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# Todos Somos Juárez:

## An Innovative Strategy to Tackle Violence and Crime

by Felipe Calderón

Ciudad Juarez lies in northern Mexico just across the border from El Paso, Texas, one of the cities with the lowest delinquency rates in the United States. In recent years, Ciudad Juarez has been known as the world's most violent city because of its high murder rate, but that is starting to change due to an innovative and comprehensive program implemented in 2010.

The story of Ciudad Juarez is largely driven by economic and social factors. Motivated by a strong expansion of the manufacturing sector after the country opened its economy in the 1980s, thousands of Mexicans from across the country migrated to Ciudad Juarez seeking better job opportunities. The city's population increased 67 percent between 1990 and 2010, and now numbers 1.3 million inhabitants.<sup>1</sup> While the newcomers often found adequate employment, they established themselves in areas that lacked basic services such as water, electricity, sewage, and paved streets. These neighborhoods also lacked transportation and recreational infrastructure. For decades, authorities failed to organize properly the city's urban development and to provide citizens with basic services.

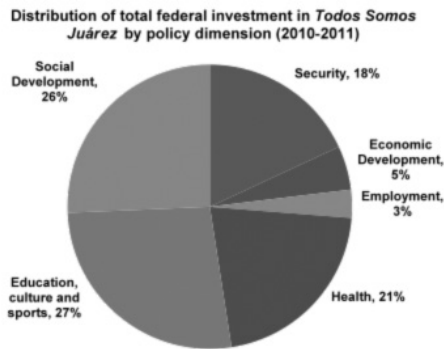
In addition, manufacturing businesses, known as *maquilas*, hired mostly women because the tasks performed required the precision of small hands. This, in combination with the lack of schools, day care facilities, community centers, and organized sporting and cultural activities, set in motion a perverse social dynamic as working mothers were forced to leave their children at home without proper supervision. The abandonment and vulnerability of these children facilitated the eventual spread of antisocial behaviors like alcoholism, drug abuse, domestic violence, and gang involvement.

Other factors that contributed to the deterioration of the social fabric in Ciudad Juarez include its geographical location—it facilitates the trade of drugs, people, and weapons across the border—and the lack of social cohesion of its mostly migrant adult population. The recent worldwide financial crisis, responsible for a 24 percent loss of the city's formal jobs, significantly above the 4.8 percent Mexican national average, according to the Mexican Institute of Social Security, was also a key factor.

Unemployment, the absence of social development opportunities, the spread of antisocial behaviors, and limited community participation created a fertile soil for crime and violence, leading to an insecurity bubble that burst in January 2010, when fifteen young people were murdered at a party as they were mistaken for rivals by one



Figure 1 — Distribution of federal investment in Todos Somos Juárez.



Source: Federal Public Administration.

of the city's criminal organizations. It was clear that the situation was not sustainable and that innovative public policies were needed to restore order and the social fabric of the city. As a result, the Mexican federal government, along with civil society and governments at the state and municipal levels, launched the strategy Todos Somos Juárez (TSJ) on 17 February 2010.

TSJ aims to solve the insecurity problem from its roots and has three main characteristics: community participation, a holistic, comprehensive approach, and coordination and co-responsibility within the three levels of government (federal, state, and municipal). In this strategy, community leaders participated in the design, implementation, and supervision of the program. Participants in the strategy decided that solutions needed to be comprehensive and cover a wide range of policy dimensions, such as public security, economic development, employment, education, health, and social development. For each of these dimensions, one civic council was created; all civic councils included representatives from the community and the three levels of government in

order to ensure proper coordination and permanent community participation.

Once the civic councils were created, they designed a set of policy interventions aimed at addressing not only the effects but also the sources of violence and crime. This translated, at first, into 160 specific policy actions, with a historical federal investment in the city of \$263 million in 2010. In 2011, the councils agreed on 118 additional actions with a federal investment of \$138 million, resulting in a total investment of \$401 million and 278 policy actions. The distribution of the budget reveals the strong social component of the strategy, with 74 percent of resources targeted to health, social development, education, culture, and sports (see Figure 1).

TSJ has achieved some notable results two years after its launch, including:

- **Education, culture, and sports.** More than a thousand schools were included in the "Safe Schools" program, promoting healthy environments through addiction- and violence-prevention plans, and seventy-one schools in poor urban areas extended their school hours. The number

Felipe Calderon, president of Mexico.



Source: [www.presidencia.gob.mx](http://www.presidencia.gob.mx).

of scholarships increased dramatically, and school infrastructure was enhanced significantly so that more youths could obtain a proper education. For example, according to the Mexican Ministry of Education, 14,552 new scholarships were given to high school and college students, the basic infrastructure of 205 schools was improved, five new high schools were built, and five new buildings in three colleges were completed.

- **Health.** Universal health coverage was achieved through a massive affiliation to the Seguro Popular, a free medical insurance program. Four health care facilities were built or remodeled, and programs to prevent and treat drug addictions were given a significant boost, according to the Mexican Ministry of Health.

- **Social development.** Nineteen public spaces, including sports facilities, community centers, parks, and others were rescued or improved so that families had adequate spaces for athletic or recreational activities. Beneficiaries of the antipoverty program Oportunidades, which gives conditional cash grants to low-income families who enroll their children in school and medical examinations, were more than doubled and now number 21,808 households. Also, the subsidized day care

network grew significantly to 105 centers, which now take care of 3,700 children, according to the Mexican Ministry of Social Development.

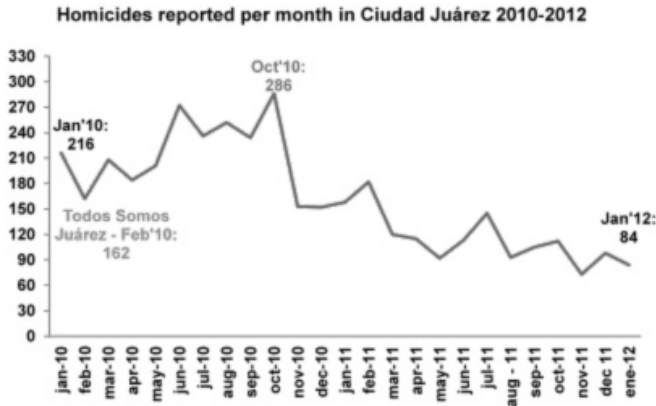
- **Economic development and employment.** Microcredits were received by 1,379 small and medium-sized enterprises, which allowed the preservation of 18,073 jobs, according to the Mexican Ministry of Economy. Additionally, 10,240 job seekers received job-training scholarships, and 25,872 people participated in soft skills workshops, according to the Mexican Ministry of Labor.

- **Security.** To increase law enforcement capabilities, almost 5,000 federal police officers were deployed to Ciudad Juarez: 4,500 for patrolling duties and 500 for the investigation, intelligence, and anti-drug divisions, according to the Mexican Ministry of Public Security. Particular attention was given to strengthen efforts against kidnapping and extortion, which were particularly painful for the citizens of Ciudad Juarez.

The combined effect of these actions has been a tangible reduction of crime in Ciudad Juarez. In January 2010, violence was widespread, and 216 homicides were reported in the city. TSJ was launched the next month, but the strategy did not have a visible impact in the short run, and homicides continued to increase, peaking in October 2010. However, since then, the murder rate has shown a significant decrease. In January 2012, the reported murders went down to 84, a 71 percent decrease since its peak (see Figure 2). Kidnapping and extortion also decreased dramatically.

These results are clearly related to TSJ. Reaching this point has been difficult, but the experience has given us five useful

Figure 2 — Homicides reported per month in Ciudad Juárez 2010-2012.



Source: Mexican Ministry of Public Security.

lessons for cities facing similar situations and hoping to replicate the program:

**1. A holistic approach is key to solve the complex problem of crime and violence.**

In other words, a public policy that tackles economic, social, educational, labor, and health shortcomings, not only security challenges, is necessary.

**2. Community participation is crucial.**

The actions of any government will never be enough if they are not based on community participation and appropriation of the strategy. For example, the young are particularly vulnerable to crime and violence, but they should not be seen as the problem; instead, they must be key players that should contribute to the identification of their own challenges and help develop innovative solutions.

**3. Central governments cannot do it alone.** The federal government should not substitute local governments in the development and implementation of crime-prevention strategies; it must only complement their efforts.

**4. There are no magic recipes, but common sense goes a long way.** Insecurity problems are heterogeneous in each community,

which means that the degree of violence in every city varies. Nonetheless, comprehensive strategies for crime prevention should prioritize those neighborhoods with the highest levels of insecurity and tackle those problems that the community believes are the most urgent.

**5. Be patient.** Results from social and crime-prevention strategies come with sustained and constant efforts in the long run. Participants should not give up if results take time to materialize, and proper care should be taken to communicate to citizens the need to be patient.

Ciudad Juárez has by no means solved all of its problems, and continued effort is needed to consolidate the gains to date. However, the city has certainly turned a corner and faces a more promising future. It is our hope that the difficult experience it has gone through can serve as a model for other cities facing some of the same problems.

**ENDNOTE**

<sup>1</sup> According to Censos de Población y Vivienda 1990 y 2010, Instituto Nacional de Estadística y Geografía.

# Including Latin America's Poor in the Economic Boom:

## A Vision for New Solutions in the Market

*by Luis Alberto Moreno*

Latin America's economies are experiencing record growth. The continent's middle class is expanding, and new jobs are flourishing in the global information economy. Yet, even as people are moving up from extreme poverty, 360 million citizens of Latin America and the Caribbean remain at what is known as the "bottom of the pyramid," according to figures from the Inter-American Development Bank. Basic services are not available to them, and many other obstacles block their path out of poverty. They have no markets, no collateral, and no credit. Traditional development approaches have repeatedly fallen short in addressing these root problems and in providing solutions on the scale needed.

The Opportunities for the Majority (OMJ) Initiative of the Inter-American Development Bank (IDB) looks at these challenges and huge unmet demands with a new vision. Lingering social issues are more than public-sector responsibilities. They are private-sector opportunities. Millions of people in Latin America and the Caribbean living on less than US \$300 a month represent a \$500 billion market, according to figures from the Inter-American Development Bank.

Tapping that market is a great opportunity for the private sector to develop new products and business models. OMJ works with companies that see strategic advantages in engaging with Latin America and the Caribbean's low-income population as stakeholders, suppliers, clients, and entrepreneurs.

We believe that development challenges must combine both public- and private-sector collaboration. To harness the capacity to improve people's lives, partnerships are crucial. At IDB, we have learned that the best partnerships are not short-term or standalone projects. They are long-term commitments to share knowledge and create platforms for collaboration.

In five years, we have built a portfolio of thirty-three projects and corporate deals totaling more than \$200 million under this unique initiative. Moreover, we have leveraged \$1 billion from partners and other investors. Our approvals of loans have increased by more than 50 percent in the last three years, and total disbursements reached \$10.6 million. Currently, thirty technical cooperation agreements are being carried out. Our work generates excitement from businesses across the continent, and

investments will keep growing. In a short time, our initiative has gone from pilot to pioneer. As IDB and OMJ blaze this trail, others can benefit from what we have learned and invest in equally exciting opportunities.

### **OMJ'S INVESTMENTS: MAKING A DIFFERENCE IN PEOPLE'S LIVES**

Our projects bring affordable water, light, and banking to low-income communities off the grid and far away from bank branches. They allow the poor to borrow so they can build homes, educate themselves and their children, eat better, and become healthier. They also incorporate small agricultural producers into lasting value chains and open markets to their products. And they bring financial democracy by backing institutions with cutting-edge techniques for giving credit to those outside the formal credit system.

For example, estimates show that the bottom or base of the pyramid spends almost \$330 billion a year on housing. Using construction as a platform, OMJ finances strategies that are making inroads into this market. In Colombia, we finance Credifamilia, which partners with builders of affordable housing to give mortgages to low-income clients without credit histories or collateral. Credifamilia will originate an estimated 15,893 mortgages in five years. And in Peru, we are financing a network of microfinance institutions so they can offer housing loans and mortgages—mitigating their risk while extending their market penetration.

Much of Latin America's population is engaged in microentrepreneurship, working on a very small scale. OMJ has incubated several projects that tap into that entrepreneurial spirit. In Brazil, Tenda Atacado is giving working capital to vendors who make meals and snacks to

buy supplies and equipment as well as offering training for individuals to grow their businesses. Peru's MiBanco is reaching out to support female entrepreneurs also through loans and training. OMJ expects to benefit 10,000 and train more than 100,000 women.

Our projects are exciting and encouraging. Yet, compared to the possibilities of the mass market, they are still modest. We believe that our pioneering investments can be repeated and extended on a massive scale, becoming a real economic force to help improve the livelihood of a majority of our region's population.

### **HOW IT ALL STARTED: IDB AS A PIONEER**

We at IDB wanted to pilot new approaches to solving poverty with private companies. So, we expanded our traditional focus on large lending to the private sector for infrastructure projects, capital market formation, trade finance, and small and medium enterprise finance.

In doing so, we founded OMJ in 2007 as a center of excellence whose aim is to capture and incubate new and practical ways for businesses to enter low-income markets in meaningful and sustainable ways.

As a small and nimble team operating within IDB's Private Sector Group, our Opportunity for the Majority Initiative is the first and only operational base-of-the-pyramid business unit set up within a multilateral development bank. Through OMJ, IDB provides medium- and long-term loans and partial credit guarantees, as well as non-reimbursable technical assistance. Though small, OMJ's team benefits from IDB's large footprint and vast experience in the region to design new business models and support companies interested in moving into low-income markets for strategic reasons.

Our initiative became operational in 2008. First, the team studied publicly traded companies in eleven countries in Latin America and surveyed hundreds of top executives in thirteen countries who were already working with the base of the pyramid or who were interested in doing so. Later, we mapped private-sector companies and studied where private-sector solutions would clearly make a difference: housing, health, information and communication technology, and nutrition.

Backed by research, we started working with and funding companies and financial institutions, designing new business models targeted to the poor. These models are market-based, high impact, and strategic. They are meant to improve a company's core business. To be eligible for financing, projects must engage multiple stakeholders, be financially sound, and be able to move beyond the pilot stage. OMJ finds that companies typically do not need support to innovate products. Where they need support is in finding innovative ways of distributing their good or service. That is where OMJ's expertise in penetrating low-income markets comes to bear.

We also learned that a model's success depends on whether a company's senior management is committed to moving into base-of-the-pyramid markets and has a creative and well-designed strategy to do so. Projects that meet our criteria and are financed can leap to the next stage, be brought to scale, then replicated across the region and beyond.

One example is Salvadoran family-owned pharmaceutical company ANCALMO. Thanks to OMJ funding, it is becoming the first local producer and distributor of micronutrient powders to tackle the alarming levels of child malnutrition in the

region. After rolling out its new product in El Salvador, ANCALMO is in a position to sell to Guyana, Guatemala, Nicaragua, and the Dominican Republic. Governments there have resources to buy and distribute their micronutrients through conditional cash transfer programs, benefiting up to a million children. With experience producing for children, ANCALMO will be in a position to manufacture a formula for pregnant women and target that underserved market.

### **OMJ INNOVATIONS: CRACKING THE CODE IN CONNECTING BUSINESSES WITH THE BASE OF THE PYRAMID**

Private companies take a risk when they enter low-income markets in part because the poor is largely unbanked and has no credit history. OMJ shares some of the risk by designing guarantees for pools of microborrowers. If a pool's repayment dips below a certain percentage, the guarantee is triggered. This way, we can share risks with large corporations to support microborrowers who buy goods or services through installment payments. That is a new way of applying principles of microfinance to corporate deals so that firms can meet the needs of the poor.

A good example is OMJ's partial credit guarantee of up to \$10 million to expand the highly successful Patrimonio Hoy program, launched by Mexico-based multinational cement producer CEMEX. The program gives low-income consumers who are largely shut out of the traditional banking system access to microloans to buy construction materials. With its guarantee, IDB shares in CEMEX's risk as Patrimonio Hoy scales up beyond Mexico to Colombia, Costa Rica, Dominican Republic, and Nicaragua, giving a million families the chance to improve their homes or build new ones.

In addition to providing financing, we forge partnerships to connect the private sector more deeply with underserved markets. To do it efficiently and affordably, OMJ connects businesses and utility companies, public agencies, retail operations, community savings and loans associations, homebuilders and nonprofits. This innovative use of distribution channels is dubbed “cracking the code.” In cracking the code, we bring projects to scale much faster and more effectively than starting with a small pilot project that must be tested and brought to scale gradually. The right platform also ensures a company or financial institution connects with its target market.

Only business models that meet our specific requirements receive technical assistance. Assistance is meant to enhance and flesh out solid ideas and improve their penetration as they are rolled out in the market.

To ensure success, all projects are subject to a rigorous evaluation against IDB’s operating principles, credit risk analysis, environmental safeguards, and a scorecard that weights innovation, social impact, and potential to scale and replicate. In addition to measuring economic and financial viability of projects, we evaluate the targeting of investments to benefit low-income populations in the IDB’s twenty-six borrowing member countries.

In addition, our initiative is a pioneer in measuring the social impact of our projects. A powerful new software system serves clients and IDB as they report on the social return of the portfolio. In addition, we measure social outputs and outcomes of investments through industry reporting and investment standards. Furthermore, each project’s economic rate

of return is tracked, as is the project’s performance over the life of the IDB credit. Clients are required to report quarterly on indicators measuring a project’s commercial and social performance. All of this careful tracking makes it clear that the private sector has a unique and powerful role to play in development.

### **PRIVATE-SECTOR SOLUTIONS CLOSE THE INEQUALITY GAP**

In supporting businesses that are helping to close the inequality gap, the IDB creates employment and enables micro-entrepreneurs and consumers to participate in the formal economy. Through partnerships with companies and financial institutions, we offer businesses the chance to make effective contributions to solving poverty’s challenges. The time has come to think about working on a significantly larger scale. In years to come, successes in Mexico will be adapted and replicated in Chile as well as the other way around. Seeing what the competition is achieving, companies will rush to develop base-of-the-pyramid business plans of their own. Pilot projects will be scaled up to reach millions.

Reaching the unreached is all about having the vision to recognize and act on the vast and untapped market potential of the base of the pyramid in Latin America and the Caribbean. Word of OMJ’s steady growth and project success is spreading, and our pioneering work is being adopted by the mainstream. As demand for doing business with low-income communities rises, bankers throughout development institutions are thinking differently about business models. The IDB is proving that engaging in market solutions for the base of the pyramid in Latin America and the Caribbean increasingly provides lasting benefits for investors and consumers.

# The Yasuní-ITT Initiative: Daring to Think Outside the Box

by Alberto Acosta

*“First they ignore you, then they laugh at you, then they fight you, then you win.”*  
— Mahatma Gandhi

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Breaking traditions and myths will always be a complex endeavor. The so-called realism slows down change. Those whose privileges may be affected resist change. And there will always be those who, invoking pragmatism, will seize opportunities to set back those changes. Therefore, the idea of not exploiting the 850 million barrels of crude oil from Ecuador’s Ishpingo, Tambococha, and Tiputini (ITT) fields, located in the Yasuní National Park, in exchange for international financial contributions has shocked many and generated plenty of resistance. In a global economy addicted to oil, the proposal of not extracting crude appears to be complete madness—more so for an underdeveloped country that is highly dependent on oil revenues. What’s surprising is that this crazy idea has been generating followers and gaining momentum.

While the acceptance of this idea by Ecuadorian President Rafael Correa and his continued support have been important, Correa’s doubts, repeated inconsistencies, and incoherent actions have also threatened the Yasuní-ITT Initiative.

## A PROPOSAL THAT EMERGED THROUGH RESISTANCE

Ecuadorian civil society had been supporting this initiative long before it found its way to President Correa. This proposal was built collectively and has no sole owner. When I was Minister of Energy and Mines in January 2007, I was in the right position to introduce it to the rest of the government. And it is quite likely that the idea to discontinue all oil-related activities was first conceived in the minds of those who have suffered firsthand the disastrous effects left behind by oil companies in the Amazon region.

The plight of these Amazonian residents became known internationally via a lawsuit referred to as “the trial of the century.” In 1993, indigenous communities and local settlers of Ecuador’s Amazonian rain forest filed a multi-billion dollar lawsuit against Texaco, bought by Chevron in 2001, for fouling their land. An \$18 billion ruling against Chevron in the eighteen-year case was upheld by an appeals court in Ecuador in early



2012. This case has set a historical precedent by prosecuting one of the most powerful oil companies on the planet.

The proposal of placing an oil moratorium on the center-south region of the Ecuadorian Amazon emerged within these circumstances, during a long and arduous process of resistance against oil-extraction activity. This proposal, formulated in various spaces and forums, was publicized in the book *El Ecuador Post-Petrolero (Post-Oil Ecuador)* in 2000 (Oilwatch 2000). In the year 2001, various groups questioning Ecuador's foreign debt offered the possibility of a historical agreement in which international creditors would suspend debt service in exchange for the ecological conservation of the Amazon region; this proposal follows the same logic as the ecological debt demand, in which rich countries appear as debtors. A couple of years later, the oil-moratorium thesis was formally presented to the Ministry of the Environment by several ecological foundations.

In a different area of the Amazon, the resistance and protests of the Sarayaku Kichwa community, in the province of Pastaza, were able to stop the oil activities of the Compañía General de Combustibles in Block 23. This was a great triumph of a small and organized community, considering that the aforementioned oil company received armed support from the state. The same community, which garnered active international solidarity, was able to obtain a historical pronouncement from the Inter-American Commission of Human Rights in July 2004, when this institution dictated a series of provisional measures in favor of the indigenous people of Sarayaku. During the first half of 2007, the Ecuadorian government finally

accepted this resolution. However, soon after, the Sarayaku were again threatened. In the contract renegotiation of Block 10, between President Correa and the company AGIP, which took place in November 2010, national authorities gave the company a piece of Block 23, directly affecting the territory of several Amazon indigenous communities.

All of these proposals and initiatives became the building blocks for the oil-moratorium proposal, which progressively found its way into the national political agenda. In a historical moment that consolidated these and many other struggles, the oil-moratorium became part of the Government Plan 2001-2011 of Movimiento País (now the political party Alianza País), written in 2006.

In June 2005, a proposal to stop crude extraction from Yasuní was unveiled as part of an ample oil-moratorium scheme in “Un Llamado Eco-lógico para la Conservación, el Clima y los Derechos” (“An Ecologic Call for Conservation, Climate and Rights”), a position document written by Oilwatch (2005b) during the first meeting of the special group of experts on protected areas, which took place in Montecatini, Italy. Later, the same thesis was incorporated in the book *Asalto al Paraíso: Empresas Petroleras en Áreas Protegidas (Paradise Assault: Oil Companies in Protected Areas)* (Oilwatch 2005a).

I want to emphasize that the most relevant details of the initiative to leave crude oil in the ground were defined long before the beginning of President Correa's administration.

## THE ESSENCE OF THE YASUNÍ-ITT INITIATIVE

The Yasuní-ITT Initiative is based on the following four pillars:

1. To conserve the area's unparalleled biodiversity (planet-wide, the largest biodiversity registered by scientists to date)
2. To protect the territory and the lives of indigenous people in voluntary isolation
3. To care for the world's climate by keeping underground a significant quantity of crude oil, avoiding the emission of 410 million tons of CO<sub>2</sub>
4. To take Ecuador's first step toward a post-petroleum transition, which could serve as an example to others

We could assume that a fifth pillar is to collectively find—as mankind—concrete answers to the grave global problems we have originated that have exacerbated climate change, especially in the latest phase of global capital expansion.

As a counterpart measure, Ecuador expects a financial contribution from the international community, which would signal that it is owning up to its shared and differentiated responsibility as a function of the level of environmental destruction caused by the many societies of the planet, particularly by the most opulent ones. This proposal is not about vulgar compensation to continue forcing “development,” as President Correa sometimes interprets it.

A vital issue in the initiative is how we will use the financial resources. Through a complex process of internal discussions, the Ecuadorian government has already defined the use of the profits from the capital fund created to not exploit the ITT oil fields. The trust fund will be super-

vised by the United Nations. There are five stipulated goals: the transformation of the energy matrix via the development of alternative sources of energy in the country; conservation of protected areas; reforestation; promotion of sustainable social development, particularly in the Amazon region; and investment in technology research.

Beyond Ecuador, the initiative proposes profound changes in the relationship between world societies and nature with the establishment of an ecological global legal precedent. Within this new order, the developed countries, which are mostly responsible for the world's environmental deterioration, are required to contribute more to the solution of global environmental problems. Additionally, based on this new paradigm, the logic of international aid must be fully restructured. This should be absolutely clear: the expected financial contributions are not part of the so-called aid for development.

In summary, this proposal opens the door to worldwide changes. Within Ecuador, change must be understood as a necessary step to force a structural transformation of the extraction regime as well as a transformation in the energy matrix. This initiative proposes a move to a post-petroleum economy with the goal to de-carbonize the atmosphere.

## THE DIFFICULT MARCH OF A COURAGEOUS INITIATIVE

Shortly after the initiative's official announcement, encouraging voices multiplied rapidly, more so abroad than in Ecuador. The possibility of crystallizing something that seemed unthinkable increased in many societies as well as in the legislative bodies and governments of several countries. The positive commentaries reproduced with an accelerated

pace when the possibility of confronting global warming became palpable.

The path in Ecuador proved to be extremely tortuous. In the beginning, the proposal to keep crude oil untouched underground, which I formulated as Minister of Energy and Mines, clashed with the decision of the executive president of Petroecuador, who was focused on extracting crude oil as fast as possible.

