

## EMnet Latin America Meeting Background Note

### “Navigating Uncertainty: Strategies for Innovation and Growth”

9 June 2017 – French Ministry of Economy and Finance – Paris, France

#### Session 1: Strategies for growth amid uncertainty and risk of protectionism

*Latin America is expected to return to positive growth in 2017 after two consecutive years of recession. Yet the region is facing increased social vulnerability, productivity stagnation and growing global protectionism. To counterbalance uncertainty, commitment to innovation and skills development will be crucial.*

Latin America is expected to grow 1-1.5% in 2017, after two years of negative growth. Yet, economic performance varies widely between countries in the region. Better integration into global value chains and stronger trade ties with the United States has boosted growth in places like Mexico and Central America. In contrast, Argentina and Brazil exhibited negative growth rates in 2016, but are expected to recover in 2017. Conversely, in Venezuela the collapse of oil prices, a high fiscal deficit and restricted access to external financing has driven the country into a sharp recession.<sup>1</sup>

In addition to this modest economic recovery, Latin America still faces structural challenges and remains vulnerable to external shocks. Socio-economic progress in the region has been remarkable in the past two decades; poverty rates between 1990 and 2014 decreased from 48.6% to 28.2% but the region remains the most unequal region in the world. High informality rates increase the population’s vulnerability to loss of income or unemployment. Labour productivity relative to more advanced economies has been in decline over the past decade as well. And the region is highly vulnerable to changes in US policies. Uncertainties around the new US administration and its policy decisions are being watched by Latin American governments closely. New trade barriers could gravely affect countries that are dependent on exports to the United States.<sup>2</sup>

These challenges and risks demand a strong response from the private and the public sector to boost productivity. Investing in skills and greater innovation could stimulate long-term growth. However, the region is lagging behind in providing the workforce with adequate skills for the labour market.<sup>3</sup> The private sector could remedy this skills shortage by developing innovation and training centres, following the examples of companies like BBVA, Airbus and Huawei Technologies.<sup>4</sup>

#### QUESTIONS FOR DISCUSSION

- Is doing business in Latin America still attractive in the light of structural constraints and economic uncertainties?
- What impact does economic and business uncertainty have on trade and private investment?
- How can Latin America’s businesses adapt to rising global uncertainty?

<sup>1</sup> OECD/ECLAC/CAF (2016), *Latin American Economic Outlook 2017: Youth, Skills and Entrepreneurship*, [www.oecd.org/publications/latin-american-economic-outlook-201725140.htm](http://www.oecd.org/publications/latin-american-economic-outlook-201725140.htm).

<sup>2</sup> Ibid.

<sup>3</sup> Ibid.

<sup>4</sup> <http://www.airbus.com/support-services/services/training/training-centers-network/airbus-training-mexico/>;  
<https://www.bbva.com/es/programas-becas-estudiar-latinoamerica/>;  
<http://www.bnamericas.com/en/news/technology/huawei-opens-brazil-innovation-center>

## Session 2: Unlocking investment in innovation in Latin America

*Labour productivity in Latin America has declined in the past decade in comparison to more advanced economies. Innovation can play a key role in the region to support productivity improvements. What role can the private sector play in bringing investment in innovation up to speed?*

Labour productivity in Latin American countries has decreased over the last ten years compared to the United States and other high-growth countries in Asia, such as China and South Korea.<sup>5</sup> To boost long-term growth the region must increase knowledge-intensive production and innovation. More investment in innovation is needed to stimulate the development of new technologies or advancements in processes or methods. Brazil is the only country in the region that invests more than 1% of GDP<sup>6</sup> on Research and Development (R&D), half coming from the private sector. Meanwhile, other Latin American economies invest much less in innovation. For example, Chile, Colombia and Peru all spend less than 0.5% of GDP on R&D.<sup>7</sup> Patent registrations in the region remain very low compared to OECD countries also. Since 2010 in Latin America, the annual average patent registration per million inhabitants has been 0.9, far below the 132 patents per year per million inhabitants in OECD countries.<sup>8</sup> Furthermore, private investment in innovation is particularly low in the region compared to public expenditure. In 2010, R&D expenditure was mainly concentrated in large firms, and only represented 0.4% of sales compared to 1.61% in European companies and 1.89% in OECD countries.<sup>9</sup>

