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Monetary and financial cooperation in Latin America and regional asymmetries that impact regional integration

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ABSTRACT

This article analyzes the prospects for monetary and financial cooperation in Latin America, as the integration process returns to the discussions due to the latest global crises. The concepts of regional integration, monetary and financial cooperation, and regional asymmetries are presented; from this theoretical-conceptual discussion, the article seeks to present which are the asymmetries that affect the process of monetary and financial integration. Through this literature review and the theory of optimal monetary areas (TAMO), we seek to understand how Latin America is positioned in relation to monetary and financial integration. It follows that monetary and financial cooperation is sometimes seen as a means of fostering integration, but also as a proposal to provide long-term resources and as a source of foreign exchange liquidity for countries. Thus, there are indications that the economies of the region do not have the necessary conditions for regional integration.

Keywords

Regional Integration. Monetary and Financial Cooperation. Latin America. Asymmetries.

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ARTIGO

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A cooperação monetária e financeira na América Latina e as assimetrias regionais que impactam na integração regional

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RESUMO

Esse artigo analisa as perspectivas da cooperação monetária e financeira na América Latina, pois o processo de integração volta às discussões devido às últimas crises globais. Apresentam-se os conceitos de integração regional, cooperação monetária e financeira, e as assimetrias regionais; a partir dessa discussão teórica-conceitual, o artigo busca apresentar quais são as assimetrias que afetam o processo de integração monetária e financeira. Por meio desta revisão bibliográfica e pela teoria das áreas monetárias ótimas (TAMO), busca-se compreender como a América Latina se posiciona em relação a integração monetária e financeira. Conclui-se que a cooperação monetária e financeira é por vezes vista como um meio de fomentar a integração, mas também como uma proposta de fornecimento de recursos de longo prazo e como uma fonte de liquidez em divisas para os países. Assim, há indícios de que as economias da região não apresentam as condições necessárias uma integração regional.

Palavras-chave

Integração Regional. Cooperação Monetária e Financeira. América Latina. Assimetrias.

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1. Introduction

In the future, people will recognize the coronavirus pandemic (COVID-19) as the worst in a century, as it generated a health crisis and, consequently, a global economic crisis characterized as the worst since the Great Depression and recently experiencing the subprime crisis (GEORGIEVA, 2020). Specifically, in Latin America, the pandemic has started to have remarkable effects on affected people and mortality in several countries. Regarding economic issues, the pandemic hit the region after five years of low economic growth, a period of the lost half-decade (OCAMPO, 2020a; OCAMPO, 2020b).

As middle-income countries, Latin American countries have limited access to financing, so this limitation is one of the main shortcomings in structuring an anti-crisis program. Besides, access to international capital markets has become increasingly complex as portfolio capital outflows from emerging markets, driven by non-residents, reached unprecedented levels in recent months (UNSDG, 2020). The result of this capital flight is a considerable depreciation in the exchange rate of some countries in Latin America and the Caribbean, corroborating the seriousness of the situation.

Within the context of foreign capital flight and the impossibility of accessing the international financial markets, the strategies for actions are reduced; that is, a limited economic policy causes countries to seek financial assistance mainly in the International Monetary Fund (IMF) or in the World Bank (HERNÁNDEZ, 2020). This pandemic can allow governments to carry out a joint reflection on a complete restructuring of their development models and strengthen socio-economic cooperation in Latin America.

The proposal of monetary and financial cooperation in Latin America is connected with the policies and programs focused on intensifying regional integration. In recent decades, the countries have highlighted some guidelines in this area: liquidity provision via regional funds, mutual credit mechanism among the countries of the regional bloc, and the proposed new tools for long-term financing; this cooperation between countries demonstrates the need to overcome existing regional deficiencies (BAUMANN; MUSSI, 2011).

In Latin America, initiatives to promote monetary and financial cooperation have been motivated much more by the traumas caused by external shocks than by efforts to promote regional integration. This thinking is based on the idea that increased commercial and financial integration requires greater policy coordination between authorities to mitigate external shocks (BASNET; SHARMA, 2015). There have been numerous attempts to revitalize regional cooperation initiatives, either by the typical development idea in each region or neoliberal regionalism. Other theories have emerged, many of them seeking answers to historical problems of the Latin American reality.

