Some Notes on Economic Growth in Argentina and Brazil during 2003–2015

Andres Lazzarini

The present paper critically discusses the main features of the economic growth processes during 2003-2015 in Argentina and Brazil, two Latin American countries that witnessed a remarkably positive economic performance during the 2000s decade, except for the 2009 international slowdown. More specifically, for the 2003-2008 period Argentina grew at a yearly average rate of 7.8 per cent, while during 2006-2010 the same rate for Brazil was 4.5 per cent. One of the arguments usually put forward by economic studies to explain the boom in Latin America is the extraordinarily substantial improvement in the external conditions facing these economies, which allowed them to cope with the rising requirements for international currency during the growth processes in those years (Amico, 2010; Crespo and De Lucchi, 2012; Serrano and Summa, 2012).

As is well-known, one of the salient features of Latin American economies is their recurrent need of international currency during a growth process involving some type of import substitution industrialisation. The "unbalanced productive structure" that characterizes these economies has periodically led them to economic crises followed by substantial deficits in the balance of payments (Diamand, 1973), leading to exchange rate shocks, volatile inflation rates and economic recession. In these productive structures there exist some sectors with absolute higher levels of productivity than their international counterparts (normally, in natural resource based commodities), while at the same time there are other sectors with lower absolute levels of productivity (manufacturing sectors) than their international counterparts (Crespo and Lazzarini, 2016). It is also important to mention, as Raúl Prebisch (1949) highlighted quite a while ago, that the difference in the income elasticity of the demand for industrial goods relative to the elasticity of demand for primary and natural resource based commodities results in the deterioration of the terms of trade for Latin American countries, since the region is internationally competitive in the latter group of commodities. Any industrialization strategy pursued as a means of addressing the deterioration of the external balance, as for example the import substitution industrialization implemented after World War II in most Latin American countries until the 1970s-1980s, requires, however, more international currency to pay for the much required imported capital goods. Thus the import substitution industrialisation programme has to be deepened so as to encourage both the domestic production of capital goods and the exports of industrial commodities. But, since both the primary and the industrial sectors take their respective terms of trade as given from the international market (at least in the Latin American countries and for a vast number of commodities), those possibilities in industrialisation are bounded by the external constraint, while they will be broadened to the extent allowed by a positive balance of payments.

As we shall see in Section 2, both the rise in exportable commodities' prices and the extraordinary increase in international demand for these commodities after China's entry into international trade have been the two key factors that eased the pressure of external constraints in the recent period. However, there have been some controversies on the main targets that economic policies should aim at in order to keep the account balance positive. One of the most entertained views put forward by some scholars (*e.g.*, Frenkel, 2008) is that Latin American countries should exclusively focus on keeping exchange rates competitive (*i.e.*, depreciating national currencies). According to this analysis, the objective should be to raise exports using an allegedly price-competitive effect that would, in turn, follow the devaluation of the national currencies. However, not only do exports not always react to currency devaluation, but also the remarkably good economic performance in these countries for most of the decade cannot exclusively be explained by the increase in exports. While it is true that exports are of paramount strategic importance for economic development, income policies to boost domestic demand - which then facilitate expansionary fiscal policies - and an improvement in income distribution in these countries make for better conditions for economic growth through increases in domestic consumption and investment, with further positive effects on poverty reduction and other social indicators. On the other hand, exchange policies oriented almost exclusively to achieve competitive exchange rates have been, more often than not, followed by sudden inflationary jumps and drastic drops in economic activity and employment (such as those experienced by Argentina in 2014 and now in 2016, and by Brazil since 2014).

In Section 3 we then show that both Argentina and Brazil have been characterised over the last few years by a strong deceleration in their growth rates. For 2011-2015 Brazil's GDP rate was 0.7 per cent (year average), while roughly the same modest average rate (0.65 %) was attained by Argentina during the period 2012-2015. This phenomenon of low economic growth in both countries cannot, however, be explained by the same causes. In the case of Brazil, the causes of the strong deceleration must be sought in the internal shifts in macroeconomic policy orientation, which had a negative impact on domestic demand, rather than in structural problems connected with external conditions (Serrano and Summa, 2012). In Argentina, on the other hand, the main causes of its deceleration must be sought in a combination of factors: on the one hand, structural causes linked to the external constraint; on the other, the generally accepted belief in both academic and policy circles that competitive exchange policies are the guarantee for sustained economic growth, which led to the adoption of currency depreciation policies (only gradually between 2011 and 2013, and then drastically by 2014). As will be argued, this orientation in the Argentine exchange rate policy actually drove the economy to very low growth rates, a drop in the real wage and a standstill in the general improvement in income distribution of previous years. Finally, some general conclusions and remarks on the short-to-medium term scenario are put forward in Section 4 with some linkages with the current political scenario in both countries.

Accelerated growth period: Argentina (2003-2008) and Brazil (2006-2010) in the context of *decoupling*

Over the last fifteen years, a salient feature in peripheral economies has been the remarkable improvement in their external conditions. Indeed, since the 2000s, the economic growth rate in the South increased at a noticeably higher rate than the industrialised, developed world. This phenomenon has been labelled in the literature as *decoupling* of the peripheral economies' growth rates from the average rate for developed countries.

One of the factors that explain the positive performance attained by these peripheral economies (Asia, Africa, Latin America and Caribbean, Middle East) is the sharp rise in the levels of exports of natural resource-based commodities and the consequent increase in their relative share in world trade. In fact, it is after China's entrance into the international trading system that we witness a sharp increase in global demand for exports from peripheral countries, including those in Latin America. At the same time, the phenomenon of *decoupling* followed a significant improvement in the terms of trade of countries exporting raw materials and natural resource based commodities, in comparison to the value of imports of industrial manufactures, which, in turn, China managed to increase at a tremendous pace in recent years.

Data on the terms of trade for some peripheral countries point to their relative stability in the last decades of the 20th century, and, later on, their gradual and sustained improvement at the beginning of the 21st century. Although they have not been the most dynamic in the sample, there was a perceptible improvement in the terms of trade for Argentina and Brazil, as can be seen from the graph below. In contrast, China witnessed a deterioration in its terms of trade, especially because of the relative fall in the costs of production of Chinese manufacturing goods in the last few decades. As argued in Crespo and De Lucchi (2012), the fact that China has unfavourable terms of trade has not prevented the Chinese economy from growing at remarkable rates in the last fifteen years (though currently it has dropped its pace). The improvement in the external conditions for Argentina and Brazil in the 2000s has not only resulted in higher levels of exports (see below) but also in a significant rise in international reserves, which no doubt helped sustain positive current account balances that backed up the growing imports of capital goods demanded by the manufacturing sectors in both countries.