To increase innovation, countries in the region need more private-sector investment in knowledge-intensive sectors. Some firms have already started investing in cutting-edge technologies. For example, in Brazil Iberdrola has increased its R&D activities in smart grid projects, promoting a more sustainable and clean consumption of energy.<sup>10</sup> Governments have a role to play to create the enabling conditions for private investment in innovation. In addition to financial incentives and regulatory requirements, improvement in competition policy and education can support progress. Market competition pushes firms to innovate as competitive pressures or entry threats make innovation necessary to survive. Adopting new technologies or processes will require a more skilled workforce. Public policies that align tertiary education and vocational training programmes with needed skills are thus an essential component to encourage innovation.

### QUESTIONS FOR DISCUSSION

- How is innovation changing business models and improving productivity in Latin America?
- Where are the islands of excellence in the region at the forefront of private innovation?
- How can governments go further to help unlock more private investment to support innovation?

<sup>5</sup> OECD/ECLAC/CAF (2016), *Latin American Economic Outlook 2017: Youth, Skills and Entrepreneurship*, [www.oecd.org/publications/latin-american-economic-outlook-20725140.htm](http://www.oecd.org/publications/latin-american-economic-outlook-20725140.htm).

<sup>6</sup> OECD/IDB (2016), *Boosting Productivity and Inclusive Growth 2016*, [www.oecd.org/latin-america/Boosting\\_Productivity\\_Inclusive\\_Growth.pdf](http://www.oecd.org/latin-america/Boosting_Productivity_Inclusive_Growth.pdf).

<sup>7</sup> United Nations Educational, Scientific and Cultural Organization (UNESCO) (2014), *Gross Domestic Expenditure on R&D (GERD) database*, <http://data.uis.unesco.org/Index.aspx?queryid=74> (accessed 29 May 2016).

<sup>8</sup> OECD (2016), *Promoting Productivity for Inclusive Growth in Latin America*, [www.oecd.org/economy/promoting-productivity-for-inclusive-growth-in-latin-america.pdf](http://www.oecd.org/economy/promoting-productivity-for-inclusive-growth-in-latin-america.pdf).

<sup>9</sup> IDB (2016), *The New Imperative of Innovation: Policy Perspectives for Latin-America and the Caribbean*, [publications.iadb.org/handle/11319/7417](http://publications.iadb.org/handle/11319/7417).

<sup>10</sup> Iberdrola (2017), "We promote smart grid development", [www.iberdrola.com/sustainability/innovation/our-businesses/networks](http://www.iberdrola.com/sustainability/innovation/our-businesses/networks).

### Session 3: The future of work

*Innovation is changing the labour market, shifting the demand for skills towards new activities. This could aggravate regional skills mismatches.*

Companies require a workforce with the necessary skills to integrate innovative technologies and processes. A workforce equipped with the right skills is thus vital to boost innovation.

In an increasingly digitalised world, new technologies are changing the labour market. Mastering ICT (information and communication technologies) skills is a requirement for employment in most sectors now. Yet, 43% of adults in 28 OECD countries surveyed had little or no ICT skills, according to the 2015 OECD Survey of Adult Skills (PIAAC). The situation is suboptimal in Chile, for example, where 78% of adults surveyed had limited or no ICT skills.<sup>11</sup> These skills are also becoming as important as other “soft” skills such as leadership, communication and team-work when looking for a job.

Meanwhile, employment restructuring is occurring in Latin America due to sectoral shifts: by 2030, 3.4 million jobs could be lost to automation in the construction and the manufacturing sectors while numerous jobs requiring human skills will be created in retail and services, transport and logistics, information and communication as well as new digital industries.<sup>12</sup> This will modify the core skills demanded by employers. Developing ICT knowledge together with solid literacy, numeracy, systems thinking and problem-solving skills are crucial to ensure that young generations in the region can benefit from new opportunities but also to keep the current workforce in the labour market.