This first confrontation was settled with the intervention of President Correa at Petroecuador's board of directors meeting on 31 March 2007. At that meeting, it was decided that the first option would be to leave the crude in the ground as long as the international community provided at least half of the funds that would have been generated from the oil extraction. As a second option, in case the initiative did not prosper, the oil extraction was agreed upon. Since then the struggle between these two options has remained in a latent state with various degrees of intensity; this serves to acknowledge that the two options clearly reveal divergent positions on how to approach oil production and development itself.

On 18 April 2007, the national government, with the approval of the president and under the initiative of the Ministry of Energy and Mines, promulgated the Policy for the Protection of Communities in Voluntary Isolation. And on 5 June 2007, the Yasuní-ITT Initiative was officially presented at the presidential palace. That same month, on 14 June 2007, the Ministry of Energy and Mines established the Energy Agenda 2007-2011.

Later on, during a phase of continuous struggle, the initiative would experience stellar moments as well as moments of increasing doubt. President Correa

received high praise from the international community when he presented the proposal to protect the Amazon region and thus avoid a major negative impact on the global climate. The proposal was presented in various international summits including the United Nations, OPEC, and the World Social Forum.

Germany's initial support is worth highlighting. Representatives from all factions of the Bundestag, the German parliament, publicly pronounced themselves in favor of the Yasuní-ITT Initiative in June 2008 and called upon their government to decisively support it. This endorsement opened up multiple doors, and therefore, it came as a great surprise when, in September 2010, the German Federal Minister for Economic Cooperation and Development Dirk Niebel decided to give the initiative an unexpected low blow by publicly criticizing the proposal and therefore officially withdrawing German support. Niebel's decision had an undermining effect on the possibility of consolidating additional financial support because many other potential contributors assumed that Germany was a solid supporter of the initiative.

The Ecuadorian government's actions are also worth noting. Acting with incoherence, the Ecuadorian government continued promoting the possibility of extracting at least part of the oil in the ITT fields. The option of oil exploitation in the Tiputini, and even in the Tambococha field, is still being discussed in the highest government spheres.

The government project to leave crude oil in the ground finally consolidated with the establishment of a new negotiating commission in July 2008. With this new commission, Ecuador overcame a

complex phase characterized by a procedural vacuum to make practical decisions. A couple of months later, in December 2008, a new Minister of Foreign Affairs who was in favor of the initiative was sworn in, giving the initiative a much needed boost. Finally, in February 2009, the government declared an indefinite period for collecting the expected financial contributions, and the Ministry of Foreign Affairs took responsibility for continuing all actions related to the initiative.

Civil society also started interesting debate regarding the initiative, which later on achieved greater intensity and depth. Different civil society segments from within Ecuador as well as abroad have contributed with several documents and other valuable inputs. Thanks to this debate, the initial proposal based on international compensations or donations was modified to give way to the new thesis of international contributions based on shared and differentiated responsibility via the basic principle of ecological global justice. The discussion also clarified the initiative's multiple financing options.

### **AN INITIATIVE TRAPPED IN ITS OWN SUCCESS**

When the project began to show clear signs of success, President Correa himself gave the initiative an unexpected blow. Though he was the only dignitary in the world with a solid and novel proposal for confronting global warming, he decided, without a valid argument, to exclude himself from the United Nations Climate Change Conference (COP15) that took place in Copenhagen in December 2009.

Additionally, after having authorized the Ecuadorian representatives to ratify the international trust fund for the Yasuní-

ITT Initiative at COP15, President Correa changed his mind at the last minute. It is important to highlight that the document was written by the Ecuadorian government without any external involvement. A few days later, at the beginning of January 2010, he made an unwise declaration in which he even attacked potential contributors to the Yasuní-ITT fund, dissolving the negotiating commission and inducing the resignation of the Minister of Foreign Affairs.

Due to the aforementioned presidential statements, the apparently lethargic oil companies' representatives and shysters launched a massive disinformation campaign with the goal of discrediting the initiative. President Correa's actions have had international impact. In simple terms, President Correa, consciously or subconsciously, decreased the initiative's credibility and momentum. Ever since, he has gravitated toward a negative position against this revolutionary idea.

Paradoxically, many people in Ecuador heard about the initiative for the first time because of the negative impact of President Correa's public statements. Civil society's positive reactions were viewed as a wake-up call.

The new negotiating commission did not have the high profile or the influence of the former. The person in charge of overseeing negotiations, Ivonne Baki, does not appear to have the necessary socio-environmental knowledge for the position. Additionally, she has a controversial political history, having stood up for Texaco's interests, as well as being known as the "great cheerleader" in favor of the bilateral Free Trade Agreement with the United States. This agreement was settled due to popular protests against it. Toward the end of 2011, Baki

presented a list of potential contributors to the initiative representing \$116 million, from which less than 2.5 percent were solid contributions.

There is a generalized suspicion that the oil companies' interests have once again become the priority. The envisioned success of the initiative generates new and complex threats. There is no doubt that the initiative is besieged by President Correa's hesitations and the oil companies' permanent pressure. It seems as if the initiative is beyond the presidential ability to truly understand it and take favorable action.

### **MANY THREATS HAUNT YASUNÍ**

Under current conditions, clear signs are still needed to ensure the proposal will become a reality. Coherence and consistency at the government level are essential to the success of the initiative. The trust fund must provide the necessary assurance to potential contributors without affecting Ecuadorian sovereignty. The balance between assurance and sovereignty is crucial for the appropriate use of the financial resources. However, a solid trust fund is not sufficient to keep the initiative going forward.

President Correa must repair the problems that he himself has created, and it is his duty to provide new and strong support signals for the initiative. It would be beneficial if he formally agrees not to exploit the ITT during his administration, which would provide a stable time period for negotiations. Additionally, he should not tolerate oil-related activities in the margins of the ITT, including any action that could endanger communities living in voluntary isolation in the Amazon region. Moreover, the government should stop other threats to the Yasuní area such as deforestation and illegal extraction of

wood, single-crop farming and its contaminating effects, uncontrolled settlements, illegal tourism, and the construction of the multimodal infrastructure project Manta-Manaos, a project within the context of the Initiative for the Integration of the Regional Infrastructure in South America. In short, the government should control the activities in the adjacent oil blocks and the surrounding roads servicing these blocks that give way to the harmful activities previously mentioned.

In addition, it would be wise to incorporate Block 31 to the Yasuní-ITT initiative. This oil block is located on the west side of the ITT and contains little amounts of low-quality crude oil. This block can only become profitable by exploiting the ITT fields. Similar actions are necessary in the neighboring east regions of Peru, given that only a third of the oil reserves are located on the Ecuadorian side. A potential expansion of such magnitude would ensure a protected area with similar characteristics of mega biodiversity inhabited by indigenous communities in voluntary isolation. All these blocks added to the intangible area in the south of the Yasuní Park would result in an important life reserve.

This initiative is probably the best proposal to confront global warming since it defines common and differentiated responsibilities designed to ease everyone into the transition to a new oil-free economy with alternate sources of energy. As a reaction to carbon markets, the initiative focuses on oil. In the context of the neoliberal commerce of emissions, the initiative proposes a scheme close to the acknowledgement of the ecological debt, where industrialized countries are the debtors.

The Yasuní-ITT Initiative proposes avoiding carbon emissions altogether, and by doing so, it thwarts the logic of current environmental policies. This initiative must go against the logic of commodifying and privatizing air, forests, trees, and the earth itself; in essence, it must go against the expansion of the frontiers of capital colonization.

### THE UNDISPUTED SUCCESSES OF AN UNFINISHED PROJECT

Beyond the existing threats, nourished by the incoherent actions of the Ecuadorian government and the voraciousness demonstrated by the oil lobby, the initiative already shows satisfactory results even before crystallizing. The Yasuní-ITT debate is well-positioned within national and international arenas.

In Ecuador, there are those who claim, with powerful arguments, that even without international financial contributions, the Yasuní-ITT oil should be kept underground. This third option could actually become a reality if we enforce the constitutional provision that in order to extract resources from protected areas, there must be a well-supported petition issued by the Executive along with an official favorable statement from the National Assembly. This body even has the authority to call for a referendum on the matter if it deems one necessary. In other words, the Ecuadorian people would make the final decision.

Given the circumstances, civil society must stay alert. It should remain absolutely clear that the only guarantee of success of the Yasuní-ITT Initiative is in the hands of civil society in Ecuador and the rest of the world. We must transform our domestic and international setup, which is currently dominated by oil interests that are ready to do the impos-

sible to tame the innovative potential of this revolutionary proposal.

The Yasuní-ITT oil represents 20 percent of Ecuador's reserves and only nine days of energy to humanity.<sup>1</sup> Keeping this oil underground will promote a much needed communion between humankind and nature and will open the door to a new era without fossil fuels, as the biophysical limits of oil are foreseeable.

I hope that many similar initiatives will flourish around the world, setting aside egotistical and myopic agendas. The motto is to create two, three, and many more Yasunís.

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### ENDNOTE

- <sup>1</sup> Current global oil demand is around 90 million barrels of oil per day according to the International Energy Agency. Yasuní-ITT holds around 850 million barrels of oil.

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# Cultural Policies for Strengthening Identity and Cohesion in Latin America

*by Susana Baca and Cesar Recuenco*

Thanks to its history, the Latin American reality is peculiar and unique. The Latin America in existence today is a product of its past, starting with the miscegenation, or racial blending, that occurred along with acculturation in the Mesoamerica and Andean regions. Additionally, it is a clear example of transculturation. Latin America was built from the encounters and clashes and the resistance and adaptation of the many civilizations and social and human groups who have inhabited it.

With the arrival of European colonizers, who denominated the region as Latin America, the existing civilizations and cultures in the continent found their vision of the world and their livelihood altered and violated. Nonetheless, an autochthonous, or indigenous, sentiment became part of the continent, including an approach brought by the Iberians. This marks the first step in the process of defining the Latin American identity. A second important moment was the arrival of the third race of Latin America: the African population. Brought over in infamous conditions, this population was not able to exclude itself from the process. From that moment, the Black, the indigenous, and the Spanish became the foundation of what we now know as the roots and formations of the cultural processes and the richest forms of the Latin American identity, where life, with more or less symmetry and asymmetry, is celebrated or lamented.

The interactive framework of this culture, shaped through a long and unfinished process that has been influenced by many historical episodes, has allowed for the enrichment and the strengthening of a self-identity, formed by the continent's diversity. Consequently, Latin America is multiracial and multiethnic; its past and current civilizations have contributed their own knowledge regarding ways to live, to view life, to dance, and to carry on traditions, the manifestations of which are, at the same time, intrinsic to the identity of each people and yet able to be shared as a common culture. For this very reason, it isn't advisable to try to put an order of importance on these elements because none can be excluded.

A popular proverb goes, "One who has not played the drum has shot arrows." This describes what it means to be a part of Latin America. This identity does not try to define us or differentiate us, but rather reaffirm us. We were born as a result of undeniable historical episodes, and we sustain ourselves in a need for belonging, so we can feel



as one and, at the same time, also see ourselves reflected in a common history with European, African, or indigenous roots.

Therefore, once we locate ourselves in the context of our America is the time when we require our peculiarities to be able to design our own cultural policies, which are a product of reflections from a region named Peru. Peru is a country with multiple languages and a diversity of wisdoms, traditions, and values. It has a history of suffering and courage, of dialogue and struggle with nature, and of traumatic and/or cooperative cultural encounters. All of these have led the human group that defines society to have different perceptions of and perspectives on life. Maybe there are no common cravings among people other than inclusion, peace, respectful dialogue, and concern for living in a country where colonial relationships are still present in the institutional and economic realms, which have impacted ancestral communities almost to extermination. So, then, in a place where cultural tradition and even religious systems express themselves with bitter violence and long-lasting and ferocious rejections, in the three Americas attempts are made to improve intercultural dialogue, inclusion, peace, and development.

It is evident that the birth of a Latin American nation like Peru cannot dismiss the indigenous, Black, and European (Moresque Spain) contributions to its formation. We believe that the end result is not a mathematical sum of these three elements but rather a union in which the individualities of each remain distinct. And thus, our identity proclaims us as a country of multiple ethnicities. It must be clear that Peru did not start as state of symmetry in well-being, or in mutual knowledge and respect, or in lack of oppression, death, and violence as a

means to resolve disputes, or in the experience of divestiture. Realistically, no one has yet to achieve the good life. The state of well-being and moral satisfaction is expressed in friendship with nature, in respect for rights, in opportunities for the talents of all, in the active search for the well-being of those less fortunate, and in the caring for the orphan, the widow, the elder, the ill, the foreigner, and the wanted by justice.

The artists of each country—signers, writers, painters, sculptors, dramaturges, choreographers, dancers, directors, actors, mimes, and artisans—are exceptional witnesses of society. Their masterpieces portray the magnificent splendor of both the present and the potential future of their country. But they also show the pathetic nature of injustice and misery. The artists, in their work, manifest the Latin American reality to make it accessible to all through a culture of peace, which reminds all of us of the good life. For that reason, ensuring the health and security of artists is an important issue for both the state and society.

However, this is easier said than done. Addressing the protection of artists requires a high level of will and interest from the community as a whole in addition to changes in the legal framework of culture. This is why in Peru many efforts have been carried out—and must continue to be carried out—to consult managers and cultural producers, artists, and entrepreneurs, ethnic organizations and community federations, archeologists, and thought leaders regarding the goal of proposing a new “general law of culture.” This exercise requires dialogue amongst all social actors of a country. It also entails the intervention of political actors like ministers and those responsible for culture so that the legal framework

finds correspondence with the dynamic realities of the continent and thus achieves the desired identity that the Latin American people need.

Having introduced the topic of a Latin American identity, it is impossible to ignore the idea of a social identity. Social identity is the constant and self-defined practice of each human group, taking into consideration the interests that define and defend the group's existence in a context where the convergence of distinct interests is imminent. Thus, it is essential to examine the construction of the identity in Latin America in order to understand the past events and the elements that have built and strengthened it. Those elements contribute to forming and/or strengthening a sense of belonging to the social nucleus, thus generating the appearance (or recognition) of the social-cohesion phenomenon.

The development of media and cultural industries is vital. They offer a way to see into the experiences and creations that are at the core of our people and to gain a better understanding of countries with a similar cultural heritage.

Today, songs are sung everywhere, and they already belong to every Latino (allowing them to feel identified), thereby promoting cohesion. And in the imagination of each individual inhabit the characters of multiple authors. Film and television have enabled the introduction of a global culture, rapidly changing, according to some, while perversely consistent and conservative, according to others. Meanwhile, each country moves forward at its own pace, reducing inequalities, recognizing the rights of all, and discovering and valuing the heritage of their peoples. These actions help in the recovery of cultural knowledge, which

reduces the impact of other human activities that have a detrimental effect on cultures.

There is no doubt that only the intercultural dialogue and respectful attention of knowledge and values will allow the acquisition of tools to prevent further social dislocation or to correct past mistakes. Peru, for example, has begun to lay the groundwork for a national system of defense and enhancement of tangible and intangible heritage of the various peoples that make up our country. The efforts of the first artist minister, in charge of the Ministry of Culture during the first term of Peruvian President Ollanta Humala's administration, have outlined a system that integrates various levels of authorities, community leaders, and student brigades. The system mobilizes volunteers to guard archaeological and historical sites and calls on student reporters to monitor and to know the value of each of the cultural elements. These actions are promoted in the interest of appealing to investors and raising community awareness regarding the relationship between culture, tourism, respect, and development. It is urgent to place new value on the historical facts, making them known and giving them the meaning and importance that they deserve, because through this recognition we will generate commitment to the conservation of tangible and intangible cultural heritage.

The rethinking of past events through cultural policies that place renewed value on them allows for the search of a certain future and shapes citizens' ability to critically analyze the common problems that plague our continent. It is known that the destruction or disappearance of expressions of culture of a people (for example, due to acculturation) leads to loss of social identity

(with adverse outcomes) and does not allow us to advance on the path to cohesion and integration. Forgetting the past is an obstacle in the construction of our identity, preventing us from becoming part of the traditions that make up the cultural background of our people. The construction of identities and their strengthening will give us a sense of belonging, a necessity inherent to every human being, and thus, this still is—and will be—the great dilemma of Latin America.

With respect to a commitment to development goals, it is necessary to allow for a culture in which every family knows what is best to defend the lives and talents of their children. It is recommended to promulgate a culture of respect for the individual in schools, to not accept as normal the idea of failure or insufficient learning. It is also recommended to promote a culture of respect for the worldview of all populations and minorities that inhabit the continent. With respect to a commitment to a culture of peace, we need to promote dialogue and peaceful resolution of conflicts. We must commit to fair trade, which promotes the recognition of the efforts of the less fortunate. And without a doubt, an important point is to reduce the arrogance of trying and pretending to civilize groups with different cultures. It is also important to increase the interest in and approach to our own values and knowledge. We must begin by promoting respect for the view that cultures and civilizations (now a minority) have of the world. More than 500 years ago, local cults were destroyed to impose Western ideas that were very different from those of the people of the Americas. Such events cannot happen again in the name of so-called modernity because they reverse the principles of coexistence needed by all people.

There is no doubt that culture impacts the social and economic development of people. In Peru, only cultural industries grow at a rate of 11 percent annually, which is high compared to other industries, and the impact of cultural heritage on tourism is recognized and remarkable. Expanding cultural industries and the wonders of its heritage creates jobs and benefits communities. The challenges in this field would be measured by the price of losing Machu Picchu, Kuelap, Caral, Pachacamac, Chavin, Sicán, Cao, or Sipan, to name a few of the archaeological sites of Peru (although there are at least twenty monuments in need of shelter or renovation, and the cost of losing any of them, either through carelessness or overexploitation, would be priceless).

On the other hand, it is clear that population growth and urban expansion have significantly increased the pressure on the Peruvian paleontological, archaeological, and historical sites, threatening their integrity. Beyond the thirty most spectacular and well-known heritage assets, nearly 10,000 sites have been identified and must be described, registered, investigated, placed on value, and disseminated. A dispensable topic of cultural policy implies that the presence of these sites in communities and districts where they are located becomes a factor of development of the culture of the country and society. There are places that have been invaded and looted; in other cases, certain materials have been recycled into utilitarian family buildings, thereby facilitating the loss of unique pieces. This has been a constant reality in Latin America and in Peru, as it is the principal place of development of the Andes. However, making known to all citizens the symbolism and meaning that these archaeological complexes contain, as well

as their importance in the context of the culture of the country, will awaken a sense of belonging by engaging neighboring populations in their care and protection.

In addition, the cultural industries, whose growth rate is admirable, require resources for national casts and conditions necessary for the promotion of living cultures. For example, the development of national libraries and general archives involves the allocation of resources to overcome situations of vulnerability and to open up their services to the general public and to specialized researchers. This last one is important for a simple reason: there is no worse poverty than the poverty without peace, beauty, and memory and with the loss of history and dignity.

Finally, promoting new dialogue at the highest level, through the ministries or institutions representing culture in the Americas, about the relationship between culture and new technologies and the impact and possibilities that they bring to inclusion, peace, and development is necessary and indispensable. Developing great cultural dialogue is required to achieve consensus that allows the collective development of society in a continent such as Latin America that brings together all ethnicities. Therefore, we must renew our faith in the potential of culture and in the dialogue between artists and cultural managers. Culture is no longer the last round and should be recognized as an investment for peace and development in Latin America. This is the challenge and commitment that must be achieved in favor of the welfare of the people of Latin America.

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# Inclusive Development:

## College Students and Settlers Working Together

*by Agustín Wolff*

Young people have always mobilized in favor of causes they find unjust and that they want to change. Their power to organize and make their voices heard is a phenomenon that can be clearly seen today in different parts of the world. Their power has been increasing globally.

It is through these people that Un Techo para mi País (TECHO—A Roof for my Country) has worked for the past fifteen years. The organization's goal is to build a just society, where there are no people living in extreme poverty or suffering vulnerabilities of their human rights.

By working together with families in slums and with university students, TECHO has summoned society to work toward a common goal of all people having equal opportunities to develop their capabilities and exercise their rights.

In this joint effort between volunteers and families, the needs of communities are identified and a number of solutions and programs are executed in order to overcome those needs. The tools that TECHO makes available to the community to work on those needs are framed in the social empowerment program. This program runs in slums and settlements and takes different forms and approaches, such as building emergency housing and making plans for education and work, in response to the local situation and opportunities.

TECHO facilitates volunteers and settlement residents working together to conquer a shared goal. This way, TECHO aims to have an immediate, as well as a long-term, impact. The long-term effect comes into play with the thinking that when these volunteers become the decision makers in their countries, they will make ending poverty part of their work.

Thanks to constant innovation of its social intervention model, as well as the mobilization of volunteers committed to ending the extreme poverty in which thousands of families live, TECHO is now present in nineteen countries in Latin America and the Caribbean. In all these countries TECHO's volunteers are gathered around the shared indignation of seeing families living in precarious conditions, the motivation to achieve structural changes in poverty, and the conviction that overcoming extreme poverty is possible when all sectors of society are involved.

The hallmark of these interventions is that settlement families are the protagonists of their own change; TECHO is only an enabler. The work being done in these communities is not *for* them, but rather *with* them. This motto delivers a distinctive seal to the whole intervention.

With different innovative initiatives, TECHO makes a clear statement to society that the poverty figures that currently exist in the world are scandalous and intolerable. One such initiative was the first Latin American Meeting of Slum Leaders, held in October 2011, where more than one-hundred settlement leaders met in Peru with the goal of discussing common issues, sharing experiences, and proposing new ways to work.

The conclusions from this meeting were written in a manifesto, which included the duties that leaders pledged to fulfill and the rights that they would demand, while taking charge of their own development and proposing partnerships with other organizations and governments.

This example shows how the work with communities is participatory and self-motivated, driven by the desire to break the cycle of poverty.

The volunteers are the engine that keeps TECHO's work alive. They have been the main characters in promoting growth and innovation through different actions dedicated to solving the problems in the settlements. They have taken on the challenge to fight injustice in their own countries after completing their contribution to TECHO, making it a life goal to end poverty from the different sectors where they will work in their professional lives.

During its fifteen years of work, TECHO has been recognized worldwide by various international organizations and institutions, which have noted that the intervention model is innovative and represents great progress in overcoming poverty and exclusion.

The challenge continues, and every day the targets become more ambitious and more difficult. While the identified needs of those most excluded in society are great, there is no choice but to reinvent oneself constantly and to look for different support networks, to professionalize the interventions, always placing the settlement families at the center of the efforts, and to work closely to achieve a more just society.

#### UN TECHO PARA MI PAÍS BY THE NUMBERS

- Presence in 19 countries in Latin America and the Caribbean.
- More than 76,000 transitional houses built in 18 countries in Latin America.
- More than 500,000 young volunteers mobilized under a single commitment: to transform the reality of thousands of families in poverty.

## The CONNECTAS Project: Going Beyond Local

by Carlos Eduardo Huertas

For those who don't know much about the countries south of the U.S.-Mexican border, it is likely surprising to learn that Carlos Slim, a Mexican, ranks as *Forbes'* richest man in the world for the third consecutive year. Eike Batista, the richest man in Brazil, comes in at number seven on the *Forbes* list of wealthiest individuals in the world (Forbes 2012). This means that 20 percent of the ten richest people in the world are in Latin America. How is this possible? A newcomer might wonder, wasn't this region only about beautiful beaches and fun music?

Even more surprising is the fact that the region's indicators are strengthening thanks to both growth in internal demand and outside demand of raw materials. It's not a coincidence that an increasing number of the biggest enterprises in the region, in terms of export income and subsidiaries, are now part of the *Fortune* 500 (Fortune 2011). According to analysis by the Boston Consulting Group (2009), many of these enterprises, which have come to be dubbed "multilatina," are among those businesses that have a high global projection.

According to the World Bank, since 2004 the combined region of Latin America and the Caribbean has sustained an average gross domestic product growth rate above that of the rest of the world and well above that of the United States (World Bank n.d.). In all of this, however, the most surprising discovery may be whether such apparent success is having an effect on the lives of the more than 500 million inhabitants in the region. While such growth does help to increase employment rates and reduce poverty, it seems that the historical gap in the region is so deep that the majority of the people who live there are not experiencing much change despite the positive overall financial results being observed.

The current concern is whether the region's momentum will actually improve the lives of its inhabitants, taking into account that this is not Latin America's first economic boom. There have been others in the past, due to, for example, petroleum, food, and, of course, gold, which largely guided its conquest. What will make the difference this time?



## DEMOCRACY, INTEGRATION, AND A TRANSNATIONAL PERSPECTIVE

While this current growth takes place amid many changes from the eras of past periods of growth, the biggest difference is likely that today's economic boom is happening inside new political regimes of democracy.

In a not-so-distant past, about two decades ago, many countries in the region experienced a parade of oppressing military regimes. Nowadays, Latin America experiences the growth and strengthening of a vibrant civil society that actively participates and keeps power accountable. This phenomenon is easily seen in the big urban centers, despite the limitations posed by the *caudillo*, or military dictator, spirit of some presidents and the slow modernization of their institutions.

Such social organizations find their strength through alliances with similar groups, located not only inside their countries but also beyond their borders, that is, with foreign organizations from around the continent. This strategy has served to publicly decry human rights violations and to amplify the voice of indigenous communities facing powerful threats against their livelihoods. Yet civil society should use the current communication networks in a way that goes beyond only denouncing abuse; they must seize the chance to use such networks as a way to form a new perspective on development issues and human well-being.

Information with a transnational perspective has a special value. Yet this perspective is not really evident in Latin America despite the obvious advantages of sharing a common culture, history, and language. CONNECTAS, a nonprofit

journalism project, is a proposal to fill this gap.