Figure 1: Terms of trade for a set of countries of Latin America, China and India (2000=100).

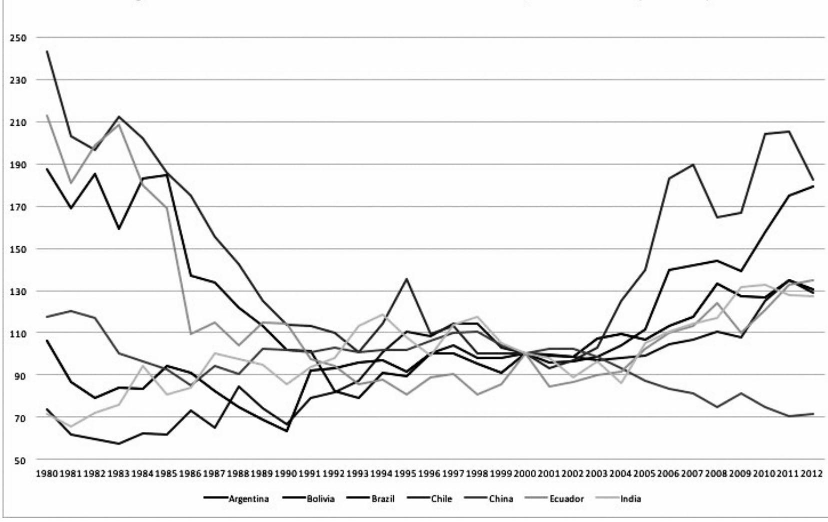

Table 1 Argentina and Brazil: International reserves (as a percentage of GDP), 1994-2013.

	1994-1998	1999-2003	2004-2008	2009-2013
Argentina	5.9%	7.4%	12.2%	8.9%
Brazil	6.4%	6.8%	9.4%	15.0%

Source: World Bank database

The rise in exports certainly helped boost GDP growth in both countries. As shown in Tables 2 and 3, total exports of the two countries were characterized by a remarkable increase. Note that in the case of Argentina, its export trade with Brazil jumped in the 1990s after the MERCOSUR agreement and the set-up of the customs union. This trend has continued in the early 2000s, after which it rose as a consequence of reciprocal trade agreements between the two countries, in particular in the automobile industry, that led to Argentine imports of parts and components from Brazil and exports of finished cars from Argentina to Brazil.

At the same time, there was the important and undeniable role of the Chinese economy, especially for peripheral countries, in boosting the economic performance and exports of both economies. In this regard, it is noteworthy that one of the main questions raised in the debate about the factors that have driven growth in these countries, has been whether accelerating growth can be explained only by the improvement in the external conditions. Those who focused their analysis exclusively on the role of foreign markets argued for exchange rate policies oriented to achieving "competitive" exchange rates, that is, a real depreciation of national currencies, which would allegedly promote an increase in exports through the effect of export price-elasticities (Frenkel, 2008). However, recent studies have provided both theoretical and empirical evidence showing that such an argument is flawed (Amico, 2010; Serrano and Summa, 2012). In the case of Brazil, the evidence clearly shows that exports continued to grow at a remarkable pace even when an "appreciated" exchange rate was dominating during the period 2003-2011, with the exception both of 2008 when the national currency depreciated, and of 2009 when Brazilian export growth dropped in the wake of the international slowdown (Serrano and Summa, 2013).

Table 2 Brazil, total exports and exports to China, nominal USD, and share of China.

	Total	China	
1970	2,738,712,832.0	1,327,122.0	0.0%
1975	8,669,454,336.0	67,357,912.0	0.8%
1980	20,132,055,040.0	72,225,672.0	0.4%
1985	25,638,731,776.0	817,582,208.0	3.2%
1990	31,396,964,352.0	381,792,448.0	1.2%
1995	46,145,355,776.0	1,203,741,184.0	2.6%
2000	54,743,553,226.0	1,085,301,597.0	2.0%
2005	118,069,804,976.0	6,834,996,980.0	5.8%
2010	195,546,557,878.0	30,752,355,631.0	15.7%

Source: COMTRADE

Table 3 Argentina, total exports and exports to China and to Brazil, nominal USD and shares.

	Total	China		Brazil	
1970	1,773,170,432.0	2,516,097.0	0.1%	138,561,088.0	7.8%
1975	2,961,259,776.0	21,448,888.0	0.7%	213,480,560.0	7.2%
1980	8,019,175,936.0	188,788,736.0	2.4%	764,968,256.0	9.5%
1985	8,395,986,432.0	311,004,064.0	3.7%	496,293,408.0	5.9%
1990	12,351,521,792.0	240,968,608.0	2.0%	1,422,653,184.0	11.5%
1995	20,962,545,664.0	285,730,784.0	1.4%	5,484,101,120.0	26.2%
2000	26,244,851,702.0	796,927,268.0	3.0%	6,990,801,568.0	26.6%
2005	39,963,954,009.0	3,154,288,661.0	7.9%	6,328,294,321.0	15.8%
2010	66,174,370,291.0	5,798,633,567.0	8.8%	14,424,597,623.0	21.8%

Source: COMTRADE

In the case of Brazil, the extraordinary performance of its exports seems to be linked more to the increase in international demand (especially for commodities), than to the implementation of more or less successful competitive exchange rate policies domestically. Indeed, exports have not been the one and only factor explaining the positive trend in output growth in Brazil, especially for 2006-2010. As can be seen from Table 4, all com-

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ponents of domestic demand have contributed positively, especially household consumption, government spending (especially public investment), and private investment, which have shown greater dynamism than exports. This dynamism attained by Brazil's GDP growth, while in part the result of the improved external conditions (which allowed it to cope successfully with the external constraint in order to meet import requirements), was also the result of a deliberate policy since 2005 of *relative diversion* from the so-called macro-prudential policies of inflation control, fiscal surpluses and a floating exchange rate (Serrano and Summa, 2012; 2013). Regulations of monitored utilities' prices (electricity, telephone, oil) through taxes and subsidies increased the levels of public investment, and promotion of consumer credit, especially for car consumption and housing, at relatively low levels of interest rates, among other measures, helped boost consumption. Rapid economic growth followed in Brazil during 2006-2010, thanks to the remarkable increase in autonomous aggregate demand.

