ADJUSTMENTS DURING CRISIS: GOVERNMENT EXPENDITURES AND REVENUES IN LATIN AMERICA, 1975-1988

Norman L. Hicks*

ABSTRACT

This study examines public expenditure and revenue data for 15 Latin American countries for the period 1975-1988, although the focus of the analysis is generally on the period of 1979-1988 during which fundamental changes in public finance and external economic relations were occurring. The study focuses largely on consolidated central government expenditures, which exclude public enterprises, and generally relies on unweighted averages of the individual country data.

Overall, the study notes that after 1980, budget deficits rose from about 2 percent of GDP to a peak of about 6 percent in 1982. After 1982 there was a slight decline in the overall deficit, but they nevertheless averaged about 5 percent of GDP in 1988. The increase in the average deficit can be attributed largely to an increase in current expenditures, which rose from 15 percent to about 20 percent of GDP. However, only about half of the increase in current expenditures was due to an increase in interest expenses; other expenditures also increased during the period. Offsetting the rise in current expenditures were a number of factors which indicate attempts by governments to made adjustments to the changing situation. These include an increase in revenue mobilization, largely from non-tax sources, and reductions in capital spending.

Perhaps the most interesting finding of the study is that despite rising interest costs, social sector expenditures (including social security) increased as a share of GDP and on a per capita basis. Within the social sectors, however, there appears to have been a decline in education spending, and in some countries there has clearly been a reduction in overall social sector spending.

SÍNTESIS

Este estudio examina los datos sobre gastos públicos e ingresos para 15 países Latinoamericanos durante el período 1975-1988, aún cuando el enfoque del análisis se centra, en términos generales, en el período de 1979-1988 durante el cual se estaban verificando cambios fundamentales en las finanzas públicas y en las relaciones económicas externas. El estudio aborda fundamentalmente los gastos consolidados de los gobiernos centrales, que excluyen las empresas públicas y que, por lo general, se fundan en promedios no ponderados de los datos para los países considerados individualmente.

Globalmente, el estudio señala que, con posterioridad a 1980, los déficits presupuestarios aumentaron de alrededor de un 2 por ciento del PIB a un nivel máximo cercano a un 6 por ciento en 1982. Con posterioridad a 1982 hubo una leve declinación en el déficit global, pero, sin embargo, ellos promediaron alrededor de un

5 por ciento del PIB en 1988. El aumento en el déficit promedio puede ser atribuido en gran medida a un aumento en los gastos corrientes, que subieron desde un 15 por ciento a alrededor de un 20 por ciento del PIB. Sin embargo, sólo cerca de la mitad del aumento en gastos corrientes se debió a un aumento en los gastos por intereses; otros gastos también aumentaron durante el período. El aumento de los gastos corrientes fue conpensado por un número de otros factores que ponen de manifiesto los intentos de los gobiernos por hacer ajustes para adaptarse a la situación de cambio. Estos incluyen un aumento en la movilización de ingresos, en gran medida de fuentes no tributarias, además de reducciones en los gastos de capital.

Tal vez, el hallazgo más interesante del estudio lo constituya el que no obstante el aumento en los costos de los intereses, los gastos del sector social (incluyendo la seguridad social) aumentaron como una proporción del PIB y sobre un base per cápita. Dentro de los sectores sociales, parece, empero, haberse producido una baja en los gastos por educación, y en algunos países ha habido claramente un disminución en el gasto del sector social como un todo.

* Latin America and Caribbean Region, World Bank.

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1. INTRODUCTION

The economic events of the 1980s, with alternative shocks from higher oil prices, high interest rates, and declining terms of trade, have forced most Latin American countries into periods of profound adjustment and change. Adjustment and stabilization programs, supported by the Bank and the Fund, have been designed to realign internal and external demand/supply balances by reducing public sector deficits, realigning exchange rates, removing price and interest rate controls, liberalizing trade, and encouraging private sector production and exports. Adjustment programs have focused particularly on the public sector, since it has been a major source of inflationary pressure, and a major source of inefficiency through the over expansion of unprofitable state-owned enterprises, expensive social programs, and excessive employment. As a result, major efforts have been made to bring public sector accounts into balance through tighter controls on public sector spending, including the operations of central banks, privatization of public enterprises, improvements in public sector pricing and tax collection, tax reform, and the elimination of redundant employment.

The overall resulting shifts in the public sector in Latin America are fundamental, but there has been little analysis of overall trends. A recent book by Larrain and Selowsky (1991) looks largely at the individual country experiences of the larger countries, but does not contain aggregate data for the region as a whole. These country studies make the point that while some countries reacted to the oil crisis by making internal adjustments, others relied heavily on external borrowings and did not adjust, or delayed adjustment until the debt servicing problems became insupportable. They also note that there has been long-term trend (1970-1985) for the public sector in Latin American countries to become a larger and larger share of total output.

Other studies (Hicks (1991), Hicks and Kubisch (1984), Hicks (1989)) looked at the pattern of expenditure reductions in countries which were experiencing declines in real government spending. This work tended to confirm the generally held views that capital spending bears a disproportionately heavy

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share of the adjustment in spending. However, it also showed that social sector spending and defense spending were relatively highly protected, whereas the heaviest reductions came in infrastructure and the productive sectors. These studies also examined trends for countries with high debt burdens, noticing that expenditure reductions caused by the crowding out from heavy debt service costs led to similar types of reductions by sector and by type of expenditures. Earlier work by Tait and Heller (1982) attempted to develop a methodology for finding "normal" levels of spending for every country based on a number of economic variables, so that countries that spent "too much" or "too little" could be identified. The methodology consists of developing linear regression models to explain cross-country differences in the ratio of various categories of government expenditure to GDP. An update of this study (Heller and Diamond, 1990) has used this methodology to explain shifts in the shares of expenditures. They find results broadly similar to the studies by Hicks and Kubisch (1984), in that capital spending declined after the oil crisis, but with different priorities in different regions. In the western hemisphere, for instance, high priority was accorded to the defense, social security and welfare sectors relative to infrastructure and agriculture. In contrast, in Africa, for example, defense and social security seem to have borne a greater share of the adjustment.

Grosh's study (1990) examined trends during the 1980s for nine countries in Latin America, based on data gathered by World Bank missions. She found that real per capita public social spending on health education and social security fell during some part of the 1980s in every country in the study. The shares of health and education in total government expenditures fell, while that of social security rose.

In contrast to previous studies, the objective of this study is to examine overall trends in public finance and public expenditures in Latin America, to better understand how the region adjusted to changes in the international environment. The study examines overall trends and patterns for Latin America as a whole, aggregating the experiences of individual countries, in an attempt to describe common experiences.

The data in this paper are drawn largely from the IMF's *Government Financial Statistics Yearbook* data bank, supplemented with Bank and Government reports where data is missing. Coverage in this paper is limited largely to consolidated central government expenditures, which includes central government, social security and extrabudgetary accounts, but excludes regional and municipal governments, autonomous agencies and public enterprises.[1] In addition, somelimited data on the consolidated non-financial sector, which includes state and local governments as well as public enterprises is also examined, although the coverage for this data is much more limited. This data has been culled from various Bank and IMF reports.

