## LATIN AMERICA

# A vain search for inflation cures

The short-term outlook for Latin America is bleak. There seems to be no end in sight for the region's hyperinflation, as price increases are expected to continue to average 75%. That figure is heavily weighted by triple-digit inflation in Brazil and Argentina. But all the major countries are suffering from high double-digit inflation (chart).

Hyperinflation has trapped government policymakers in an intractable bind. Most are attempting to combat inflation by pursuing tight monetary and fiscal policies and maintaining strong currencies. Restrictive macro policies are doing little so far to slow inflation, but they are damping economic growth, which is expected to average 2.5% and 4% in the next two years, well below the historical average. Foreign exchange policies and low commodity prices are causing the balance of payments in most countries to remain in the red. This is forcing Latin American countries to borrow heavily, adding to the region's other major problem—soaring foreign debt.

Argentina is pursuing a somewhat different and seemingly inconsistent set of policies. The new government is trying to curb its inflation with high interest rates and restrictive fiscal policy. At the same time it is changing its trade policy. Outgoing Economic Minister Martínez de Hoz tried to control inflation by keeping the peso overvalued to lower the cost of imports. But this hurt local industries, causing high unemployment and a slowdown in production.

In contrast, the incoming administration is trying to stimulate exports by periodically devaluing the peso. This will accelerate inflation but is unlikely to increase overall growth. Domestic activity has been chilled by a number of large bankruptcies and by lack of confidence in the government policies. As a result, growth will remain sluggish and inflation should soar.

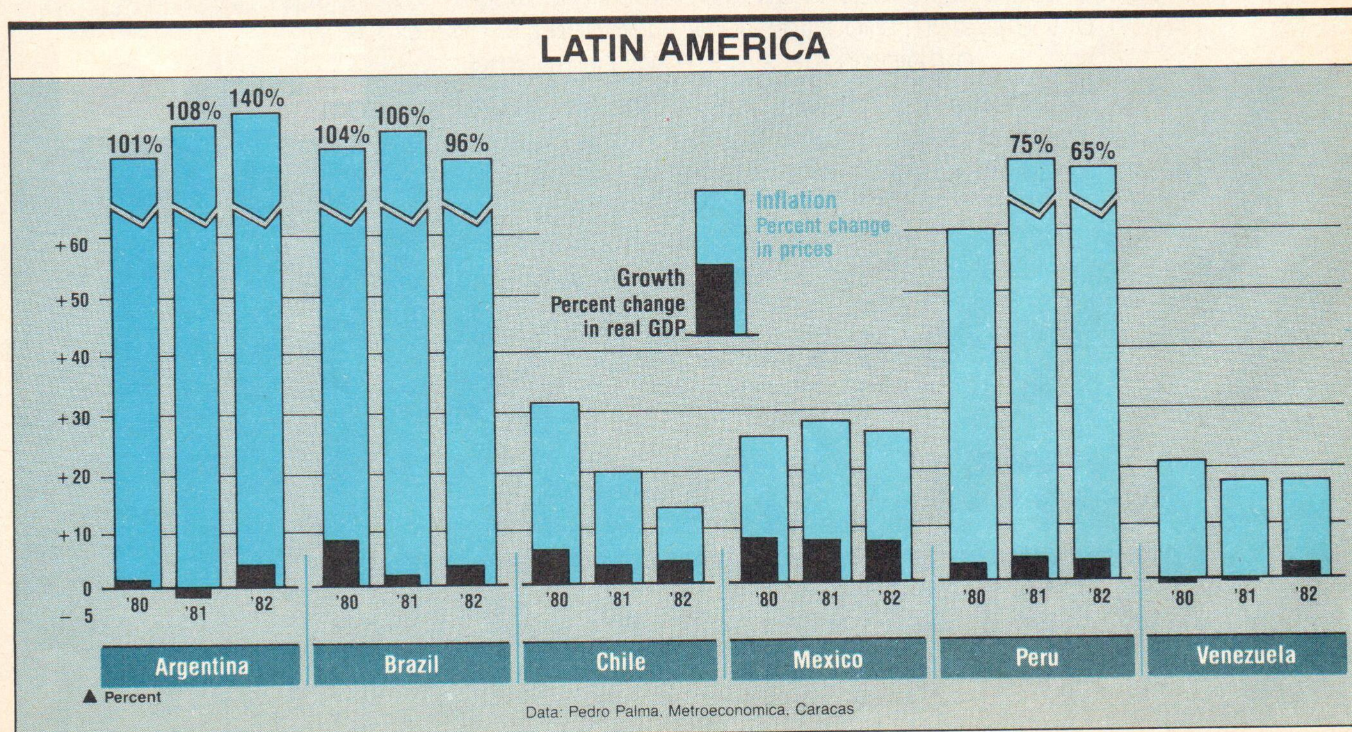
**Current accounts.** In Chile, the government is maintaining an overvalued peso to reduce the inflation rate while following a moderately restrictive monetary and fiscal policy. Inflation is expected to slow to 20% this year from 31% in 1980, and to decelerate to 14% in 1982. But the foreign exchange policy is boosting the current-account deficit to nearly $4 billion and threatens to increase foreign debt to $15 billion by the end of 1982. At this level, debt service would absorb about 40% of Chile's total export earnings, making its external position more precarious.