Thus, since 2006, the combination of better external conditions, an increase in the international reserves, very fast export growth, induced increase in private spending, and a rise in public spending (reducing public primary surplus) along with a remarkable drop in the levels of public net debt (even to negative levels)[1], allowed Brazil's economy to accelerate its growth during the second half of the 2000s.

Table 4 Brazil: Selected key variables. Annual growth rate, 2004-2011.

Year	GDP	Households Cons.	Govt. Cons.	Govt. Invst'nt	Total Invst'nt	Machinery & equipment	Construction	Exports	Imports
2004	5.7%	3.8%	4.8%	-2.3%	9.1%	13.1%	6.2%	15.3%	13.3%
2005	3.2%	4.5%	6.8%	3.4%	3.6%	5.7%	1.0%	9.3%	8.5%
2006	4.0%	5.2%	4.6%	0.9%	9.8%	14.5%	4.9%	5.0%	18.5%
2007	6.1%	6.1%	7.3%	18.5%	13.9%	22.0%	5.5%	6.2%	19.9%
2008	5.2%	5.7%	4.8%	34.7%	13.6%	18.3%	9.3%	0.6%	15.4%
2009	-0.3%	4.4%	4.7%	29.7%	-6.7%	-12.5%	1.0%	-9.1%	-7.6%
2010	7.5%	6.9%	7.2%	12.9%	21.3%	30.4%	12.9%	11.5%	35.8%
2011	2.7%	4.1%	0.4%	-8.6%	4.7%	6.0%	3.9%	4.5%	9.8%
Avrg rate 2004-2010	**4.5%**	**5.2%**	**5.8%**	**14.0%**	**9.2%**	**13.1%**	**5.8%**	**5.5%**	**14.8%**

Source: Serrano and Summa (2013); IBGE; DIMAC-IPEA.

If we turn our attention to the Argentine economy, one of the important issues that must be acknowledged is that the exchange policy of small scale depreciations during 2003-2008 was accompanied by a strong fiscal stimulus, with a significant expansion of public spending investment (Amico, 2010; 2013). Since 2003 there has been a deliberate economic policy to boost demand. Indeed, thanks to these demand stimulating policies, carried out by the government through redistribution of income via taxes and subsidies, it was possible for consumption and investment, both private and public, to reach remarkably high levels.

In this connection it is important to note that the government has also pursuing a policy of income redistribution via taxes. Since as early as the dismal crisis of 2002, the government has imposed a levy on exports of primary commodities, such as soy bean, corn, wheat, and some foodstuff. These exports taxes (also called rights to export) helped both decouple domestic prices of those products from their international counterparts in order to avoid sharp inflation (and falling real wages), as well as redistribute those incomes to other sectors of the economy, especially the manufacturing sector.[2] In this connection, it is worth noting that a new wave of the so-called Import Substitution Industrialization process (ISI) has, since 2003, taken place. Argentine manufacturing sectors such as machinery, automobiles, chemicals, petrochemical, software, iron and steel, apparel, shoes, not to mention manufactures of primary origin such as food, beverages, tobacco, etc., all grew at remarkably high rates. Such growth is explained, from the supply side, by the benefits of having enjoyed relatively lower unit labour costs (via devaluation of the currency) but also, from the demand side by the extraordinary rise in domestic investment (especially machinery and equipment) which, measured as a ratio to the GDP, grew from a 11.2% in 2002 to a 23.0% in 2008 (Abeles, 2009). As other research has shown (*e.g.*, Fiorito 2009), it must be kept in mind that more often than not investment is tied to the trend in demand and this is why aggregate consumption has been quite decisive in explaining the growth process, helped by income policies to sustain the poorest sectors and by the new situation facing the working class, whose members began finding employment and hence enjoying a permanent (and adjustable) wage.

As the Argentine manufacturing sector, like most peripheral economies, has not had access to the technology actually used by its international competitors (which determines the international prices),[3] the industry has historically lagged behind internationally. Moreover, a deliberate policy of exchange rate depreciation to boost non-traditional sectors, like manufacturing, has proved to be very problematic, because of distributional conflicts which can turn disruptive in a context of devaluation. For these reasons the manufacturing sector has historically relied on the domestic market, and, also, on the regional market (especially Brazil and other MERCOSUR country members)[4]. That is why the creation of a dynamic domestic market thanks to progressive demand and income policies turned out to be a key factor for the manufacturing sector and for the whole economy. Thus, formal employment creation in the manufacturing sector, rise in profit margins, rise in consumption, and rise in investment (and hence rise in tax collection) allowed for a virtuous phase of the economic cycle that was reflected in the extraordinary figures of economic growth. As Figure 2 depicts, economic growth in Argentine reached an impressive average rate of 6.5% for the whole decade (2003-2012), or, if we exclude the gloomy year 2012 (see Section 3, below), that rate reached 7.1%.

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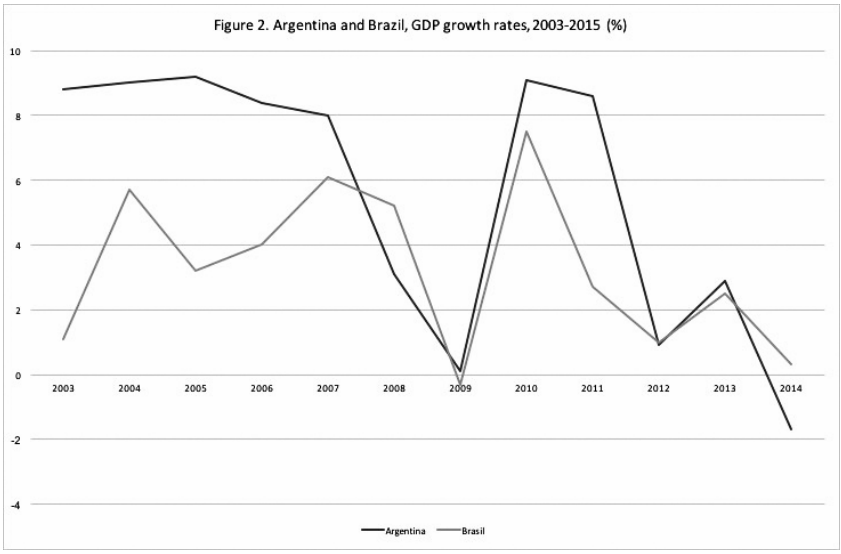