[1] See IMF, (1990), for individual country data and IMF (1986), for the definition of terms.

TABLE 1

SUMMARY OF REVENUES AND EXPENDITURES FOR CENTRAL GOVERNMENT, LATIN AMERICA AND THE CARIBBEAN REGION, 1975-1988
(% of GDP)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	Dif. between 1988 and 1979
Total Revenues & Grants	18.41	17.72	18.00	18.26	18.24	19.53	20.13	19.14	19.74	19.24	20.65	19.70	20.55	20.38	2.15
Total Revenue	18.06	17.50	17.82	18.06	18.06	19.36	19.91	19.00	19.65	19.10	20.38	19.56	20.32	20.22	2.16
Current Revenue	17.99	17.37	17.74	17.95	17.92	19.28	19.85	18.93	19.54	19.03	20.29	19.51	20.26	20.17	2.25
Tax	15.55	15.23	15.46	15.48	15.44	16.45	16.56	15.67	16.11	15.75	16.90	16.53	16.29	15.41	-0.02
Nontax	2.44	2.14	2.27	2.51	2.44	2.80	3.13	3.23	3.31	3.15	3.29	2.87	3.85	4.71	2.27
Capital Revenue	0.10	0.15	0.12	0.11	0.18	0.11	0.14	0.10	0.15	0.09	0.10	0.05	0.07	0.06	-0.12
Grants	0.35	0.22	0.17	0.20	0.18	0.17	0.22	0.14	0.09	0.14	0.27	0.15	0.21	0.16	-0.02
Total Exp. & Lend-Repayment	20.62	20.02	20.01	20.27	20.00	21.14	23.61	24.83	25.29	23.37	24.36	23.66	24.72	25.14	5.14
Total Expenditure	19.23	18.82	18.89	19.16	18.90	20.09	21.82	23.75	23.61	22.26	22.87	22.65	22.67	22.77	3.87
Current Expend.	15.02	14.73	14.74	15.33	15.33	16.57	17.81	19.99	19.87	19.26	20.13	20.05	19.71	19.80	4.47
Expend. Goods & Services	8.87	8.95	8.81	8.90	8.98	9.74	10.07	10.05	10.12	9.85	10.02	9.71	9.60	9.94	0.96
Wages and Salaries	6.25	6.19	6.24	6.20	6.18	6.63	6.82	6.68	6.58	5.71	5.65	5.43	5.67	5.84	-0.34
Other Goods & Services	2.62	2.76	2.57	2.70	2.80	3.12	3.25	3.37	3.54	4.15	4.38	4.28	3.93	4.10	1.30
Interest Payments	1.07	1.01	1.21	1.25	1.35	1.38	1.62	2.14	2.58	2.63	3.25	3.64	3.74	3.84	2.48
Subsidies & Other Curr. Transfers	4.94	4.58	4.63	5.11	4.93	5.38	6.05	7.60	7.01	6.64	6.73	6.58	6.07	5.89	0.95
Transfers Abroad	0.14	0.19	0.09	0.08	0.07	0.07	0.07	0.20	0.15	0.13	0.13	0.11	0.29	0.14	0.08
Capital Expenditures	4.28	4.44	4.06	3.92	3.65	3.70	4.13	3.81	3.90	3.21	2.82	2.74	3.16	3.15	-0.50
Lending Minus Repayment	1.38	1.20	1.12	1.12	1.10	1.05	1.78	1.08	1.68	1.11	1.50	1.01	2.05	2.37	1.27
Current Account Surplus	2.97	2.64	2.99	2.87	2.68	2.70	1.99	-1.06	-0.29	-0.23	0.16	-0.53	0.55	0.52	-2.16
Gross Capital Formation	NA	NA	NA	NA	2.21	2.40	2.79	2.71	2.26	1.82	1.50	1.52	2.03	1.92	-0.29
Overall Surplus/Deficit	-2.21	-2.30	-2.01	-2.02	-1.75	-1.61	-3.47	-5.68	-5.55	-4.17	-3.97	-4.13	-4.33	-4.93	-3.18
Financing	2.21	2.30	2.01	2.02	1.75	1.61	3.47	5.68	5.55	4.17	3.97	4.13	4.33	4.93	3.18
Abroad	0.91	1.31	1.09	1.05	1.40	1.64	1.30	1.46	1.63	1.32	2.10	2.19	1.23	1.34	-0.06
Domestic	1.30	1.00	0.92	0.96	0.34	-0.03	2.17	4.23	3.92	2.85	1.87	1.94	3.10	3.59	3.24

Sources: IMF.

Note: Includes fifteen countries: Argentina, Bahamas, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Guatemala, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela. Financing does not include Bahamas, Brazil and Costa Rica. Gross Capital Formation does not include Colombia.

2. CENTRAL GOVERNMENT TRENDS

The data in this study cover 15 Latin American countries, which together represent about 95 percent of the region's GDP.[2] In general, the data reported here are simple averages of the individual country data, and not weighted averages. This approach is favored, since it treats each country as a behavioral unit. It does, however, have the unhappy effect of giving equal weight to Brazil as to the Bahamas. While weighted average data do not give a fair view of what has happened to the average country, they do give a more accurate view of the effect of government policies on the average person, and are therefore used during the discussion of social sector expenditures. An examination of other expenditure and revenue trends using weighted average data does not materially change the conclusions reported here.[3]

As shown in Figure 1, total revenues and expenditures rose gradually during the period 1975-1988. Expenditures rose rapidly after 1980, without a corresponding increase in revenues, resulting in a sharp increase in budget deficits (Figure 2). While some adjustment was made after 1983 to increase revenues and reduce expenditures, the magnitude of the adjustment was not sufficient to fully reduce deficits to their 1980 levels. While deficits declined somewhat between 1982 and 1985 (see Figure 2), they began to rise again during the period 1985-1988.

The detailed data behind these graphs are shown in Table 1. Prior to 1980, revenues averaged about 18 percent of GDP, expenditures averaged 19-20 percent, and deficits were about 2 percent. These deficits seem to have been financed both by domestic and foreign borrowings, although the share of foreign borrowings in the total deficit increased as the decade ended. After 1980, there is a sharp increase in current expenditures, moving upward from about 15 percent of GDP in 1979 to 20 percent of GDP by 1982. While there is a gradual increase in current revenue, the impact of increased spending is largely reflected in higher deficits, which rise quickly from less than 2 percent of GDP in 1979 to almost 6 percent in 1982.

[2] The countries included are Argentina, Bahamas, Brazil, Chile, Colombia, Costa Rica, the Dominican Republic, Guatemala, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela. The inclusion of other countries was precluded by the absence of complete data, and thus the results may be biased from what would be indicated from a data set that included all countries in Latin America. Background data tables available in Hicks (1992).

