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ISSUE BRIEF

The Role of the Private Sector in Catalyzing Inclusive Economic Opportunities in the Northern Triangle

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INTRODUCTION

As in every democratic country in the world, the private sector in Central America's Northern Triangle (Guatemala, Honduras, and El Salvador) has a central role in generating employment, driving economic growth, and spurring innovation. But in a region plagued by one of the highest levels of economic informality, weak government institutions, and pervasive corruption, private enterprises—both decades-old industry behemoths and newer startups—can have a more positive influence in steering the Northern Triangle toward inclusive and sustainable economic development. This is not to say that business leaders in Guatemala, Honduras, and El Salvador have been absent in unlocking growth and innovation in the countries, especially since the end of the civil wars in the late 1990s. But in this unique moment of global crisis and renewed attention from the United States, the Northern Triangle's private sector should seize the opportunity to further position itself as a committed, trusted partner and galvanizing force for positive change.

Seeking to address the root causes of unauthorized migration to the United States—including lack of quality economic opportunities, weak rule of law, and violence—the Biden administration's four-year, $4-billion plan for the Northern Triangle seeks to implement a whole-of-society approach to improve the living conditions of Guatemalans, Hondurans, and Salvadorans. The plan comes at a time when Central America, already reeling from structural institutional challenges to its ability to govern and improve its economies, grapples with the effects of the COVID-19 pandemic and two back-to-back hurricanes. As conditions deteriorate on the ground and create additional push factors for would-be migrants, the US government should devote special energy and attention to laying the groundwork for strategic partnerships with private sector actors who are positioned—despite contending with pandemic-induced burdens of their own—to catalyze economic opportunities for their fellow citizens. The business community can be a pivotal player in long-term change that seeks to improve the rule of law, tackle corruption, and open new opportunities for inclusive economic growth.

This issue brief takes a deep dive to unpack why a lack of sustained and inclusive economic opportunities—among the three main drivers of unauthorized migration—have eluded the Northern Triangle and how the private sector can help reduce informality, invest in employment-generating sectors, resolve the human capital paradox, and catalyze greater infrastructure investment and digital connectivity.[1] While there is an emphasis on high levels of informality causing economic insecurity, it is also true that economic insecurity and lack of investment in economic development also drives informality.

This is the first of three issue briefs as part of the Adrienne Arsht Latin America Center's latest Central America initiative, in partnership with the DT Institute, to inform and mobilize key stakeholders at the national, regional, and international levels behind new policy solutions to tackle the Northern Triangle's most pressing issues. This issue brief is the outcome of a meeting with the Center's Northern Triangle Advisory Group, which met in February 2021, and will meet regularly during the first six months of 2021 to help inform the three issue briefs.

FORMALIZING THE NORTHERN TRIANGLE ECONOMIES: HOW CAN THE PRIVATE SECTOR HELP?

The Challenge: According to official government data from Guatemala, Honduras, and El Salvador, the pre-pandemic average unemployment rate in the Northern Triangle was relatively low, at 3.9 percent in 2019, eight percentage points lower than that of Costa Rica.[2] So, why are sustainable economic opportunities lacking in the Northern Triangle when the unemployment rate is less than that of a soon-to-be Organisation for Economic Co-operation and Development (OECD) country? While more than eight million people of the total (active) labor force are calculated to be formally employed, around 60 percent—higher than the average across Latin America—have informal, low-quality jobs with no safety net.[3] In Guatemala and Honduras alone, four in five people work as street vendors, as domestic workers, in unregistered microenterprises, in service sectors (mainly restaurants or hotels), and in agriculture.[4] These low-paying jobs are insecure, inconsistent, often involve long hours in poor working conditions, and barely provide for basic family needs. As nontaxable employment, informal work cannot guarantee access to government pensions or credit from financial institutions.

Informal jobs in the Northern Triangle are also highly vulnerable to minor demand shocks, climate disasters, and, most recently, the health effects of a pandemic and the stringent measures used to combat it. Due to lockdowns, curfews, and restrictions on public gatherings, informal workers—most of whom cannot afford to work remotely—have been unable to generate income. One consequence: the skyrocketing rise in food insecurity

1 Seven of every ten migrants—74 percent—list economic reasons as one of the main motivations behind their decision; this is a stronger reason for migrants from Honduras (75 percent) and Guatemala (87 percent) than for those from El Salvador (68 percent). See Emmanuel Abuelafla, Giselle Del Carmen, and Marta Ruiz-Arranz, In the Footprints of Migrants: Perspectives and Experiences of Migrants from El Salvador, Guatemala and Honduras in the United States, Inter-American Development Bank and the US Agency for International Development, 2019, https://publications.iadb.org/publications/english/document/In-the-Footprints-of-Migrants-Perspectives-and-Experiences-of-Migrants-from-El-Salvador-Guatemala-and-Honduras-in-the-United-States.pdf.

2 Statista, "Unemployment Rate in Latin America and the Caribbean in 2019 and 2024, by Country," Statista, April 2019, https://www.statista.com/statistics/1009557/unemployment-rate-latin-america-caribbean-country/.

3 Statista, "Latin America & the Caribbean: Employed Population Share by Status and Country 2019," Statista, November 2019, https://www.statista.com/statistics/862286/distribution-employed-population-status-latin-america-country/.