## THE ROLE OF CONNECTAS

On one side we have the interconnected social movements, and on the other we have a vibrant business community whose dynamics are increasingly more regional. Yet somehow both sections go about their operations in partial ignorance when it comes to information. The majority of information available is a collection of tightly bounded horizons dealing with local issues without systematically addressing the regional transnational reality. Some journalistic works do count as obvious exceptions, but even many of these exist only because they have been blessed with luck.

That is why I founded CONNECTAS, an initiative I am pursuing as a 2012 Nieman Fellow. CONNECTAS is a nonprofit journalism project that promotes the production, sharing, training, and dissemination of information with a transnational perspective on key issues for development in the Americas. It aims to create alliances with journalism and media organizations and operate as a logistical hub that provides technical and professional support, facilitates training programs, and conducts fundraising for activities related to its mission.

The CONNECTAS project focuses its attention on key information to develop a transnational perspective for all sectors, including governments. Transnational cooperation in the region is gradually becoming a trademark of diverse government policies and projects. The past few years in Latin America have witnessed a higher degree of openness among countries that support all types of cooperation, ranging from market integration to the construction of transnational mega projects. Moreover,

the mandates derived from multilateral presidential encounters, which used to be regarded as simple ceremonial procedures, are gaining importance. For example, the accords (or lack thereof) made at the various Summit of the Americas start defining the political agenda of the region. Paradoxically, most of the media is busy just recording the daily tribulations of the meetings and is easily distracted by eventualities. This levity was evident in the last Summit of the Americas meeting in Cartagena, Colombia, in April 2012, where members of the U.S. Secret Service and the U.S. military were involved in a prostitution scandal that then became a big topic of conversation.

Meanwhile, at this point, the fight against organized crime—perhaps the most transnational activity in the region—is particularly relevant. Organized crime is one of the region's main development barriers, and it relishes in illicit cultures, weaknesses in justice systems, and the absence of law enforcement. There are other relevant plights in the region such as the fight against poverty and inequality, two of the area's most visible characteristics, as well as the protection of the environment, due to the privileged physical conditions of the region.

It is important to highlight that the mandatory agenda for regional development is also enriched with new issues, including physical integration, through roads, for example; the strengthening of technology in the region; and access to and use of information and communication technology.

Yet when the general public turns to the press, it cannot find answers for key questions such as: How are these transnational policies implemented? How are budgets allocated and spent? What is their

real impact? Who is responsible? What are the tangible benefits for the region and its citizens?

### THE MISSION OF CONNECTAS

With this provocative agenda concerning transnational issues, journalism owes citizens more. The mission of CONNECTAS is to fill this gap.

The project's working model incorporates and goes beyond producing news articles about what is happening in the region. It also functions as a logistics center, as mentioned above, that supports journalistic activities and targets fundraising for journalistic organizations in the region that share a drive toward quality reporting. CONNECTAS also seeks to facilitate the implementation of technological platforms to exchange its own data as well as data obtained through the application of laws that facilitate access to governmental information. The results of these efforts will be journalistic products that will be targeted to a massive audience or to niche audiences.

The collaborative nature of CONNECTAS and its interaction with other areas of knowledge will be a source of diverse histories and of points of view regarding the complexities in the region. In this way, decision makers, the growing world of business, and especially civil society will have elements that will keep feeding the vibrant changes in the region.

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# Sustainable Development in Colombia

*by Frank Pearl*

According to the World Business Council for Sustainable Development, in 2050 the world will have a population of around 9 billion people, of which 75 percent will live in urban dwellings. This population will demand more food and water than the Earth can provide and thus will put enormous pressure on ecosystems all around the world. This will mean that, by 2050, we will need 2.5 Earths to supply the global population demand for food and water. As this trend is not sustainable, we need to modify our current consumption and production patterns to avoid such a stark forecast.

How do we modify our consumption and production patterns today? Private companies need to become more efficient in the use of energy and natural resources and need to invest in new technologies in order to depend less on fossil fuels and more on renewable materials that will not become scarce in the near future. On the other hand, consumers need to change habits to put a premium on cleanly and/or efficiently produced goods and services. Additionally, governments can help provide information to both producers and consumers about efficient ways of creating goods and services, investing in research and development to create innovative ways to maximize resource utilization, and valuating the natural capital on which production is based.

## COLOMBIAN GROWTH

In 2011, according to Departamento Nacional de Planeación, Colombia grew at 5.9 percent, a significant rate given the global slowdown of the past couple of years. Growth was based basically on mining, oil production, and construction. In fact, the national government has based economic development for the presidential period 2010 to 2014 on five growth motors or “locomotives”: energy, agriculture, transport infrastructure, cities and households, and innovation. However, although these sectors are generating wealth, creating jobs, and pushing the rest of the economy forward, the action plans to support these sectors did not originally include sustainability criteria, and thus the government, through the Ministry of the Environment, is now designing a sustainable development policy to ensure that the country’s model of growth is based on sustainability criteria.

## COLOMBIA'S SUSTAINABLE DEVELOPMENT STRATEGY

Colombia has adopted the United Nations Environment Programme's (UNEP) vision of sustainable development and the construction of a green economy. As summarized from UNEP's Web site, the strategy's goal is to improve human well-being and social equity while significantly reducing environmental risks and environmental scarcities. In its simplest expression, a green economy is low carbon, resource efficient, and socially inclusive. In a green economy, growth in income and employment are driven by public and private investments that reduce carbon emissions and pollution, enhance energy and resource efficiency, and prevent the loss of biodiversity and ecosystem services.

In order to design a sustainable development policy for Colombia, however, the ministry will build on the policies and programs it has been working on for the past few years that help push forward the sustainable development aspiration. The following are a few examples of programs already in place:

- **Low carbon development strategy.** The low carbon development strategy was launched in mid 2011. It aims to achieve the national level of expected growth while keeping greenhouse gas emissions (GHG) stable and understanding Colombia's mitigation potential as a tool for decision making. Although, according to the Ministerio de Ambiente y Desarrollo Sostenible, Colombia accounts for only 0.37 percent of global GHG emissions, its growth path will entail a steady rise in emissions unless a national mitigation strategy is implemented. In this sense, Colombia has decided to become part of the solution before it becomes part of the problem.

The strategy will thus identify alternatives for the greatest potential for emissions reduction within each sector of the economy, the costs, and the expected effects on economic growth, employment, international competitiveness, and quality-of-life standards. With this information, and together with the private sector and academia, the Ministry of Environment will design action plans for each economic sector that will include both public policy instruments and complementary private-sector actions that will contribute to mitigating GHG emissions that result from productive activities.

- **Sustainable production and consumption policy.** This is an initiative to work together with the private sector to promote sustainable production practices among producers and create awareness among consumers about sustainably produced goods. This strategy launched the Colombian Ecological Seal to differentiate food products that were produced according to international ecological standards and the Environmental Seal for sustainably produced non-food goods and services.
- **Economic instruments to internalize externalities that arise from the use of environmental services.** These economic instruments refer to a tax on water use, a retributive tax for waste spills, and economic compensations for loss of biodiversity. These and other tax instruments currently in a planning stage aim to value the cost of natural resources so as to incorporate it in accounting and project evaluation, thus maximizing their value and their use.
- **Bio trade.** Bio trade refers to activities that involve collection, production, processing, and trade of goods and

services that come from the country's native biodiversity, under strict environmental and social criteria. Colombia is currently working with the production and trade of Amazonian fruits, bamboo, and ecotourism.

### MOVING FORWARD

Although the above policies and programs are moving forward and have a significant effect on promoting sustainable development, the Minister of Environment judged it necessary to bring all the efforts together and design a new, comprehensive roadmap that will transform sustainability policies in Colombia. Thus, the ministry has determined that in order to achieve sustainable growth through a green economy, Colombia will work on three fields of action:

1. Improving resource efficiency and productivity
2. Channeling economic activities toward sectors that maximize social well-being, prioritizing poverty reduction and long-term sustainability
3. Driving to new ways of achieving the above, for example, through research, development, and innovation

Following UNEP's framework, the government, together with the private sector, will focus the three fields of action on three main spheres: investment in natural resources, investment in energy and resource efficiency, and investment in the enabling environment for a green economy (see Figure 1).

Therefore, for each sphere of investment, there will be action items related to improving productivity or resource efficiency, supporting activities that directly impact poverty and improve the local community's quality of life, and

promoting innovation that helps achieve the previous two goals.

The Ministry of the Environment, together with all the national government ministries relevant for each area, is in the process of designing specific action plans and indicators to monitor and evaluate progress in each field. However, during the United Nations Conference on Sustainable Development (Rio+20) in Rio in June 2012, Colombia plans to propose sustainable development goals (SDGs) for five key areas: agriculture, oceans, water, cities, and energy. While these are key to the Colombian development plan and its local context, other countries can choose other sectors within the matrix in Figure 1, given their national priorities. Colombia's goal is to have action plans for all ten areas, but understanding the complexities of negotiating goals and indicators in a multinational context, Colombia will present only five areas with simple indicators for each.

### SUSTAINABLE DEVELOPMENT GOALS

Colombia is currently in the process of building simple, measurable indicators for each of its five priority areas. The process entails multiparty negotiations between government entities involved in each area, thus a finalized version of the SDG indicators is still to be determined. As of the time of this writing, only the energy sector has final indicators, shown in Figure 2. The government goal is to have similar short, simple, and measurable indicators for agriculture, oceans, water, and cities to showcase at Rio+20.

Figure 1 – Three fields of action on three spheres of investment.

Spheres of Investment  Fields of Action	Investment in Natural Capital				Investment in Energy and Resource Efficiency					Investment in Enabling Conditions
	Agriculture	Fisheries	Water	Forests	Energy	Transport	Manufacturing	Tourism	Cities	Institutional Framework
Improving productivity or resource efficiency										
Channeling economic activities toward sectors that maximize well-being										
Promoting innovation										

Figure 2 – Energy sector indicators.

Dimension	Indicator	Units
Social	1 Electric energy service coverage	%
	2 Use of wood burning for cooking	% households
Economic	3 Per capita energy consumption	Btu
	4 Reserve/production ratio (oil, gas, and coal)	%
	5 National energy intensity	GDP in millions of pesos
	6 Renewable energy/total energy production	%
Environmental	7 Energy emissions intensity	TBD

# The Role of Trade Integration in the Diversification of Peruvian Exports

*by Carlos Posada Ugaz*

According to modern economic theory, states assume an active role in the economy as advocates and leaders of the various forms of economic organization, and within this context, they exercise control over the strategic resources and manage their use for the benefit of the population. However, states cannot develop in a self-sufficient, self-enclosed manner and isolated from the world, especially in the context of a globalized world where the barriers of time and space have been radically transformed. In this sense, the modern state must develop and implement economic, political, and social plans and strategies in order to achieve sustainable economic growth.

It is at this level that states supplement their markets and are able to exploit economies of scale in order to reduce costs and enhance the benefits that foreign trade brings for companies and consumers, promoting economic growth.

Indeed, exports are a key tool to boost productive development and competitiveness of enterprises. Thus, national policies do not rely on a production system intended only for the extraction and export of raw materials but rather on the development of value-added products that increase productivity and competitiveness in the country.

From the point of view of foreign trade, the first step is the coherent identification of specific goals to guide international trade negotiations. Less than ten years ago, Peru's Ministry of Foreign Trade and Tourism (MINCETUR) launched a national trade policy with the aim of achieving integration with the world's major economies through the signing of trade agreements and the strengthening of international and regional integration processes.

For Peru, trade integration is a constant of the foreign trade policy, which promotes the creation of strategic alliances in the economic and political realms as well as spaces that favor free trade of goods, services, capital, and people. The implementation of integration policies not only allowed Peru to build export markets but has also been a key element for the promotion of exports of value-added goods and services, generating employment and active participation of small and medium-sized enterprises (SMEs).

In short, we can say that Peru's final goal is to contribute to sustained economic growth over time, after positioning itself as one of the most stable economies in the world. Of course, it is key to diversify and strengthen the presence of Peruvian companies, products, and services in international markets, and for that to be true, integration



schemes that respond to visions of long-term growth are appropriate.

### **INTEGRATION AND ITS ROLE IN FOREIGN TRADE**

Integration nowadays goes beyond reducing tariffs and non-tariff measures, encompassing more and more disciplines, including those related to the liberalization of services, attracting of investment, protection and promotion of intellectual property rights, strengthening of competition policies, and trade facilitation, among others.

Furthermore, these processes involve social, environmental, and cooperation issues that contribute to economic growth in a comprehensive and sustainable fashion, which has the goal of achieving a persistent improvement of the population's living standards.

Regional integration processes subsist despite their conceptual differences, diversity of ideologies, and economic and cyclical crises because the ideal of cooperation between its member states prevails. These processes involve several stages or degrees of economic integration among states, establishing preferential tariff zones, free-trade areas, customs unions, common markets, economic and monetary unions, and complex economic integrations. Indeed, there are many forms in which integration can manifest, as its nature is flexible and dynamic.

### **THE CONVERGENCE OF FACTORS FOR REGIONAL INTEGRATION**

Depending on their physical proximity, countries can establish integration into blocks or regions, which seek to build a single geographic area where political and economic stability prevail. In addition, other factors like social cohesion, productive transformation, and competitive

insertion into the global economy are important.

Today, regional integration requires a convergence of several factors. According to Felix Peña (2011), the first is the plurality of options adopted by countries to achieve integration, engaging with key strategic partners and shortening distances. This way, one can choose between multilateral, bilateral, or regional integration schemes. A second factor has to do with the will to simultaneously harness the options previously mentioned, taking advantage of synergies and exploiting existing cooperation mechanisms. Additionally, a third factor involves the development of strategies for mutual benefit in terms of trade, services, and investments.

From the perspective of Peru, the link with key strategic partners has been carried out using different integration schemes. Indeed, the perpetual link with most countries in the framework of the World Trade Organization has allowed taking joint positions on various negotiations that are conducted in that forum. However, this mode of integration has often resulted unsatisfactorily in many respects, given the slow progress and little flexibility to innovate in the context of the dynamic pace of international trade. As for the spaces of regional and subregional integration regarding matters of foreign trade, Peru belongs to the Latin American Integration Association (ALADI), the Andean Community (CAN), the newly formed Pacific Alliance, and cooperation forums such as the Asia-Pacific Economic Cooperation (APEC), and Arch of the Pacific.

From these integration spaces, one can highlight the experience of CAN, in which the three factors mentioned above

converge partially. Indeed, CAN was established as an area of regional integration that aims to achieve an expanded market. It has also served as a platform to begin joint negotiations with its major trading partners, which are the United States and the European Union, although the negotiations concluded in bilateral agreements due to particular circumstances. Ultimately, CAN has the primary objectives of balanced development, the reduction of external vulnerability, economic growth, and harmonious development of its members, through integration, economic, and social cooperation, which seeks mutual benefit of its members.

### THE IMPORTANCE OF INTEGRATION FOR PERUVIAN EXPORTS

The current integration schemes and the strategies to insert Peru into international markets openly involve the industrial and business sectors of the country.

Particularly, integration with the countries of the region aims to achieve SME participation in the export chain. The development and growth of the SME sector, a priority in recent years in Peru, seeks sustainable economic growth of its population as well as equitable and social inclusion.

Overall, the integration processes are part of Peru's trade strategy to improve its market access and, at the same time, to set clear rules and disciplines that promote the exchange of goods, services, and investment. These strategies, together, have contributed to the positive trend shown by the Peruvian economy, whose average growth rates are more than 6.9 percent in recent years (Banco Central de Reserva del Perú 2012).

Currently, Peru has thirteen existing free trade agreements (FTAs) with major

economies in the world and another five treaties signed that are about to take effect. Additionally, it has a long tradition of integration as a founding partner of the oldest regional integration processes in Latin America, such as ALADI and CAN. Additionally, Peru has been actively participating in the Pacific Alliance, a regional initiative along with Colombia, Chile, and Mexico, with the goal of moving progressively toward the free movement of goods, services, capital, and people and promoting higher growth and competitiveness of their economies, becoming a springboard into the Asia-Pacific region.

Regarding CAN, one of its greatest achievements was the creation of a free-trade area between Bolivia, Colombia, and Ecuador, functional since 1993 and signed by Peru since 2006. This implies that products originating in member countries can be traded within the territory, completely free of tariffs or other restrictions. However, its perfecting requires a series of actions, such as the elimination of all non-tariff liens and restrictions on trade, the creation of a customs agenda, and a new regime of international road transport, some of which are being worked on in this space of subregional integration.

In addition, CAN has developed specific programs to support SMEs at the community level so that these programs will contribute to national policies of the member states, promoting partnerships and strengthening competitiveness and productivity. Currently, there is an Andean Observatory of MIPYME, which provides current information and tools for practical use to those interested.

Peru is also part of ALADI, a regional international organization, created

through the signing of the Treaty of Montevideo in 1980, which replaced the Latin American Free Trade Association. ALADI aims for the gradual and progressive establishment of a Latin American common market in order to achieve a harmonious and balanced economic and social development of the region. ALADI has twelve member states: Argentina, Brazil, Bolivia, Colombia, Chile, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay, and Venezuela, which soon will be joined by Panama and Nicaragua, which are currently following the admission procedures.

In 2011, Peruvian exports to ALADI countries reached US \$7.21 billion, representing 15.8 percent of Peru's total exports to the world, while imports from the countries of ALADI were a total of \$10.631 billion, representing 29.8 percent of Peru's total imports. It should be noted that exports to this region grew by an average of 21 percent over the period from 2000 to 2011, while imports grew by 15 percent (MINCETUR 2011).

Moreover, Peru has also redoubled its efforts to join the Asia-Pacific region, especially amidst the risks currently facing the global economy. These efforts take the form of existing free trade agreements with China, Korea, Japan, Singapore, and Thailand, as well as efforts in the context of APEC.

Indeed, the basis of integration with the Asia-Pacific region seeks to maintain and increase the flow of trade and investment. Peru has been working on strategies to diversify exports in this market, focusing on nontraditional agricultural products, organic and natural products, fish products, alpaca and fine hair textiles, and others that are considered an important market niche in countries with high purchasing power.

APEC has initiatives involving trade and investment facilitation programs, among others, destined to reduce transaction costs and facilitate business between member economies. It also encourages the development of activities to improve the participation of SMEs in global supply chains as well as cooperation in innovation, science, and technology.

Thus, Peru's economic growth shown in recent years has been driven in part by an increase in Peruvian exports of both traditional and nontraditional products in the last decade. For this reason exports grew 293 percent between 2000 and 2009, and the trade with the world expanded by 241 percent, despite the international crisis. In 2011, exports reached \$45.366 billion, showing an increase of 29 percent over 2010. This positive result was driven by an increase of 28 percent of traditional exports (\$35.034 billion) and an increase of 31 percent of nontraditional exports, which exceeded \$10 billion for the period of 2010 to 2011 (MINCETUR 2011).

As for nontraditional exports, in the last five years they grew at an average annual rate of 14 percent, representing approximately 22.6 percent of total exports from Peru to the world. In 2011, the main destination of nontraditional exports was CAN (as a block, plus Venezuela) reaching \$2.762 billion, accounting for 27 percent of the total, a larger share than is exported to the United States (23 percent) and the European Union (20 percent) (MINCETUR 2011).

## CONCLUSIONS

The following points can be highlighted as conclusions:

- Regional integration systems play an important role in the foreign trade policies of countries, because they are based on principles of solidarity,

cooperation, and reciprocity that promote economic growth.

- Peru's foreign trade policy consists of two major policy instruments: international trade negotiations at the multilateral, regional, and bilateral levels and the development of international trade on the foreign and domestic fronts.
- From Peru's experience, integration has allowed the improvement of strategic alliances on the economic and political fronts; it has favored economic growth by diversifying the export base and the consolidation of Peruvian companies in these markets due to physical proximity and similarities in culture, language, and legal basis, which are factors that are attractive to SMEs and other companies new to exporting.
- Currently, the regional integration processes not only regulate market access, reductions of tariffs, and other non-tariff measures but also involve matters related to trade of services, investment, intellectual property, trade facilitation, and more. In addition, many processes called "third generation" also contain obligations on social, environmental, and cooperation matters.
- The integration processes have evolved with the globalization and dynamism that has been adopted by international trade. Nowadays, integration requires the convergence of at least three factors: (1) the diversity of integration options; (2) the will of states to take advantage of integration; and (3) the development of strategies for the mutual benefit of the system.
- The integration efforts have enabled the creation of strategic alliances for the elimination of trade barriers of goods and services, the liberalization of capital markets and the movement of people, the reduction of transportation and customs costs, and the implementation of common policies in various aspects of foreign trade.
- Peru's sustained economic growth in recent years is due in part to increased exports, both traditional and nontraditional. The regional integration policies promoted by the Peruvian government are directed toward the building and strengthening of nontraditional exports, primarily by SMEs.
- Additionally, the goal set forth by the Peruvian government by the year 2016 is to create 8,000 new businesses, which when added to the 7,600 existing companies will achieve a quota of more than 15,600 exporting companies nationwide.
- Finally, the increase of exports of goods and services and the diversification of their destination markets, with better access conditions, will help Peru's economy to maintain its growth rate despite the global crisis. In this sense, it is important to strengthen economic and commercial ties with countries in the region, mainly through trade-integration initiatives.

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# States that React and Criminals that Innovate

by *Juan Carlos Garzón Vergara*

“I urge you to be more innovative. When it comes to emerging threats such as cyber-crime, environmental crime, and counterfeiting, we must stay one step ahead of the criminals,” affirmed Ban Ki-moon, secretary-general of the United Nations, in a speech read by a representative at the Twelfth United Nations Congress on Crime Prevention and Criminal Justice in Salvador, Brazil, in April 2010 (United Nations Information Service 2010).

In an ideal world, the state would always be one step ahead of crime. Nevertheless, evidence shows that it does not generally occur this way. For a variety of reasons, the state and its institutions advance slowly while crime adapts to the changes that occur. Why does crime innovate so easily while the state has a hard time doing so?

Innovation is a condition necessary for crime to subsist in markets that, like legal ones, have intense competition, face changing conditions, and are therefore unstable. A criminal organization that is not capable of adapting to new circumstances and that does not respond to the changes of supply and demand, as well as to the restrictions imposed by the state on its activities, has few probabilities of surviving in an illegal world. On the other hand, the state may exist without innovation. In fact, public administration is usually conservative and looks forward to preserving the conditions that justify its own existence. State institutions usually go for the known solutions and reproduce the routines that make sense for their actions.

## WHY IS INNOVATING SO EASY FOR CRIMINALS?

You might be wondering if innovating is really that easy for crime organizations. This might be controversial, but you and I will probably agree on the fact that, in comparison to the state, the innovation rhythm of criminals is much faster. Criminals are constantly looking for new ways to evade state actions, to obtain more benefits, to open new markets, and to optimize their processes in order to reduce costs. Every now and then, newspapers or television news channels refer to new means of drug transportation from the producing countries to the consumption zones. Some of these approaches have terrible consequences, such as the use of human beings as stupeficient containers where numerous citizens choose to put their life in danger in exchange for money.

Maybe one of the most surprising pieces of news that evidences the innovation capacity of crime is related to the finding of a submarine, capable of transporting three tons of cocaine, on the Colombian coast. The ship, which costs approximately US \$5

million, is able to navigate in the deep parts of the sea without being detected by radars and can transport drugs from South America to the United States without making stops. This innovation is not only interesting technologically, but it could also have important implications. If the high levels of violence in the countries of the “Northern Triangle” (Guatemala, El Salvador, and Honduras) and Mexico are—partly—explained by the dispute of the drug corridors, then would the use of a new technology such as submarines reduce the flow of drugs through these countries and therefore reduce the level of violence? It is hard to have an answer since only a little more than a year has passed after the finding of the first submarine (the first was found in early 2011). However, considering this notion allows us to reflect upon the relevance that innovation has for the dynamics of crime organizations.

The innovation capacity of crime organizations is associated with different factors that facilitate the adaptation to new and changing circumstances. An important consideration is that the category of “organized crime” includes a broad sense of illegal activities. Not all the groups operate at the same scale (some are local, others are global), not all of them have the same resources available (the level of profits are different), and not all of them operate in similar contexts. Therefore, innovation levels will depend on each specific organization and its role in the local and global illegal market.

Generally, innovation is associated with:

- The need to evade the law and the state actions
- The optimization of resources
- Enterprise entrepreneurs that set the goal of opening new products or markets

- The exploitation of new available resources (e.g., technologies)

The last point deserves further attention because one of the characteristics of crime organizations is their capability to “cannibalize” the legal world. By this, I refer to their ability to use legal resources (technology, financial systems, elections, and international trade) to obtain non-legal profits and advantages. A clear example of this is money laundering. The Information and Financial Analysis Unit of Colombia has identified forty-four ways in which criminal organizations provide a legal appearance for the resources obtained in an illicit way. This list shows the weaknesses of the financial system through which every year millions of dollars are filtered. The Decalogue also shows that crime organizations can easily take advantage of currency and commercial transactions made by citizens.

The remarkable profits obtained from the illegal market, the existence of flexible structures that adapt and learn, and a short-term perspective accompanied by a high level of risk make innovation an easy step for crime organizations. In addition, the abundance of available distribution networks, the existence of multiple competitors within a fragmented market, and an important number of consumers that demand every kind of product facilitate the adoption of ingenious alternatives by criminals.

To sum up, it must be stated that illegal organizations are structures that work under informal rules that may be changed according to the demands of the circumstances. In other words, they are not linked to regulations or rigid procedures. Under this framework, the coordination and fulfillment of the deals are a must, and this facilitates the ability of criminals to be entrepreneurial.

