

GUATEMALA: ITS EVOLUTION AND TRADE POTENTIAL

presented by

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ABSTRACT

The authors, who have spent considerable time studying and teaching in Guatemala, begin their overview of Guatemala during a time of great economic impact in the country by United Fruit Company (UFC is now owned by Del Monte) of the United States.

They analyze the long and gradual development, spurred by UFC, of Guatemala's agricultural sector to the exclusion of its value-added manufacturing sector.

The resulting build-up of agriculture as the nation's economic engine is proposed by the authors to have been a contributing factor leading to the economy's current low literacy level, low earnings per capita and overall depressed state of human capital.

As the authors bring the economic overview current, they explore the recent economic impact of the Inter-American Development Bank in stimulating the economy toward a higher state of literacy, education, income and economic performance.

INTRODUCTION

Adam Smith believed that under a system of free and unregulated trade each nation should specialize in producing the goods it could produce more efficiently--that is, those goods in which it has an absolute advantage, either natural or acquired.ⁱ

He believed that nations would achieve the greatest gain from trade based upon production within a system of reliance upon absolute advantage, defined in general terms as *the capability of one nation to produce more of a good with the same amount of input than another country employs to produce the same good.*ⁱⁱ

While this paper is not intended to set the stage for a theoretical debate as to the fine points of absolute advantage nor comparative advantage, the point to be made is that Guatemala is in a marginal state of economic prosperity today precisely because of its natural, or absolute, advantages in the agricultural sector:

Guatemala's natural advantages are those that contribute to the continued focus upon production in the agriculture sector:

- year-round mild growing climate,
- fertile land,
- low wage structure among a *field-hand* employee base, and
- predictable rainfall needed for seasonal crop production.

It is no surprise, then, that Guatemala's top three export categories are coffee, sugar and bananas, all commodities, generally unbranded products exported on the basis of price competition in response to price sensitivity among corporate buying specialists.ⁱⁱⁱ

These product categories have little "value added," little or no brand strength to overcome price vulnerability, and the product "standards and grades" are, in reality, established for U. S. buyers by the U. S. Department of Agriculture, not by the sellers in Guatemala.

The Guatemala economy is based upon family and corporate agriculture, which accounts for about two-thirds of all Guatemalan exports.^{iv} About thirty per cent of the country's total exports were destined for the U. S. in 1996.^v

AN OVERVIEW OF GUATEMALA

The country's almost 12 million population base is growing at an annual rate of about 2.5%, a high rate, and typical of a developing nation's growth pattern.^{vi} The population is of mixed ethnicity—Spanish and Amerindian. The majority, 56%, is Mestizo (of mixed Amerindian-Spanish ancestry).

A small number of families and corporations own the largest parcels of land, the largest homes, and control the county's capital base.

EARLY ECONOMIC DEVELOPMENT AND THE UNITED FRUIT COMPANY

The role played in Latin American economies by U. S. policy makers and multinational corporations has been discussed extensively, notably by Adams (1914), Dosal (1960), Karnes (1978), and Schlesinger and Kinzer (1982).

Adams (1914), in describing "the creative enterprises conducted by the United Fruit Company," praised its work. UFC was credited for building the semblance of an economy, educating workers, and providing health care to the country's low- socio-economic workers,

while Adams ignored any degree of potential exploitation of the country and its resources by UFC.

In the same breath, one could both praise and damn UFC for its many years of developing the banana industry in Guatemala, laying railroad lines throughout the country, and for building loading docks to move bananas to customers around the world.^{vii}

One could argue that any interest in the health and welfare of the workers was derived from UFC's end goal of exporting bananas, through a monopolistic distribution system which it controlled, to foreign markets.

While considerable attention was paid by UFC to their health and ability to work in the fields, less attention was given to workers' lack of literacy and chronic lack of basic education.

Its impact as an employer, mentor, landlord and master allowed UFC to set the stage for economic development policy in Guatemala for decades to come.

To this day, the economic profile of the country still carries characteristics of a third-world developing nation with a high birth rate, low literacy level, and lack of infrastructure to support most economic growth not based upon agricultural enterprise.

GUATEMALA'S DEMOGRAPHIC PROFILE

Whether demographic profile determines the economy or economic profile determines the demography, the two profiles have moved in tandem in Guatemala since the early 1900's.