Figure 2. Argentina and Brazil, GDP growth rates, 2003-2015 (%)

Income distribution and poverty reduction

As a result of positive economic growth in both economies, with favourable external conditions and significant increases in the components of aggregate demand, employment and wages, both economies witnessed a remarkable improvement in income distribution and significant poverty reduction. In the case of Brazil, one of the main causes for the decline in the poverty rate has been the continuous rise of the minimum wage, which year after year was raised in keeping with inflation.[5] This is crucial due to the fact that Brazilian pensions are linked to the minimum wage level which in the case of rural populations implies an extraordinary improvement in life conditions. But also, as Serrano and Summa (2012, p. 81) have explained, the rising minimum wage policy directly raises the wages and salaries of lower level public servants, and has a positive effect on the bargaining power of less skilled workers in the private sector. Also higher wages for lower-skilled workers cause an increase in the consumption levels of the lower-middle classes, thus pushing up household spending.

If we look at Figure 3 it is remarkable that the increase in the minimum real wage after 2004 was probably one of the key factors in determining a consistent fall in inequality measures. As can be seen from Figure 4, the Gini index dropped from an average for the second half of the 1990s of 0.60 to of 0.51 by 2014. Taking into account the fact that Brazilian income distribution is one of the most unequal worldwide, the poverty reduction that this country underwent during this period of economic growth is indeed remarkable.

Besides the positive impact of a growing economy on wages and on reducing poverty, public policies targeted to provide basic relief for the lowest strata of the population have had a very important role. One of such policies set up in 2003 by the Lula's administration is the *Bolsa*

Familia (family allowance), which gives families with per-capita incomes below the poverty line (Reais 164) a monthly basic benefit according to the number of children attending school.[6] This income policy has been covering around 13-14 million families, which all in all comprise more than 50 million people (by 2015). It is important to highlight that between 2011 and 2015 an estimated 22 Brazilian citizens have exited extreme poverty thanks to this policy. Thus, the improvement in poverty reduction in Brazil, especially after 2004/5 is basically related to the rise in minimum wages as well as public income policies addressing the lowest income strata of the population.

Figure 3. Brazil: Real minimum wage, 1994-2015 (Real)

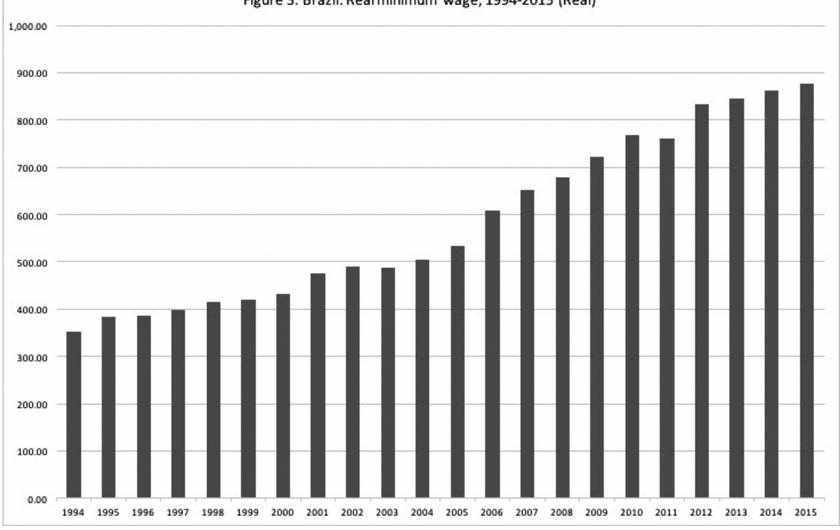
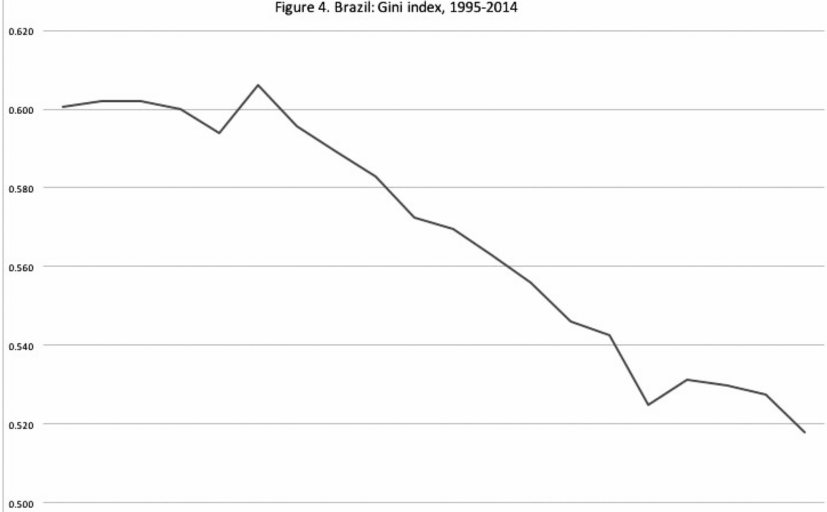