This whole proposition of financial cooperation policies comes from the explanation that divides this monetary and financial integration into two modalities: i) funding for development, infrastructure, and commercial investment programs and projects; ii) macroeconomic cooperation mechanisms and related economic cooperation, funding for liquidity during the balance of payments crisis (OCAMPO, 2006). The second modality mentioned above is also known as cycle synchronism. It is based on the premise that countries' discipline is essential in the face of pressure and being a mechanism for reducing macroeconomic oscillations and strengthening countries' credibility (MACHINEA; ROZENWURCEL, 2006).

In the perspective of some studies (OCAMPO, 2006; UNCTAD, 2007), there are no proposals for structural reforms in the international monetary system in the short term. Also, there is a trend towards a multi-currency system (EICHENGREEN, 2010). Both findings identified in the surveys point to the proposition of an integrated regional model of the monetary and financial market as an alternative.

The present work covers Latin American regional integration's theme to assess monetary and financial cooperation conditions in Latin America. Thus, the proposal is to answer the question: what are the significant existing obstacles for Latin American monetary and financial cooperation (integration)?

This article is structured in five sections, the first of which contains this introduction. The second section has some considerations on Latin American regional integration. The third part presents the concepts, the importance, and the impacts of monetary and financial cooperation in Latin America. The fourth section discusses some regional asymmetries and the paths to monetary and financial integration. Finally, in the last section, we make the final considerations arising from the study.

2. Regional Integration in Latin America

Regional economic integration is a post-war phenomenon, as many countries have favored greater integration between their economies. According to Garcia (2016), nations cannot structure regional integration based only on economic theories; it is crucial to consider principles and critical analyzes of previous projects. In Latin America, ECLAC (Economic Commission for Latin America and the Caribbean) started its first discussions in the 1950s. However, the proposals for regional integration took shape only in the late 1960s and early 1970s, with the Andean Pact and the Latin American Free Trade Association (MEDEIROS, 2018).

During that period, ECLAC centered its integration vision on issues related to the region's aggregate development rather than on trade gains. For Amado and Mollo (2004), this focus provides limited and protectionist regional integration, since in this case, the profits from the goods free movement and production means are discarded.

In the understanding of Belluzzo (2016), many economic integration programs or projects in the Latin American region, between the 1960s and 1980s, failed due to political instability. This instability was generated by the cold war and the resistance of Latin American oligarchies (entrepreneurs and politicians) that held political control and economic interests with the primary export economic model.

The entry of peripheral countries into the scope of financial globalization in the 1980s and early 1990s was significant to provide a new economic dynamism. However, according to some authors (LINS, 2003; CUNHA, 2008; FANELLI, 2008; DEOS; MENDONÇA; WEGNER, 2013), this entry did not bring solutions the structural problems of the lack of capital for the long-term financing of these countries. Thus, nations could see and understand globalization by measuring their costs and benefits (CUNHA, 2008).

The 1990s in Latin America were characterized by a series of regional trade agreements. In total, 14 treaties were signed, in addition to the formalization of MERCOSUR (Southern Common Market), which, within its limitations, was a proposal for regional integration (BASNET; SHARMA, 2015).

Compared to the European Union, the Latin American integration process takes place in a context radically different from that experienced in Europe. There is no guaranteed financial and exchange rate stability. There are significant divergences in macroeconomic policy, and institutional initiatives remain weak and do not have powerful bodies capable of leading sub-regional groups and representing regional interests (GHYMERS, 2005). This low motivation to integrate arises exclusively from commercial aspects. Therefore, it is possible to observe customs unions or free zones with no supranational authority, and the initiatives or practical mechanisms for coordinating other economic policies are still very fragile.

It is important to note that the last decades' international scenario has shown high financial variability and an increase in crises. In this way, monetary and financial integration assumes a crucial role, especially in peripheral economies, to foster long-term financing policies and reduce external vulnerability (DEOS; MENDONÇA; WEGNER, 2013). There is empirical evidence that greater integration of financial markets can reduce the likelihood of financial and foreign exchange crises by increasing the quality and diversity of instruments for risk management, resulting in more significant economic growth (FANELLI, 2008). In other words, if Latin American countries opted for a macroeconomic cooperation policy, they would be less fragile to economic and financial turbulence (LINS, 2013).