## WHY IS INNOVATING SO HARD FOR THE STATE?

When we think of the state, we probably recall the image of a heavy, inefficient, expensive, and conservative structure. Innovation does not seem to be one of its virtues. On the contrary, the reform processes of institutions and the implementation of policies that propose shifts to the established paths usually take too long. Moreover, within the Latin American context, citizens believe that the state works to benefit a few powerful groups: according to a *Latinobarómetro* 2011 poll, 65 percent of surveyed citizens from eighteen countries believe that the state “is governed by a few powerful groups that work for their own benefit.” This perception is accompanied by high levels of distrust regarding the institutions; according to *Latinobarómetro*, 67 percent of the people surveyed do not trust the police department, and 69 percent do not trust the legal system.

Reflecting upon innovation will surely lead us to the conclusion that the state and its institutions have strong incentives to keep the status quo. This is explained by the internal dynamics as well as by the pressure and influences coming from agents that are outside of the state. The bureaucracies in charge of security and justice have in their DNA self-conservation, therefore, they privilege maintaining procedures, many times in spite of the results. They defend their competences and frontiers and, above all, look to guarantee the budget lines and their privileges, which makes it difficult to articulate actions on an institutional level. In these contexts, the efficacy and cost-reduction procedures are regarded as threats for they can compromise the stability of the public employees. Another detail that must not be underestimated is that both the armed forces and the police

department can have access to the use of violence, which in specific circumstances may be used as a pressure tool to avoid reforms and processes of change.

A good example of internal resistance to innovation is what has happened in Latin America in relation to the efforts of police reform, with a few exceptions. To mention just two cases, there is evidence that police institutions from Chile and Argentina have exerted important pressure mechanisms to avoid reforms, and once they were implemented, they have done all that is possible to reverse the norms into what previously existed (Fuentes 2005). This same situation has occurred in countries such as Guatemala and Honduras, where after peace treaties have been enacted, the steps forward into the police’s modernization have faced resistance from different angles.

An issue scarcely studied but one that determines the resistance to innovation is the existence of external agents that reject the possibility of implementing new ways of dealing with the challenges of insecurity and that have an influence on the decision and implementation processes of the policies. An important question here is how the security policies of Latin America are decided. The public policies emerge from a decision-making process that involves a number of stakeholders. The result of this political game may contribute to the stability of the policies or surrender them to the movements; it may facilitate their adaptation or keep them excessively rigid; it may also produce policies that promote public well-being or those that privilege private interests (Scartascini et al. 2010).

In what relates to the external factors that oppose change and innovation processes, at least four determining areas can be highlighted:<sup>1</sup>



1. Privatization of security services
2. The influence of crime organizations on the institutions
3. Public opinion that demands “hard measures”
4. The influence of an international agenda based on prohibitions, which privileges repressive measures

With regard to the first area, the supply and demand of private security services has increased in Latin America, providing employment for more than four million people within a market that does not have many regulations and that is available to anyone who has the resources to pay for protection. At the present moment, it is not clear how the agents that benefit from the privatization influence the state, but a good index of their intervention capacity relates to the few institutional advances on the control of this service. Not all sectors lose due to insecurity, and those whose profits rely on the demand of protection from citizens who feel threatened will do anything to maintain the risk perception.

On the other hand, there is evidence that shows how crime organizations influence the design and implementation of public policies in many countries. This happens both at national and local levels. Especially in this second dimension, we find what Edward Gibson (2006) calls the authoritarian subnational regimes that resist the democratization processes from the outside. In this case, we talk about criminal structures that in alliance with public stakeholders look forward to keeping the local power and preserving their autonomy margins, resisting every change that aims to impact their operating rules or that looks to impose new regulations. In some countries, this situation may scale up to national levels

with the presence of congressional representatives who defend criminal interests (through corruption or force) and public employees who are paid by the crime organizations. In the middle of this pollution of the public service, what Luís Jorge Garay and Eduardo Salcedo (2011) call the co-opted state reconfiguration,<sup>2</sup> it is very unlikely that innovation processes occur, unless they favor the criminal structures.

Moving into the third area, it is important to consider how public opinion may go against the innovation processes within the state. Frequently, the demands of society in highly unsecured contexts (real and/or perceived) are linked to the agenda of “hard measures,” that is, the perception that insecurity must be handled via repressive measures that may even restrict the guarantees and rights that citizens have. Under this scenario, it is very likely that when the authorities propose new ways of facing insecurity with approaches that provide strength to prevention and reinforcement for a legal culture, citizens judge these actions as being too shy against delinquency. The next step will be that the initially proposed innovations lose strength and the politicians may have to go back to the more conservative agenda (i.e., the reappearance of “hard measures”).

In relation to the former idea, a strength that weakens the internal innovation efforts of the state is called “penal populism,” which is a practical, rapid, and direct way of showing the capacity of governmental or legislative actions toward combating rising levels of insecurity with proposals to increase punishments, diminish the age of penal accountability, and deliver greater control capacities to the police institutions (Dammert 2009). This Decalogue of

initiatives is not ingenious and has been proven ineffective: there is no empirical evidence that leads to stating that the increase of punishments has any impact on delinquency.

Finally, with respect to the fourth area mentioned above, it is important to consider the role that international agendas play within the internal situation of countries. Cooperation is generally regarded as being positive. However, it may be that international influence is what actually does not allow the promotion of innovative policies. A good example of this situation is the so-called War Against Drugs. Even though its limited effectiveness has been shown, it still has a strong influence on the actions implemented by Latin American states against drug trafficking. The rigidity of the prohibitionist agenda, supported by the agencies in charge of assessing the Vienna Convention, has closed the debate regarding the possibility of trying other alternatives to face drug trafficking. Written essays, op-ed pieces, and the like by the presidents of the region in order to open a debate are an important effort in the search for innovative answers. Nevertheless, the lack of consensus among the countries and the strong resistance from the United States contributes to the inertia of the actual model.

### **A FINAL REFLECTION ON THE INNOVATION OF THE STATES**

This discussion comparing the innovation capacity of criminals and states has shown that the way states operate is not functional in regard to the objective of diminishing crime's influence in our societies. The aforementioned is not only related to the operating way of bureaucracies, but also to the influence of external stakeholders that resist any innovation

attempt made by the institutions. Under these circumstances it is very unlikely that the state could stay one step ahead of the criminals for several reasons: it is overwhelmed with procedures; there is a lack of coordination among its institutions; conservative ways of thinking prevail in the public sector; and especially, there is a lack of autonomy based on the strong influence of stakeholders with factual power as well as the importance that opinion surveys have on the authorities' management actions.

In terms of recommendations, clearly, leadership is needed among the political elites in order to support the reform processes. Institutional articulation and honest public employees who compromise in order to be efficient in the fulfillment of their duties are also required. If I were to say that the state is corrupt, that it has failed in the performance of its duties, that it has a short-term vision, and that it privileges the interests of a few powerful groups—some of them illegal—then I could probably arrange the wide-ranging publication of this article in the media. However, that is only one part of the story.

The fact is that behind all states' activities—all the policies that are implemented and the obtained results—there are a number of stakeholders that are generally unnoticed. There is no doubt that the state is responsible for citizens' security and that this duty cannot be delegated. But, the state does not work within an abstract space; actually, it is the result of the interaction of different legal and illegal agents that have varying degrees of legitimacy that increases or decreases the state's autonomy. Therefore, when reflecting upon what the state does or does not do, we have to keep in mind the importance that the agents that have

an influence in its construction or deconstruction have.

Under this framework, if the economic elites keep insisting on the privatization of security, if the political elites govern according to what is established by the surveys, therefore limiting public management to a short-term perspective (evading the responsibility of building new ways of thinking and proposing new alternatives), if the scared citizenship demands “hard measures” without reflecting much upon it, and if the international agenda closes the possibility of proposing new solutions to the existent problems, then the state will always be one step behind the criminals. In order to change this situation, it is necessary to focus our efforts on the analysis of the high levels of criminality and institutional deficiencies, as well as on understanding how the characteristics of the political system and the way in which the public policies are decided have an influence on the state’s ability to be as capable of change as the crime organizations.

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## ENDNOTES

<sup>1</sup> Claudio Fuentes (2011) refers to the ways in which the market impacts the ideas of security and public policies and identifies three areas: the relationship between the privatization of the public security services and its impact on public policies; the link between the market of illegal goods and its relationship with the political system, and the growing internationalization of the “market of ideas” related to public security.

<sup>2</sup> Luís Jorge Garay and Eduardo Salcedo (2011) redefine the capture of the state—understood as a social relation established in one direction, from the illegal agents outside the state to the legal agents inside the state—proposing a concept of “co-opted state reconfiguration,” defined as “the actions of the legal and illegal organizations that through illegal practices pretend to modify the systemic forms from inside the political regime in order to influence the elaboration, modification, interpretation and application of the established rules and public policies. These practices are implemented in order to obtain benefits and guarantee that their interests have a political and legal validation, as well as a social legitimacy on the long term, even if those interests do not follow the basic principle of social welfare.”

# Legalize It?

*by Andrés Marroquín and Javier Calderón*

It is time to think differently about the war on drugs. The mess we are in cannot continue. The poor and disadvantaged suffer the most. Cocaine must be legalized and regulated, and heroin should follow. The prohibition of drug markets has generated more violence. It is clear that we must regulate, but the question is how.

We believe a multilateral initiative is preferable to a unilateral approach and that support from the United States is needed more than ever. We also argue that regulation is in the United States' best interest. It is, by far, the developed country with the highest incarceration rate in the world, mainly due to drug-related crimes. This has a high cost at a time when many U.S. local governments are on the verge of bankruptcy (The Pew Center on the States 2011).

This article explores the issues surrounding regulation as they relate to a new approach that is gaining support in Latin America, started by a move by Guatemala.

## THE GUATEMALAN PROPOSAL

For the first time in history, a Guatemalan president has proposed drug regulation to reduce violence in the region. It is the first time since the 1950s that a Guatemalan government explicitly contravenes official U.S. international security policies. This may be a symptom of the loss of power of the U.S. government in the Western hemisphere. Christopher Sabatini (2012) and Russell Crandall (2011) suggest that the focus on the wars in Iraq and Afghanistan, an outdated and naive understanding of Latin America among U.S. academics and politicians, and increasing economic prosperity and political stability in Latin America may be some of the causes of this loss of power. But as Guatemalan President Otto Pérez Molina indicates, the main reason is simple: the war on drugs has failed (Pérez Molina 2012).

Drug regulation implies decriminalization. President Pérez Molina is trying to persuade other presidents in Latin America to form a united front to regulate drug markets. President Felipe Calderón of Mexico (Economist 2012) and President Juan Manuel Santos of Colombia (Doward 2011) support drug regulation as do former presidents Fernando Henrique Cardoso (Brazil), Cesar Gaviria (Colombia), and Ernesto Zedillo (Mexico). President Pérez Molina argues that drug markets need to be regulated because: (1) the supply of drugs has increased dramatically and market forces cannot be suppressed; (2) drug addiction and the problems it generates should be seen

Figure 1 — Homicide rate in Guatemala, 2003–2011.

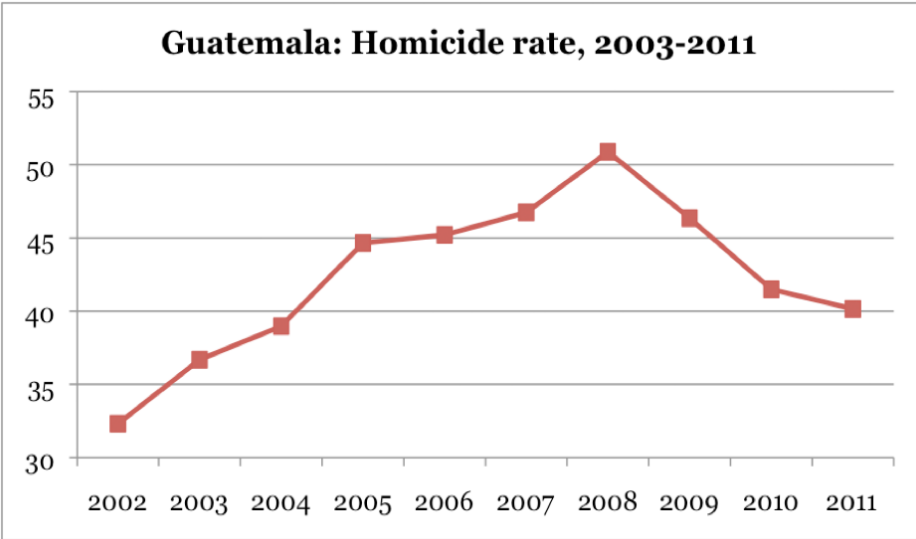
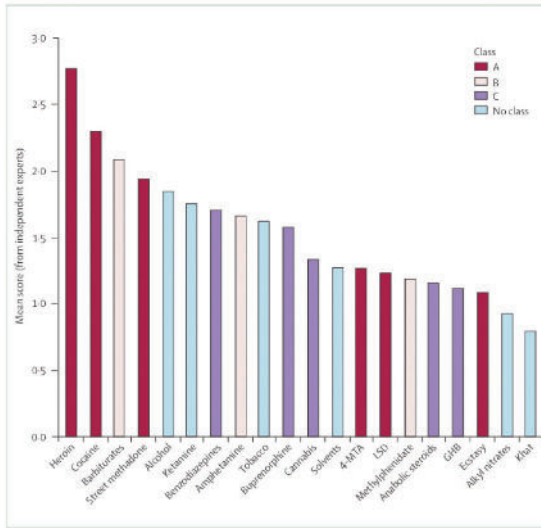


Figure 2 — Homicide rate in Guatemala, 2003–2011.



**Figure 3 — Mean harm score for 20 substances. Classification under the Misuse of Drugs Act, where appropriate, is shown by the color of each bar. Source: Nutt et al. (2007).**



Source: Nutt et al. (2007).

as a public health problem, not as a criminal problem; and (3) it is the only way to reduce associated violence.

Drug-related killings have escalated to unprecedented levels in the region. In Guatemala, for example, from 1999 to 2009, the homicide rate increased around 90 percent.<sup>1</sup> As can be seen in Figure 1,<sup>2</sup> the number of homicides per 100,000 inhabitants increased from 32 in 2002 to 40 in 2011, with a peak of 51 in 2008. Most of the homicides were committed with firearms.

While the homicide rate has decreased recently in Guatemala, it has increased in Honduras. With more than 80 homicides per 100,000 inhabitants, Honduras has the highest homicide rate in the world; this figure compares to about 5 per 100,000 in the United States (Ungar 2012). San Pedro Sula, the most violent

city in Honduras, has almost twice the national average of the homicide rate (Arce 2012). In 1975, the costs of crime and violence amounted to 7.3 percent of the gross domestic product in Guatemala (PNUD, 2006) and 7.7 percent in 2008 (Serrano-Berthet and López 2011).

## EVIDENCE

There is systematic evidence of the link between the war on drugs and drug-related violence. Dan Werb et al. (2010) found “a significant association between drug law enforcement and drug market violence. . . . [G]un violence and high homicide rates may be an inevitable consequence of drug prohibition.”

Gabriel Demombynes (2011) argues that the areas of intense drug trafficking in Central America have higher homicide rates. He indicates that traffickers are

more resourceful and have corrupted state institutions. He shows that in Guatemala 66 percent of adults say that local police officers are involved in crime (Demombynes 2011, 7).

In a different take, MIT economist Melissa Dell (2011) looks at how violence responds to the election of a PAN party candidate in Mexico. President Calderón, the leader of PAN, declared a frontal war on drug cartels in early 2007. Dell found that “the probability that a drug trade–related homicide occurs in a municipality in a given month is 8.4 percentage points higher after a PAN mayor takes office than after a non-PAN mayor takes office.” As indicated by Ray Fisman (2011), “Dell estimates that the drug-related homicide rate almost doubles relative to ‘control’ towns where the PAN wasn’t elected.”

At a national level, the statistics seem to support Dell’s study. Mexico’s homicide rate more than doubled between 2006 and 2010, from 10 to 23 per 100,000 inhabitants. There was a downward trend in the number of homicides in Mexico before the war on drugs. Figure 2<sup>3</sup> is illustrative. After a declaration of war on drug cartels at the beginning of 2007, the homicide rate increased dramatically.

The legal framework that allows some drugs and forbids others has also been questioned. David Nutt et al. (2007) interviewed experts to assess the harm of twenty different types of drugs. The authors found that the expert assessment varied significantly from the classification scale found in the Misuse of Drugs Act of the United Kingdom (see Figure 3). The act ranks drugs in three categories: A, B, and C, with A being the most harmful. The authors conclude that the legal classification that determines what drugs must be illicit is arbitrary. In fact, alcohol

and tobacco, the most commonly consumed drugs, occupy positions five and nine, respectively, on the overall scale of harm. The authors conclude: “[T]he fact that the two most widely used legal drugs [alcohol and tobacco] lie in the upper half of the ranking of harm is surely important information that should be taken into account in public debate on illegal drug use. Discussions based on a formal assessment of harm rather than on prejudice and assumptions might help society to engage in a more rational debate about the relative risks and harms of drugs.”

### The Economics of Decriminalization

The economic rationale is that decriminalization will increase the supply of drugs. As a result, more drugs will be consumed at a lower price. Production, distribution, and consumption will occur in the formal market. Lower prices will make the economic returns of drug production converge toward normal market returns. The current economic incentives that make narcos kill each other (and innocents) to gain territory and transportation routes will disappear and violence will go down. In addition, the thinking is that robberies will decrease because many individuals steal or commit crimes in order to pay the high prices for the drugs they consume. Producers, intermediaries, and consumers will pay taxes. The taxes could be used to fund social programs for people with drug addictions. Entities that would supervise the quality of different drugs would emerge. “Legalize, regulate, and tax” is the economic conclusion.

The economists’ arguments, however, have not been very effective in persuading politicians. But now that the violence toll is unbearable, politicians are considering

different options. President Pérez Molina argues that he does not propose a total liberalization of the drug market, but instead a regulated market in the same way that alcohol and tobacco markets are regulated.

Many people in Guatemala are not convinced. In fact, more people supported Pérez Molina's arguments in the UK *Guardian* (2012) version of his recent article than in the local newspapers in Guatemala. It is interesting, however, that in the comments section of the articles in *Prensa Libre*, the largest local newspaper, some said that they changed their minds in favor of regulation after reading the article. If President Pérez Molina wants to regulate drug markets, he will have to work harder to change popular opinion in Guatemala. This will help him gain democratic legitimacy for his proposal. One thing is clear: the general public is so affected by day-to-day violence, either through personal experience or through the media, that an opinion shift in favor of legalization is possible, and it is beginning to happen.

## IMPLICATIONS

Given the evidence and the timing, countries in Latin America need to decide if they will stick to the status quo or if they will regulate drug markets. If they regulate the market they need to decide if cocaine, marijuana, heroin, or all three will be regulated. Each country needs to decide its position with respect to other Latin American countries and then as a region with respect to the United States. A reasonable strategy is to regulate the cocaine market first through a united front. As the evidence in Figure 2 shows, the levels of physical and social harm and addiction are similar for alcohol and cocaine.

President Pérez Molina and President Santos know the broad direction of a new drug policy, but they do not know what to do specifically. Pérez Molina asked four key questions in his *Guardian* article:

1. How can we reduce the violence generated by drug abuse?
2. How can we strengthen public health and social protection systems in order to prevent substance abuse and provide support to addicts and their relatives?
3. How can we provide economic and social opportunities to families and communities that benefit economically from drug production and trafficking?
4. Which regulations should be put in place to prevent substance abuse (prohibition of sales to minors, prohibition of advertising in mass media, high selective consumption taxes for drugs, etc.)?

One of the problems is that we don't really know how much violence there would be under a regulated system, but presumably it would be lower than what there is now. There will be important social costs due to health provisions for addicts. It is usually assumed that taxes will increase; this is uncertain. It will happen for those countries or regions that regulate first, but as more and more countries and regions start producing drugs legally this might change; drug companies might lobby successfully for lower taxes. We should take into account that tax evasion in Latin America is high. However, it might be possible to exercise more focused auditing on companies and individuals that produce, transport, and distribute drugs, especially if multinational corporations enter into the business, which is very likely. Resources that are currently dedicated to the war on drugs can be transferred toward consumption prevention. At least for cocaine,



where the social harm is shown to be similar to alcohol, the laws and practices to regulate the market should be similar to what currently exists for alcohol.

One concern is whether regulation should start unilaterally or multilaterally and with or without the support of the U.S. government. If one country regulates unilaterally it will likely generate a domino effect where others will follow. This is because the country that regulates first will likely see a reduction in enforcement costs and an increase in public and private income from taxes and sales. It will transfer its enforcement costs to its neighbors. It will only take one country to start for the whole region (and perhaps the whole world) to do so as well. This does not come without complexities such as the possibility of armed conflicts with neighboring countries and even with the United States.

It might be possible to do a field experiment. A drug or some drugs could be regulated in one region (the treated region), using another region as a control. In fact, nowadays this is a popular approach to evaluate socioeconomic interventions. Hypothetically, one could regulate the cocaine market in a region in Guatemala, such as Petén, for example, where violence is very high in relative terms, taking the rest of the country as a control group, and then evaluate violence and other socioeconomic indicators after some time. This possibility raises important concerns, such as how to choose the treated region. One can even think of a provincial plebiscite for voters to decide if they want to be part of the treated region.

Multilateral regulation will be seen as more legitimate. It would be much easier to implement for the following reasons: first, because it would not be seen as an

isolated effort of one particular government against the status quo but as an international consensus to decriminalize and regulate drug markets; second, because most of the governments in the Americas are popularly elected and work under democratic regimes, so their stance in favor of drug markets' legalization will not be seen as an authoritarian decision of one particular leader; and third, because the business of illegal drugs respects no boundaries, so for a decriminalization and regulation policy to work effectively it needs the support of all or most of the countries where the chain of value works. If one link is kept rotten, it will have negative externalities for the country involved and for its neighbors.

#### **WEAK INSTITUTIONS AND SOCIOECONOMIC CIRCUMSTANCES**

Latin America's weak institutions and socioeconomic problems are its fundamental reasons for continuing to fight the war on drugs. Drug violence and corruption are symptoms. However, it can take decades or centuries to fix the institutions. The regulation of drug markets can reduce the pain.

Formal institutions in Latin America haven't had the ability to adapt quickly and effectively to recent changes in criminality. In the case of Guatemala, the national police started a process of reform only in 2011. The initiative began as a response to the rise in criminality in the country, and it was institutionalized through a presidential commission. However, this commission will need to show results to prove it is having an effect. In the case of the military, it is beginning to recover after its reduction in 1996 due to the peace process in Guatemala. However, it is still unclear if the government will make equipping the military a

priority, and if so, if it will be able to do it in the short term.

For other countries, like Mexico and Colombia, the situation of their enforcement institutions has been better than that of Guatemala. But, still, that hasn't been enough to put an end to the business of drugs in those countries. On the contrary, the war on drugs has endangered public institutions in the Americas while creating the incentives for corruption.

## CONCLUSIONS

Drug-related violence is affecting everyone in most Latin American countries, one way or another. The most affected, however, are those who can't pay for private security, those who use public transportation, and those who are at the mercy of drug cartels in urban and rural areas. They are the poorest. If nothing is done, violence and corruption will continue. This is the logical outcome of a market where the producers live in low-income countries, with weak institutions, and where the consumers live in high-income countries, with strong institutions. If no action is taken, illicit drugs will continue crossing international boundaries, creating vast profits for the few and incalculable suffering for the many.

The policy direction is clear. But lobbying by a group of presidents, although extremely important, might not be sufficient. Civil support is very important as well. The fight against the war on drugs has to come from the top and from the bottom of society. This means that think tanks, intellectuals, and local leaders must participate in the discussion. This is especially important considering the sentiment expressed in a recent White House briefing in which it was said that

President Barack Obama considers this a legitimate debate (White House 2012). This opens a window of opportunity to change the U.S. discussion and policy toward the business of drugs.

A huge responsibility lies with universities, especially those in the most recently affected areas like Mexico and Central America. Universities need to contribute to the debate by supporting sound research to give us clear answers about what to do and when to do it. The public and private sectors must support these efforts.

Portugal and the Netherlands have advanced in the direction of drug regulation. What lessons can we learn from these cases? This requires deep and prompt academic research. Drug regulation is not a magic formula; it comes with significant costs. What are those costs? What is the best way to face them? These are challenges for research in the Americas if the "problem of drugs" is to be solved for both producer and consumer countries.

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## ENDNOTES

<sup>1</sup> Figure created by authors from information from the Ministerio de Gobernación in Guatemala. There has been an important reduction recently. From 1999 to 2011, the homicide rate increased "only" 60 percent.

<sup>2</sup> Figure created by authors from information from the Policía Nacional Civil and the Instituto Nacional de Estadística, Guatemala.

<sup>3</sup> Figure created by authors from information from the Instituto Nacional de Estadística y Geografía of Mexico and International Monetary Fund.

# Youth Participation in Latin America: A Fraud or a Myth?

by *Lilia Aguilar and Mariana Filgueira Risso*

If you asked scholars or political analysts who helped U.S. President Barack Obama win the presidential election in 2008, the answer would likely be “the Millennials.” In 2008, 23 million Millennials voted in the United States, casting ballots for Obama by a greater than 2:1 margin (Hais and Winograd 2008). Surprisingly as well, of the 56 percent who voted for President Hugo Chavez of Venezuela in 1998, around a third were younger than the age of thirty. The same thing happened in Argentina when Cristina Fernandez de Kirchner was reelected as president with 54 percent of the vote (Barrionuevo 2011). The Millennial Generation, also known as Generation Y, is the generation of digital communication and social media. It is positive about political processes and highly identified with cultural, social, and political liberal movements. Some scholars (Welzel and Inglehart 2009) affirm that these Millennials will determine the shape of the coming civic realignment in the world. This article aims to elucidate if the participation of young people in Latin America is a myth, meaning an activity that only exists in the governments’ public policies and publicity spots, or a fraud, in which the young are being used, sent to the streets to do the hard work on political campaigns but patronized by policies that disempower them (Inglehart 2003).