Figure 4. Brazil: Gini index, 1995-2014



In Argentina, both implementing income policies and increasing the minimum wage have been the two main drivers for the progressive path in income distribution and poverty reduction since 2003. In fact, the authorities have willingly resumed, since 2003, free bargaining negotiations between employers and employees overseen by public authorities every year. During all the years of economic growth, wage recipients have enjoyed annual readjustments in their wages which, in general, more than offset the inflation rate, especially for private sector workers. The Argentine tradition of strong trade unions and the deliberate public policy, at least until the end 2015, to encourage negotiations for nominal wages to keep pace with inflation have both been two important factors determining the path of income distribution in those years (see Figure 7, below). As to public policies to boost aggregate demand, a series of income policies were set up by the national administration, especially since 2009. In this regard, two remarkable policies have to be mentioned: first, the universal child allowance (*Asignación Universal por Hijo* or *AUH* for short) which is a direct government benefit to mothers (of children under 18) who either are single and have no formal job, or are married but their husband have no formal occupation.[7] Second, a universal pension scheme for the elderly has been established, under which over 65-year-old people become recipients of a monthly income independent of whether they contributed or not in the past (see Figure 5). The coverage of the state pension system amounts to almost 6 million.[8] Naturally, these types of government policies have had an equalizing effect on income distribution. Indeed, if we compare the rate of growth of the Gini coefficient for Argentina between 1992-2002 and 2002-2010, one can observe that the *rate of growth* of the Gini index was 8.2% for the 1992-2002 period, while the same rate decreased sharply over 2002-2010, at a negative rate of – 9.0 %[9]. Note that these income policies actually amounted to a huge injection of fresh resources into the economy that helped boost domestic demand.

Growth Deceleration in Argentina (2012-2015) and Brazil (2011-2015)

As pointed out above, Latin America has been characterized by recurrent balance of payments crises since the adoption of Import Substitution Industrialization strategies in the 1940s and 1950s until the reversal of such strategies fuelled by the ideological criticism of the new wave of neoliberal thinkers from the 1970s until the 1990s. Historical evidence suggests that, because of the existence of an unbalanced economic structure (Diamand, 1973), the region's exports have recurrently lagged behind the needs of foreign currency to import the basic requirements for the industrialization strategy. In the recent period, on the other hand, favourable external conditions allowed both Argentina and Brazil achieve a better external situation than both countries (especially Argentina) experienced in the past, with

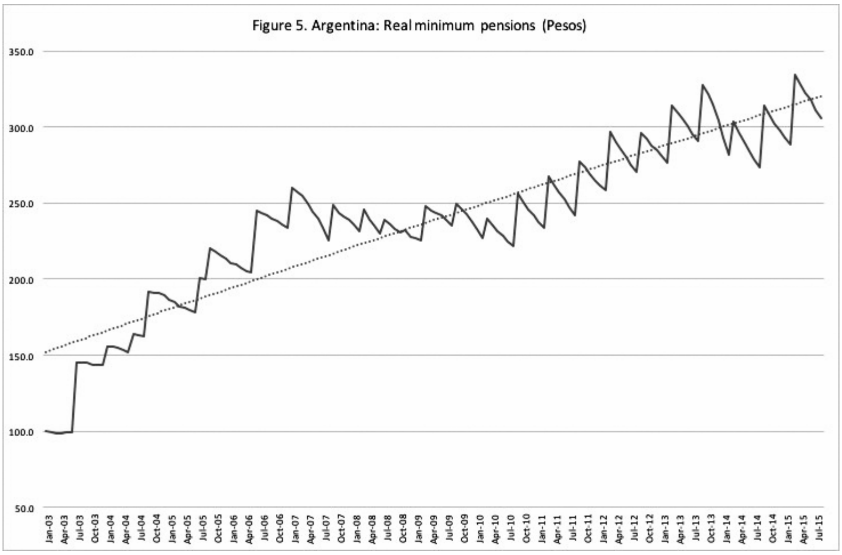


Figure 5. Argentina: Real minimum pensions (Pesos)

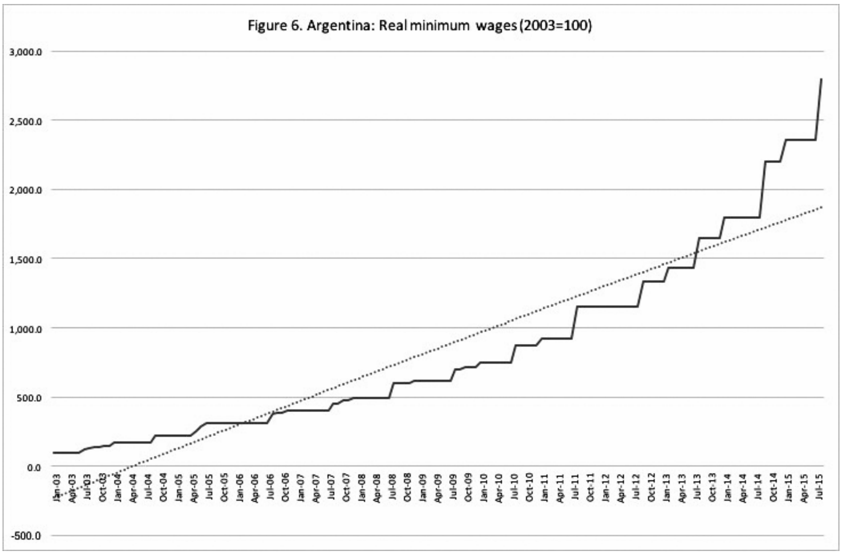


Figure 6. Argentina: Real minimum wages (2003=100)

positive (or close to zero) current account balance for almost the whole period analysed. These better external conditions allowed these economies to increase manufacturing output and thus the level of employment.

However, in Argentina, the positive balance in the current account was waning as the processes of industrialisation progressed, because of the rise in imported capital goods and raw materials essential to the domestic industry. The dynamic effects of industrialization on the Argentine economic structure can be recognised by examining its international trade by type of commodities traded. Thus, after 2010, the share of manufactured goods exports in total exports (35.1%) was higher than both the exports of primary products (22.1%) and exports of agricultural manufactures (33.4%).