[3] The weighted average data can be found in the background paper, Hicks (1992).

FIGURE 1

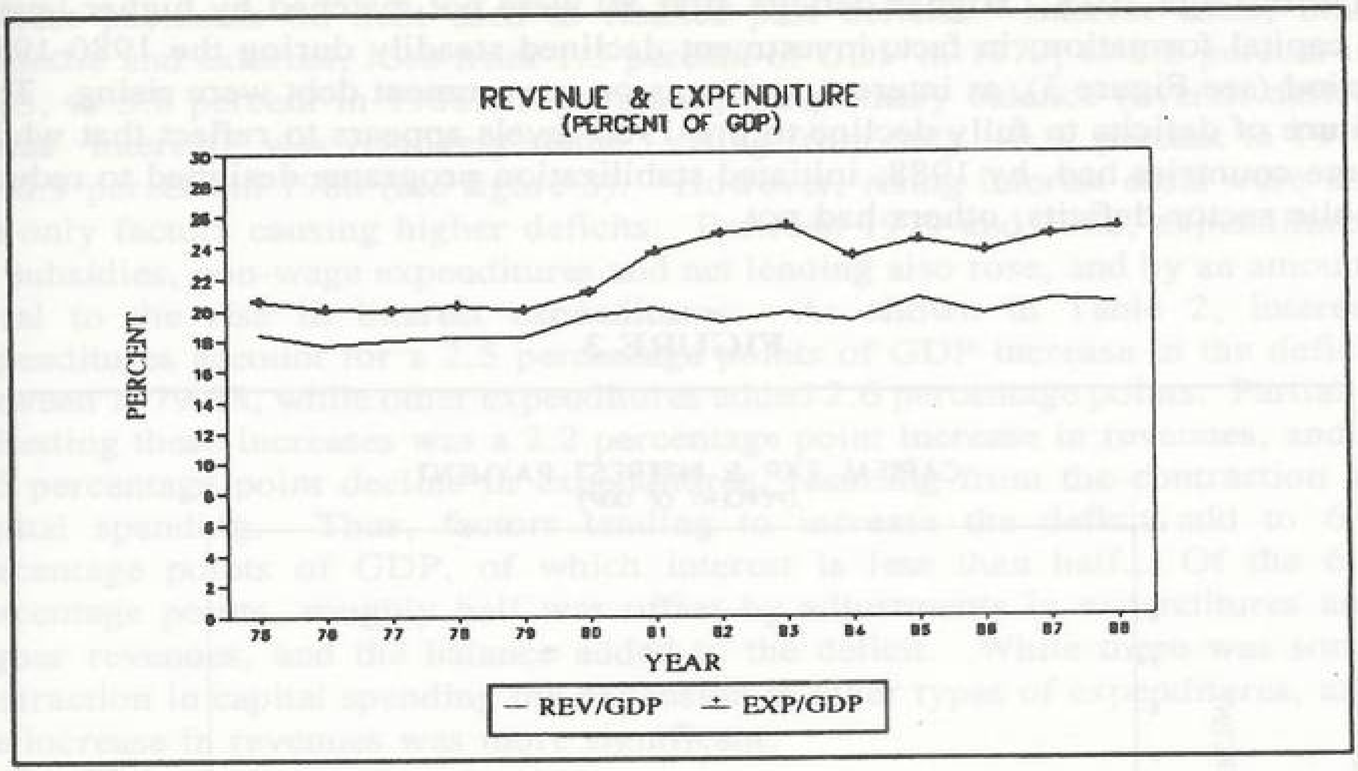
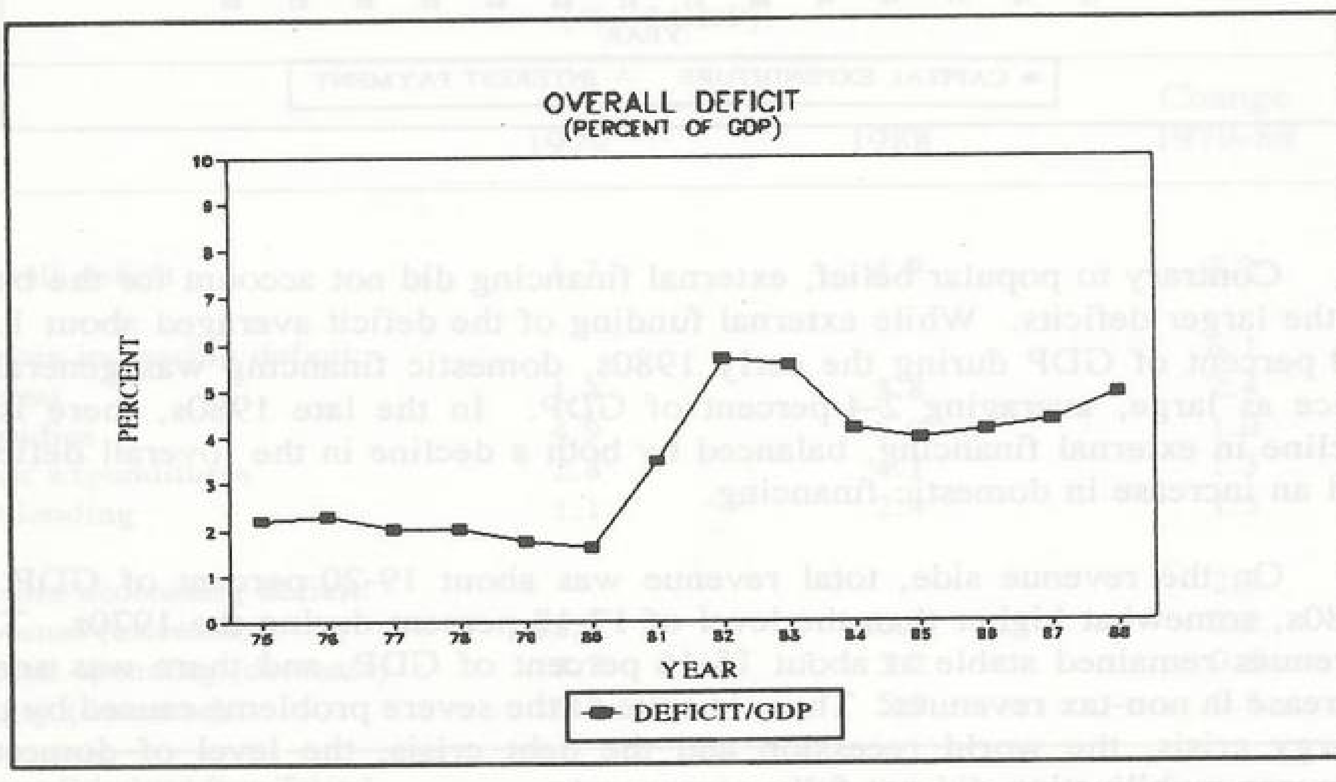
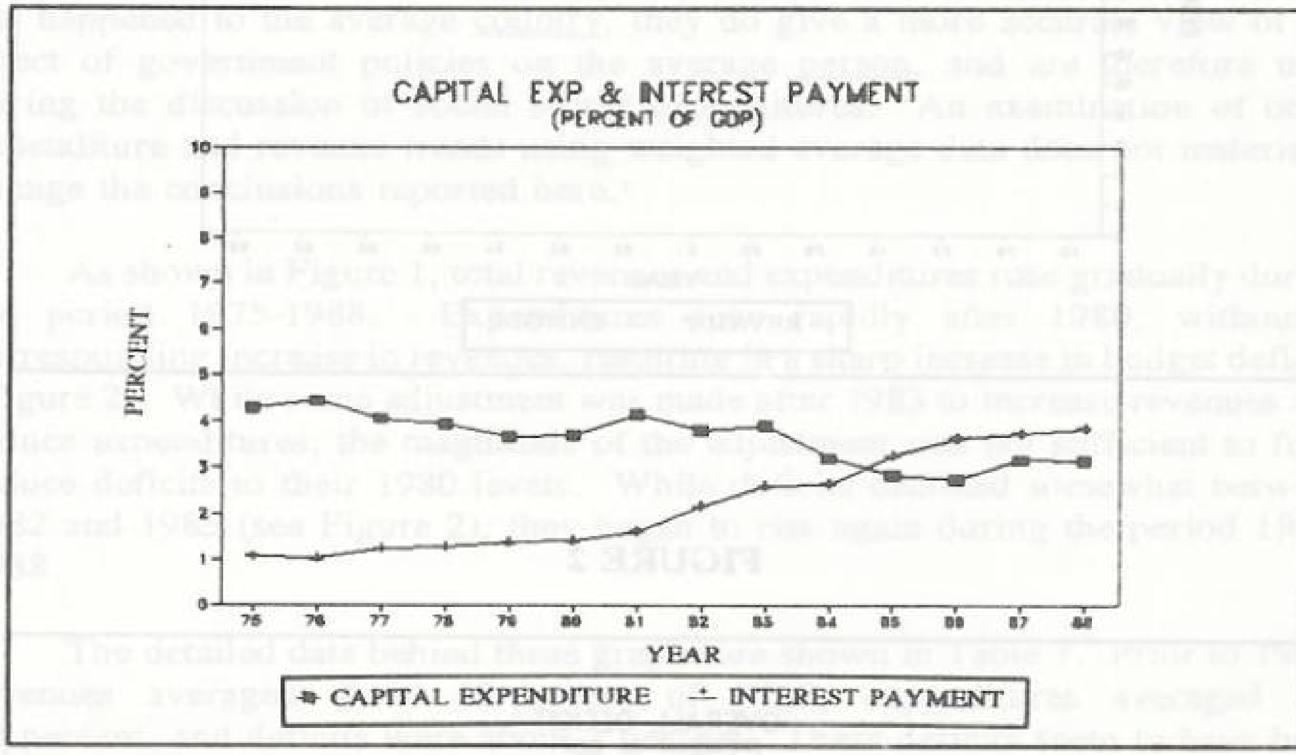