Another appealing aspect is the possible benefits of regional integration. For Basnet and Pradhan (2017), these benefits include aspects related to reduced transaction costs, falling prices for consumers, more efficient use of resources, the economy of scale, a larger competitive business market, new investments in several areas, advancement technological development, and productivity gains. These findings come from two procedures connected to integration: reducing trade barriers and encouraging human capital mobility. Thus, these new regional arrangements provide more significant benefits and can contribute to the economic growth of member countries.

Thus, Latin American economies are not immune to turbulence in the international market (BAUMANN; MUSSI, 2011). On the contrary, there is a dependence of these economies linked to exports of agricultural and mineral commodities. That is, they are connected to dollarized international markets.

In the study on regional financial cooperation, Ocampo (2006) states that an organizational policy or structure for collaboration among border countries can be effective in times of crisis. Thus, lower-income countries should pursue this complementarity with more significant and larger partners to obtain large-scale financing. This monetary and financial integration will only work when free trade agreements are implemented and become a key element (MACHINEA; ROZENWURCEL, 2006).

Therefore, the studies and arguments of several authors have a convergence. All of them present the features or elements that seek to establish an integrated regional market with propositions and initiatives that favor greater integration of the Latin American countries. This scenario occurs because regional integration can also lead to deeper assimilation and complement multilateralism, setting a precedent that other countries have failed to achieve individually (CARBAUGH, 2015).

Thus, Latin American integration should be developed as a strategic project and not just a landmark of traditional regionalization mechanisms aimed at creating free trade zones or promoting investments. Developing this integration as a strategic project appears as the best method considering that this process requires careful analysis and verification concerning the diversified productive structures and different levels of development among countries (AMADO; MOLLO, 2004). This conception expresses, above all, a political view of the construction of a Latin American continent articulated in the most diverse dimensions, with the internal objective of fully exploring the synergies and potential opportunities, and with the external objective of strengthening the possibilities and the political weight of the region in the face of global issues, in a multipolar world (SIMÕES, 2011).

However, when we consider how governments have developed the countries' economic and social strategies, the bases of the economic structure, and the construction of political power in recent years in Latin America, we note that they contradict this proposal for cooperation. Some regional asymmetries hinder the integration process and produce embryonic inefficiency in proposals and initiatives (MEDEIROS, 2018).

3. Monetary and Financial Cooperation in Latin America

Whenever the implementation of economic integration between countries is under study, it is kept in mind that systems, procedures, and agreements will be the means to facilitate economic relations between them and to liberalize markets.

When starting an analysis of monetary integration procedures, it is essential to use the Optimum Currency Area Theory (OCA), developed from the 1960s, in the pioneering works of Robert A. Mundell, R. I. McKinnon, and P. B. Kenen. The basic proposal of this theory is to assess under which situations a group of countries renounces the autonomy of macroeconomic management in favor of advantages in the monetary areas (MUNDELL, 1961; MCKINNON, 1963; KENEN, 1969).

According to the understanding of Amado and Mollo (2004), there are two reasons for the defense of monetary integration in the orthodox view of OCA: i) protection of market liberalization and ii) the currency is neutral in the short or long term. In this way, both the mobility of factors and the weight of consumer goods would increase with economic liberalization, currently globalization. These facts are justified, in the opinion of orthodox authors, to encourage monetary integration.

For some post-Keynesian authors, the monetary areas face difficulties, and such areas are related to the liquidity preference among countries/regions and their development levels.

In other words, in times of uncertainty, liquidity is a form of protection, and the interest rate is an instrument capable of making agents renounce liquidity. This result tends to increase regional inequalities and not reduce according to the orthodox theory (OCA) since there will be greater demand for liquidity in less developed regions and protection against more significant uncertainty. This scenario impacts the increase in interest rates, hampering investment and economic growth (AMADO; MOLLO, 2004).

Therefore, to break these vicious circles of increasing inequality, the State would be responsible for coordinating heterodox monetary policies to foster the performance of state-owned banks in such regions. This view is quite skeptical about the advantages of monetary integration. However, it understands that an advance in a regional integration process results in greater financial integration between countries.