In an agricultural economy, many young strong workers are needed to harvest the crops. With few employment opportunities beyond agriculture, and with the blessing of the Catholic religious leaders, families have continued to be large.

The country's population pyramid (Chart I) is typical of that of a developing nation. The tendency for high birth rates to build a large youthful segment is seen in Guatemala. The US population pyramid (Chart II), on the other hand, is typical of that of a developed nation—one which might have "bulges" at some point, but one which is characterized by a lower birth rate and an aging population.

In nations exhibiting a population pyramid of a developing nation, it is typical that literacy rates and education levels are lower than that of developed nations. Such is true in Guatemala. These demographic characteristics discourage foreign direct investment from multinational corporations seeking more than just low-wage production and a work force that is literate and educated.

The residual income profile of this demographic data is that there is great wealth and economic control in the hands of a few (Chart III). The middle class segment controls little; the lower class segment controls even less. As a result, entry into economic ownership opportunities is limited and most workers are left to remain just that—workers—often at the hands of controlling corporate owners or landlords.

GUATEMALA'S POLITICAL AND ECONOMIC PROFILE

Guatemala is not an economic growth leader in Latin America. Its political strife, 36-year civil war,^{viii} alleged election fraud and still-unexplained disappearances of thousands of protesting citizens have scared away foreign investment, and that has led to slowed economic development as shown below.^{ix}

Guatemala's Economic Growth: 1981-1997

<i>Country</i>	<i>Period</i>	<i>Period</i>
	1981-90	1991-97
Argentina	-2.1	4.2
Bolivia	-1.9	1.6
Brazil	-0.4	1.6
Chile	1.4	6.3
Colombia	1.6	2.2
Costa Rica	-0.6	1.1
Cuba	2.8	-4.3
Dominican Republic	0.2	2.8
Ecuador	-0.9	1.3
El Salvador	-1.4	2.8
Guatemala	-1.6	1.4
Haiti	-2.4	-4.3
Honduras	-0.8	0.7
Mexico	-0.2	1.0
Nicaragua	-3.9	-0.2
Panama	-0.7	2.9
Paraguay	0.0	0.0
Peru	-3.3	3.7
Uruguay	-0.6	3.5
Venezuela	-3.2	1.0

Source: Economic Commission on Latin America and the Caribbean, *Report on the Americas*. March/April 1999, Vol XXXII, #5, page 23.

Guatemala was ranked 14th in growth among the 20 nations listed above for the period 1981-1990, and 11th for the period 1991-1997.

Its continuing absence of a national economic policy emphasizing value-added manufacturing leaves in place its age-old dependence upon the land, agricultural production and the exporting of commodities—unbranded agricultural goods.

The agricultural sector consumed 60% of the nation's productive capacity in 1994, yet accounted for 25% of the GDP. Further, compared to nearby nations in Latin America, it is less likely to generate a favorable GDP level in US\$ (Chart IV). Mexico, as an example, with 28% of its labor force in agriculture, produced a dollar output per agricultural worker of US\$1790; Guatemala's dollar output per agricultural worker for the same period was US\$1462.

On the other hand, Guatemala's industrial sector employs 12% of the labor force but produces 18% of the GDP (Chart V).

RECENT DEVELOPMENTS

A. The Peace Accord signed by the Guatemalan government on December 29, 1996, has been widely hailed as the first step to political and economic recovery from 36 years of civil war. President Alvaro Arzu's economic goal associated with the signing of the Accord was to modernize the economy with the help of peace-related foreign capital inflow.^x

B. The Guatemala government, taking notice of the *maquiladora* program growth in Mexico, has adopted its own *maquiladora* program. It allows “in bond” production, mostly assembly work. The sector has provided jobs for those with skills and literacy in a way that hard manufacturing and basic agriculture have not and cannot in that it is work in a clean environment with payroll being honored at a predictable date and time. In addition, bus transportation is often provided for maquiladora workers from the plant to a central receiving point.^{xi}

C. Foreign direct investment 1986-1991 was an annual average of \$127,000,000, but the specific year FDI was erratic, perhaps in response to political unrest as well as other concerns.^{xii}

D. International trade trends 1991-1997 are reflected in the table below. Over the seven year period documented, imports show a cumulative ratio of 1.69. For every dollar of merchandise exported, the country has imported \$1.69 in value during the period shown.