FIGURE 2



After 1982, deficits tend to decline slightly, averaging about 4-5 percent of GDP through 1988. Higher deficits after 80 were not matched by higher levels of capital formation; in fact, investment declined steadily during the 1980-1988 period (see Figure 3), as interest payments on government debt were rising. The failure of deficits to fully decline to pre-1980 levels appears to reflect that while some countries had, by 1988, initiated stabilization programs designed to reduce public sector deficits, others had not.

FIGURE 3



Contrary to popular belief, external financing did not account for the bulk of the larger deficits. While external funding of the deficit averaged about 1.5-2.0 percent of GDP during the early 1980s, domestic financing was generally twice as large, averaging 2-4 percent of GDP. In the late 1980s, there is a decline in external financing, balanced by both a decline in the overall deficit, and an increase in domestic financing.

On the revenue side, total revenue was about 19-20 percent of GDP in 1980s, somewhat higher than the level of 17-18 percent during the 1970s. Tax revenues remained stable at about 15-16 percent of GDP, and there was some increase in non-tax revenues. Thus, in spite of the severe problems caused by the energy crisis, the world recession and the debt crisis, the level of domestic resource mobilization did not fully compensate.

One of the major reasons for the continuation of high deficits is the rising interest payments on debt used to finance past deficits. Interest costs, both domestic and external, rose from 1.3 percent of GDP in 1979, to 2.6 percent in 1983, to 3.8 percent in 1988. As a result, the primary balance (overall deficit minus interest) was relatively stable, rising from only -0.3 percent in 1979 to -0.9 percent in 1988 (see figure 3). However, rising interest costs were not the only factors causing higher deficits. Between 1979 and 1988, expenditures on subsidies, non-wage expenditures and net lending also rose, and by an amount equal to the rise in interest expenditures. As shown in Table 2, interest expenditures account for a 2.5 percentage points of GDP increase in the deficit between 1979-88, while other expenditures added 2.6 percentage points. Partially offsetting these increases was a 2.2 percentage point increase in revenues, and a 0.5 percentage point decline in expenditures, resulting from the contraction of capital spending. Thus, factors tending to increase the deficit add to 6.1 percentage points of GDP, of which interest is less than half. Of the 6.1 percentage points, roughly half was offset by adjustments in expenditures and higher revenues, and the balance added to the deficit. While there was some contraction in capital spending the expansion in other types of expenditures, and the increase in revenues was more significant.

TABLE 2

FACTORS CHANGING DEFICITS, 1979-88

(% of GDP)

	1979	1988	Change 1979-88
Overall deficit	1.7	4.9	3.2
Factors increasing deficit:			6.1
Interest	1.3	3.8	2.4
Subsidies	4.9	5.9	1.0
Other expenditures	2.8	4.1	1.3
Net lending	1.1	2.4	1.3
Factors decreasing deficit:			2.9
Revenue (increase)	18.2	20.4	2.2
Capital spending (decrease)	3.7	3.2	0.5
Wages (decrease)	6.2	5.9	0.3

Source: Calculated from Table 1.

3. EXPENDITURES BY SECTOR

The sectoral allocation of expenditures is important, since it indicates which sectors have borne the burden of adjustment. Structural adjustment programs have often been criticized for their high social costs, their adverse effect on the poor, and their impact on reducing social sector expenditures. Table 3 shows the sectoral allocation of expenditures for eleven countries having complete data in the 15 country sample, for the years 1979 and 1988. These tabulations show that social sector expenditures actually increased during the 1980s as a share of GDP, largely because of expanded expenditures in health and social security. Economic affairs and services, which includes expenditures for infrastructure services, as well as industry and agriculture, show a slight decline. Defense spending remained a constant share of GDP, and there was a slight drop in expenditures for general public services. The biggest change in the allocations, however, was the increase in "other expenditures" which went from 2.6 to 5.2 percent of GDP, primarily because of the expanded expenditures for interest. The decline in infrastructure services is in part linked to the decline in capital spending. Sectors which consist of heavy capital spending, such as transportation, will be affected more than the more labor intensive, and consumption intensive, sectors such as health and education.