In Peru, too, the current-account deficit is growing, largely due to a drop in the prices of its major exports—copper, silver, and coffee—and an overvalued currency. At the same time, tight fiscal and monetary policies are reducing growth but barely denting inflation. Indeed, higher interest rates, lower subsidies, and higher production costs are pushing inflation to 75% to 80% this year. A 65% rate in 1982 is the best that can be hoped for.

Brazil is trying to cope with its triple-digit inflation rate through a restrictive monetary policy. At the same time, to curb high-cost imports, especially oil, the government is periodically devaluing the cruzeiro. While these policies will have little effect on inflation until 1982, they may help correct Brazil's large external imbalance. High interest rates will bring in foreign capital and help offset the still-mounting current-account deficit that could exceed $13 billion in 1981 and 1982. These steps, however, will stunt GDP growth.

**Slow growth.** Even Mexico, whose oil revenues have enabled the government to pursue an expansionary fiscal policy, is facing tougher times. Production bottlenecks, especially a shortage of skilled labor, combined with the indexation of some costs, is worsening inflation and curbing growth. If the government slows down its public expenditures, the reduction in GDP growth will be even more severe. Even so, Mexico's current-account deficit is going to increase. The leveling off of oil exports while imports are increasing will push the deficit from $6.6 billion in 1980 to $10.5 billion in 1982.

Venezuela's economy has been stagnant in recent years and will probably



remain so. The government is hoping that the recent decontrol of interest rates will stem the outflow of capital that has hurt domestic investment. Ironically, higher domestic interest rates could enable the government to ease other credit restrictions and spur investment.

Continued slow growth will gradually lower Venezuela's inflation rate, however. At 18% this year, inflation is high by the nation's historical standards. Also on the bright side, large oil exports and only moderate increases in imports will help maintain the nation's healthy current-account surplus.

Latin America's smaller countries, such as Ecuador, Bolivia, Paraguay, and Uruguay, all face deteriorating trade balances, in several cases because of lower export prices. Lower coffee prices will particularly hurt Colombia.

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## FAR EAST AND SOUTHEAST ASIA

# Restructuring to cope with high costs

The Far East and Southeast Asian nations have made a concerted—and mostly successful—effort to restructure their economies to absorb the double shock of higher energy prices and more expensive external financing. There has been a widespread encouragement of more energy-efficient production, greater investment in advanced technology, and less reliance on labor-intensive products. These efforts to offset rising labor and energy costs are one reason real growth in the Pacific Basin is expected to average 7% and 7.6% in 1981 and 1982, compared with 5.6% last year. And this improvement will occur even though most countries have tightened monetary and fiscal policies to rein in inflation.

Performance is also improving because more attention is being paid to regional cooperation. Several joint projects are under way, and preferential tariff deals are being adopted. Exchange-rate adjustments to boost exports have also been more frequent.

**HONG KONG.** Despite sluggish exports and high interest rates, Hong Kong's brisk growth continues. The increase in real gross domestic product is likely to be about 8% again this year, although much of this strength comes from domestic demand stimulated by higher government spending, lower personal and business taxes, and an overheated real estate market. However, rapidly growing demand at home has created a widening trade deficit, and this has caused the Hong Kong dollar to fall against the U. S. dollar.

**SOUTH KOREA.** Real GDP growth is expected to reach 5.5% this year and 6.1% in 1982. Greater political stability after last year's upheavals, improvements in agriculture, and strong export growth—particularly to the U. S.—have contributed to the upturn. Primarily because of high interest rates, however, and the size of Korea's external debt, the current account deficit will probably remain large. Because of this deficit, Korean authorities are likely to continue letting the won devalue rapidly.

Even though the Korean won is depreciating, inflationary pressures are apparently abating in the wake of slower advances in import prices and wage rates as well as sluggish domestic demand.

**TAIWAN.** After a decade of double-digit advances, GDP growth slipped to 6.8% in 1980 and is expected to sag to 6.4% this year. Taiwan is also facing record inflation rates, the highest since the quadrupling of oil prices in 1973-74. The latest escalations are largely the result of rising oil prices, big wage increases, and a productivity slowdown.

Growth has been slower this year because of weak exports and the tight monetary policies instituted at yearend 1980 to fight inflation, which is expected to slow to about 15.3%. The country achieved a small trade surplus in the first half, and authorities devalued the currency 5% against the U. S. dollar in August to increase exports. But the current account deficit will, nonetheless, be about $1.1 billion for 1981.

**SINGAPORE.** Although the recent slowdown in foreign investment and the slump in the industrialized world are