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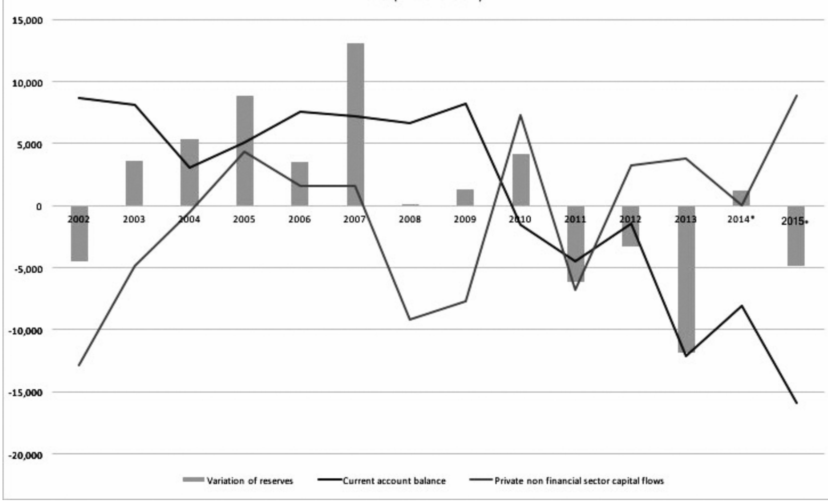
In addition, CEP (2009) has shown that Argentine capital goods exports increased by 217% between 2003 and 2008, while for total manufacturing sector and for total exports the increase were 186% and 138%, respectively. However, during the same period imports of capital goods necessary for the expansion of the productive capacity increased by more than 297% for the economy as a whole, and 221% for the manufacturing sector only (CEP, 2009). Official data show, that even if the level of exports throughout the decade 2003-2013 was higher than the level of imports, the import growth rate was higher than the exports growth rate: while exports almost trebled between 2003 and 2012, imports have multiplied by 5 times during the same period. Thus, even though the trade balance is positive for the entire period, in 2011 the *current account* of the balance of payments turned negative, due particularly to the negative results on the income sheets (including interests and gains and profits). The problems on the financial side began seriously affecting the dynamics of the economy by 2011. In fact, capital flight began to rise steeply in that year, and foreign exchange reserves accumulated by the Central Bank began to fall sharply. In 2011 the Central Bank lost USD 6.1 billion in international reserves. In 2012 the external constraint got even tighter: USD 3.3 billion left the economy. Once again, although with a lower degree of intensity, the balance of payments constraint reappeared in an underdeveloped country such as Argentina.

In such a negative context of lack of international reserves to pay for the rising imports of capital goods to sustain the pace of growth (especially energy), the government adopted a number of policies to delay the effects of a crisis on the balance of payments. First and foremost, it took over of the main oil company, YPF, which had been privatised in the 1990s, in 2012; and secondly, it set up import barriers and restrictions on the purchase foreign currency for private savings purposes. Although the first policy was spot on from the point of view of taking back from foreign capital one of the key resources for industrialisation and development, the latter policies had not been adequately planned to serve the purpose of avoiding the external crisis and sustaining the pace of economic growth. In fact, the effects of these import restrictions on the economy have been really disappointing. The import restrictions were not carried out on the basis of any strategic plan to strengthen the process of industrialisation, the main objective being reducing capital flight in order to keep positive (or roughly above zero) the current account. Still, the general situation got worse. Since 2012 certain industrial sectors started displaying bottlenecks in their production processes, as the production capacity could not be enhanced due to restrictions on the imports of capital goods, not to mention the negative effects of a much felt shortage of foreign exchange. One of the main strictures in criticism of the lack of long-term planning of the industrialisation process on the part of the authorities has been that all measures have been of a very short-term nature. Indeed, as can be seen from Figure 2 above, the years

2012 and 2013 were one of very low growth (0.9% and 2.9%, respectively), especially if these figures are compared with the average annual growth rate of 7.5% during the period 2003-2011. There remained little doubt that the strategy adopted to stop the drain of foreign currency was to freeze the economy (see Figure 7).

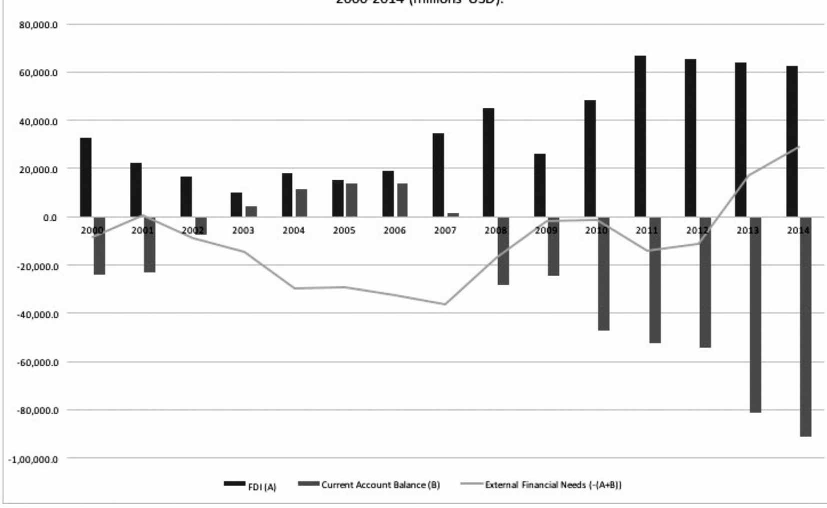
Figure 7. Argentina: Current Account balance, capital flows, variation in international reserves, 2002-2015 (millions USD)



Arguably, as a consequence of the policies carried out by the turn of 2011-2012, the problem of the external constraint in Argentina was getting worse, and in January 2014 the national currency was sharply devalued by 30%, leading to a drastic fall in activity level of about 1%, an increase in the inflation rate (somewhat around 30-32 % in 2014) and a check on job creation in the formal sector. The social consequences of both the recession and price inflation led to a decline in real wages and, consequently, to a lower consumption level. Then a fall in manufacturing production followed suit, with the manufacturing sector shrinking for roughly twenty-four months in a row in 2014 and 2015, thus reinforcing the economic recession. By November 2015 the governing party lost their presidential bid against a conservative candidate who soon after taking office started a process of policy regression with a package of policies of neoliberal flavour.[10]

Unlike Argentina, where the structural causes of external constraints were essentially the main factors affecting economic performance since 2012, Brazil underwent a sharp slowdown in its economic growth since 2011 due to reasons of a domestic nature that shifted the macroeconomic policy orientation (Serrano and Summa, 2013). Indeed, Brazil, as the vast majority of countries where the commodity boom was a key factor in their economic expansion, was badly hit by the international recession of 2008-2009 and, indeed, the exports levels (till 2011) did not recover the dynamism of previous years (see Table 4, above). It could be argued, then, that the slowdown in the Brazilian economy was due to the lack of dynamism of exports. But, in fact, total exports have a minor share in the total aggregate demand, reaching only about 11% of GDP (Serrano and Summa, 2013). At the same time, thanks to their monetary policy involving high relative interest rates, the international reserves remained at very high levels (around USD 370 billion in 2015), which would plausibly pave the way to solving the problem of a deterioration in the external accounts. However, although the positive balance of payments slightly dropped after the worsening of the financial crisis, in August 2011 this balance was still positive. This means that as of 2011 although the balance of the payments worsened it was on the positive side of the balance. The empirical evidence suggests that external conditions have not worsened that much in Brazil, and that the lower level of exports alone cannot explain the drastic slowdown evidenced domestically. Naturally, the explanation for the poor results in terms of growth for Brazil in the last few years (see Figure 2) would have to be found in other components of aggregate demand.