	Exports*	Imports*
1991	1202	1851
1992	1295	2532
1993	1340	2599
1994	1522	2781
1995	2156	3293
1996	2031	3146
1997	2344	3852
Cumulative Flow	\$11,890	\$20,054
Cumulative Ratio		1.69

Source: International Monetary Fund, *Direction of Trade Statistics Yearbook 1998*.

*shown in millions of US dollars.

E. The country’s recent economic and political stability can be attributed to rule by a center-right government. Oscar Berger, candidate of the ruling National Action Party (PAN) and current mayor of Guatemala City, is favored to win the November 1999 presidential election. Improving the climate for international business is a fragile process, and despite progress in implementing the peace accord with the guerrillas, crime and other social disorder still threaten the business climate (Global Business Newsletter 1999). *The government lacks the capacity to restrict drug dealers and other criminals, and it lacks adequate revenue to fulfill its spending promises. If it falters, the result could be ...a military coup...the climate for business would substantially deteriorate.*^{xiii}

PROGRESS THROUGH AID

Since its inception in 1959, the Inter American Development Bank has made 88 loans totaling \$1,757,000,000 to Guatemala (Inter American Development Bank, 1997).

Typical of the loans made to address the challenges facing Guatemala are the following selected 1997 disbursements:

1. Infrastructure and Investment Sector Reform

Amount: \$107,650,000 in loans and \$1,150,000 in grants

Purpose: To expand coverage, improve service and reduce costs in

the sectors of aviation, telecommunications and electricity.

2. Housing Reform

Amount: \$60,000,000

Purpose: To increase investment in low income housing to improve the equity and efficiency of housing markets for the poor.

3. Education Reform

Amount: \$15,360,000

Purpose: To improve the quality of preschool and primary education through teacher training, educational materials and technical assistance. This project includes activities designed to benefit the country's most vulnerable groups, particularly girls, indigenous persons and the rural poor.

This project supports the educational mandates of the 1996 Peace Accords which emphasized increased education spending, expanded coverage, bilingual education and equity among genders. In particular, it is directed to the fewer than one in five children who attends preschool and the small percentage who attend primary school.

4. Care of Children in Extremely Difficult Circumstances

Amount: \$580,000 in grants

Purpose: To expand social services for street children in Guatemala City, including family reintegration, drug treatment, job training, and assistance for teenage mothers.

Of particular focus in this program are services directed to the more than 5,000 children who live on the streets in Guatemala City and almost 750,000 children living in extreme poverty in the City.

5. Technical Training in Rural Areas

Amount: \$2,880,000 in grants

Purpose: To strengthen the capacity of private training institutions to develop technical training methods which will improve the competitiveness of rural producers or various ethnic groups.

6. Development of a Securities Registry for Capital Markets

Amount: \$1,550,000 grant

Purpose: To strengthen the Registry, created by the Ley de Mercados de Valores approved in 1996, which was created to bring oversight and greater transparency to the presently unregulated over-the-counter market.

7. Private Participation in Civil Aviation

Amount: \$1,150,000 in grants

Purpose: To provide and extend coverage of services in civil aviation sectors by attracting technical and operational capacity and mobilizing financing and private sector resources.

CONCLUSION AND POLICY NEEDS FOR MOVING FORWARD

Specific needs are identifiable in the economy in order to promote the development of the social fiber and the production sector of the country.

A. Literacy: With only about 56% of the population over age 15 who can read and write, literacy development is critical.

B. One language for trade: Only 60% speak Spanish and the remaining 40% speak some 23 Indian dialects. Preserving language heritage is important; developing a language for trade is critical.

C. Unemployment: Official unemployment rates reported are usually below 5% but underemployment may reach as much as 50% of the population. Employing the unemployed and underemployed in higher paying, value-added manufacturing jobs is important.

D. Confidence: Investor confidence is weak because of political instability concerns and because of the low level of literacy in the work force. Promoting investor confidence is important as a part of the plan to attract foreign capital.

E. Migration: Seeking jobs, the citizens leave. The net out migration rate in 1997 was estimated to be (2.04) migrants per 1,000 population--more people are leaving than are coming into the country (CIA 1998).

F. Birth Rate Pressures: Economic pressures created by the high birth rate are such that unachievable new job creations are needed each year in order to maintain a semblance of employment to stave off militant uprisings from a population striving to put food on the family table (Chart VI).