## **GENERATION X AND GENERATION Y: THE OFFSPRING OF THE BABY BOOMERS**

The so-called Baby Boomers led the social movements and rebellions of the world in the 1960s and 1970s. It was a time of change, contradiction, conflict, and radicalization. The youth of Latin America were on the front line, moving their countries toward modernization and a more just society—supporting the evolution of their homelands (Winograd and Hais 2008).

Some scholars argue that this situation changed after the economic crisis of the 1970s and the onset of the welfare state. The new social system based on impoverishment, exclusion, and breaking community initiatives dissolved youth groups and blocked their communication through power and societal pressure. This created a new youth attitude of disillusionment and nonparticipation toward social and political problems (Cotlear 2011).

There is wide discussion regarding the denomination of the youth generations after the Baby Boomers. The Millennial Generation, also known as Generation Y or Echo Boomers, are the children of the Baby Boomers and were born somewhere between the

mid-1980s and the mid-1990s. Generation X, or Gen X, what scholars used to call in Latin America “the lost generation,” were born somewhere between 1975 and 1985 (Winograd and Hais 2008).

Millennials can be identified by numerous shared characteristics. They have familiarity and dependence on emerging communications and digital technologies. They can be characterized by embracing liberal cultural issues that divided generations before them, such as ethnic diversity, tolerance and comfort with gay rights, and the equality of women. The Millennials believe in preserving standard universal values because they are sure that social rules help improve their communities. They are more individualistic and less communitarians. They grew up hearing that they were special; they were pushed to study hard and to be the “trophy kid,” to be competitive in a world of winners. Millennials are highly trusted, optimistic, team-oriented, and comfortable with their parents’ values (Huntley 2006).

Gen X, on the other hand, were raised by Baby Boomers in the midst of notable economic crises, political violence, volatility, lack of institutional security, and poor prospects of development and employment in their regions. “We are the offspring of dictatorship and crisis,” most Gen Xers say (World Bank 2007). Thus, they grew up not only individualistic but also disenfranchised from civic engagement. However, they are also team players, and even though they lived through the paradigms of the Cold War, they are tolerant to social diversity.

The characteristics of these new youth generations and their size give them vital relevance in today’s political and public

life. According to the World Bank, out of the 578,010 million total population of Latin America and the Caribbean, 109,000 million are Millennial and 91 million are Gen X. In the whole developing world, the number of twelve- to twenty-four-year-olds is the largest the globe has ever seen: around 1.3 billion currently, with a projected maximum of 1.5 billion in 2035 (World Bank 2006).

As a result, Latin America is experiencing what is known as a demographic window of opportunity that will last until about 2030 to 2050 (Cotlear 2011). Reduced infant mortality and fertility rates have led to a lower dependency ratio, an increase of females in the labor force, and a general increase in the people of working age, or the youth population (ECLAC 2007). Thus, we face a unique opportunity for economic growth if the correct policies are implemented, including those that foster youth’s participation in the public sphere (Inglehart 2003).

In sum, during this window of opportunity, the realignment of Gen X and Gen Y has the potential of leading change in the resolution of long-standing economic issues and of pushing for the revitalization of national institutions against the highly ideological, social-oriented, and antagonist shift of their parents’ generation.

### **PARTICIPATION OF LATIN AMERICA’S YOUTH AND DEMOCRACY**

A Latinobarómetro 2011 poll indicates that an average of only 58 percent of respondents believe that democracy is preferable to any other form of government; 17 percent feels that an authoritarian system is better, and 18 percent is indifferent. The distribution of ages on these answers is equal, meaning that these

numbers apply for the youth and their perception of democracy. This leads us to two conclusions: the idea of democracy is not consolidated yet in public opinion as a preferable form of government among Latin Americans; and since there is no democratic culture in the region, changes related to economic crises, such as the one in 2008, or high levels of violence, such as in Mexico, cause public opinion to immediately change regarding democracy and to ask for more “strong hand” governments (Welzel and Alexander 2008).

At the same time, dissatisfaction with democracy ranges from more than 80 percent of young people in countries such as Brazil, Ecuador, Paraguay, and Peru to less than 50 percent of dissatisfaction in countries such as Uruguay and Venezuela, according to *Latinobarómetro*.

In the past, young people were key for putting social pressure on governments for better services and for a more just system. The youth was the segment of the population that kept the checks and balances on the governments in the region, especially in the 1960s and the 1970s.

Alas, nowadays, youths in Latin America discredit the role of political institutions, they do not identify with any party, and only a minority has political and ideological preferences. Young people seem to be far from interested in traditional political processes. For example, in a survey, Mexican youth declared that they prefer to be part of an act in favor of gay rights than to attend a party assembly (*Instituto Mexicano de la Juventud* 2002). Thus, youth participate in community volunteering, through virtual networks, in global issues that spark their interest such as environment and human rights and in

other forms of collective action from graffiti to music. To the youth of today, political institutions are not seen as reliable conduits of change (CEPAL 2007).

Furthermore, according to the World Development Report of the World Bank (2007), “newspaper reading, watching politics on TV, knowledge of current events, voting, and the belief that voting is a civic duty have all fallen among youth in almost all established democracies,” including those of Latin America.

The problem is that, today, young people face a problematic tension between opportunities and threats. In proportion to their level of education, they face more unemployment problems than did their parents’ generation. They manage more information than ever, but this does not guarantee them more access to decision-making processes. Their specific health problems such as teenage pregnancy, abortion, sexually transmitted diseases, and HIV/AIDS have little recognition, and they are the most exposed group to violence and victimization, according to *Latinobarómetro* reports in 2005 and 2011.

The youth is the focus of attention of multinational organizations such as the United Nations and the World Bank, which have devoted global reports to the challenges faced by youth and the policies toward them (Rodríguez 2003).

However, many of these policies end up patronizing young people who are not included in projects for the promotion of their own development. As the World Bank states, “The situation of young people today presents the world with an unprecedented opportunity to accelerate growth and reduce poverty . . . more young people are completing primary

school and surviving childhood diseases. They must be equipped with advanced skills beyond literacy. . . . Because labor is the main asset of the poor, making it more productive is the best way to reduce poverty. So providing basic education and health care, especially for children—to provide the foundation of basic skills and well-being is crucial” (World Bank 2007, 137).

The youth in Latin America is often used for political campaigns as supporters for political ideologies; they are also the targets of endless programs and resources allocated through the World Bank and other multilateral institutions. Nonetheless, youth has been always the period in which citizenship and social and communitarian character is built. It is in this period of time that most of the countries of Latin America give their youth the right to vote (after the age of eighteen) and when they can become accountable for their actions in criminal activities. In sum, youth is the stage of life when people become full citizens in the democratic life of their countries with the right to vote and to be voted for (World Bank 2007, 160).

Policies should be aimed at fostering participation, promoting opportunities, protecting the vulnerable, and most importantly, empowering young people, not patronizing them.

Empowerment is the consequence of participation (Hart 1992). It means that individuals should exercise their rights and influence the decision-making processes that shape their lives (Kabeer 2002). In other words, it refers to the delegation of power or authority, so that citizens transition to a state in which they have more control over events (Williams 2004). In fact, participation is not just a

right; it is important because it develops critical thinking, dialogue, and citizenship skills like cooperation, respect for the law, and social responsibility (PNUD El Salvador 2008; UNICEF 2003).

### NEW FORMS OF PARTICIPATION

Analysis of data from the World Values Survey suggests that youth interest in politics might be rising in China, India, and Nigeria but falling elsewhere including in countries in Latin America. In China, India, Nigeria, Vietnam, and Zimbabwe, young people are at least as interested in politics as older people. In Indonesia and the Islamic Republic of Iran, interest in politics is highest among the young and steadily declines with age (Welzel and Alexander 2008).

The riddle starts here. Could it be that the youth in Latin America are in fact participating in public life but in unconventional ways? Is it that young people in Latin America have no access to the government if it is not through conventional ways such as political parties, which are co-opted by the Baby Boomers? Is this group really less involved than its parents or does it just simply have less access to conventional activities?

We can say that in Latin America the participation of young people has shifted from the political arena (i.e., low levels of party affiliation or participation in elections, student movements, or trade unions) to assume forms of smaller scale, lower horizon, and more modest change, outside of political parties (CEPAL 2007) (i.e., different ways of cultural participation that are used as tools for personal and community development) (Butler and Princeswal 2010).

The Gen X and Millennial generations are not interested in public service for

different reasons. Technology has increased the power of nonstate actors and reduced the prestige and power of the state; as a result, the incentives of the youth to participate in traditional politics have decreased. This reflects a conventional decline in both opportunities for participation and civic interest on the part of youth.

Notwithstanding, alternative forms of civic participation may be emerging to overcome this lack of access to power and conventional ways of participation. Forms of involvement “that are more opportunistic and less stable might have increased such as ‘monitoring citizenship,’ in which individuals evaluate governments from afar through electronic media; targeted protests; or ‘checkbook activism,’ in which individuals spend money on consumer goods and nongovernmental organizations (NGOs) that match their values” (World Bank 2007, 160).

Regardless of whether or not trends in youth participation resemble the declines of traditional, visible ways of participation, in Latin America it is the work of the young to find new forms of youth political engagement. We must encourage active political citizenship along with the social and economic dimensions of citizenship.

In Chile, the latest social movements of students have shaped the way in which civil society is influencing the development of the country. University students in 2011 have managed to gain empathy from most of the Chilean society in their protests regarding improvements in public education. They understood that it was necessary to focus their message on a problem that affects the whole country: economic inequality. Through this new framing, the demands of the students

became the demands of the whole nation. A high-quality, free, public education for everyone would be the solution to the inequality in the distribution of the national wealth. It is not a surprising that this new broad message received the support of more than 90 percent of the Chilean population.

Another example is *Un Techo para mi País* (A Roof for my Country) in Chile, a nonprofit organization founded by a group of university students with the goal of building emergency housing for the thousands of Chileans who were living in precarious conditions. *Un Techo para mi País* invites the society to recognize the injustices of poverty and acknowledge its responsibility to address the lack of opportunities and the poor living conditions of the most marginalized families in Latin America and the Caribbean,” according to the organization’s Web site. The NGO started its expansion in 2001 and is now working in nineteen countries around Latin America, with the collaboration of more than 400,000 young volunteers.

Thus, not everything seems hopeless. Members of Gen X and Gen Y around the world, and also in Latin America, are committed to alleviating extreme poverty and are demanding that their governments create a more fair society with equal opportunities for everyone. They are doing so in new, creative unconventional ways.

## CONCLUSION

In the last ten years, Latin America has experienced on average a good economic stability despite the economic crisis of 2008, according to *Latinobarómetro*. The construction of a political culture is imperative for the region to develop a stronger democratic system. It is proven



that there is a direct correlation of .54 between the existence of a democratic culture and the construction of strong democracy systems and an even higher correlation of .72 between democratic culture along with economic development stability and strong democratic systems (Inglehart 2003).

The role of Gen X and Gen Y in the construction of a political culture and the construction of a strong democratic system that will change the face of the region will be decisive. These generations hold a set of values directly related to the construction of a political culture. These values such as tolerance, diversity, and appreciation for freedom, also known as empowering values or self-expression values, are intrinsic to Gen Y and Gen X, as we explained before (Welzel and Inglehart 2009).

During the two decades from 1990 to 2010, Latin America's youth remained asleep. Little by little, they seem to be waking up. In this second decade of the 2000s, Millennials started to engage in social, civic, and political movements such as the student movements of Chile. Youth seems to be recovering their vitality and assuming responsibility to create a more just and equal world.

They have started to participate in the public and political spheres through unconventional ways, such as through social media or involvement in nonprofit organizations. However, politicians still utilize their idealism to support election campaigns. Other times, youth find their ways to intervene in society through traditional protests and student movements. Most of the time, policies for youth rest in the offices of bureaucrats who can never implement them.

Youth participation in Latin America is indeed at times a fraud . . . as well as a myth, but, moreover, it is an opportunity. The size of Gen X and Gen Y together—200 million in Latin America—is astonishing. Their characteristics and potential if they ally and work together is promising.

Gen X, the sons and daughters of the dictatorships and the crisis, grew up when “politics” had become a bad word, a synonym of death and immorality. They did not want to fight; their parents’ experiences had been too dramatic. Gen Y grew up in a period of relative political stability; the deep economic and political crises were over. They were raised in moments of peace, security, and certainty. Thus, they grew up without a clear cause. Nonetheless there is something they have in common: social awareness. They care, profoundly, about the world that surrounds them: the poor and the rich, the excluded and included, the children and the elders. They have what author Jeremy Rifkin has called global empathy, the ability to connect with others and nature.

Gen X and Gen Y are starting to take the lead. They are generating and accessing public spaces in order to change economic, social, political, and cultural circles. It is not enough to participate and support presidential elections as in Venezuela or Argentina. The New Great Generations, as some scholars call them, own the present and will have to build the future. The NGO Un Techo para mi País spreading its value all around Latin America is a perfect example. Gen X will provide the experience, their disappointments, and their frustrations; Gen Y will provide their energy and their vigor. That is the opportunity that Latin America should embrace. These citizens, empowered by each other, will bring the trans-

formation that the region needs, the consolidation of its formal and informal institutions in order to make real progress.

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# Latin America:

## Amazing Progress, Persisting Challenges, and the New Power of Innovation

by Angel Gurría

### ABSTRACT:

*Latin America has been making significant progress of late and has even weathered the recent global economic crisis fairly well. The region needs to take advantage of the opportunity it is facing for significant increases in development. However, it must first confront its persisting challenges of poverty, inequality, productivity, and education. As explored in this article, the key to achieving the region's potential for growth lies in innovation.*

Latin America has been making remarkable progress. After the so-called lost decade of the 1980s, the political, economic, and social reforms of the 1990s and 2000s have borne important fruit. Between 2003 and 2008, the region experienced its most remarkable expansionary period since the 1970s. Most of its countries managed to build resilience, which helped them weather the global financial and economic crisis fairly well. Today, most of these economies have solid macroeconomic stability, relatively healthy fiscal positions, manageable public debts, and the trust of financial markets, in contrast with a great number of non-Latin American Organisation for Economic Co-operation and Development (OECD) countries.

Many of these Latin American countries have also developed increasingly modern and reliable regulatory frameworks for foreign investment and broad networks of free trade agreements. This has not only fostered an impressive growth of foreign direct investment inflows and exports, but it has also produced a considerable reduction of poverty ranks and the emergence of a meaningful and stabilizing middle class. While many non-Latin American OECD countries are experiencing a weak recovery, Latin America's average gross domestic product (GDP) expanded by nearly 6 percent in 2010 and 4.3 percent in 2011, according to estimates from the Inter-American Development Bank. Hope and optimism are back in force. Positive expectations are growing. Some even talk about the Latin American decade.

Much of this expansion, however, has been fueled by remarkable rises in international commodity prices and by consumers and investors from other parts of the world. Latin America still needs to improve its capacity to generate endogenous growth. Social and economic improvements in the past decade have been impressive, and they now

constitute a solid base to build on, but the reality is that most of these countries are still confronting myriad complex structural challenges, which translate into comparative disadvantages and economic vulnerabilities.

### **PERSISTING LATIN AMERICAN CHALLENGES**

Reducing poverty and inequality are at the top of the list of challenges. With respect to curbing poverty, the region has made recent important progress. According to estimations by the Economic Commission for Latin America and the Caribbean, poverty in Latin America has dropped by 17 percentage points over the past twenty years to around 31 percent of the total population. However, nearly 45 percent of Latin Americans under the age of eighteen are still living in poverty (Economic Commission for Latin America and the Caribbean 2012). This is a worrying figure, considering that childhood poverty has a longer lasting impact and that Latin America is one of the regions with the youngest populations in the world.

Moreover, Latin America is still the region with the largest inequalities. Recent studies reveal that ten out of the fifteen most unequal countries in the world are in Latin America and the Caribbean (United Nations Development Programme 2011). Within the OECD, Chile is the country with the largest inequalities. The second is Mexico. The recent OECD study “Divided We Stand: Why Inequality Keeps Rising” reveals that income inequality has recently fallen both in Chile and Mexico, but the richest in these two countries still have incomes more than twenty-five times those of the poorest. And in the case of Brazil, this difference is fifty times (OECD 2011a,

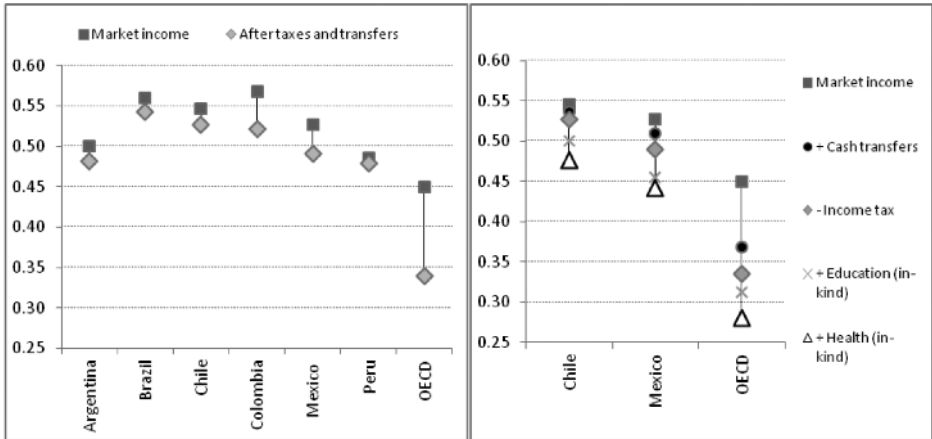
17). These huge disparities have become a major obstacle for achieving greater competitiveness and productivity as well as a source of social polarization, organized crime, and insecurity. According to the “Global Study on Homicide 2011” by the United Nations Office on Drugs and Crime, Latin America has the highest percentage of homicides by firearm in the world, with South America as the leading subregion (United Nations Office on Drugs and Crime 2011, 10). The most effective way to combat organized crime and insecurity is by reducing socioeconomic disparities. This is a challenge that Latin American countries must keep tackling through innovative policies, local development programs, and enhanced regional and multilateral cooperation.

Transforming fiscal systems into effective development instruments is a pending mission in practically all Latin American countries. Fiscal policy in Latin America does little to reduce inequality due to low levels of direct personal taxes and public social expenditure as well as inadequate targeting of such expenditure. This explains the significant differences in the effectiveness of fiscal policy at reducing inequalities in Latin America compared with other non-Latin American OECD economies (see Figure 1). These differences are most significant for cash transfers rather than for in-kind transfers such as expenditure on education and health. To reverse this situation, governments must reinforce income transfer programs for low-income households and the solidarity pillars of social protection systems, in particular, the pension system, while taking care not to create incentives that would favor the informal economy or encourage people not to work.

Another key structural challenge that most countries in Latin America are

**Figure 1 — Fiscal policy does little to reduce inequality in Latin America (Gini indices).**

Source: OECD for non-Latin American OECD countries and for Argentina, Brazil, Colombia, and Peru; estimations based on household surveys for Chile and Mexico.



facing, with some variations but with a shared sense of urgency, is the need to improve productivity levels. In spite of recent improvements in some countries, Latin American productivity remains low, and this affects its competitiveness. In fact, the productivity gap between Latin America and non-Latin American OECD countries has been widening, while other emerging economies have been catching up (Daude and Fernández-Arias 2010). According to the latest available comparative figures (from 2010), Chile and Mexico are the OECD countries with the lowest labor productivity, with less than \$20 in GDP per hour worked, in contrast with an OECD average of nearly \$43 or with countries like Luxembourg or Norway that have more than \$70 in GDP per hour worked (OECD 2011b, 66). This productivity gap reflects, among other things, the limited diversification of the region’s economies and their specialization in nontechnology-intensive sectors. Labor productivity in technology-intensive sectors in Latin America was just 18 percent of the productivity in the same sectors in the United States in 1990 and

12 percent in 2007, reflecting little structural change in the region. Latin America’s ability to raise its output per worker will determine to a great extent the efficiency and competitiveness of its key sectors, its capacity to attract productive investments, its capacity to diversify its industrial platform, its strength and/or vulnerability in international trade flows, and, in the end, its capacity to adapt to a new, more competitive, and permanently changing global economy.

Reducing the region’s dependence on finite natural resources as a source of exports and economic growth is another important structural challenge. With the exception of Mexico, the Latin American export mix has not varied much in the past twenty-five years in contrast with other emerging economies like Korea and Singapore. Natural resource-intensive sectors in Latin America still account for around 60 percent of total manufacturing value added. These models have their limitations, and some Latin American countries are already reaching them. To base a national growth and development

strategy on the systematic exploitation of finite natural resources, even if these are relatively abundant, can lead to instability, as commodity prices are highly volatile. Some OECD countries like Australia, Canada, Norway, and New Zealand have higher per capita commodity exports than many Latin American countries, but that has not prevented them from diversifying their economies into sectors with high-tech value added and services. As Andrés Velasco (2012), the former finance minister of Chile, emphasized in a recent article, “the region’s challenge is to transform its huge natural-resource wealth into the kind of wealth that does not run out, because it’s constantly enlarged by human creativity.”

This is one of the greatest challenges that Latin American countries will face in the coming decades: the need to develop efficient and world-leading innovation systems. One of the central explanations behind Latin America’s low productivity and modest competitiveness is the scant attention paid to innovation. Public and private investment in research and development (R&D), one of the key ingredients of any innovation system (although not the only one, of course), remains very low: Latin American countries allocate just 0.3 percent of regional GDP to R&D, compared to an average of 2.33 percent in the OECD (OECD 2012a; World Bank n.d.). It is important to recognize that in the big five Latin American economies (Argentina, Brazil, Chile, Colombia, and Mexico) knowledge-intensive industries have been growing at higher rates than other industries, especially during the 2000s; however, with the exception of Brazil and to some extent Argentina, this knowledge-intensive growth has not been widely spread and is owed to a large extent to the automobile industry—mainly an assembling industry, in most

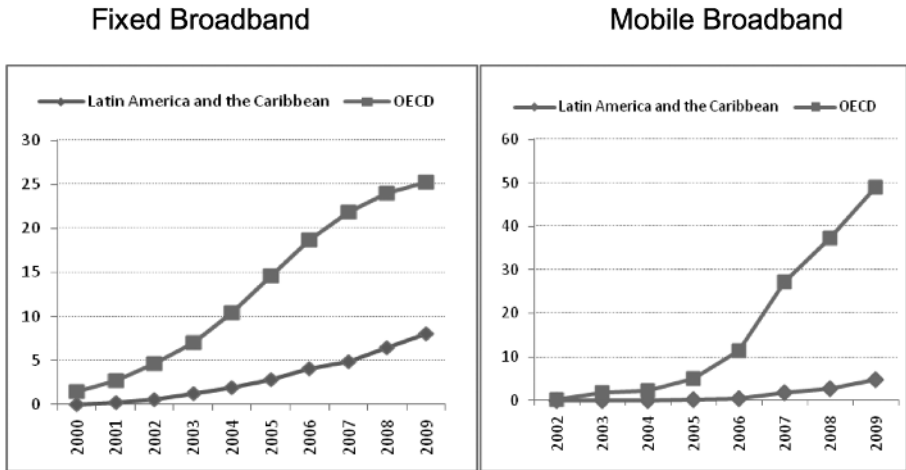
cases characterized by weak upstream domestic linkages. This needs to change.

### **“LATINNOVATION”: SWITCHING ON THE NEW POWER**

Latin American countries need to put innovation at the center of their development strategies. During the next fifty years, investment and growth will be increasingly driven by knowledge-based capital (KBC). In many non-Latin American OECD countries, firms now invest as much or more in KBC as they do in physical capital such as machinery, equipment, and buildings. In the years to come, the environment for investment in KBC will have a strong impact on the economic performance of countries, because it will determine which countries retain or move into the highly value-adding segments of which industries. For example, in 2006, the iPod accounted for 41,000 jobs, with 27,000 outside the United States and 14,000 inside. But U.S. workers—where investments were occurring in forms of KBC such as design, R&D, software, and marketing—earned a total of \$753 million (in terms of total wages), while those abroad earned \$318 million (OECD 2012b, 2).

Promoting efficient national innovation systems is essential in order to build these new sources of growth. Latin America needs to promote a new pro-innovation business culture that facilitates the propagation of business start-ups. In many of these countries, this will imply a substantial increase in domestic competition in key network sectors and among providers of services, which are essential for business start-ups to flourish. Innovators in Latin America very often have to pay high prices for key inputs like Internet access, telecommunication services, or energy, which are the result of poor competition and monopolistic practices in such countries.

**Figure 2 — The broadband gap in Latin America is large and increasing. The figure shows fixed and mobile broadband subscribers as a percentage of the total population. Source: Regional Broadband Observatory in the International Telecommunication Union database. Note: The regional average is a simple average.**



Source: Regional Broadband Observatory in the International Telecommunication Union database. Note: The regional average is a simple average.

In the past few years, a number of countries in the region have taken important steps to build a favorable environment for innovation. A recent study by the OECD Development Centre and INSEAD (2011) reflects how several Latin American governments have launched strategic initiatives like the 2007-2010 PACTI plan in Brazil and the Special Science, Technology and Innovation Program 2007-2012 in Mexico. Elsewhere, key reforms have been introduced such as the creation of a Ministry of Science, Technology and Productive Innovation in Argentina, or the channeling of commodity export earnings into innovation projects in Chile.