TABLE 3

SECTOR DISTRIBUTION OF EXPENDITURES
(% of GDP)

	1979	1988	Difference 1979-1988
General public service	2.61	2.20	0.41
Defense	1.38	1.30	-0.08
Social Sectors	9.91	10.63	0.72
Education1	3.12	2.87	-0.25
Health	1.97	2.20	0.23
Social Security	4.06	4.69	0.63
Housing	0.57	0.64	0.07
Other	0.21	0.24	0.03
Economic Affairs and Services	4.49	3.06	-1.43
Fuel and Energy	0.43	0.37	-0.06
Agriculture	1.08	0.67	-0.41
Mining, Manufacting	0.36	0.23	-0.13
Transport, Communications	1.55	1.18	-0.37
Other	1.07	0.64	-0.43
Other Expenditures	2.58	5.19	2.61
Total	20.67	23.17	2.50

Note: Covers eleven countries only: Argentina, Bahamas, Brazil, Chile, Costa Rica, Dominican Republic, Mexico, Panama, Paraguay, Uruguay and Venezuela.

For the social sectors, there appears to be an increase in the share, although a large part of this is caused by an increase in social security expenditures. However, the increase would still be positive even if social security expenditures were eliminated. At the same time, however, per capita GNP was falling, which partially offsets this increase. From a welfare standpoint, the data in Table 3 are not useful, since they are simple averages of countries, regardless of population size. What is of interest is the level of real government services delivered per capita, or real public expenditures per person in real terms. To calculate this, the simple average of country performance shown above can be replaced by weighted averages of the countries. The weighted average data, however, show a similar trend. Total social sector spending increases from 9.5 percent of GDP in 1979 to 10.4 percent in 1988; without social security, the numbers are 5.1 percent and 5.4 percent respectively (see Table 4). The percentage change in the overall share is 8.9 percent, but against this must be set a 1.4 percent decline in per capita income. As a result, per capita social sector expenditures grew by 7.4 percent over the nine year period. This is not very substantial, but neither is it a decline. Subtracting social security payments, the growth would be 3.6 percent. It is important to note that while health and social security expenditures increased on a per capita basis, education expenditures declined. Thus, not all social sectors were equally protected. Within the social sectors, the data do not indicate much in the way of distribution, for instance, between primary schools and universities, or between urban hospitals and rural health clinics. The data do indicate that over 80 percent of health expenditures are for "hospitals" and 20 percent of education expenditures are for the tertiary sector, but data on the trends in these subcomponents are lacking. Thus, it is difficult to infer what was the impact of these expenditures on the poor. However, it is possible that even a decline in social sector spending may not hurt the poor, and an increase may not have helped them.

TABLE 4

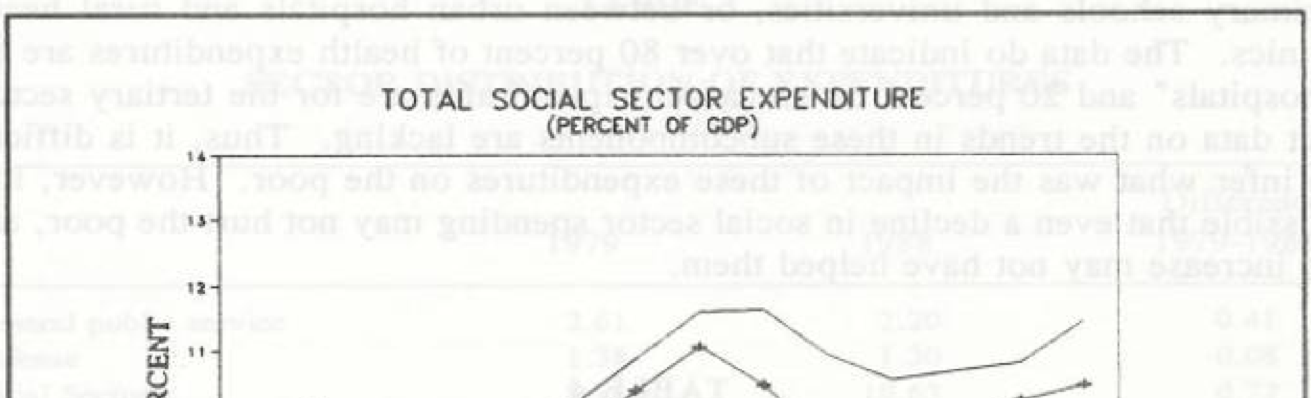
SOCIAL SECTOR EXPENDITURE SHARES, WEIGHTED AVERAGES

	Shares of GDP		Percent change (1979-88)		
	1979	1988	Share	GNP/N	Expend./N
Education	2.66	2.43	-8.6	-1.4	-10.1
Health	1.69	1.85	9.5	-1.4	8.0
Soc. Security	4.43	5.02	13.3	-1.4	11.7
Others	0.73	1.07			
Total	9.52	10.37	8.9	-1.4	7.4
Total w/o S/S	5.09	5.35	5.1	-1.4	3.6

Note: N = population; data for social sector shares weighted by GDP.
Based on eleven country sample (see Table 3)

This finding of increasing per capita social spending is somewhat surprising, and appears to contradict Grosh's study which reported a decline in per capita social expenditures. She found that per capita social expenditures declined about 20 percent during the period 1980-1985 for a sample of eight countries. Differences in timing, data sources, sample size, and composition of countries in the sample may account for these differences. Grosh's data used the period 1980-1985, for instance, and she used unweighted averages. Her data only included health, education and social security, while the data used here also includes housing, welfare, and recreation/cultural expenditures. Looking at the data on a year by year basis, one can reconcile (somewhat) these two findings (see Figure 4). Social sector spending appears to have been a fairly stable share of GDP during the last half of the 1970s, but rose sharply between 1980 and 1982. Between 1982 and 1985 there was an equally sharp decline, which seems to be the trend noted by Grosh (although starting somewhat later). After 1985, there is another upward trend, so that the decade ends at a level slightly higher than it began. While the decline between 1982 and 1985 is a drop in the share from 11.0 to 9.3 percent of GDP, this occurred at a time that per capita GDP was also declining.[4]

FIGURE 4



[4] It is estimated that real per capita GDP declined about 1% during 1982-1985 for these countries.