Figure 8. Brazil: Current Account balance, Foreign Direct Investment and External Financial Needs, 2000-2014 (millions USD).



In fact, one of the most salient economic policies in the last few years has been a strong fiscal adjustment, trying to put the public balance back to the levels of public surplus of the early 2000s. It is remarkable to note that one of the components that fell most during this period was public investment, which had grown at an annual average of 14.8% in the period 2004-2010, but which sharply shrank in 2011 (–12%). Also, public consumption, which had grown at an annual average of 5.8% during 2004-2010, experienced a drastic fall to a rate of only 0.4% in 2011. This gloomy scenario unfortunately repeated itself during the last quarter of 2014 and over 2015. The general economic situation during the 2016 got even worse (see Section 4). As expected, all these macro prudential policies carried out in Brazil were followed by declines in consumption and private investment. Finally, it is worth noticing that while in 2014 the minimum wage was increased so as to just cover the annual inflation rate (6.41%), the nominal increase of minimum wages (8.8%) did not cover the inflation rate in 2015 (10.7%).

As a consequence, the combination of relatively less favourable external conditions (but which did not affect either the level of international reserves or the indebtedness situation of the country)[11] with fiscal adjustment policies resulted in very low growth rates over the years 2011-2015. In fact, the outlook for the Brazilian economy has turned even more fragile after the devaluation of the national currency (Real) during most of 2015, with an annual depreciation of around 50% in comparison to 2014. Such depreciation was deliberate, as Brazil has not actually had a problem with the balance of payments. This means that both fiscal adjustment and macroeconomic prudential policies along with exchange rate depreciation affected the economy, making the GDP growth to fall to about 3.2%, with increasing levels of inflation. In such a negative economic scenario, unfortunately, the progressive income distribution policies carried out thus far are at serious risk. These negative implications for poverty reduction started emerging in 2015 and continued in 2016, when some fiscal cuts also touched the *Bolsa Familia* benefits and others too, such as *Minha Casa, Minha Vida* (My Home, My Life programme) that provides the poor with cheap credit for access to state-built housing.

Since the external constraint in Brazil does not seem to play the traditional role of being a major obstacle to growth and industrialization (*i.e.*, the developing country problem of needing increasing quantities of foreign exchange to import capital goods and to pay foreign loans), one might legitimately ask what it is that led to the downfall of the Brazilian economy with such negative social consequences. As argued in some recent literature on Brazil (*e.g.* Serrano and Summa, 2013), the causes of the slowdown in that country must be sought not in allegedly bad external conditions, but rather in its domestic situation. In particular, they should be sought in deliberate economic policies adopted to contain inflation that impinged on consumption and, subsequently, on investment. Such policies involved, in particular, permanent policies to keep interest rates high, more restrictions on consumers' credit, an increase in the levels of legal requirements by the Central Bank to private banks (which reduces the availability of loans to the general public), an increase in the minimum capital requirements for lending, and an increase in taxes for financial transactions, and, recently, large fiscal budget cuts. The fierce opposition to government spending programmes has recently been accompanied by calls for privatization of some public utilities as well.

A U-turn in the government's economic orientation, back to neoliberal policies, seems to have been the main driver of the current situation (Merlin and Serrano, 2015). As Kalecki points out (1943, pp. 323), "if labour, plant and raw materials are in ample supply" then there is no reason to be afraid of inflationary pressures if the government intervention aims at achieving full employment through spending programmes. However, there are "political problems involved in the achievement of full employment" (*id.* p.324). Relying on the historical experiences of the 1930s (US, France and Germany before Hitler), Kalecki argues that big business consistently opposes government intervention (especially public deficits to finance massive consumption) to drive the economy towards full employment. On the one hand, this seems to be rather paradoxical because full employment policies not only benefit the workers but also entrepreneurs as profit margins rise during economic boom. But, on the other:

> [U]nder a regime of permanent full employment, the sack would cease to play its role as a disciplinary measure. The social position of the boss would be undermined and the self-assurance and class consciousness of the working class would grow. Strikes for wage increases and improvements in conditions of work would create political tension. (*id*, p. 326)

Kalecki regarded this fundamental reason as being the main cause for business leaders to oppose public investment and spending. In this connection it is notable that in Brazil, at the turn of 2011, the governing party shifted its policy by slowing down aggregate demand, unconditionally cutting taxes to benefit private investment, and strongly devalue the national currency (only stopped in 2016) with drastic consequences for real wages and pensions. In other words, the economic policies of the last few years seems to have abandoned the strategy centred on active fiscal expansion, credits, and public investment, which in fact had led the economy to the highest growth rates of the whole period.

Concluding Remarks and Perspectives

In this paper we have examined some main features of economic growth in two peripheral countries, Argentina and Brazil during 2003-2015. As we have seen both countries had enjoyed extremely good external conditions (fuelled by the commodity boom) which allowed them to cope with the external constraint for most of the period analyzed. High economic growth and export rates have allowed increases in wages, pensions, fiscal expansion and a general improvement in income distribution and poverty reduction. However, after the economic crisis of 2008-2009, the external conditions have turned much more challenging to developing countries than they used to be in the recent past.

The fall in commodities prices, the slowdown of the Chinese economy, Brexit and the critical standstill in the European economic situation will plausibly impinge on the short-term economic situation in Argentina and Brazil. There is evidence of a change in the international situation for developing economies, since a process of *recoupling* of the growth rates is under way. The perceptible slowdown in China, the reversal of the trend of terms of trade for developing countries' exports, the persistent devaluation of national currencies (now even the Sterling) against the dollar, the relative defeat of progressive governments in Latin America and a return to neoliberal-oriented policies, are all indications that the developing countries face gloomy prospects in the coming years.