Training programmes to keep skills up-to-date can help to ensure that employers have a productive and innovative workforce. Anticipating this, Governments need to develop education and skills policies to ensure the workforce can adapt to the changing labour market. Firms also play a role in reskilling or upskilling workers through on the job training and knowledge transfers. Schneider Electric, for example partnered with the French Ministry for National Education, Higher Education and Research and the Escuela Tecnológica Instituto Técnico Central (ETITC) in Colombia to establish a training centre to enhance skills in Colombia’s energy sector.<sup>13</sup> Fostering similar dialogue and partnerships between the private sector, government and educational institutions can help better understand the skills needed in the labour market.<sup>14</sup>

#### QUESTIONS FOR DISCUSSION

- Which are the new essential skills and competencies demanded by the private sector in the region?
- Are there region-specific skills that need to be developed to keep up with innovation?
- What are successful examples of the public and private sector working together to reduce the skills mismatch for innovation?

<sup>11</sup> OECD (2016), *Policy Brief on the Future of Work: Skills for a Digital World*, [www.oecd.org/els/emp/Skills-for-a-Digital-World.pdf](http://www.oecd.org/els/emp/Skills-for-a-Digital-World.pdf).

<sup>12</sup> OECD/ECLAC/CAF (2016), *Latin American Economic Outlook 2017: Youth, Skills and Entrepreneurship*, [www.oecd.org/publications/latin-american-economic-outlook-201725140.htm](http://www.oecd.org/publications/latin-american-economic-outlook-201725140.htm).

<sup>13</sup> Schneider Electric (2015), “Schneider Electric creates a new centre of excellence in Colombia to further support its actions towards vocational training”, Press Release, 27 January 2015, Schneider Electric website, [http://www2.schneider-electric.com/corporate/en/press/press-releases/viewer-press-releases.page?c\\_filepath=/templatedata/Content/Press\\_Release/data/en/shared/2015/01/20150127\\_schneider\\_electric\\_creates\\_a\\_new\\_centre\\_of\\_excellence\\_in\\_colombia\\_to\\_f.xml](http://www2.schneider-electric.com/corporate/en/press/press-releases/viewer-press-releases.page?c_filepath=/templatedata/Content/Press_Release/data/en/shared/2015/01/20150127_schneider_electric_creates_a_new_centre_of_excellence_in_colombia_to_f.xml).

<sup>14</sup> OECD/ECLAC/CAF (2016), *Latin American Economic Outlook 2017: Youth, Skills and Entrepreneurship*, [www.oecd.org/publications/latin-american-economic-outlook-201725140.htm](http://www.oecd.org/publications/latin-american-economic-outlook-201725140.htm).

## Session 4: Infrastructure for innovation

*Innovation needs a vast network of infrastructure in place. How is infrastructure developing across Latin America? What type of infrastructure to support innovation could be improved throughout the region?*

Mega trends such as the ageing population, climate change and urbanisation are reshaping societies and subsequent infrastructure needs.<sup>15</sup> New technologies are emerging to address these challenges. Cities are gaining efficiency through innovations such as smart grids and traffic optimisation. Utilities and transport networks have become more performant as they are increasingly interconnected through advanced technologies.<sup>16</sup>

Latin America needs better infrastructure to support technological advances. Internet access, for example, remains one of the main challenges to the expansion of digital services. The share of the population connected to the Internet more than doubled in Latin America from 21% in 2006 to 47% in 2013, while remaining low compared to the OECD average of 79%.<sup>17</sup> Nonetheless, an estimated 300 million people still do not have access to the internet in Latin America and the Caribbean countries.

Policies targeting the expansion of broadband services and the improvements of networks should be a priority to enable the expansion of digital services and new technologies. They should be matched with efforts to increase literacy and digital skills, which companies will require of their workforce. Broadband services should also be accessible and affordable which requires investment in networks and in the supply of broadband services as well as a regulatory framework that supports competition. In many countries of the region, market shares are highly concentrated.<sup>18</sup> Stimulating broadband competition and network expansion could increase affordable access to services in areas where high-speed networks are not developed. More competition could benefit urban areas especially where there is room for several operators to compete on services and prices.<sup>19</sup>

### QUESTIONS FOR DISCUSSION

- Are there sufficient investments in digital infrastructures in the region?
- What are the challenges for infrastructure development in Latin America and how can they be overcome?

<sup>15</sup> OECD (2016), *Science, Technology and Innovation Outlook 2016*, [www.oecd.org/sti/oecd-science-technology-and-innovation-outlook-25186167.htm](http://www.oecd.org/sti/oecd-science-technology-and-innovation-outlook-25186167.htm).