Aggregate data such as used in this report may also obscure differences between countries and variations in behavior which are being averaged together. Since the conclusion relative to the increasing share of the social sectors is somewhat at variance with popular belief, it may be useful to disaggregate this data and examine trends in individual countries. Table 5 presents the underlying country data for the changes in social spending as a share of GDP, as well as the change in the actual GDP itself. It is clear that some countries were increasing their social spending as a share of GDP (notably the Bahamas, Panama and Uruguay), while others were declining. Most of the countries that were increasing their social sector expenditures did so through an increase in social security and welfare expenditures, most of which is in social security. There appears to be little or no correlation with the change in per capita income. Of the six countries with declining social sector expenditures, three had increasing per capita incomes, and three had declining per capita incomes. In addition, five countries increased social sector spending despite falling per capita incomes.

TABLE 5

CHANGE IN SECTORAL ALLOCATION OF EXPENDITURES
(% of GDP)
Difference Between 1979 and 1988

	Total Soc. sector	Education	Health	Soc. Secur. & welfare	Percentage change in per capita income
Argentina	0.19	-0.02	0.01	0.21	-16.4
Bahamas	3.11	0.68	1.14	1.29	15.9
Brazil	-0.18	0.27	0.46	-0.9	13.3
Chile	-1.21	-1.21	-0.13	0.12	9.1
Costa Rica	-0.41	-1.59	-0.16	1.34	-10.8
Dom. Rep	-1.13	-0.65	0.05	-0.53	-1.5
Mexico	-1.96	-0.64	-0.29	-1.03	-3.2
Panama	3.33	-0.34	1.06	1.92	-5.6
Uruguay	4.60	0.05	0.16	4.38	-2.6
Paraguay	-0.27	-0.30	-0.12	0.15	4.6
Venezuela	0.79	0.39	0.30	0.11	-17.4

Note: Data for Paraguay are changes from 1979 to 1987.

4. BUDGET SHARES

The analysis so far has concentrated on data expressed as a share of total GDP. It is also useful, however, to look at the share of each sector as a share of total expenditures, in order to understand relative priorities of policy makers in making adjustments. This can be done by simply taking the data from Table

3, and dividing the sector shares with respect to GDP by total expenditures with respect to GDP (see Table 6). On this basis, "other" expenditures, which includes interest payments, expanded its share of the total while all other major sectors had a declining share. The share of the social sectors fell from 48 percent to 46 percent, defense from about 7 percent to 6 percent, and economic services from 22 percent to 13 percent. The decline in the social sectors comes largely from a decline in the share of education expenditures, as noted above. However, the declines in social sectors and defense spending are relatively less severe, and these sectors were relatively more protected, than other sectors. This finding is similar to that found in previous studies of countries undertaking expenditure reductions (Hicks, 1990).

TABLE 6

BUDGET SHARES BY SECTOR
(% of total)

	1979	1988	Difference 1979-1988
General Public Service	12.6	9.5	-3.1
Defense	6.7	5.6	-1.1
Social Sectors	47.9	45.9	-2.0
Education	15.1	12.4	-2.7
Health	9.5	9.5	0.0
Social Security	19.6	20.2	.6
Housing	2.8	2.8	0.0
Other	1.0	1.0	0.0
Economic Affairs and Services	21.7	13.2	-8.5
Fuel and Energy	2.1	1.6	-.5
Agriculture	5.2	2.9	-2.3
Mining, Manufact.	1.7	1.0	-.7
Transport, Comm.	7.5	5.1	-2.4
Other	5.2	2.8	-2.4
Other Expenditures	12.5	22.4	9.9
Total	100.0	100.0	

Note: Based on eleven country sample (see table 3).

5. THE TOTAL PUBLIC SECTOR

It is important to note that many public sector infrastructure services are provided through public enterprises, which are not included in this data, or through regional government bodies. To establish some idea of trends for the consolidated public sector can be gathered from Table 7, which shows consolidated public investment and overall deficit/surplus for eleven countries, in consolidated public sector can be gathered from Table 7, which shows consolidated public investment and overall deficit/surplus for eleven countries, in contrast with the same figures for the fifteen country sample. Figures for consolidated non-financial public sector include the current deficit/surplus of public enterprises and autonomous agencies, as well as the capital expenditures, and are drawn largely from IMF and World Bank country reports. These reports generally report the net deficits of public enterprises, not their total expenditures and revenues. Larrain and Selowsky (1991), however, note that if all expenditures of public enterprises were to be included, the public sector would average over 50 percent of total GDP for the six major Latin American countries that they dealt with.

TABLE 7

COMPARISON OF TOTAL PUBLIC SECTOR AND GENERAL GOVERNMENT

(% of GDP)

Public Sector[a]	1985	1986	1987	1988	1989
Capital Expenditure	8.8	8.2	7.7	7.5	6.6
Overall Surplus/Deficit	-7.3	-6.5	-6.6	-7.8	-5.7
Central Government[b]					
Capital Expenditure	2.8	2.7	3.2	3.2	N/A
Overall Surplus/Deficit	-4.0	-4.1	-4.3	-4.9	N/A

[a] Covers eleven countries: Argentina, Chile, Colombia, Costa Rica, Guatemala, Mexico, Nicaragua, Panama, Paraguay, Uruguay, and Venezuela.
[b] Covers 15 countries as per Table 1.

In general, capital expenditures for the total public sector exhibit a gradual decline during the 1985-1989 period, while those for the central government are relatively stable. Total capital spending during 1985-1988 averages 8 percent of GDP for the total public sector, compared to only 3 percent for central government, indicating that the bulk of capital spending takes place in the enterprises and autonomous agencies. Likewise, the overall public sector deficit averages about 7 percent, compared to 4.3 percent for the central government. Thus the previous findings, which focused only on central government expenditures, may misstate the true extent of sectoral adjustments. However, since most government decisions are made at the budgetary level, and public enterprises include revenues and expenditures for telephone, power and other infrastructure services which are not discretionary, it is not entirely clear that this level of aggregation is necessarily superior. It is also interesting to note that while social security expenditures increased from 4.1 to 5.1 percent of GDP, social security tax revenues increased only from 4.8 to 4.9 percent. Part of the that are outside of budgetary control, and may be rising more as a consequence of the aging of the population in Latin American countries, than from any conscious decision on the part of the Governments to expand or preserve social expenditures. The finding that social security tax revenues are less than social security expenditures is symptomatic of a region-wide problem of legislated generous benefit systems that are not paralleled with adequate revenue systems, particularly when accounting for the actuarial liabilities that are being made.

6. RESOURCE MOBILIZATION

As noted above, there were no major shifts in resource mobilization by the government sector during these years. However, detailed data are available for only eight countries (see Table 8). For these countries total revenues increased by about 3.3 percentage points during the period. Tax revenues increased only by 0.2 percentage points. While there was some increase in taxes on international trade, this was offset by declines in other categories. In general, the mix between direct and indirect taxes remained unchanged. The biggest increase took place in non-tax revenue, particularly in profits and rental income. This appears to represent better cost recovery policies in public enterprises, and may represent compensation by public enterprises for external debts which were taken over by central governments and rescheduled.