A study by UNCTAD - United Nations Conference on Trade and Development (2007) on financial cooperation among developing countries concluded that the best way for these countries would be to create regional mechanisms. Therefore, the higher the degree of integration, the more connected the business cycle between countries, the higher the chances of successful implementation (SARRIERA.; CUNHA; BICHARA, 2010). Thus, economic theory and historical experience show that the viability of monetary integration is conditioned by several factors (ALESINA; BARRO; TENREYRO, 2002):

i. the depth of commercial and financial ties of the countries that make up the proposed integration;

ii. the factor mobility between economies (factor flexibility);
iii. the convergence degree between the economic cycle of these countries (prices, income);
iv. standardized institutional basis regarding fiscal, monetary policies, where the distortions are minimized, avoiding arbitration; and
v. the existence of regional leaders willing to carry out the integration by creating institutional stabilizers to mitigate potential and actual conflicts.

The incentive to create and strengthen regional financial institutions does not mean that we must replace the IMF (International Monetary Fund) as the leading institution in the international monetary system. No regional fund would have the volume of resources such as those of the IMF or the political capacity to articulate rescue plans on a global scale when needed. Besides, many global financial problems go beyond the regional level and require global solutions and proposals.

Regional funds can serve as an essential link between countries and a strengthened and reformed IMF, providing the system with a greater capacity to promote international financial stability. Furthermore, if reform at the international level did not occur, it would be even more justified for Latin American countries to strengthen their lines of defense against financial crises by enhancing regional cooperation (regional funds) (AGOSIN, 2001).

It is essential to differentiate between economic coordination and economic cooperation. Economic coordination is an extension of cooperation, which is just an exchange of information and meetings between countries. Therefore, cooperation would not result in changes in countries' economic policies. However, coordination would be a deeper level of integration, as it assumes that governments must create communication mechanisms and establish standard political guidelines (agreements) (SARRIERA; CUNHA; BICHARA, 2010).

The role of regional cooperation is related to the political mechanisms of a group of countries located in a geographical area to achieve common goals capable of expanding social well-being. It is impossible to achieve such objectives through an individual effort of the countries (BASNET; PRADHAN, 2017). When it comes to definition, the understanding of financial cooperation is related to using mechanisms that facilitate nations 'financing and reduce the countries' external vulnerability (FANELLI, 2008; DEOS; WEGNER, 2010).

In the view of Ocampo (2006), when addressing the issue of financial cooperation, we must divide it into two modalities: i) development financing and ii) macroeconomic and related financial cooperation. Chart 1 presents a summary of the modalities.

Chart 1 | Financial Cooperation Modalities

Development Financing	Macroeconomic and Related Financial Cooperation
Multilateral Development Banks and Related Multilateral Financial Institutions	Dialogues, Consultations and Macroeconomic Policy Supervision
Fiscal Transfers	Liquidity Provision in Times of Crisis
National and Regional Securities Markets	Exchange Policy Coordination

Source: Adapted from OCAMPO (2006).

The modality "Financing for Development" is divided into three categories. The first includes multilateral development banks and related multilateral financial institutions, that is, sub-regional financial institutions: the Andean Development Corporation (CAF), the Central American Bank for Economic Integration (CABEI), and the Caribbean Development Bank (CDB). In the absence of supranational institutions, regional and sub-regional development banks play a fundamental role in integration processes, especially in solving regional problems that require collective action (OCAMPO, 2006). The second model of "Development Finance" refers to fiscal transfers with explicit redistribution goals at the regional level. As an analysis of UNCTAD (2007), it is of utmost importance that integration gains distribution among members of a regional bloc and between their agents is fair. A priori, one could argue that smaller countries and companies would benefit from a broader market. However, the play of free-market forces can accentuate disparities when the initial conditions are uneven. Finally, the third mechanism consists of the development of regional securities markets. In this sense, the development of deeper regional securities markets would help avoid this intermediation, helping to consolidate financial centers. It would also act as a crisis prevention instrument by mitigating it. It would also serve as a crisis prevention tool by mitigating the time lags and currency mismatches in private agents' portfolios.