While these and other measures are promoting the creation of national innovation systems, much remains to be

done. The indicators show that, even on a broad definition of innovation, Latin American countries lag way behind their OECD counterparts and other emerging economies. For example, there is still a very wide gap in the number of patent applications between Latin America and non-Latin American OECD countries. According to OECD data, Brazil and Mexico, the region's most advanced countries, filed 359 and 133 patent applications, respectively, with the European Patents Office in 2009, compared to the 6,406 filed by Korea (OECD Development Centre and INSEAD 2011, 22). Brazil, Chile, and Mexico are ranked last among OECD member and partner emerging countries in terms of the share of information and communication technologies in use in value-added ways and the number of scientists for every 1,000 employees (OECD 2010a, 155-163).



One determinant factor in Latin America's effort to promote innovation is the low levels of broadband Internet penetration in most of these countries (see Figure 2).

Latin American countries need to embark on a regional crusade for innovation. It is essential to share experiences and best practices in the creation of national innovation systems. And it is important to identify priorities and target efforts on key areas for development, such as infrastructure, taxation, water management, and e-government, or on channeling remittances into productive projects. One particular sector where Latin American countries can see their pro-innovation efforts produce fast and relevant results in terms of jobs and quality of life is green growth. Promoting green innovation that harnesses the industrial metabolism of Latin American economies into growth that respects and improves the environment could be a very rich source of growth and employment for Latin American people. Korea, for example, has been implementing a "Green New Deal" that has created about 960,000 new jobs between 2009 and 2012 (OECD 2010b, 27).

The OECD is working with several Latin American governments to help foster regional cooperation efforts to strengthen the regional links in science, technology, and innovation programs within the framework of its Latin American and Caribbean Initiative. Promoting the emergence of national innovation systems in Latin America demands an all-of-government response, through which policies can be coordinated and synchronized around this important objective, as well as enhanced regional cooperation and exchange of best practices. But it will also demand a particular focus on one single

strategic area in which most Latin American countries still face enormous challenges: education.

### **HIGH-QUALITY EDUCATION: THE MAGIC INGREDIENT**

An essential factor in promoting innovation in Latin American countries is the need to invest in people. Human capital is the region's main asset and should be the cornerstone of any innovation policy. But this is precisely where the countries of the region face one of their greatest challenges.

In the 2009 evaluations of the OECD's Programme for International Student Assessment (PISA), students from all of the Latin American countries that participated (Argentina, Brazil, Chile, Colombia, Mexico, Panama, Peru, Trinidad and Tobago, and Uruguay) achieved worryingly low results, which ranked them in the lowest places in subjects such as reading and mathematics, in contrast to other emerging economies such as China, Korea, and Singapore, which were ranked among the highest. If we take a look at Latin America's higher education, the challenges are even greater. The region has advanced in the "democratization" of higher education, making it more and more accessible, but in most countries it has lagged in terms of quality and equity. The differences in the quality of higher education between public and private institutions are still high in many countries, but even the best private higher education institutions are well behind their peers in other, non-Latin American OECD countries. The fact that there is only one Latin American university (the University of Sao Paulo) among the world's top 200 universities (in place 178) according to the *Times Higher Education* ranking is quite telling (Economist 2011).

Recent analysis by the *Economist* highlights the big challenges higher education institutions in Latin America are facing, underlining that “research output is unimpressive, teaching techniques are old-fashioned and students drop out in droves” (Economist 2011).

Education is still the Achilles heel of Latin America. It is the source of many of its problems but also of the much needed solutions. The OECD can provide major support to improve the quality of education in Latin American schools, sharing the experience of programs such as PISA, the Assessment of Higher Education Learning Outcomes, and the Teaching and Learning International Study. Improving education systems in Latin America has a direct impact not only in terms of reducing disparities, but also by increasing the capacity and intensity of innovation in the region. Education and innovation should be the two great wings of Latin America’s new progress.

Latin Americans have a unique opportunity to take a quantum leap toward development. The region can’t afford to waste this collection of favorable preconditions: stable democracies, solid economies, robust financial systems, a young and hard-working population, abundant natural wealth, and increasing international relevance. The region should make innovation the live wire that binds and empowers these elements and enables us to create stronger, fairer, and cleaner economies as well as a more prosperous and brighter future for all Latin Americans.

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# Challenges and Opportunities for Small Developing Economies in the New Trade Environment

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## ABSTRACT:

*The new global trade and investment environment can have a powerful impact on small economies. As global value chains grow in importance, small countries have access to investments that would not have been possible before. But if the benefits of global value chains are accentuated in small economies, so too are the risks. Global supply chains make industrialization easier, but they also make it shallower. Jobs are often specific to a single specialization, not diverse and apt to foster the spread of industry-related knowledge. This article explores how small countries can leverage the potential of value chain oriented investment by building competitive domestic firms and establishing effective linkages between foreign investors and the domestic economy.*

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## INTRODUCTION: GLOBAL VALUE CHAINS AND SMALL ECONOMIES

In 2009, an EU-based chemical manufacturer opened a plant inside one of FYR Macedonia's recently established special economic zones. The plant began production of catalysts, a type of emissions-control component used in automobiles. Two years later, this investment drove chemical products to the third-highest spot on Macedonia's export list, lessening the country's reliance on metals and textiles.

In Nicaragua, low labor costs and a better security situation compared to its neighbors have contributed to a dramatic expansion of investment in the *zonas francas*<sup>1</sup>, attracting producers of electronic wires and medical devices and expanding the country's manufacturing exports outside the already well-established apparel sector. Between 2006 and 2008, for example, the relatively obscure product "ignition wiring sets for vehicles" was the country's fourth-biggest export.

These two examples demonstrate the powerful impact that the new global trade and investment environment can have on small economies. Increasingly, as global value chains grow in importance, small countries such as Macedonia and Nicaragua have

access to investments that would not have been possible before. As economist Richard Baldwin (2012) asserts, with the fragmentation of production into global value chains, “exporting is easy.” No longer do countries need to nurture firms through a competitive domestic environment through which the most productive emerge as exporters. In fact, in a value chain environment where export platform investment is the norm, even the “new-new” trade models of heterogeneous firms (Melitz 2003) become obsolete. Traditional perspectives of sectoral specialization based on comparative advantage have also become obsolete in this value chain world. No longer is the lack of an industrial complex an impediment to attracting “born to export” firms. Neither Macedonia nor Nicaragua have any automotive assembly operations, any strong engineering capabilities, and hardly any attractive consumer markets for automobiles, yet they have managed to attract significant export-oriented investments in the sector. And because these economies are small, such investments have a dramatic impact on the level and composition of the export basket; both countries can now count themselves as having a “revealed comparative advantage” in the automotive sector. Moreover, these investments have allowed both Macedonia and Nicaragua to enjoy substantial increases in exports and diversification away from traditional industries. Exporting is easy indeed.

But if the benefits of global value chains are accentuated in small economies, so too are the risks. Global supply chains make industrialization easier, but as Baldwin (2012) points out, they also make it shallower. Macedonia may have a couple of successful automotive components factories, but it does not have a complex, integrated auto industry. The

automotive exporters are exclusively foreign-owned, they rely almost completely on imported inputs, the technologies are largely company-specific, and the markets are outside Macedonia. The same pattern holds for wire harnesses and even longer-established activities like apparel in Nicaragua. The one thing that is clearly Macedonian or Nicaraguan about these exports is the workers who produce (or perhaps more appropriately, assemble, them). But here too we see that in most cases the jobs are specific to a single specialization, not diverse and apt to foster the spread of industry-related knowledge. In fact, the jobs often have little to do with specialization of skills at all but are rather simply a function of relative wages. In the worst cases, even minimally specialized technical jobs take place outside the country or by foreign workers. In such an environment, the host country runs a serious risk of being simply a source of cheap labor, with its export industry vulnerable to any small change in the economic formula that brought the investment in the first place. This vulnerability is particularly acute for small, developing countries as they are unable to offer domestic markets or the potential for scale economies, two factors that larger developing countries can use to embed value chain investors.

#### **EXPERIENCES FROM THE FIELD: ATTRACTING VERSUS EMBEDDING FOREIGN DIRECT INVESTMENT**

Working with regional teams and using a tool called the Trade Competitiveness Diagnostic (Reis and Farole 2012) to assess countries’ trade environments, we in the World Bank’s International Trade Department have seen firsthand both the opportunities and challenges this new environment brings in small economies. In some ways, the phenomenon is an

extension of the long-established experience of “offshoring” basic production functions, particularly when they are sequestered in enclaves such as export processing zones, where companies receive tax benefits and other targeted incentives. In the past two decades, small economies throughout Central America (including Nicaragua but also Honduras, El Salvador, and to a lesser degree Guatemala) have watched offshore investments by a small set of investors, mainly those manufacturing clothing for the U.S. market, transform their exports. More recently, this offshoring process has spread beyond the apparel sector to include the automotive value chain, the medical and pharmaceutical sectors, and even services like call centers and back-office processing.

The experience of these countries suggests that while such investments offer significant short-term benefits and dynamic potential, strategies that are focused simply on attracting investment may have serious limitations in terms of sustainable economic growth and, most importantly, in reducing poverty. The problem is that these investments, from the catalyst plant in Macedonia to garments and wire-harness factories in Central America, tend to be well-integrated into global value chains but not necessarily into their domestic economies. They offer jobs—often a large number of them—but little outside of this.

This reality poses a whole new set of policy questions. While job creation is valuable in its own right, without additional spillovers, the value of jobs created by foreign investment may be outweighed by the incentives the government offers to attract the investment in the first place. If the country offers little more than cheap labor, it might not retain “footloose” investors without restraining wages over the long term. But by keeping

wages down, the country reduces its chances of development and significant poverty reduction.

Before moving forward, it is legitimate to ask if there is evidence that foreign direct investment (FDI) that is attracted only by the low cost of labor is volatile. Since there may be large sunk costs for FDI to establish in new countries, one could argue that these investments have come to stay. On the other hand, much of the value chain investment going into small countries in Central America is going into sectors in which labor costs account for 50 percent or more of operating costs. Moreover, the *zonas francas* in which many of these firms are based have been established precisely to reduce the investment risk of FDI, offering ready-built factories on relatively short leaseholds and, in some cases, reduced obligations toward workers. In short, the *zonas francas* contribute to the volatility of investment by allowing investors to be increasingly footloose; indeed it is the footloose nature of these investors that allowed them to be attracted in the first place. Anecdotally, sunk costs appear low in many of the industries considered. In Nicaragua, for instance, some auto parts plants were established there as an alternative to Mexico. They are run by Mexican managers and can easily return to Mexico if local conditions deteriorate. In the case of Macedonia, the automotive investors are established in special economic zones where even the factory construction was subsidized by the state; moreover, these investors are courted by even more attractive subsidies available in several neighboring countries.

In this context of footloose, global value chain oriented investment, the key to embedding FDI, and capturing greater spillovers, is facilitating greater linkages between the export-oriented foreign

investors and the domestic economy. This can happen through three broad channels: (1) supply chain linkages (vertical linkages), most importantly the use of domestic suppliers of goods and services, and also selling into downstream domestic firms; (2) horizontal linkages, including collaborations between foreign investors and domestic firms or institutions (e.g., universities); and (3) the movement of skilled workers in and out of foreign firms. It is through these channels that foreign firms transmit globally acquired skills and knowledge to the domestic economy as well as facilitate improved productivity and upgrading. While many countries fail to leverage this potential, there are some notable successes, even among relatively small economies. In Asia, Malaysia and Singapore combined aggressive FDI strategies (including the use of EPZs) with active supply-side policies focused on education, technology, and targeted supply chain development. This worked to embed FDI and upgrade domestic firms. In Latin America, Costa Rica's success was a result of its well-known capture of the Intel investment with a somewhat less-documented, but equally critical, strategy of building local supply linkages and developing competitive, export-ready small and medium-sized enterprises (SMEs).

### **FACILITATING SUPPLY CHAIN LINKAGES**

Embedding foreign investors into the local economy depends crucially on establishing links in the domestic supply chain, both forward and, most importantly, backward to local suppliers. Such links also facilitate the spillover of technology and knowledge from foreign investors to local firms and workers. Multinationals may expect high interna-

tional standards from local input and service suppliers, for example, for product quality and delivery time, as well as technological efficiency that increases their overall productivity (Paus and Gallagher 2008). Besides better products, foreign firms may increase the demand for more specific intermediates, which will increase input variety in upstream sectors (Javorcik 2008). Multinational affiliates might also help local producers to upgrade their technological capabilities directly through sharing of production techniques and product design and assisting with technology acquisition (Paus and Gallagher 2008), or, more generally, through technical support, assistance with obtaining quality certifications, and improved access to finance (including advance payment).

Most of the available empirical evidence suggests that deepening linkages has positive benefits both for FDI and local firms in the supply chain. For example, a study for Ireland in the late 1970s (McAleese and McDonald 1978) shows that local purchasing of inputs increases as the foreign firms mature. More recently, a study for Vietnam (Le and Pomfret 2008) shows that domestic firms with backward linkages in FDI-dominated industries have higher productivity than other firms. Finally, another study (Blalock and Gertler 2008) shows that in Indonesia FDI generates a positive externality (lower prices and greater output), benefiting suppliers, final goods markets, and consumers.

But how can these linkages be encouraged and strengthened?

Before discussing this, it is important to recognize what not to do. The imposition of local content requirements, a kind of demand-side policy, has been widely used

lately in many countries, including in Latin America. In general, while some regulatory push is often needed to facilitate foreign investors to establish local supply links, most local content policies have been ineffective and distorting. Despite relatively scarce empirical investigation about these policies, a number of basic principles are now well-understood.

First, local content policies tend to be more effective in extractive, rent-generating sectors, like oil and gas and mining and, more controversially, in sectors with strong backward linkages, like automotive. These are sectors where the main (if not the only) justification for using this policy—fostering knowledge transfers and learning spillovers—applies. For example, for raw materials-based low-income economies, the promotion of backward linkages is important to diversify and gradually move away from the extractive sectors and integrate further in the global value chain (GVC), while building on their factor endowments. On the other hand, in countries that are already well-integrated in the assembly end of GVCs, it is the promotion of backward linkages that could arguably be of more importance as a means to upgrade the value-added content of their exports. This should be kept in mind when comparing experiences across countries. This would also lead to a discussion about the merits and challenges posed by diversification and specialization. After all, as it is well-known, under competitive circumstances, domestic content requirements act as a tax increasing the cost of intermediate goods and, consequently, the price of the final good, leading to higher prices and an inevitable reduction of consumer surplus. Although consumer surplus is partially transferred to producers, there is a deadweight loss that reduces country welfare.

Second, middle-income (and large) countries are in a much better position to deliver on local content than are small, developing countries. They have an advantage because of scale, deeper specialization in the workforce, and a large domestic customer base. Looking at the Brazilian experience, for instance, local content policies seem to be one of the drivers behind the recent increase in FDI in the oil and gas sectors, but this experience is probably difficult to replicate in less developed and smaller countries. In fact, most low-income countries struggle with local firms that are not competitive, lack relevant experience and technical capabilities, and have poor production quality and reliability.

A related point to be considered here is the role of the existing infrastructure and of the logistic potential of the host country (assessed not only from a purely isolated national point of view but also in terms of the country's potential to integrate itself in the wider global economy as part of a greater regional market). This could improve both its attractiveness to the eyes of foreign investors and the ability of local firms to explore the spillover channels. In this regard, the size of the economy in itself should not be seen in isolation.

Where a country does decide to initiate local content policies as part of efforts to facilitate FDI linkages, it is important to clarify that the objective should be to increase local value addition, not local content per se. For example, let's take the Macedonian automotive foreign investor: if there is a blunt policy forcing or incentivizing them to buy certain components from a "local" (i.e., Macedonian) supplier, the result may be to encourage the creation of local



distributors or agents who simply import the components and add a margin. The result is to reduce the competitiveness of the investor (by raising the costs of inputs) while simply enriching a single local distributor, with no real employment or technology spillovers. By contrast, a fully foreign-owned firm may come to Macedonia to manufacture the component. It seems clear that the second adds more value and has greater spillover potential (through skills, technology, etc.). But there are a lot of gray areas between these two extremes, leading to significant confusion and risk of distortionary outcomes.

In this context, initiatives to develop the supply side are much more promising avenues through which to support the development of linkages. Developing competitive local suppliers requires a strong, competitive local industry base and the absorptive capacity of firms, institutions, and workers. This tends to vary significantly across countries and is dependent not only on structural characteristics (again, small, developing countries are at a disadvantage), but also, critically, on the policy environment. The characteristics of the business environment, notably the degree of homegrown competition pressure, and the degree of exposure to foreign competitors in the domestic and external markets are issues to take into account. Recent research (Van Assche 2012) argues that, in the fragmented global value chain environment, governments can boost their positions by establishing: (1) clear rules and enforcement (to enable risk-free contracting); and (2) effective institutions.

More tactically, governments can facilitate contacts and provide incentives for foreign investors to use local sources for production inputs. So-called FDI-SME linkage

programs have been established in a wide variety of industries and country contexts. In most cases, they focus on a small set of large foreign investors who contribute time and resources to supporting the technical upgrading of local SMEs, with the aim of identifying potential supply partners. One of the most successful in Latin America was Costa Rica's Supplier Development Program (part of the Proveen Program), which facilitated SME linkages in high-technology sectors following the influx of high-technology FDI linked to the Intel investment. This program and others like it show the potential of establishing sustainable supply chain partnerships even in small, developing countries. But they also highlight the importance of an aggressive and resource-intensive effort on the part of government (typically through an investment promotion or SME agency) to support these initiatives.

### **STRENGTHENING THE ABSORPTIVE CAPACITY OF LOCAL FIRMS**

The key to ensuring that local firms participate in and benefit from global value chain investments lies in improving the competitiveness of these firms. While intensive technical support is a starting point, benefiting from the knowledge and technology of foreign investors is critically dependent on the local firms' absorptive capacity. Among the most important policies here are those focused on the local learning and innovation environment infrastructure, including investments in education, interactions between institutions of higher learning (e.g., training centers) and the private sector, and existing and well-embedded technological research institutes. This generally requires coordinated government actions among the relevant institutions. But it can also involve

public-private initiatives to support targeted skills development.

Policies should also target the elimination of barriers to firm growth. Access to finance and practices of competitors in informal sectors, for instance, have been shown to be major concerns of small firms in developing countries. Easing access to finance and implementing regulations to reduce informal competition might be the right steps to foster firm growth and, consequently, local firms' capacities to absorb FDI spillovers. Improved financing terms are often components of linkages programs, for example, offering suppliers faster payment terms or leveraging the low credit risk of the large foreign investors to facilitate access to financing of better terms for local suppliers. For example, the NAFIN factoring program in Mexico transfers the credit risk of the small suppliers to highly creditworthy buyers and enables the bank to offer financing without recourse or any collateral from SMEs.

### **BUILDING COMPETITIVE DOMESTIC EXPORTERS**

Finally, ensuring success and sustainability in the new trade and investment environment, particularly for small, developing countries, requires going beyond attracting "ready-to-export" FDI, such as the catalyst manufacturer in Macedonia or the numerous apparel and now automotive wire-harness firms dotted throughout Central America. While large, foreign investors may still account for the majority of exports, over the long term, sustainability of export flows will rely on the emergence of competitive domestic exporters. Indeed, the ability of local firms to survive the rigors of foreign markets is, in effect,

proof that the domestic sector has come of age. One can imagine a sequence by which locally owned, SMEs first become suppliers to export-oriented FDI and then integrate into global supply chains themselves. The widely recognized connection between productivity and exporting suggests that SMEs could improve through a learning-by-exporting dynamic, and countries would thus facilitate the emergence of agile, mid-sized exporters.

A focus on SME competitiveness in exporting will require governments to intervene in a more in-depth and targeted way to build competitive firms, while avoiding a traditional regulatory mindset or the compulsion to "pick winners." It can be viewed as creating programs for "export enterprise development." This requires export promotion agencies to move much further upstream in the value chain from areas like new market penetration, where they are traditionally accustomed to operating. Instead, under this model, resources are targeted to improving the productivity of firms that are seen to have high "export potential." Support may cover issues like production capabilities, market research, logistics, designing marketing plans, accessing finance, and preparing for exporting.

Two particular challenges emerge from this "export enterprise development" approach. First, given how resource intensive they are and the large number of potential SMEs that might be supported, it is critical to pre-screen to identify firms of highest potential. Second, the role of export promotion and of SME development becomes much more tightly integrated under this model. Successful implementation therefore requires close coordination between the agencies responsible for SME

development and for export promotion. Chile's highly successful export promotion efforts are in part based on a highly effective export enterprise development model.

## CONCLUSION

Developing countries have benefited enormously from the dramatic changes in the global trade and investment environment brought about by the development of global value chains. For small economies in particular, value chain oriented investment has brought with it export industries on a wholesale basis. But when this export sector functions as an enclave, countries are failing to take advantage of the dynamic potential of FDI and, worse, are vulnerable to the footloose nature of value chain investments. Leveraging the potential of value chain oriented investment requires building competitive domestic firms and establishing effective linkages between foreign investors and the domestic economy. These are essentially two sides of the same coin. Indeed, embedding foreign investors is achievable only when effective supply-side programs are put in place, not when local content is enforced by dictate. No doubt building up supply-side capacity is a longer-term and more difficult challenge, but, if done effectively within the context of global supply chains, it may be possible to leverage FDI as a platform for the development of a sustainable national export sector, on the back of competitive, globally integrated, local firms.

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## ENDNOTE

<sup>1</sup> "Zonas francas" is a term commonly used in Latin America to describe free trade zones and export processing zones (EPZs).

# Financial Sector Development and Innovation in Mexico

by Jose Antonio Meade

## ABSTRACT:

*This article reviews the lessons offered by the history of the Mexican financial system on how to address the challenge of promoting financial development, including through innovation, while avoiding the market failures that are prevalent in financial systems. After the privatization of commercial banks in the late 1980s, an explosive growth of credit in the context of a weak regulatory framework led to the 1994-1995 crisis. In response to it, Mexico embarked on a series of reforms to improve and modernize regulation, which successfully laid the foundation for a stable system where innovation takes place in a sustainable manner.*

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A financial system that works properly is a key element in the process of economic development. By fulfilling a series of vital functions—such as allowing for an effective way of making payments, transferring resources between savers and investors across space and time, and allowing individuals, firms, and the public sector to insure themselves against risks—a financial system can have enormous benefits for a society. Unfortunately, financial systems are also plagued by market failures, leading in the extreme to the financial crises that have been observed over time throughout the world, including in Mexico and Asia in the 1990s and in industrialized countries more recently. Often, these crises follow a period of financial innovation that can have genuine benefits for society but that can also lead to excess leverage and asset bubbles.<sup>1</sup>

As a consequence, society and policy makers always face the challenge of how to promote the development of the financial system, including through innovation on new financial instruments and services, while at the same time avoiding the associated market failures and the very costly crises that can be caused by them. After discussing in greater detail the benefits and market failures arising from financial development and innovation, this article reviews the evolution of the Mexican financial system during the last two decades with the purpose of extracting some lessons on how to move from a vulnerable financial system to a more stable one where sustainable innovation has been taking place.

## FINANCIAL SYSTEM DEVELOPMENT: BENEFITS AND RISKS

The potential benefits from a well-functioning financial system are very significant. While going into full detail is beyond the scope of this article, it is nevertheless worth briefly reviewing the key ideas to emphasize the importance of the financial system.<sup>2</sup>

First, the payments system is essential in order for all the transactions that take place within an economy to be carried out in an effective way. Second, the transfer of resources from individuals or organizations with savings to borrowers, in exchange for future repayment, has significant benefits to both parties. Good mechanisms for savings, including pension accounts, allow households to accumulate assets for future consumption—such as during retirement—and for bequests to children. Credit is crucial for investment by firms and for households to carry out large purchases, such as a house or an automobile. Moreover, it can be a great equalizer of opportunities, as entrepreneurs with good ideas but limited or no wealth can use capital or credit from third parties to try to develop their ideas. Third, insurance through financial institutions or markets allows all agents in an economy to reduce their financial exposure to different negative shocks. Fourth, developed financial markets convey an enormous amount of information about the expected evolution of crucial economic variables such as interest rates, exchange rates, the expected performance of companies, or the perceived creditworthiness of different counterparties. Fifth, by allowing for changes in ownership, structure, and control, financial markets increase the chances that companies are structured in

the best possible way and are controlled by the most capable hands.

Unfortunately, there is probably no other sector in the economy that is as subject to market failures as the financial system, and while some of these problems can be solved by private intermediaries, many of them require government intervention. The most important problems, which are pervasive across financial operations and the entire financial system, are moral hazard, adverse selection, and coordination problems.

Moral hazard arises in a credit relationship because a person who funds an investment project with credit might not put the same amount of effort in the project as he or she would if it were financed entirely out of his or her own resources. In the case of insurance, a person can behave more recklessly if he or she has insurance, knowing that the insurer will bear part of the costs of any mishap.

Adverse selection refers to the fact that individuals with more risky projects are more likely to ask for a loan or that people who are more reckless are also more likely to be asking for insurance. In these situations, private intermediaries traditionally solve the problems by asking for collateral in the case of credit, by requiring copayments in the case of insurance, and by obtaining information about the history of potential clients. While these are effective forms of reducing these problems, they have the undesirable effect of limiting access to financial services. For example, low-income individuals with worthwhile projects but limited collateral will have more restricted access to credit.<sup>3</sup>

Bank runs are one of the best-known instances of coordination problems in the

financial system. The problem arises because the assets of a bank, such as mortgage credit or project finance, are long term in nature and are repaid only gradually, while the liabilities are short term and in the extreme case can be withdrawn at any time as is the case with deposits in checking accounts. Given this mismatch in the maturity of assets and liabilities, it is possible that a sound bank fails due to a coordination problem. If everyone keeps their deposits in the bank or withdraws them at a regular pace, the bank would have no problem. But if everyone suddenly decides to withdraw their deposits simultaneously, the gradual amount of repayments on the mortgage or project credits would be insufficient and the bank would not be able to meet the demand for withdrawals. Bank runs were a relatively common phenomenon during the nineteenth century until the establishment of deposit insurance. By guaranteeing that most people would not lose their deposits irrespective of what happened with the bank, this reduced significantly any incentives for bank runs. Unfortunately, deposit insurance also has the unintended consequence of leading to moral hazard problems, as depositors who are guaranteed have no incentives to supervise if the bank is doing a good job, and therefore the bank can undertake more risky operations. This has also led to additional government intervention in the form of financial regulation to try to avoid this moral hazard problem.