TABLE 8

REVENUE BY TYPE, 1975-1988
(% of GDP)

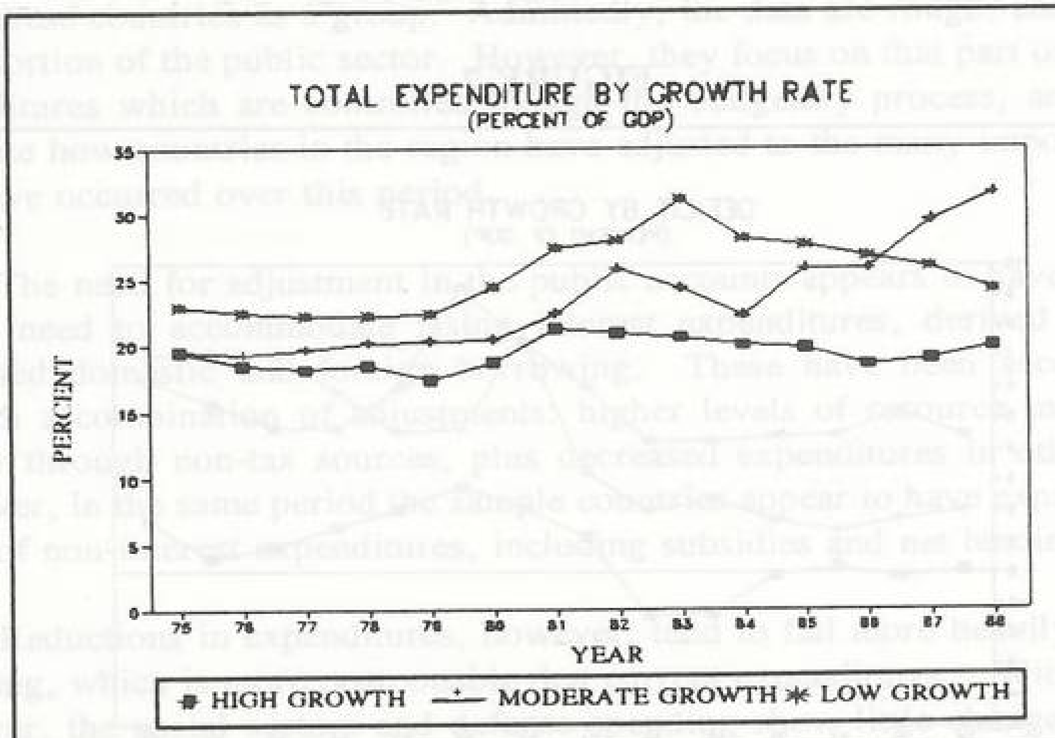
	1975	1979	1988	Difference 1979-1988
Total Revenue and Grants	20.3	20.6	23.9	3.3
Tax Revenue	16.1	17.5	17.7	0.2
Income Taxes	3.4	3.5	3.5	0.0
Social Security Taxes	4.6	4.8	4.9	0.1
Domestic Trade	4.6	5.3	5.4	0.1
International Trade	3.3	3.0	3.7	0.7
Others*	0.7	0.9	0.2	-0.7
Non-Tax Revenue	2.4	2.7	6.1	3.4
Profits	1.2	1.5	3.9	2.4
Others	1.2	1.2	2.2	1.0
Capital Revenue and Grants	0.5	0.3	0.2	-0.1

Note: Includes eight countries only: Brazil, Chile, Costa Rica, Dominican Republic, Mexico, Panama, Paraguay and Uruguay.
* Includes adjustments to cash basis.

7. GROWTH AND PUBLIC FINANCE PERFORMANCE

The sample of countries being examined here combines those that have done relatively well during the period, with those that have not. In order to look at the possible correlation between economic growth and performance in the public sector, the sample has been disaggregated into three sub-groups: the high growth countries, whose average GDP growth during 1978-1988 was 0.4 percent or greater on a per capita basis (four countries), the moderate growth group (five countries) whose growth ranged from 0.3 to -0.6 percent on a per capita basis, and the low growth countries whose per capita GDP was -1.0 percent or less during the period (also five countries).[5] Broad trends are shown in Figures 5-7; details are available in the background paper. All countries seem to have been at about the same position in the early 1970s with regard to aggregate expenditure levels (see Figure 5), but the low and moderate growth countries expanded expenditures after 1980; the level of expenditures was relatively stable in the high growth countries.

FIGURE 5



[5] The countries are; (i) Low Growth: Argentina, Guatemala, Nicaragua, Peru and Costa Rica; (ii) Moderate Growth: Panama, Mexico, Uruguay, Dominican Republic, and Brazil; (iii) High Growth: Bahamas, Chile, Colombia and Paraguay.