Regarding macroeconomic cooperation between developing countries, at least two reasons justify macroeconomic collaboration between these countries, especially in emerging economies: (i) the construction of defense walls against financial crises and (ii) the prevention of distortions in competition between export-oriented economies (OCAMPO, 2006).

For the authors Machinea and Rozenwurcel (2006), the procedures for macroeconomic coordination progress gradually, given the complexity of the factors and the need to generate mutual understanding and the necessary confidence. The macroeconomic coordination steps are presented in Chart 2.

Chart 2 | Macroeconomic Coordination Steps

Initial Step - Loose Coordination	**Objective:** trust among members • Information exchange • Supranational technical forum • Investment in institutions • National macroeconomic stability (relevance of the exchange rate and the more prominent members)
Second step - More Demanding Coordination	**Objective:** long-term stability • Institutions to promote fiscal and monetary responsibility, the flexibility of nominal prices, and the mobility of factors. • Goals to achieve convergence: exchange rate, fiscal scenario, inflation, and the external sector: - Establish goals does not mean they will be achieved. - However, the convergence commitment can increase stability.

Source: Adapted from MACHINEA; ROZENWURCEL (2006).

The information exchange between economies is, in a way, an initial modality of cooperation policies, as it allows countries to understand the features and circumstances of others. In summary, the initial step known as loose coordination consists of structured procedures to create trust between members through information exchange, periodic meetings, standardization of statistics, and the creation of supranational forums on policies. (MACHINEA; ROZENWURCEL, 2006).

After the initial step solidification, the second step of macroeconomic coordination is the stability maintenance in the long term, which requires the adoption of more explicit coordination mechanisms, for example: establishing goals for convergence of a set of macroeconomic variables, the strengthening of the fiscal and monetary responsibility policy and finally, the flexibility of nominal prices and the mobility of factors (MACHINEA; ROZENWURCEL, 2006).

4. Regional Asymmetries in Monetary and Financial Cooperation Development

Regional cooperation between countries can generate asymmetric effects between the component regions of these countries. The analysis and study of some authors showed some regional monetary and financial asymmetries between Latin American countries. Regarding the monetary aspect, some studies found asymmetries and pointed to the presence of significant divergences in the trajectory of the main variables: prices (inflation and exchange rates); fiscal (debt-to-GDP ratio); external (foreign trade, absorption of external resources); and actual performance (growth, unemployment) (CUNHA; BICHARA, 2005). Other surveys highlight that this evidence carries a high cost of coordination of macroeconomic policies between countries; these costs constitute a barrier to implementing cooperation policies (FANELLI, 2000).

However, the financial variables are expressed in terms of market size, depth, level of concentration, level of economic openness, the importance of the capital market, and the presence of mechanisms for long-term financing. At the same time, this reflects the current institutional context in each of the systems and the heterogeneity of the economies concerned (DEOS; MENDONCA; WEGNER, 2013). Given these structural asymmetries (monetary and financial) and the lack of coordination among countries, the tendency is to reinforce and increase the differences between nations rather than reducing them (AMADO; SILVA, 2000).

In turn, the political aspect found in almost all countries should not be linked solely to the ideological affinity between governments. By definition, integration transcends governments and should constitute State policy. In practice, however, governments are led by individuals strongly influenced by domestic public opinion since they are elected in democratic processes and depend on the population's approval to renew their mandates (ROSALES, 2011). In other words, a regional integration project is a result of the countries' democratic articulation, political will, which in their diversity, are capable of providing identity and autonomy to the process (GARCIA, 2016). Thus, the authors demonstrate that the implementation and success of regional integration rely heavily on non-economic considerations, policies and politicians' role, and special interests (BASNET; PRADHAN, 2017).

In general, the Latin American countries are trapped in a typical sub-optimal strategy of non-cooperation. This situation gives rise to three different facets, and, in a way, all of them contribute to the sub-optimal conditions. Thus, one can interpret these three facets as further obstacles to regional cooperation (GHYMERS, 2005). These three obstacles are examples coming from monetary, financial, and political aspects already mentioned, such as structural asymmetries, manifested through the prisoner's dilemma, the Latin American centralization syndrome, and the lack of reputation and institutional credibility.