G. Conversion of the Economy: Developing an economic policy for converting the labor force away from heavy dependence upon agriculture and toward employment in value-added manufacturing is important for raising rates. Only manufactured goods with their branding promotional potential can create a buyer brand loyalty among foreign buyers to ease the price pressure on agricultural exports.

H. Infrastructure: Development of railroads, telecommunication systems, the stock market capital formation system, and other systems fundamental to a developing economic plan—these are critical elements which should be addressed at the national policy level.

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FOOTNOTES

ⁱ See “Jousting for Advantage.” *The Economist*, September 22, 1990, pp. 5-39.

ⁱⁱ See a general discussion of international trade theory in Donald A. Ball and Wendell H. McCullough, Jr., *International Business: The Challenge of Global Competition*, Sixth Edition (Richard D. Irwin, 1996), pp. 72-113.

ⁱⁱⁱ For a complete examination of the country’s profile, see the CIA World Factbook page on Guatemala at <http://www.odci.gov/cia/publications/nsolo/factbook/gt.htm>

^{iv} Ibid.

^v Ibid.

^{vi} Ibid.

^{vii} For a history of banana growing in Guatemala, see *Banana Republic: The United Fruit Company*, <http://www.mayaparadise.com/ufc1e.htm>, (Rio Dulce).

^{viii} See an extensive review of the “Recommendations of the UN Commission for Historical Clarification” of the civil war in *NACLA Report on the Americas*, Volume XXXII #6, (North American Congress on Latin America, May/June 1999).

^{ix} For a discussion of political freedom around the world and its relationship to economic development, see the *1999 Index of Economic Freedom* published by The Wall Street Journal.

^x See an overview of economic activity associated with the signing of the Peace Accord in *Doing Business with Latin America*, (Kogan Page Ltd., London N1 9JN).

^{xi} For a daily monitoring of work-related issues, see Guatemala Weekly (in English) at <http://www.pronet.net.gt/~gweekly/>

^{xii} A more complete set of data of FDI in Guatemala and its neighbors may be found in the annual *World Investment Report*, published by the United Nations.

^{xiii} *Political Risk Letter*, Volume XX, # 12, (PRS Group, December 1, 1998).