FIGURE 6

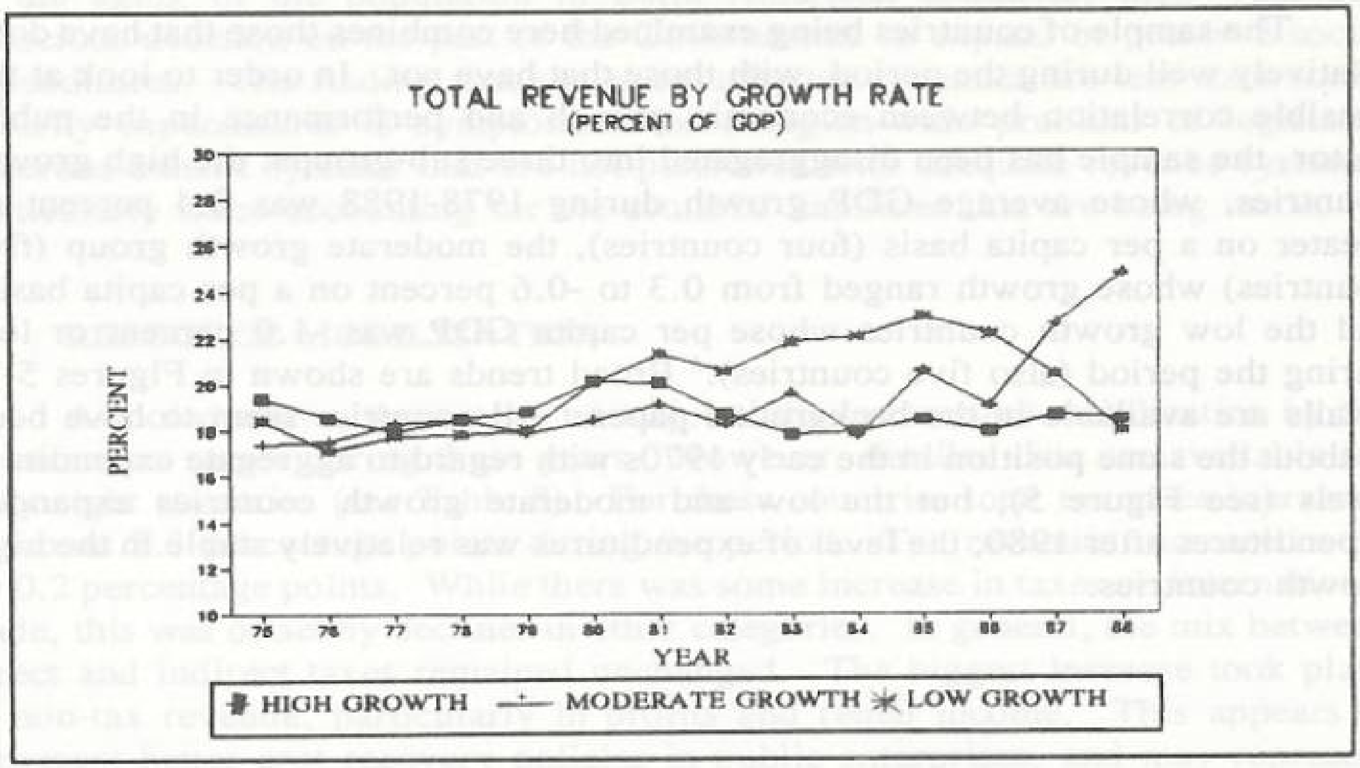
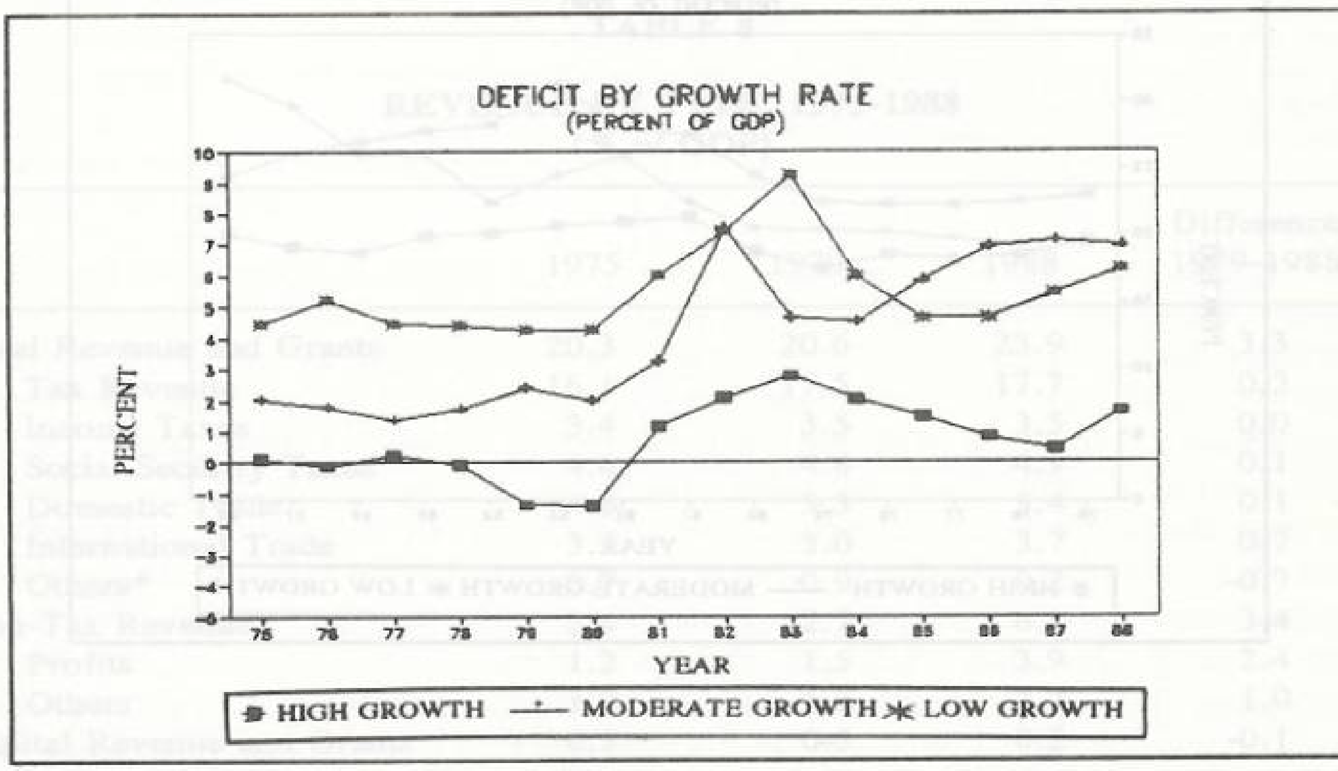


FIGURE 7



Revenues remained relatively stable throughout the period for all three groups (Figure 6), with the result that deficits grew more rapidly in low growth economies. By the end of the 1980s, deficits in low growth economies averaged about 6 percent, compared to about 4 percent in moderate growth economies, and 2 percent in high growth economies (see Figure 7).

Smaller deficits suggest greater efforts at adjustment, which should ultimately pay off in terms of higher growth. However, countries that are following good policies that induce rapid growth may also be generating public revenues that make large deficits unnecessary. Thus, while the causal relationships between growth and deficits are not entirely clear, empirically it appears that those countries which performed the best in terms of output growth also tended to have lower deficits.

8. CONCLUSIONS

The analysis of public expenditure trends presents an overview of regional directions, aggregating across countries. It is not intended to substitute for analysis at the country level, but to enable analysts to make general statements about these countries as a group. Admittedly, the data are rough, and exclude a large portion of the public sector. However, they focus on that part of the public expenditures which are controlled though the budgetary process, and as such, illustrate how countries in the region have adjusted to the many important shifts that have occurred over this period.

The need for adjustment in the public accounts appears to have originated in the need to accommodate rising interest expenditures, derived both from increased domestic and foreign borrowing. These have been accommodated through a combination of adjustments: higher levels of resource mobilization, chiefly through non-tax sources, plus decreased expenditures in other sectors. However, in the same period the sample countries appear to have expanded some types of non-interest expenditures, including subsidies and net lending.

Reductions in expenditures, however, tend to fall more heavily on capital spending, which is more postponable that current expenditures. Within sectors, however, the social sectors and defense spending show little change relative to GDP; most of the reductions come in the area of economic services. A period of reduced spending on the social sectors, 1982-1985, appears to have been followed by a correction during the years 1985-1988. The conclusion that social sector spending has not fallen, in real per capita terms, for the region as a whole does not mean that it has not fallen for certain countries in the region. The relative protection of the social sectors in the countries within this sample during this period is a hopeful sign that they recognize their relative importance in maintaining social and political stability. The fact that social spending per capita has not fallen should not be seen as an excuse for complacency. It is clear that many social sector services do not reach the poor, and within existing allocations much more could be done to protect the poor in many countries, particularly during periods of adjustment. Future programs of adjustment need to concentrate on not only preserving the current levels of social sector spending, but also reviewing how these expenditures can be better targeted to reach the poor, and in what ways the costs of providing these services to the non-poor can be offset by user charges and fees.

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