The obstacles can be understood as results of the decisions and measures adopted by each region's countries. Thus, the prisoner's dilemma would be the perception that all parties can realize that collective actions can lead to better economic results for the entire group. However, there are several exceptions at the national level, which translates itself as the failure of cooperation and less desirable results for all the parties involved.

Under Latin American centralization, this obstacle stems from the obsolete and erroneous perception that integration is only a centralization factor. However, regional integration requires transferring certain specific powers from the national level (countries) to the regional level (economic bloc). It is a trend that all integrationist programs in history that aim to centralize decision-making have resulted in a series of resounding failures. This trend also occurs with the coordination of economic policies, often confused with the demand that nations subordinate their responsibilities to supranational organizations or more powerful countries.

The third obstacle, the lack of reputation and credibility, reflects the institutional weaknesses of most countries in the region and most of their national and regional institutions. Latin America suffers intensely from this negative heritage (reputation and credibility) from the past. There is no economy in the region capable of acting immediately as an anchor country (guarantor). Besides, Latin America does not have solid regional institutions capable of giving immediate credibility to supranational commitments; on the contrary, regional commitments suffer from weak institutional compliance procedures and a lack of stable resources, which damages the reputation of regional entities. In an article, Garcia (2016) states that integration, by nature, involves the creation and strengthening of institutions. However, he asks whether Latin American institutions will issue impartial and high-quality analyses regarding the regional evolution from statistical, economic information, risk assessment, and classification point of view.

Thus, we see that regional integration tends to deepen when it is the best strategy available, individually, for each of the States. In other words, despite the consequence of losing autonomy over national policies, or at least part of them, it is argued that the deepening of monetary and financial integration and cooperation between South American countries tends to occur when this is the best option for them despite this lesser autonomy in terms of economic policy.

5. Final Considerations

This article fulfilled the initial objective of presenting and discussing the obstacles that impact the proposals for monetary and financial cooperation in Latin America. Although it is vitally important to further studies on the Latin American countries at the international level, there is a considerable asymmetry between its economic size and its current role in the global monetary system.

The process of regional monetary and financial cooperation is understood as a strategic issue for countries in market globalization and deregulation. States would probably choose to issue their currencies and maintain the autonomy of their economic policies in the ideal world. However, the actual world shows that acting together with other countries may be more advantageous than working individually, from the point of view of the particular interests of each economy. Nations do not choose integration because it is better for everyone, but it is better for themselves.

The crucial issue is that all economies involved must judge integration as the best option individually. As everything that happens has political content, regional integration does not derive from a previous or established theory but from principles of each country and a critical analysis of other experiences throughout history (GARCIA, 2016).

As observed in previous studies (FANELLI, 2000; BICHARA; CUNHA; LÉLIS, 2008; EICHENGREEN, 2010; SARRIERA; CUNHA; BICHARA, 2010), the results obtained in this research suggest that there are high costs for deepening the coordination of macroeconomic policies between the countries of Latin America. These costs are derived from the three obstacles related to monetary, financial, and political issues, which are: prisoner's dilemma, Latin centralization and, reputation and credibility.

At the same time, a more significant commitment to regional integration and cooperation would make it possible to dampen the impacts of a possible worsening of the international scenario and preserve the macroeconomic and social results achieved through progress in shaping an enlarged regional market (DURÁN LIMA; MASI, 2007).

The biggest threat hanging over the progress of regional cooperation is the international financial instability (crises). Such instability significantly increases the exchange rate volatility and internal instability in the region's countries (AGOSIN, 2001). In other words, macroeconomic instability in a fragile environment of national and regional mechanisms to contain the financial crisis hinders the consolidation of a practical integrationist agenda.

Therefore, apart from the world crisis, it is crucial to establish a plan to formulate Latin America's development strategy. This redevelopment's elements should serve as a decisive impetus for socio-economic development, with a firm and depoliticized support for regional integration (OCAMPO, 2020b).

Although these findings are based within the limits of the carried out research, at the end of this work, it remains considerable scope for further development of several issues, in addition to opening a new research agenda. Other research gaps would be: (i) the analysis of the macroeconomic results of Latin American countries in the context of the international financial crisis (ii) the alternatives of convergence and cooperation for the region.

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