Chart I

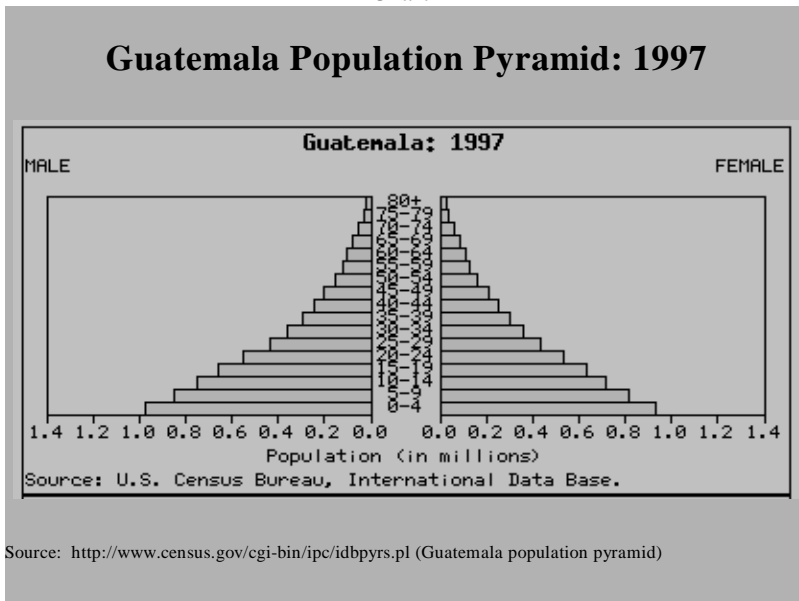


Chart II

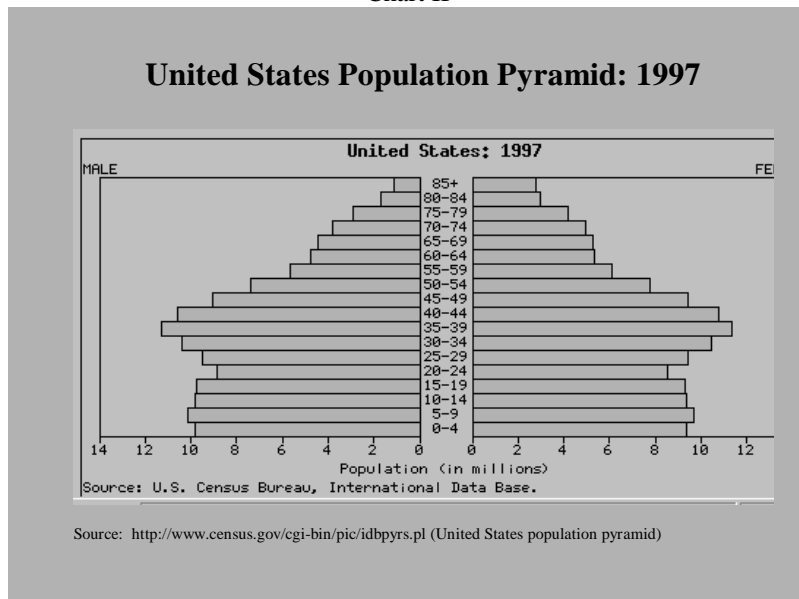


Chart III

Income Distribution Of Selected Nations: 1997

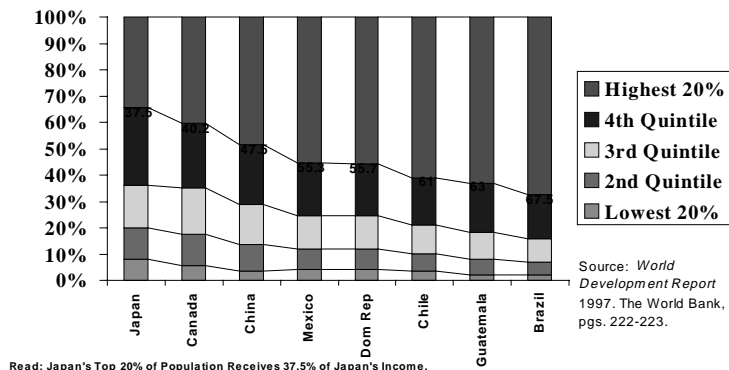
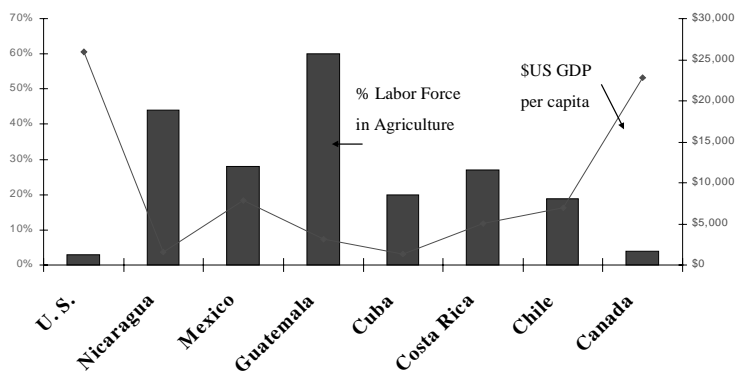


Chart IV

Relationship of Labor Force in Agriculture to GDP per capita: 1994



Source: CIA World Fact Book, 1995. <http://www.odci.gov/cia/publications/>

Chart V

Percentage Labor Force in Industry & Industry % of GDP: 1994

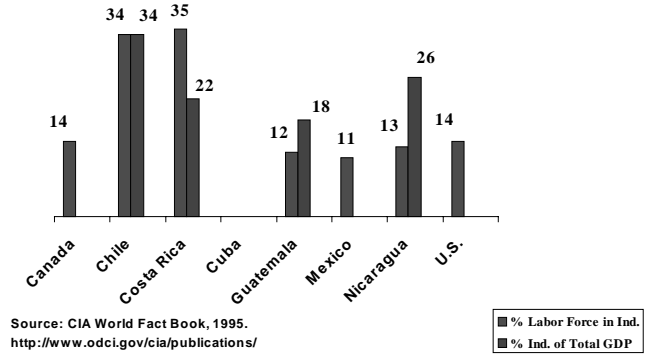


Chart VI

Years for Population to Double