Asset price bubbles and herding behavior are another important example of coordination failures. Obtaining and processing information can be costly and complicated, so some investors may just decide to see what other people are doing and follow them. This leads then to booms and busts in financial markets,

typically associated with new financial instruments or innovations. While a new product may legitimately represent an improvement and would justify greater investment, herding behavior by investors often leads to excessive investment, and when eventually the bubble bursts, the reduction in investment is also too large.

The substantial benefits from a more developed financial system together with the sizable costs that its inherent failures can impose on society imply that historically it has been necessary to find the right balance between potential benefits and costs. As with most complex problems of this nature, there are no preconceived solutions, but Mexico's history during the last twenty years contains important lessons on this issue.

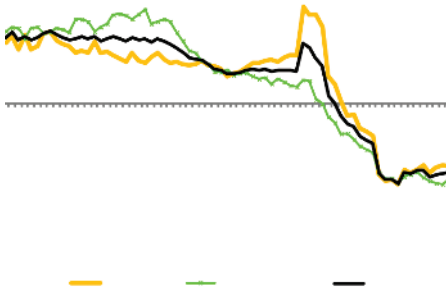
## A BRIEF AND RECENT HISTORY OF THE FINANCIAL SYSTEM IN MEXICO

### Privatization and Crisis

As tends to be the case with most financial crises, the Mexican banking crisis of 1994 to 1995 was preceded by an important "innovation" in the financial system: the privatization of commercial banks at the end of the 1980s and the beginning of the 1990s in the context of a very ambitious agenda to liberalize the entire economy. The privatization and liberalization of the financial sector led to extraordinary growth of credit in the country: real annual growth of credit to the private sector averaged 41.3 percent between 1989 and 1993 (see Figure 1), according to Secretaría de Hacienda y Crédito Público (SHCP), estimated with information from Banco de Mexico. Explosive growth was observed in credit to both firms and households with expansions of 36.3 percent and 47.8 percent, respectively. Credit to the private

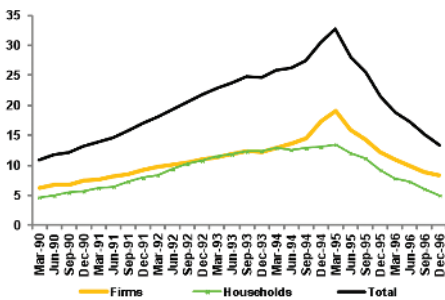
sector increased almost five times between 1988 and 1994, and as a percentage of gross domestic product (GDP), it expanded from 7.4 percent in 1988 to 30.5 percent in 1994 (see Figure 2).

**Figure 1 — Credit by commercial banks to the private sector (real annual growth rates).**



Source: Secretaría de Hacienda y Crédito Público (SHCP) estimated with information from Banco de Mexico

**Figure 2 — Credit by commercial banks to the private sector, percentage of GDP.**



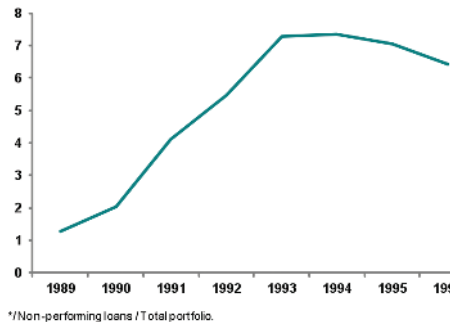
Source: Secretaría de Hacienda y Crédito Público (SHCP) estimated with information from Banco de Mexico.

While higher availability of credit during this period appeared as a positive trend in terms of all the benefits that a more developed financial system entails for an economy, an excessive expansion together with a regulatory framework that was not

strong enough resulted in a sharp deterioration in the quality of credit. This eventually led to the 1994 to 1995 financial crisis. Delinquency rates increased systematically, from 1.3 percent of total assets in 1989 to 7.3 percent in 1994, until they eventually led to doubts about the solvency of the banking system (see Figure 3),<sup>4</sup> according to the Comisión Nacional Bancaria y de Valores (CNBV).

In order to avoid a collapse of the financial system, a support program had to be adopted, as has been the case with

**Figure 3 — Delinquency rate of commercial banks, 1989–1996.**

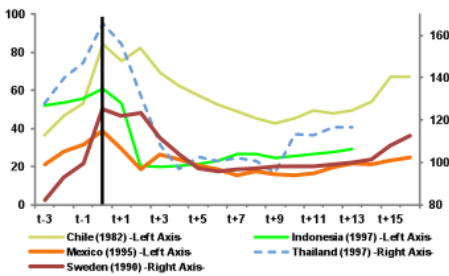


Source: Comisión Nacional Bancaria y de Valores (CNBV).

the recent financial crisis in many industrialized countries. This included resources for recapitalization and restructuring processes for most financial institutions. The program was successful in that it maintained a functional financial system and savings were protected. Nevertheless, the gradual process of balance sheet cleanup that took place after the crisis implied that credit started to recover with a significant lag, though this has been typical of banking crises in the international context including in Latin American, European,

and Asian countries, and will probably be the case as well in the current episode in industrialized countries. Although the precise timing varies by country, the typical pattern is that of an important decline in credit to GDP, which lasts for several years and is eventually followed by a gradual increase (see Figure 4).

**Figure 4 — Bank credit to the private sector in countries with financial crises, percentage of GDP.**



Source: World Development Indicators, World Bank.

## REFORMS AND RECENT DEVELOPMENTS

In response to the 1994 to 1995 crisis, Mexico embarked on a series of reforms oriented at providing the financial system with a prudent, solid, and modern regulatory framework that would allow for greater development going forward but would significantly reduce the possibility of future problems.<sup>5</sup>

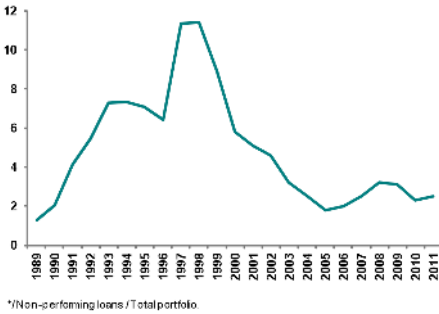
In terms of capital requirements, the Basel I accords were adopted in 1995, and the Basel II accords were adopted in 2008.<sup>6</sup> As a result of the timely implementation and enforcement of the accords and of the very solid stance of the system, Mexico is expected to adopt the new Basel III accords earlier than in most other countries. With regard to corporate governance, a reform in 2001 introduced best international practices, including the

requirement that 25 percent of a commercial bank's board members are independent. The legal framework of the financial sector has also been modified to improve the process of identification of banks with potential solvency problems, enhance the power of the authority to take preemptive measures, and guarantee that dissolution processes take place in an orderly fashion. More recently, the regulatory framework has been modified to incorporate lessons from the global financial crisis. In this context, the exposure that banks operating in Mexico may have with third parties, in the country or abroad, was limited through the introduction of a clause that establishes that operations with such parties that exceed 25 percent of the bank's basic capital will be deducted from the latter.

These reforms were very effective in strengthening the financial system, as evidenced by the fact that it did not experience any type of systemic problems or require any type of public support in spite of the sharp economic contraction and volatility in financial markets during the 2008 to 2009 global financial crisis, or the more recent volatility associated with problems in Europe. Although the delinquency rate did increase during these years, as typically occurs during recessionary periods of the economic cycle, the deterioration was similar to what is normally observed during mild recessions and was rapidly reversed. The delinquency rate reached a maximum level of 3.2 percent in 2008 and then decreased to 2.5 percent in 2011, compared with levels of 7.3 percent in 1994 and 11.4 percent in 1998 when the balance sheet cleanup process following the 1994 to 1995 crisis was still under way (see Figure 5), according to CNBV.



**Figure 5 — Delinquency rate of commercial banks, 1989–2011.**

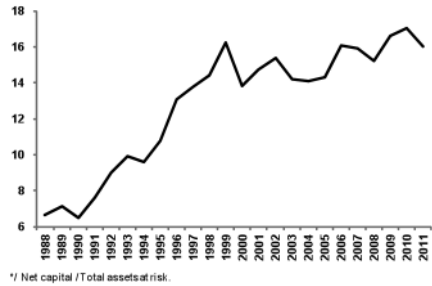


Source: Comisión Nacional Bancaria y de Valores (CNBV).

Capitalization levels for the system as a whole remained high in spite of the crisis. The average capitalization index for the entire system has remained between 15 percent and 17 percent in the 2008 to 2011 period, close to twice the international regulatory minimum level of 8 percent (see Figure 6), according to CNBV. Stress tests for the banking system are now carried out routinely, and they indicate that even under extreme scenarios the system would perform well in terms of capitalization, profitability, and liquidity.

Once the regulatory framework was strengthened and the process of mending bank balance sheets finished, a significant recovery in credit started in 2003. As a result of this, the reduction in the ratio of credit to GDP that resulted from the 1994 to 1995 crisis has been reverted gradually, with an increase of almost 6 percentage points of GDP between 2003 and 2011, in spite of the fact that the global financial crisis occurred during this period, according to SHCP, estimated with information from Banco de Mexico (see Figure 7). Given the current strong position of the system, it is likely that the

**Figure 6 — Capital adequacy ratio, percentage, commercial banks.**



Source: Comisión Nacional Bancaria y de Valores (CNBV).

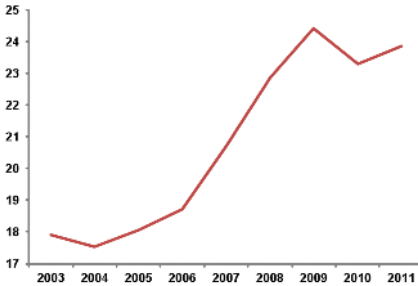
positive trend in credit to GDP will continue during the coming years.<sup>7</sup>

**CHALLENGES AND OPPORTUNITIES**

There has been substantial progress on strengthening the regulatory framework of the financial system in Mexico, establishing a base for a sustainable expansion of financial intermediation in the country. However, we still face some significant challenges, which also imply that there are large opportunities going forward. The main challenge is that in spite of significant recent progress, financial development measured as the level of financing relative to the size of the economy is still low in Mexico, as is shown by a comparison to other Latin American countries (see Figure 8).

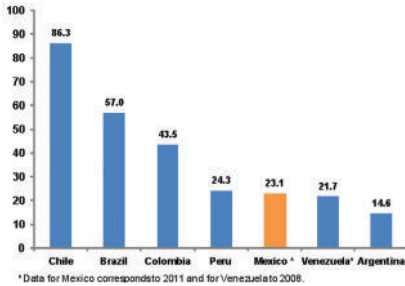
In response to this challenge, Mexico has launched a strategy to increase financial penetration and improve the operation of the financial system. The strategy has been based on seeking innovative alternatives to increase the presence of the financial system in the lives of households, but with special care to prevent vulnerabilities and imbalances from building up. In turn, this will maintain the stability and soundness of the system,

**Figure 7 — Domestic financing to the private sector, percentage of GDP.**



Source: Secretaría de Hacienda y Crédito Público (SHCP) estimated with information from Banco de Mexico.

**Figure 8 — Bank credit to the private sector, 2010, percentage of GDP.**



Source: World Development Indicators, World Bank.

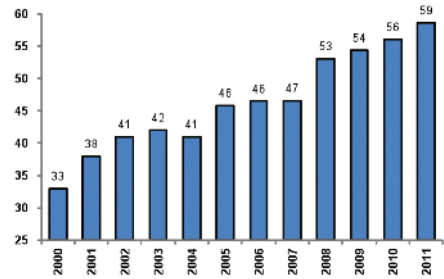
which has been gained through several years of efforts and reforms.

The key components of the strategy have been to promote the entrance of new financial intermediaries in order to foster more intense competition, to broaden the supply and access of financial services, and to complete the infrastructure of the banking system. In order to encourage more competition, the possibility of establishing niche banks, institutions that carry only some of the operations that commercial banks traditionally undertake

and that only have to comply with the regulation that is relevant for those specific operations, was incorporated into the legal framework. To improve the infrastructure of the system, the legal framework was modified to include mobile financial services. In the context of these actions, the supply of financial services for the population has increased significantly during the last decade: between 2000 and 2011 the number of bank branches increased by 63.3 percent, the number of points of sale more than quadrupled (with an increase of 432.7 percent), and the number of ATMs grew by 127.1 percent, according to CNBV. Efforts to increase the supply of financial services have been complemented with actions to improve financial education and consumer protection, including through measures to enhance the transparency of fees and commissions charged by financial intermediaries, through the establishment of rules for the disclosure of the costs of different financial services, and through legal modifications to strengthen the Agency for the Protection of Users of Financial Services. The Mexican government has also sought to improve access to financial services through development banks. In the last decade, direct and induced credit by development banks increased by 132 percent in real terms, expanding from 3 percent of GDP in 2000 to 4.9 percent in 2011, according to SHCP. Considering the past experience of the Mexican financial system, special attention has been devoted to guaranteeing that the large increase in financing by development banks does not create any type of vulnerability. As a result, development banks are currently in a very solid position: average capitalization was 15.3 percent at the end of 2011.

In addition to the previous measures, other reforms have also had large effects on the development of the financial system. In the last fifteen years, the two largest pension systems in the country—the one for private-sector workers and the one for federal government employees—were reformed, moving from pay-as-you-go to fully funded schemes, thereby increasing the supply of financial savings and widening access to financial services. This has contributed to a very significant expansion in financial savings, which have almost doubled from 33 percent of GDP in 2000 to 59 percent in 2011 (see Figure 9), according to SHCP and Banxico. To channel the greater supply of financial resources brought along by changes in pension regimes, new financial instruments have been created, such as Development Capital Certificates (CKDs) and Real Estate Investment Trusts (FIBRAs). These new instruments are designed to facilitate the allocation of savings to investment in productive sectors, like infrastructure (in the case of CKDs) and housing (in the case of FIBRAs). The federal government has also contributed to the development of domestic capital markets by establishing a domestic fixed-rate bond curve that goes out to thirty years and that is crucial for private-sector bond issuers to be able to place long-term bonds as well as develop new instruments for issuance, such as syndicated allocations that promote liquidity in secondary markets for bonds. Fifteen years ago, after the 1994 to 1995 crisis, it would have been unthinkable that Mexico would be able to issue thirty-year bonds at fixed rates in pesos at extremely competitive interest rates.

**Figure 9 — Domestic financial savings, percentage of GDP. Source: Secretaría de Hacienda y Crédito Público (SHCP) and Banxico.**



Source: Secretaría de Hacienda y Crédito Público (SHCP) and Banxico.

**FINAL REMARKS**

The Mexican financial system has experienced very profound changes during the last two decades, including a period of very rapid expansion that turned out to be unsustainable and eventually led to a crisis, a period of reforms and balance sheet mending following the crisis, and more recently, a period of expansion and development but with sustainable bases.

The main lesson that the Mexican experience offers is that it may be preferable to begin by taking measures to minimize the margin for market failures and the costs that they can impose on society first and, only once those measures are in place, then seek ways to fully exploit the benefits from the financial system, for otherwise these can turn out to be unsustainable and accompanied by larger costs in the long run. While very significant progress has been achieved, in terms of putting in place the set of rules and procedures that are necessary for a solid financial system, we need to continue with the development and innovation processes that have taken place in recent years in order to further increase the availability of financing.

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## ENDNOTES

- <sup>1</sup> For classical discussions on financial crises see Kindleberger (1978) and Minsky (1977).
- <sup>2</sup> For more detailed accounts about the potential benefits from the development of the financial system see International Monetary Fund (2001), Levine (1997), Rajan and Zingales (1998), and Rajan and Zingales (2003).
- <sup>3</sup> For detailed discussions of market failures in financial markets, the response by private intermediaries, and the regulation applied by the public sector see Dewatripont and Tirole (1994), Mishkin and Eakins (2011), and Tirole (1994).
- <sup>4</sup> For a more detailed description and analysis of the 1994 to 1995 crisis see Gil-Díaz and Carstens (1996a and 1996b), Gil-Díaz (1998), Goldstein and Turner (1996), and González-Anaya (2003).
- <sup>5</sup> Goldberg et al. (2000) and Murillo (2002) contain a description of the main reforms implemented during this period.
- <sup>6</sup> Capital requirements are an amount of net capital that banks are obliged to hold, which is expressed as a percentage of their risk-weighted assets (the ratio of the two forming the capitalization index, where the weights on assets are associated to their quality). They allow banks to absorb unexpected losses and also provide incentives for them to avoid excessive risk taking. The Basel accords specify the way in which they are estimated and their minimum regulatory levels.
- <sup>7</sup> For a more detailed description of the recent evolution of the Mexican financial system see Banco de México (2011).

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# Entrepreneurship, Ecosystem, and Competitiveness in Latin America

by Marco Kamiya

## ABSTRACT:

*Innovative policies for entrepreneurship are being promoted by countries in Latin America. The process is fueled by economic growth, the rise of a middle class, and the emergence of Latin American firms. Institutional capacity and the entrepreneurial cycle are key parts of an entrepreneurship framework that is nascent and incomplete in most of these countries. The challenges in building an entrepreneurship ecosystem are highlighted in this article.*

Entrepreneurial activities are on the rise in most countries of the Latin American region, spreading into different industries. Brazil is one of the leaders where angel funding, seed capital, and venture capital investors are supporting the birth and growth of myriad companies. In Mexico, business incubators like the Tech of Monterrey are promoting the creation of dynamic companies and linking local talent with international financing. In Chile, the Start-Up Chile program brings people with ideas and financing from overseas into the country to create a flow of knowledge that spurs a dynamic entrepreneurial economy.

The objective of this article is to discuss policy innovation and agendas for entrepreneurship including theory and measurement; to study the definition and relevance of the “ecosystem”; and to elaborate upon the institutional capacity, instruments, and programs needed to support national and local entrepreneurial initiatives.

## ENTREPRENEURSHIP: THEORY AND COMPETITIVENESS

Entrepreneurship has been long absent from economic theory, despite earlier efforts by Joseph Schumpeter who fathered the concepts of creative destruction and entrepreneurial spirit related to innovation and business cycles. The idea of entrepreneurship is difficult to grasp since it implies changes in the production function occurring external to the firm; thus, growth models or firm models cannot incorporate what is a transformation—sudden or incremental—of an industry or firm.

Robert Solow (1956) introduced the concept of technological progress into macroeconomic growth; Paul Romer (1986; 1990) integrated knowledge and human capital as determinants of growth and development; and William J. Baumol (2010) has taken

Table 1 — Government Programs, Competitiveness, and Entrepreneurship

	Government Programs*	World Economic Forum Competitiveness 2011–2012**	Early Stage Entrepreneurial Activity (TEA) Rate*
<b>Panama</b>	3.0	49	20.8
<b>Uruguay</b>	2.9	63	16.7
<b>Chile</b>	2.8	31	23.7
<b>Brazil</b>	2.4	53	14.9
<b>Colombia</b>	2.5	68	21.4
<b>Peru</b>	2.4	67	22.9
<b>Mexico</b>	2.4	58	9.6
<b>Argentina</b>	2.3	85	20.8
<b>Venezuela</b>	1.8	124	15.4

Source: Bosma et al. 2012\*; WEF 2012\*\*; GEINDEX, an alternative measurement of entrepreneurship combining GEM data with several development indicators is developed by Ács and Szerb (2009).

major steps toward embedding entrepreneurship into the model of the firm. No wonder innovation, knowledge, and human capital are associated with entrepreneurship, and those concepts are equally difficult to integrate into economic models.

Since entrepreneurship is a broad notion, quantification is also a problem. Measurement of entrepreneurship is done by the Global Entrepreneurship Monitor (GEM) and the World Bank Group Entrepreneurship Snapshots (WBGES). The GEM index is the most used and widely disseminated and includes the rate for early stage entrepreneurial activity (TEA), defined as the prevalence of entrepreneurship by firms led by individuals involved in start-ups and existing forty-two months after the firm’s birth. The GEM measure also calculates an efficiency index for government programs. The WBGES uses business registration of formal establishments as a proxy for entrepreneurship in 150 countries.

Table 1 shows the following entrepreneurship-related data for a selected group of Latin American countries: government

programs (public instruments for entrepreneurship, credit, technical assistance, etc.); the Global Competitiveness Index rankings from the World Economic Forum (WEF); and the TEA from GEM. Government programs and WEF rankings both follow an ordinal pattern and are highly correlated (for government programs, a higher number indicates better policies; whereas for WEF indicators, a lower number means more competitiveness). However, higher competitiveness does not necessarily reflect more entrepreneurship as measured by TEA rates (Ács et al. 2008).

Despite discussion about the definition of entrepreneurship and the data, several authors have produced original insights. With GEM and WEF data, Jose Amoros et al. (2011) show that the kind of entrepreneurship for self-employment or for high-value innovation matters for country competitiveness and industrial upgrading. Also using GEM data, Poh Kam Wong et al. (2005) find that entrepreneurship “by necessity,” that is, the self-employed in low-value activities, has no effect on competitiveness, but high entrepreneurship represented by firms

with rapid growth stimulates growth and competitiveness.

Though the link between growth, competitiveness, and entrepreneurship is not yet clear, there is compelling evidence that industrial upgrading is based on both knowledge and the presence of innovative firms. Historical experience also shows that innovative entrepreneurs are necessary to transition from a factor-driven economy to an innovation-driven stage. Policy makers know this, and countries across the region are implementing reforms to build better entrepreneurship-friendly environments.

### **ENTREPRENEURSHIP AND POLICY INNOVATION**

The revival of entrepreneurship in the region has been propelled by sustained economic growth, the expansion of the middle class, and the emergence of new cities. Major concern about social issues is also supporting entrepreneurship as a social policy tool. Therefore, innovative policies and programs promoting entrepreneurship are being designed by countries with public policies.

In the region, governments from different positions agree that entrepreneurship is important. In Panama, Costa Rica, and Chile, entrepreneurship is tied to innovation. In Argentina, Ecuador, and Bolivia, entrepreneurship is a component of “good” social policies. In Brazil, Peru, and Colombia, entrepreneurship is seen as a complement to open policies. In Central America and the Caribbean, entrepreneurship reforms are on their way as major regional initiatives. In the process, several countries are developing innovative public policies.

Brazil is a good example. The SEBRAE (Brazilian Service to Support Small Enterprises) program uses different

media to promote entrepreneurship, including radio broadcasts, soap operas, and social networks that spread the gospel of entrepreneurial values (SEBRAE 2012). Several public initiatives are available, such as Juro Zero (Zero Interest), which provides rapid financing to small and medium-sized enterprises (SMEs) without collateral and with minimum paperwork.

Chile created the Start-Up Chile initiative to attract early-stage, high-potential entrepreneurs to bootstrap their start-ups in Chile, using it as a platform to go global. The government provides funds via CORFO, the Corporation for Promotion of Production. Though results so far are mixed (Velasco 2012), the project, still in its early stages, brought in twenty-two start-ups from fourteen countries in 2010 (Start-Up Chile n.d.). This advanced concept follows the example of a similar program in Taiwan and is borrowing the name from StartUp America and StartUp Britain; though the program content is not the same, all revolve around entrepreneurship. Start-Up Chile aims to bring knowledge and experience to the country to generate capacity by combining ideas with financing.

Colombia is one of the leading countries in regulatory and institutional frameworks for entrepreneurship. The country has made consistent efforts to build public capacity with a regulatory framework supported by an entrepreneurship law and a specific division of entrepreneurship at the Ministry of Commerce, Industry, and Tourism, which leads the implementation of regional plans to encourage the entrepreneurial environment.

Ecuador also has entrepreneurship as a key policy for productive development as



well as for social policy. Different agencies and organizations at central and regional levels, led by the Ministry of Production, work to improve implementation of entrepreneurial agendas by organizing workshops and bringing overseas experts into the areas of financing, innovation, and incubators.

In other countries, a combination of policies and programs is being promoted by joint initiatives of the private and public sectors and academia. Peru, Mexico, Argentina, and Central American and Caribbean countries are good examples of early initiatives.

Still, when compared with international experiences, in Latin America, with the possible exception of Brazil, entrepreneurship is in a nascent stage, progressing but lacking some of the pieces required by an integrated system of innovation, entrepreneurs, and financing. International entrepreneurial hubs, such as Israel, the Silicon Valley, and Asian countries like Singapore, South Korea, or Malaysia, possess a comprehensive framework for entrepreneurship. This is what is called an ecosystem.

**ENTREPRENEURSHIP ECOSYSTEM**

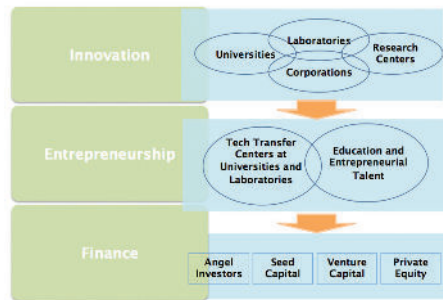
The concept of an ecosystem has its background in Michael E. Porter’s (1990) diamond framework, which explains the strength of a cluster or industrial sector as arising from an integration of different elements—all necessary. The term has been developed by Daniel Isenberg (2010) who defined the entrepreneurial ecosystem as a combination of several domains: culture, policies, and leadership; availability of finance; human capital; venture-friendly markets for products; products; institutional support; and infrastructural support.

