

**College of Social Studies**  
*Junior Economics Tutorial*  
*Elements of Latin American Economic Development*

Spring 2003

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Week VI: The Washington Consensus; Surges of capital flows into Latin America

Readings

Calvo, Guillermo A., Leonardo Leiderman, and Carmen M. Reinhart (1996), "Inflows of capital to developing countries in the 1990s," *Journal of Economic Perspectives* 10, No. 2, pp. 123-39

Corden, W. Max (1994), *Economic policy, exchange rates, and the international system*, Ch. 4  
Lissakers, Karin (1993), *Banks, borrowers, and the establishment: A revisionist account of the international debt crisis*, New York:: HarperCollins, Ch. 3

Williamson, John (1990), "What Washington means by policy reform," in John Williamson (ed.), *Latin American adjustment: How much has happened?* Washington, D.C.: Institute for International Economics

Discussion

The ISI strategy of development received a fatal blow with the debt crisis of 1982. During the rest of the decade of the 1980s Latin American countries struggled to adjust their economies so they could keep paying interest on their foreign debts. In that context the international financial institutions acquired a lot of leverage in influencing the economic strategies of the countries in the region. This is because the indebted countries were required to establish an agreement with the IMF before they could reschedule private loans or seek further financing from the World Bank or other international financial institutions.

The Washington Consensus summarizes the reform program that Latin American countries were encouraged to follow. It was expected that such strategy would allow these countries to recover from the debt crisis and resume their growth. As you read about this economic strategy you will find some resemblances with Little, Scitovsky, and Scott's criticism of ISI. In fact, that book can be considered a pioneer in the forging of the new policy consensus for the region.

The debt crisis of 1982 would not have reached the magnitude it reached had it not been for the high level of indebtedness of Latin American countries to private international banks. Why Latin Americans borrowed so much? Why banks lent so much? You will find some hints in Lissakers' article. Besides creating a potential for a crisis if foreign capital suddenly withdraws a country, as it happen in Latin America in 1982, capital inflows can also make the macroeconomic management of the recipient country very difficult. Read Calvo et al. for an overview of the Latin American experience with capital inflows in the 1990s. Corden provides a theoretical framework to interpret the connection between current account deficits and public or private excesses of investment over saving.

## Assignment

You will write a 4-5 pages paper on this week readings. One possible theme would be to describe the Washington consensus, explain how it ends ISI, and relate it with previous critical views of ISI such as that of Little et al. Other possible theme is to compare and contrast the capital surges of the 1970s and 1990s. Even another, more analytical theme, is to explain the macroeconomic effects of capital surges: why is too much of a good thing not so good? This tutorial will pave the ground for the following, which will be based on a comparison of the experiences of a pair of Latin American countries during the late 1980s and 1990s.

In addition to the paper, you will prepare a one-page data report on a country of your choice. You will use IMF Financial statistics and World Bank Development Indicators (available on-line) to get the data. You will focus on GDP growth, inflation, the exchange rate, and the balance of payments. In the tutorial we'll discuss the data you found.