As we have also argued, both economies have undergone a fall in their economic growth after 2011-2012In For the case of Argentina, although the policy of exchange rate devaluation has been stopped for most of 2015 (the national currency depreciated by about approximately 10% until mid-Dec 2015), the fresh currency devaluation by the new government at the end of that year will most likely impinge on the economy, employment, income distribution and aggregate demand. At the same time, as argued in section 3, the external constraint was being felt the most during the last few years, and was only partially alleviated thanks to the shrinkage of the economy. The foreign situation concerning the actual terms negotiated with hedge-funds (hold-outs that did not accept the Argentinean proposal to restructure foreign debt in 2005 and 2010) will add a further and highly-felt constraint on the balance of payments, and hence is likely to worsen economic growth. As the Latin American structuralist school has put it, the only way to overcome external constraints is development: a structural change that allows countries with unbalanced productive structures (Diamand, 1972) to move from basically exporting raw materials to a path of industrialisation and exports of manufactures. In Argentina, some steps in this direction were carried out until 2015, but essentially the country remains dependent on foreign exchange generated in the primary sector. The current international context is not of much help, and so are the policies adopted by the new administration.

Similarly, recent macroeconomic policies adopted in Brazil will probably lead to a further decline in domestic demand (some speculate GDP will fall by around 3 % in 2016), putting further risks on income distribution policies and poverty reduction. On the other hand, the authorities in Brazil state that all the austerity measures attempt to boost private investment. However, the actual situation is quite the opposite as investment is not being promoted by expanding aggregate demand, but by pushing down the costs of production, in particular wage costs, through currency depreciation (especially during 2015). Still worse, there is no empirical evidence suggesting that demand for labour would be increased if effective demand is not increased too. Also the reduction in public investment, along with the reduction of PAC (Growth Acceleration Program, essentially aimed at infrastructure), in a context of currency depreciation has resulted in GDP shrinkage and rising unemployment. Therefore, the Brazilian authorities now face a major challenge: in an unfavourable international context (especially due to the Chinese slowdown), the only source of growth would be domestic demand, the boosting of which, however, is not the target of

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current policies. Interestingly, the recent development concerning the process of impeachment of president Rousseff initiated in May 2016 has been precisely because of alleged unsustainable fiscal deficits during 2014 and 2015. In other words, while Brazil does not seem to face unsurmountable external constraints, there are political domestic conditions that are currently impinging on the perspectives on the economy. Thus, in the case of Brazil, and unlike the case of Argentina, the structuralist stress on external constraints as being the main barrier to industrialization and development should be dropped in favour of focus on internal constraints, of political and institutional barriers that do not allow the economy to resume economic growth with progressive income distribution and poverty reduction. Little doubt, then, that the challenges that these two economies have to face will have to be addressed in a very unstable scenario, which combine the gloomy perspective for the world economy with the domestic contexts of economic depression, worsening income distribution and rising inequality.

Notes

A previous version of this paper was presented at the International Conference on Financial Instability and Inequality in an Economically Integrated World, organised by International Development Economics Associates (IDEAs), at Tsinghua Sanya International Mathematics Forum, Sanya, China between 22-24 February 2016.

1 See figure 8, below.
2 The new government as of December 2015 eliminated exports taxes both of primary and mineral commodities. Consequently both the current and the expected inflation rates are likely to rise, thus affecting wages and pensions, and in turn the activity and employment levels. See also footnote 10, below.
3 See Crespo and Lazzarini (2016)
4 MERCOSUR is currently composed of five full members: Argentina, Brazil, Uruguay, Paraguay and Venezuela.
5 The minimum wage adjustment formula is based on the inflation rate of the previous year plus GDP growth of the previous two years.
6 The value of this grant as of July 2016 amounts to Reais 77 (circa USD 23) per vaccinated child. For 2015 its value amounted to Reais 82 (circa USD 24). In fact while the increment in nominal terms was about 6 %, the allowance in US dollars was increased by 4%, which is explained by the sharp depreciation of the Real in 2015. In any case, the latest increment of 2016 does not cover the 2015 annual inflation rate which was close to 11%. For further details see: http://www.bcb.gov.br , and http://www2.planalto.gov.br (accessed July 9, 2016).
7 The number of beneficiaries amounts to 3.5 million under-18 children (2015). Moreover, in 2011 a program similar to AUH, the *Asignación Universal para Embarazadas* (*universal pregnancy allowance*, which is a direct benefit to future jobless mothers), was set up. The number of future mothers receiving this transfer in 2013 was 64,000.
8 In 2003 the number of retired people receiving pensions amounted to 3.2 million. Since some of them might have passed away between 2003 and 2013, the real increase will have been above 2.4 million. In any case, the general widening of these benefits for the elderly meant a huge cash injection into the domestic

economy (aggregate demand). However, in June 2016 a new law fostered by the new government passed the Argentinian Congress which, as of September 2016, interrupted the moratorium on would-be pensioners' debts. That moratorium was in fact the process that allowed millions to pay for their debts on their contributions once they have obtained their right to a pension.

9 Source: CEDLAS (http://sedlac.econo.unlp.edu.ar/eng/) and World Bank, as cited in Lustig et al (2012), p. 18.

10 The new administration that took office on December 10, 2015 immediately devalued the national currency by almost 35%. Soon after this measure, a fresh set of neo-liberal policies was unfolded: plan to re-privatize the national pension system through the possibility of private sector purchase of the warrant funds backing the national system; elimination of levies on commodity exports; elimination of import duties (especially on manufactured goods); a fresh reform of the state service aiming at getting a 'more efficient' staff but which implied the firing of thousands of employees; the turn to the Pacific Alliance and the fostering of bi-lateral trade agreements, giving less importance to the regional integration associations in Latin America such as UNASUR or CELAC.

11 The ratio of total foreign debt to GDP was 90% in 1999, 16% average for 2011-2014 and 20% in 2015 (See: Serrano and Summa, 2013; Merlin and Serrano, 2015).

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Andres Lazzarini is at the UNGS/CONICET (National Scientific and Technical Research Council), Argentina.