inequality rose.

Latin American governments responded in many ways to cope with the social costs of the economic crises. Measures ranged from food assistance programs, unemployment insurance, social funds, extension of healthcare coverage to the unemployed, scholarships for children, training and retraining programs, and workfare programs. However, with the partial exception of Chile, the overall response was too little, too late. What are the lessons?

First, tackling social issues implies putting them at the center of the agenda. Too often in

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the Latin American crises policymakers' energy was devoted to restoring macroeconomic stability and implementing structural reform. East Asia has the opportunity to put social issues at the forefront. The immediate effects of the Latin America crises were falls in incomes, employment and public services. But these had widespread and complex additional consequences, including increased demands on women (who often *increased* their work in informal sector activities), pulling children out of school, and rising violence, both on the street and in the home in response to rising social pressures. It is important to take action on a wide range of areas.

Second, the design of the response can be crucial, and there were often weaknesses in the Latin American experience. Even in the case of social funds which were specifically conceived to tackle with the social dimension of adjustment, success was at best mixed because beneficiaries were not necessarily those who were left unemployed by the crisis and its aftermath. East Asia has the opportunity of drawing on the accumulated knowledge of what does and does not work, from within East Asia and elsewhere. Chile implemented a large-scale public works program that provides employment for a large fraction of the workforce--low wages ensured the most needy were the main participants. Jamaica had some success in improved targeting of food subsidies. But in Mexico and elsewhere general subsidies were cut in a crisis without introducing effectively targeted alternatives. The middle of a crisis may not be the best time to cut subsidies on wage goods, especially of goods of importance for the poor. Such cuts can fuel resistance to needed reforms. Finally, of greatest importance is maintaining support to core education and health services, to avoid irreversible losses in human investment--this was done poorly in the early 1980s.

Third, institutional issues can be central to the choice of programs. In Latin America the state apparatus--the line ministries in particular--was often in disarray at the time or as a result of the crisis and many governments lacked the resources to implement a safety net program. The alternative of setting up social funds proved useful both to mobilize external resources and respond rapidly to pressing needs. Funds are no panacea: the earlier funds were often poorly targeted and lacked genuine community participation. Many took some time to set up. There is now more knowledge on how to design such funds well. But the choice to bypass existing institutional structures needs to be taken with care and is highly country-specific: where established governmental or non-governmental institutions work (reasonably) well--as in the past in most of East Asia--it is often better to work within the system. Even if governments can resort to the social fund solution, to preserve the long term goals of growth and equity they should not neglect line ministries during times of crisis. Low and falling wages combined with protracted conflicts between the central government and the labor unions in the line ministries became their "kiss of death". Partly as a result, the quality of education in the region has become dismal even in countries where it was respectable once. Protecting line ministries in health and education should be among the goals stipulated in crisis-management strategies.

Finally, in Latin America, the debt crisis coincided with the restoration of democratic rule in many countries. At the time there were fears democracy would hinder painful but necessary

reforms or that the social disruption and violence associated with the crisis would hasten the return of authoritarian rule. Both fears were proven wrong. While an independent voice to unions, congress and other actors slowed down the process of adjustment in some of the countries, the policy measures which were undertaken in the end became more durable precisely because they had been endorsed by a more open polity. Furthermore, the suffering caused by years of repression resulted in a citizenry more ready to withstand economic sacrifices if only to preserve the advent of democratic institutions.