<sup>16</sup> Ibid.

<sup>17</sup> Katz, R. (2015), "El ecosistema y la economía digital en América Latina, Editorial Ariel, Fundación Telefónica, Editorial Planeta, Madrid and Barcelona, <http://scioteca.caf.com/handle/123456789/768>.

<sup>18</sup> OECD/IDB (2016), *Broadband Policies for Latin-America and the Caribbean: a Digital Economy Toolkit*, [www.oecd.org/publications/broadband-policies-for-latin-america-and-the-caribbean-9789264251823-en.htm](http://www.oecd.org/publications/broadband-policies-for-latin-america-and-the-caribbean-9789264251823-en.htm).

<sup>19</sup> Ibid.

## Session 5: A new chapter for trade?

*With rising protectionism, NAFTA and the TPP in question, what will trade uncertainty mean for doing business in Latin America?*

Global trade growth in 2016 was low (2%) and is expected to stay below pre-crisis levels.<sup>20</sup> In Latin America and the Caribbean, exports returned to a positive growth rate after four years of contraction. The value of exported goods was 17% higher in the first quarter of this year compared to that of the same period last year.<sup>21</sup> Yet uncertainty about trade agreements might challenge this trade growth in the region.<sup>22</sup> In January 2017, the United States withdrew as signatory of the Trans-Pacific Partnership (TPP), a treaty concluded amongst twelve Pacific Rim countries.<sup>23</sup> The US government has also more recently expressed its will to renegotiate the NAFTA agreement.<sup>24</sup> Barriers to trade are a risk for regional economies with strong trade ties to the United States such as Mexico and Central American and Caribbean countries.<sup>25</sup>

To face these challenges, Latin America should keep on diversifying their partners (focusing more on Europe and Asia, notably China), while pursuing efforts on regional integration. The latter can stimulate foreign direct investment flows. Moreover, a more integrated market allows firms access to a bigger customer pool, obtain more economies of scale and become more competitive.<sup>26</sup> Regional integration platforms such as the Pacific Alliance and Mercosur have played an important role in supporting greater commercial integration. However, interregional trade in Latin America remains lower than in other regions of (like Eastern Europe and Asia Pacific), and only represents 20% of total trade.<sup>27</sup> There is scope for improvement as there have been signs of with greater convergence between the Pacific Alliance and the Mercosur, as representatives from the two blocs met in Buenos Aires in early April 2017 to discuss greater trade integration.<sup>28</sup>

### QUESTIONS FOR DISCUSSION

- How are recent changes in trade policy affecting investment plans in Latin America?
- How have firms benefitted from regional integration to date?

<sup>20</sup> OECD (2016), *Global Economic Outlook, June 2016*, [www.oecd.org/eco/outlook/economic-outlook-june-2016.htm](http://www.oecd.org/eco/outlook/economic-outlook-june-2016.htm).

<sup>21</sup> IDB (2016), *Trade trend estimates Latin America and the Caribbean*, 2017 Edition, Update 1Q, <https://publications.iadb.org/bitstream/handle/11319/7984/Trade-Trend-Estimates-Latin-America-and-the-Caribbean-2017-Edition.pdf?sequence=11&isAllowed=y>.

<sup>22</sup> Ibid.

<sup>23</sup> White House (2017), "Withdrawal of the United States from the Trans-Pacific Partnership Negotiations and Agreement, Presidential Memorandum, [www.whitehouse.gov/the-press-office/2017/01/23/presidential-memorandum-regarding-withdrawal-united-states-trans-pacific](http://www.whitehouse.gov/the-press-office/2017/01/23/presidential-memorandum-regarding-withdrawal-united-states-trans-pacific).

<sup>24</sup> White House (2017), "Readout of President Donald J. Trump's Call with President Peña Nieto of Mexico and Prime Minister Trudeau of Canada", [www.whitehouse.gov/the-press-office/2017/04/26/readout-president-donald-j-trumps-call-president-pe%C3%B1a-nieto-mexico-and](http://www.whitehouse.gov/the-press-office/2017/04/26/readout-president-donald-j-trumps-call-president-pe%C3%B1a-nieto-mexico-and).