What is the minimum set of components needed to form an ecosystem? Three

major components are essential: innovation, entrepreneurs, and financing (see Figure 1). Innovation is made up of universities, research centers, laboratories, and overseas links. Entrepreneurs are people who are trained in and knowledgeable about entrepreneurship and technology transfer centers at universities. Financing consists of financial support from public sectors and availability of capital for seed, venture, and private equity.

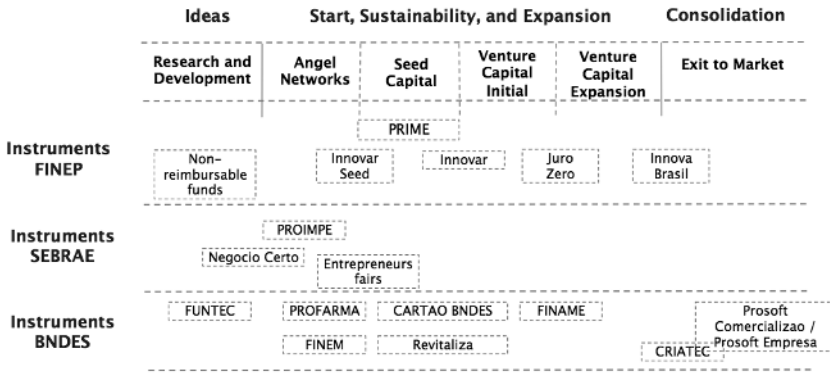
Without the presence of all three components together, an ecosystem is not possible. An ecosystem can exist, however, where innovation is poor, financing insufficient, or entrepreneurship talent scarce, but none of these components can be absent.

**Figure 1 — Basic components of an entrepreneurial ecosystem. Programs, Competitiveness, and Entrepreneurship**



In the case of Brazil, public institutions and the private sector provide instruments and programs offering support to different components of entrepreneurship. Also, for firm growth, Brazil has different institutions that provide a set of tools for enterprise development, ranging from angel investors, seed capital, and venture capital to private equity. The main organizations working in the public sector are FINEP, an agency supporting innovation and development both at the

Figure 1 —Brazil: Instruments and programs for entrepreneurship.



early and advanced stages; SEBRAE, an agency with both social and productive mandates supporting SMEs; and BNDES, a public development bank supporting financing during the different stages of a firm’s growth.

The triad composed by SEBRAE, FINEP, and BNDES provides instruments and programs for ideas, for starting, sustainability, and expansion, and for consolidation (see Figure 2). Public investment in institutional capacity for business development in Brazil is the largest in the region, reaching 0.09 percent of gross domestic product (GDP), more than double the amount than in the Dominican Republic, Chile, or Panama (Angelelli et al. 2006).

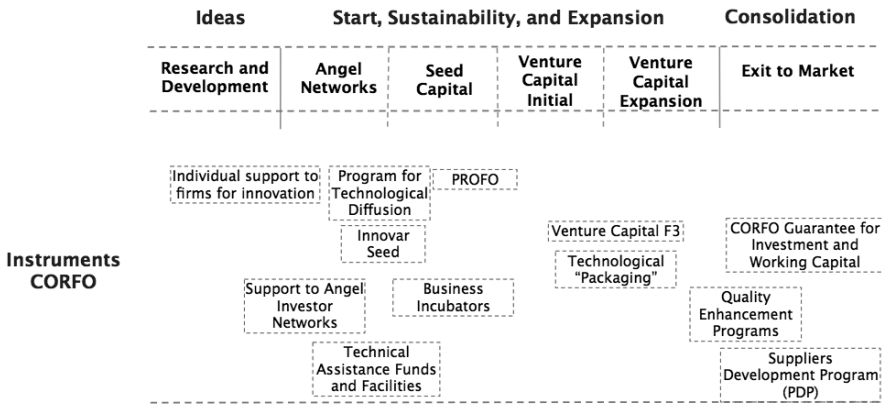
Some of the instruments in Brazil are Juro Zero, a zero interest program to support innovative SMEs in the area of technology upgrading; PROIMPE, which promotes the use of information and communications technologies in small enterprises; and FINAME, a BNDES project that provides credit to purchase machinery and equipment for companies in rural sectors.

In Chile, a similar institutional framework is offered by the public sector. For example, CORFO, founded in 1939, is the main agency delivering business services. CORFO is an umbrella organization with several institutions, such as INNOVA Chile, in charge of the Start-Up Chile program, and SERCOTEC, the agency supporting small enterprises, mostly with social objectives (see Figure 3). Finally, CORFO itself provides support to promote ideas and innovation as well as financing for each stage of the enterprise development.

As FINEP, SEBRAE, and BNDES do for Brazil, in Chile, CORFO offers instruments and programs during all stages of enterprise development from conception to market consolidation. Instruments range from support to business development to finance, and business performance and entrepreneurship in the region are linked to institutional support that exists for business development (Chrisney and Kamiya 2011).

In the region, countries like Panama and Uruguay possess strong institutional support for business development, while major rapid-growth countries like

Figure 3 – Chile: Instruments and programs for entrepreneurship.



Colombia and Peru are building programs for business support. Institutional support for business development is not necessarily a direct policy for entrepreneurship, but the existence of a framework means that an entrepreneurial ecosystem is present or relatively easy to build. Before discussing policy implications, we turn to the link between entrepreneurship and competitiveness.

**ENTREPRENEURSHIP: AGENDA BUILDING**

Entrepreneurship is a broad subject that is difficult to define as a policy objective. Theoretical efforts are beginning to integrate entrepreneurship into an economic model. Measurement is also improving; therefore, it will be increasingly possible to think of entrepreneurship as a direct lever for economic growth.

In the meantime, countries are expanding public business development services to promote entrepreneurship through a combination of financing, innovation, and education. Multilateral development banks and public agencies, therefore, cannot wait to have a complete theory of

entrepreneurship to offer support to public initiatives.

In this regard, the concept of ecosystem is useful, but it should be used as a tool to identify areas to improve. The basic components of an ecosystem—innovation, entrepreneurship, and finance—are necessary conditions in order to have an entrepreneurial environment. Countries should make an objective inventory of where they are in those areas and design agendas to improve them.

A successful ecosystem is made of strong institutions and efficient policies and programs, all of which depend on cultural background and history. For example, rather than copying the Singapore experience in small Caribbean countries, or importing Brazil’s FINEP or Chile’s CORFO to Andean nations, the best way to advance may be to look in the region and overseas, focusing not on the agencies but on instruments and programs.

The tasks are waiting. Policy makers should focus on exchanges and best practices of best instruments and policies as well as on strengthening institutions. Researchers must keep working on

theories that better integrate entrepreneurship and economic growth, while, in parallel, improving quantification and measurement. The private sector should encourage corporate entrepreneurship in large corporations and in funding initiatives in alliance with local and overseas universities. Multilateral banks must be facilitators of that process.

Finally, agents should understand clearly that entrepreneurship is not “everything.” Entrepreneurship creates value through the successful commercialization of an idea. The entrepreneurial economy is the one that has learned to both disrupt and systematically expand the production-possibility frontier.

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# Educational Reform: New Paradigms and Technologies

by Eugenio Severin

## ABSTRACT:

*The demand for better quality education has contributed to the development of multiple educational reforms in Latin America. Recently, information and communication technologies have taken an important role within the education policies of a number of countries, including important budget and management efforts. So far, evidence shows that technology itself is not able to solve the educational problems. A systemic effort of reform that modifies the present paradigms of educational service is needed. In order to achieve that, technology can and should play a central role. The experimental assessment of the “Una Laptop por Niño” (One Laptop per Child) program in Peru confirms the need for integral approaches that last.*

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## THE DEMAND FOR QUALITY

There is a general consensus regarding the need to improve results achieved by students in the educational systems of Latin America and the Caribbean. After multiple reforms and initiatives, the demand for quality and equity remains a pending issue in the region. The will for change has faced rigid educational systems, a fact that doesn't point toward a direction different from the historical one, where the interests of many stakeholders interact in order to favor the status quo.

However, the tension between the school supply and what societies actually demand has been growing. This has not only raised the concern of governments and productive sectors but also, increasingly, raised malaise among students and their families, who realize that the promise of an education that truly enables individuals to exercise citizenship and be included in the twenty-first century is hard to achieve.

This requires meaningful changes in what is taught, so that it is appropriate for the needs of this knowledge society, as well as in how things are taught, so that they take into account the educational context that twenty-first century society has created.

Information and communication technology (ICT) plays a fundamental role in the changes experienced by society, including how we communicate, produce, create, and share knowledge. Industries that took generations to create and consolidate have

changed substantially in just the past twenty years. These changes are due to both the speed at which knowledge is produced, its depth, and its impact on practical life, health, mobility, and communication as well as the ability for goods and services to be distributed more widely and less expensively.

Therefore, there is a growing agreement on the importance of including ICT in education (Kozma 2009). However, the generalized use of this terminology points to the challenge of including an external element (technology that supports information and communication) within the educational framework. ICTs are things that are “introduced” in school spaces, therefore demanding adoption, adaptation, and appropriation processes.

This article looks at educational systems from the perspective that such systems must be oriented at producing quality results. As such, educational systems should develop systemic reform actions that use technology<sup>1</sup> and make it relevant and appropriate. This article examines the need for educational technologies that are conceived, designed, developed, and distributed to support processes that aim to improve learning skills while remaining tied to educational objectives.

Ambitious programs introducing technology into schools have been implemented in Latin America since the mid 1990s, with many countries in the region having invested in computer science labs. At the beginning of the twenty-first century, a huge amount of resources was invested in training teachers on the basic use of technology, which favored access to digital educational resources through educational sites (Jara 2008; Alvariño and Severin 2009). During the last five years, with Uruguay

being the first in the region, many countries have embraced the idea of providing all students with a laptop as a step toward producing disruptive change within the educational system (Severin and Capota 2011).

But technology by itself does not produce substantive impacts on educational results.<sup>2</sup> The belief that only access to technology, whether to teachers or students, will produce substantial changes in learning practices and experiences has proven extremely optimistic.

In every educational initiative, the students should be the direct and final beneficiaries. Therefore, the expected results of all projects need to be related to student learning, and to learning in a broader sense, beyond scores achieved on standardized tests. Projects, including ICT educational projects, should relate to learning in one or more of the following ways:

- Improving students’ commitment to and involvement with the learning process
- Changing teaching practices as well as learning practices among students, teachers, schools, and communities
- Focusing on cognitive learning (curricular)
- Developing non-cognitive, or “twenty-first century,” skills, including the acquisition of skills involving the use of information and communication technologies

### IMPACT: PRESENT EVIDENCE

It is very common to declare that these kinds of initiatives are expected to have important social impact (closing the achievement gap or enabling social integration); economic impact (increasing productivity, competitiveness, or

employment); and educational impact (improving non-cognitive skills, learning, school environments, or internal efficiency). And yet, afterward, the results are only measured by math or language standardized tests. Or, given the difficulties of measuring and demonstrating educational results, the discussion only focuses on social impact.

Evidence on whether the use of technology improves the quality of education is mixed in both developed and developing countries.<sup>3</sup> Even in rigorous studies that randomly allocate treatment and control groups, the ambiguity of the effects of technology in the classroom prevails. Literature suggests that these mixed results may be due to: the initial level of knowledge among students regarding software; the attitude of teachers toward ICTs; whether ICTs are implemented inside or outside the classroom; the evaluation period; and the subject taught. It is hard to compare the results because the interventions are very different and have been implemented in different contexts. Moreover, it takes time to see an impact in the field of education.

Until now, evidence has shown that the effect of digital technologies on the learning process depends on how well the educational experience with the support of the technologies adjusts to the initial level of students' skills. Abhijit V. Banerjee et al. (2007) conducted a study based on a computer-assisted teaching program in India. In this program, children spent two hours per week using an educational package that emphasized basic math competences. The software adjusted to the student's level of knowledge, and the instructor encouraged every child to play games that challenged the student's level of comprehension. The results showed that school grades improved, and there

was a higher level of impact among lower-performing students.

Fang He et al. (2008) analyzed a teaching program where children were given a machine called "PicTalk." Using a pen, they were able to point to figures and then listen to the machine's pronunciation of the word. Unlike Banerjee et al. (2007), the results showed that the stronger students benefited more from this self-imposed learning process and that the weaker students benefited more from teachers. The authors emphasize that the software has an important role regarding the program's potential effect on students, noting that the software should consider the heterogeneity of students' skills in the classroom.

In the United States, Lisa Barrow et al. (2009) evaluated the use of a popular instructional computer program in randomly assigned classrooms in three urban school districts. The program provides a package centered on a specific topic for students to learn and includes a preliminary test, a review of required knowledge, a lesson, an accumulated review, and a final test. The students were able to advance at their own pace. The authors found that the computers offered a benefit to groups of students whose skills were more heterogeneous. The argument is that teachers could dedicate more time to each student and make an effort to find the correct pace when the class was supported by the computer lesson plans.

In this example, computers offered an efficient way of providing specific information to the user and therefore improved the students' learning results. Many other studies support this conclusion (Lepper and Gurtner 1989; Heath and Ravitz 2001).



Leigh Linden (2008) looked at a teaching program that was assisted by computers. When the computer software did not adjust to the students' knowledge level and was implemented in schools in India as a substitute for the teachers' lessons, school grades diminished. When the same program was implemented outside the school, a positive effect on the school grades was observed.

On the other hand, Barrow et al. (2009) argue that technology can have a more beneficial effect and be a substitute for teachers in certain contexts: for example, students benefit more from technology being used when the number of students per classroom rises, the variability of skills in the classroom increases, and there is a high level of absenteeism per classroom. In other words, technology has a positive effect when it is introduced as a complement and also as a substitute within contexts where the teaching coming from the teachers is limited.

However, precautions must be taken with regard to technology's role as a complement. If there is an absence of the appropriate software as well as parent and teacher supervision, having a computer may diminish the amount of time invested in studying at home. For example, Ofer Malamud and Cristian Pop-Eleches (2010) found that poor children in Romania who have a computer at home increase their digital abilities and cognitive skills but diminish their mathematics, English-, and Romanian-language grades. This finding has a lower effect in homes where parents supervise computer use.

### THE CASE OF PERU

The government of Peru has implemented a program called "Una Laptop por Niño" ("One Laptop per Child") with the objective of improving the quality of

education, giving priority to students' development and emphasizing training for teachers so that they make a better pedagogical use of technology in the rural zones. According to the Inter-American Development Bank, Peru was one of the pioneers in adopting the plan of the One Laptop per Child foundation and has considerably invested in this program. By 2011, there were 850,000 beneficiary children in 5,000 schools of low socioeconomic levels.

The program evaluation, developed by the Inter-American Development Bank with the support of the Ministry of Education of Peru, GRADE, and the Peruvian University Cayetano Heredia, took a sample of 319 rural schools eligible for participation (that is, they had electricity, were schools with more than one teacher, and had not received laptops until then) and randomly assigned computers to 209 schools out of the total available pool. The remaining schools made up the control group to use for a comparison of the results.

Among the main findings, the first is an increase in access to technology: 1.18 computers per student in the treatment group versus 0.12 in the control group. Also, 82 percent of students from the schools that received laptops reported having used a computer at school during the previous week in comparison to 26 percent of students from control schools. There are also important differences in the use at home, that is, 42 percent of students from treatment schools used a computer at home in the previous week versus only 4 percent of students from control schools. (The program gave laptops to the students under the assumption that they would use them at home.)

Most of the students from the treatment schools showed general abilities to use the laptop for simple tasks (e.g., document

processing) and to look for information available on the equipment. Access to the Internet was very limited because only 1.4 percent of schools had connectivity.

The study did not see evidence of a positive impact on learning skills in mathematics and language (in this case, Spanish). The average estimated effect for these tests was of 0.003 standard deviation and the associated standard error was 0.055.

The program did not affect the rate of school attendance, the time dedicated to homework, students' level of motivation, or teachers' and families' expectations related to the future opportunities for the students. No effects were found on reading outcomes, even though the equipment included 200 available digital book titles and only 26 percent of students from the control schools had more than five books at home.

Finally, it seems that the program did not affect the quality of instruction within the classroom. The complementary qualitative study that was part of the Inter-American Development Bank evaluation showed that the introduction of computers produced modest changes on pedagogical practices. This can be explained by the lack of software or educational contents directly linked with the areas of mathematics and language and by the lack of sufficient training for teachers.

Among the positive aspects, the study found an impact on the development of cognitive skills. At the three measured dimensions,<sup>4</sup> students from the treatment group surpassed those from the control group by 0.09 and 0.12 standard deviations, and these differences are statistically meaningful by 10 percent for the application of the progressive Raven's matrix test. Even so, the quantitative effects are interesting. A simple calcula-

tion suggests that the estimated impact of the verbal fluency test represents an expected step forward of six months for a child. All together, the results of the three cognitive abilities' tests show an impact of 0.11 average standard deviation on the measure that corresponds to the expected progress of five months ahead of students in the control group.

## CONCLUSIONS AND PERSPECTIVES

The experimental evaluation of the One Laptop per Child program in Peru represents an important effort to produce knowledge that guides the development of public policies for the use of technology in education.

It shows that the provision of equipment without adequate training for teachers and principals, sufficient educational resources, and connectivity or other technical and educational support mechanisms results in restricted effects, at least in the short term.

The use of technology in education still represents a tremendous effort related to resources and management skills for Latin American countries. Its implementation must be closely related to its potential to have a positive impact on learning to ensure the cost-effectiveness of the investments.

It is possible to state that the introduction of technology by itself does not produce the expected positive results on improving student learning. However, at the same time, the changes required to renew the pedagogical paradigms and update the educational practices to make them meaningful, both for students and society, require a serious, systemic, and sustained incorporation of educational technologies. Technologies by themselves do not create the educational reform, but the latter will not be possible without them.

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## ENDNOTES

- <sup>1</sup> The article particularly refers to digital technologies that appear as a result of the development and spread of computer science and network connectivity.
- <sup>2</sup> Some studies find a positive effect on the learning test: Banerjee et al. (2007); Barrow et al. (2009); and He et al. (2008). Others do not find such effect: Barrera-Osorio and Linden (2009); and some others even find a negative effect: Linden (2008).
- <sup>3</sup> An exercise to establish a "knowledge map" developed by the World Bank's infoDev (Trucano 2005) showed that despite the great investments that many countries have done in order to introduce ICT within the educational systems, there is limited and arguable data that support its role in improving education.
- <sup>4</sup> The three tests that were applied were: a Raven's test to measure abstract nonverbal thinking; a verbal fluency test to evaluate language functions; and a codification test to measure the individual's processing speed and work memory.

## Author Biographies

**Alberto Acosta** is a researcher at FLACSO Ecuador. As Minister of Energy and Mines in 2007, he was one of the government insiders who proposed to Ecuadorian President Rafael Correa an official framework for the Yasuní-ITT Initiative. He has studied economics, energy, economic geography, industrial economics, and business administration at the University of Cologne in Germany. This training opened the door to work as a consultant at the Latin American Institute for Social Research (IDLIS - FES) and to lead the project on Economic Situation Analysis IDLIS - FES. One of his main contributions at this stage was the study of foreign debt. His experience led him to chair undergraduate and graduate programs in universities in Quito, Guayaquil, and Cuenca, Ecuador, and at Universidad Complutense de Madrid, Spain. Acosta was the Minister of Energy and Mines from January to June 2007 and President of the Constituent Assembly from November 2007 to June 2008 during the administration of President Correa. Since November 2008, he has served as research professor at FLACSO Ecuador.

**Lilia Aguilar** was born and raised in Chihuahua, Mexico. She is studying for a Master in Public Administration at the John F. Kennedy School of Government at Harvard University, focusing on politics, government, and poverty. She has always been involved in social activism toward the creation of civility and defense of social rights for all. She has been part of youth movements in her native state and women's rights defense movements, and as a result, she has a strong belief on developing policies toward poverty alleviation and social justice based on the development of democratic institutions. She graduated from The Tec de Monterrey (Monterrey Technologic) in Mexico with a major in financial administration and holds a master's degree in public management from the same institution. She was the youngest state representative in Congress for her home state of Chihuahua in 2004. Afterward, she worked as a consultant in the Mexican Senate and Mexican House of Representatives. During the past several years, Aguilar has been part of the National Directive Board of the Labor Party (Partido del Trabajo) in Mexico, and before she came to the Harvard Kennedy School, she was a personal consultant for the governor of Chihuahua. Currently she is running for National Congress by the PR system for the 2012-2016 term in Mexico.

**Susana Baca** is the current president of the Commission of Culture at the Organization of American States (OAS). A singer-songwriter born in Peru, she has played a major role in Afro-Peruvian music research and revival. She has a degree in education and a PhD honoris causa from Universidad Enrique Guzmán y Valle, Lima, Peru. She was Peru's minister of culture from July to November 2011 under the administration of Peruvian President Ollanta Humala, becoming the second afro-Peruvian cabinet minister in the history of independent Peru.

**Felipe Calderón** is the current president of Mexico. In his early years with PAN, and at the invitation of Luis H. Álvarez, he founded and directed "Youth Action" in addition to being secretary of studies, secretary general, and PAN representative to the Federal Electoral Institute until 1995, when he became gubernatorial candidate for his native state, Michoacán. For the period from 1996 to 1999, he was elected president of the National Executive Committee. During his legislative career, he served as representative in the Mexico City Legislative Assembly and federal deputy in the fifty-fifth and fifty-eighth Parliamentary sessions. In 2003, he was director general of the National Bank of Public Works and Services and, subsequently, energy secretary. After graduating as a lawyer from the Escuela Libre de Derecho, President Calderón obtained an MA in economics from the Instituto Tecnológico Autónomo de México as well as an MA in public administration from the John F. Kennedy School of Government at Harvard University.

**Javier Calderón** currently works at the Centro de Investigaciones Económicas Nacionales, supporting the Presidential Commission for Police Reform, and at Francisco Marroquín University in Guatemala City as professor of institutional economics and Latin American economic development. He has a master's in political theory from New York University (2010) and a bachelor's in political science from Francisco Marroquín University (2006). He also worked for the Presidential Commission for Transparency and Against Corruption in Guatemala in 2005; for the Comité Coordinador de Asociaciones Agrícolas, Comerciales, Industriales y Financieras, in 2007; on the research of informal economy in Guatemala between 2006 and 2008; and on cocaine trafficking in Guatemala since 2011.

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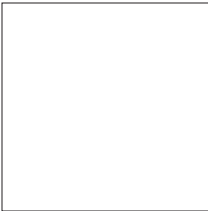
***Carlos Eduardo Huertas** is the Founder of CONNECTAS, an initiative that he is pursuing as a 2012 Nieman Fellow, with the generous support of the Knight Foundation. As a journalist in Colombia, Huertas has been with Semana Magazine for a decade and is now its Investigative Editor. In 2006, he founded the Consejo de Redacción (Newsroom Council), an organization that promotes investigative journalism. His investigative reports on corruption, human rights violations, and environmental issues have earned him several national and international awards. He was part of the team that won the King of Spain Award in 2008 and on the winning team of the Institute for Press and Society, Transparency International for Latin America award for the best investigative journalism in Latin America in 2007 and 2009. He is also a member of the International Consortium of Investigative Journalists.*

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**Luis Alberto Moreno** assumed the presidency of the Inter-American Development Bank (IDB) in 2005 and was reelected to a five-year term during a special meeting of the IDB Board of Governors in 2010. The IDB was established in 1959 as the main source of multilateral financing and expertise for sustainable economic, social, and institutional development in Latin America and the Caribbean. Besides loans, the IDB also provides grants and technical assistance and conducts research. The IDB's shareholders are forty-eight member countries, including twenty-six Latin American and Caribbean borrowing members, who have a majority ownership of the IDB. As president of IDB, Moreno also serves as chairman of the board of executive directors of the Inter-American Investment Corporation and chairman of the Donors' Committee of the Multilateral Investment Fund (MIF). Prior to joining the IDB, Moreno served as Colombia's ambassador to the United States for seven years. Before that, Moreno served a distinguished career in both the public and private sectors in Colombia. Moreno obtained bachelor's degrees in business administration and economics from Florida Atlantic University in 1975 and an MBA from the American Graduate School of International Management at Thunderbird University in 1977. For his distinguished work in the field of journalism, he was awarded a Nieman Fellowship by Harvard University to undertake studies at the university from September 1990 to June 1991.



**Frank Pearl** is an economist, academic, and Colombian politician. Prior to becoming Colombia's first Minister of Environment and Sustainable Development in 2011, he was presidential advisor for Social and Economic Reintegration of Individuals and Armed Groups, an office created by the administration of President Alvaro Uribe in 2006. In 2002, he was cofounder and president of the civil movement NO MAS! advocating for peace in Colombian society. With a vast academic and corporate experience in Latin America and Eastern Europe, Pearl holds an economics degree from Universidad de Los Andes and an MBA from Richard Ivey School of Business in Canada.



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**Eugenio Severin** is currently a Senior Specialist in Education at the Inter-American Development Bank (IADB). Previously, he served as manager of education technology in Fundacion Chile (2004-2008) and as chief of staff of the Ministry of Education in Chile (2000-2004). He specializes in the use of information technology and communication in education and participates directly in the design and monitoring of the projects the IADB supports in the region. Severin has a degree in literature from the Catholic University of Chile, a master in management from Loyola College in Maryland, and a degree in education public policy from the University of Chile.

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