<sup>25</sup> OECD/ECLAC/CAF (2016), *Latin American Economic Outlook 2017: Youth, Skills and Entrepreneurship*, [www.oecd.org/publications/latin-american-economic-outlook-201725140.htm](http://www.oecd.org/publications/latin-american-economic-outlook-201725140.htm)

<sup>26</sup> Ibid.

<sup>27</sup> OECD/ECLAC/CAF (2015), *Latin American Economic Outlook 2016: Towards a New Partnership with China*, [www.oecd-ilibrary.org/docserver/download/4115081e.pdf?expires=1495533668&id=id&accname=ocid84004878&checksum=90B2702E8A899C2F407696711B1D43F0](http://www.oecd-ilibrary.org/docserver/download/4115081e.pdf?expires=1495533668&id=id&accname=ocid84004878&checksum=90B2702E8A899C2F407696711B1D43F0).

<sup>28</sup> Ministry of Foreign Affairs of Argentina (2017), "Meeting of Foreign Ministers Mercosur-Pacific Alliance: Joint Communiqué", 7 April, [www.mrecic.gov.ar/en/meeting-foreign-ministers-mercosur-pacific-alliance-joint-communication](http://www.mrecic.gov.ar/en/meeting-foreign-ministers-mercosur-pacific-alliance-joint-communication).

## Session 6: Investing in the digital economy

*The expansion of digital technologies in Latin America is opening up new areas for business growth. However, barriers hindering the development of the digital economy still exist.*

Digitalisation has revolutionised the way people interact with each other, live and work. About 2.5 billion people are connected to the internet today (a third of the world's population) and by 2020 that number is expected to almost double to 4 billion users.<sup>29</sup>

Digital technology can be a driver of economic growth. Digital services have the potential to revolutionise a wide range of fields from health care to education with significant social and economic consequences. For example, increasing internet penetration by 10 percentage points could increase per capita GDP growth by 1.2 percentage points in emerging countries, according to a World Bank study.<sup>30</sup>

Although Latin America is lagging behind in terms of internet coverage and of digital services offered, the potential to expand digital services in the region is high. Penetration of digital technologies in Latin America still remains below the OECD average and subscriptions to fixed and mobile broadband services are lower than in OECD countries.<sup>31</sup> Nevertheless, the number of mobile phone subscriptions per 100 inhabitants in the region in 2013-2014 was high (116%) and exceeds the OECD average (106%).<sup>32</sup> There is therefore an opportunity to expand mobile broadband services. Higher quality broadband services could help not only to increase access to the internet, but can help businesses to improve efficiency.<sup>33</sup>

However, expanding digital services such as broadband coverage needs to go hand-in-hand with regulation concerning data privacy, consumer rights and digital security risk management.<sup>34</sup> Leading digital firms are also growing at an exceptional pace. It will be essential to ensure that the development of the digital economy goes hand in hand with an open and competitive market.<sup>35</sup>

### QUESTIONS FOR DISCUSSION

- How is digitalisation changing Latin America?
- What policy reforms are needed to attract more investment in the digital economy?
- What is constraining the development of digital services in the region?

<sup>29</sup> WEF/BCG (2014), *Delivering Digital Infrastructure: Advancing the Internet Economy*, [www3.weforum.org/docs/WEF\\_TC\\_DeliveringDigitalInfrastructure\\_InternetEconomy\\_Report\\_2014.pdf](http://www3.weforum.org/docs/WEF_TC_DeliveringDigitalInfrastructure_InternetEconomy_Report_2014.pdf).

<sup>30</sup> Ibid.

<sup>31</sup> OECD/IDB (2016), *Broadband Policies for Latin-America and the Caribbean: a Digital Economy Toolkit*, [www.oecd.org/publications/broadband-policies-for-latin-america-and-the-caribbean-9789264251823-en.htm](http://www.oecd.org/publications/broadband-policies-for-latin-america-and-the-caribbean-9789264251823-en.htm)

<sup>32</sup> Ibid.

<sup>33</sup> Ibid.

<sup>34</sup> Ibid.

<sup>35</sup> OECD/IDB (2016), *Boosting Productivity and Inclusive Growth 2016*, [www.oecd.org/latin-america/Boosting\\_Productivity\\_Inclusive\\_Growth.pdf](http://www.oecd.org/latin-america/Boosting_Productivity_Inclusive_Growth.pdf).