4 Susana M. Sanchez, Kinnon Scott, and J. Humberto Lopez, "Guatemala: Closing Gaps to Generate More Inclusive Growth," World Bank, 2015, http://documents1.worldbank.org/curated/en/425151468327849352/pdf/106770-REVISED-PUBLIC-GTM-Report-English.pdf, 109, and "Informal Economy Diagnosis: The Commercial Sector in the Northern Triangle: El Salvador, Honduras y Guatemala," International Labor Organization, 2020, http://www.oit.org/wcmsp5/groups/public/---americas/---ro-lima/---sro-san_jose/documents/publication/wcms_752182.pdf.

across the region, which became even more dire with the destruction of one hundred thousand hectares of crops during the 2020 Atlantic hurricane season. In Guatemala, the number of households with insufficient food during the pandemic nearly doubled compared with pre-pandemic levels, and in Honduras, food insecurity increased by more than 50 percent.[5]

A swollen informal economy in the Northern Triangle has created a vicious cycle that is partly responsible for the lack of inclusive economic advancement, and for productivity levels among the lowest in the world.[6] Guatemalan and Honduran informal sector jobs do not pay much-needed income taxes, thereby further cash-strapping national governments that were already struggling to provide quality public services before they had to mitigate the effects of the coronavirus pandemic and the hurricanes. Regional estimates from the United Nations Economic Commission for Latin America and the Caribbean indicate that the Northern Triangle loses billions of dollars in fiscal revenue due to the high levels of informality. In a region where the average poverty rate surpasses 30 percent,[7] lack of quality public services and social protections for the most vulnerable populations increases social inequality and widens the wealth gap.

How the Private Sector Can Help: A more engaged private sector is not a panacea for eliminating informality in the Northern Triangle, but private businesses can apply lessons learned from other countries in Latin America and the OECD, and collaborate with the public sector to take low-cost, high-reward steps that can help pave the way for job formalization. Employers can take a more proactive approach and leadership role in the following three areas: working with governments to design and execute active labor market policies (i.e., workforce training, apprenticeships, employability courses, labor counseling, and job matching), helping the informally self-employed and jobseekers navigate through administrative costs and requirements for conducting formal work, and participating in civil society–led pledges that commit businesses to support formalization of their own supply chains and clients. To effectively promote private sector leadership in tackling informality, governments and civil society can provide the right mix of incentives, including through tax exemptions and benefits associated with corporate social responsibility.

People shop at a fresh produce market during the outbreak of the coronavirus disease (COVID-19), in Guatemala City, Guatemala. Picture taken on May 21, 2020. A large informal economy in the Northern Triangle has created a vicious cycle that is partly responsible for the lack of inclusive economic advancement, and for productivity levels among the lowest in the world.
Source: REUTERS/Luis Echeverria

Active labor market policies (the combined set of government programs to aid the unemployed and boost formal employment) have had limited success across Latin America, but case studies from formalization and vocational training programs in Argentina and Colombia offer lessons learned for similar policies implemented in the Northern Triangle.[8] Despite the obvious country differences, both programs can offer best practices for implementing incentives that boost participation based on the specific labor and productivity needs of the Northern Triangle countries and establishing a framework for evaluating the programs' impacts. Private companies in Guatemala, Honduras, and El Salvador—especially industry leaders in manufacturing, logistics, energy, agriculture, biomedical production, and

5 World Food Program, "Battered by Climate Shocks and Bruised by Economic Crisis Millions More in Central America Face Hunger," World Food Program, February 2021, https://www.wfp.org/news/battered-climate-shocks-and-bruised-economic-crisis-millions-more-central-america-face-hunger.

6 Among the worst-performing countries with the lowest informal labor productivity relative to formal labor productivity are located in Central America: There are 6.9 informal sector workers to 1 formal sector worker in Guatemala. The ratios are 8 to 1 in Nicaragua and 14 to 1 in Honduras. See International Labour Organization, "Tackling Vulnerability in the Informal Economy," Organisation for Economic Co-operation and Development, 2019, https://www.ilo.org/wcmsp5/groups/public/---ed_protect/---protrav/---travail/documents/publication/wcms_711804.pdf.

7 Inter-American Development Bank, The IDB Group in the Central American Isthmus and the Dominican Republic, Activities Report 2019, 2020, https://publications.iadb.org/publications/english/document/The_IDB_Group_in_the_Central_American_Isthmus_and_the_Dominican_Republic_Activities_Report_2019.pdf.

8 International Labour Organization, "What Works: Active Labour Market Policies in Latin America and the Caribbean," International Labour Organization, 2016, https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_492373.pdf

information technologies—can cooperate with governments to provide buy-in for the design, implementation, and monitoring and evaluation of job training schemes and microenterprise entrepreneurship programs. To minimize the potential pitfalls of such programs, private sector participation can help identify gaps in the labor market for the unemployed or informally employed, ensure that a large portion of spending for the programs is directed to training for sectors that add to overall productivity, and guarantee that the programs meet specific objectives for increasing formal employment and building core skills rather than being used for one-off public sector projects. Private sector participation should be coupled with civil society initiatives and input to ensure that historically marginalized population groups in geographical areas known for would-be migrants, such as secondary cities, will benefit.

Employers—both existing and new businesses—can also be more proactive in guiding jobseekers and individuals running their own informal businesses through complex tax forms and extensive bureaucratic processes. But to do so, incentives for all parties must be aligned. Governments seeking to promote formalization can offer temporary tax benefits to new ventures or existing firms that will partner with fiscal agencies to promote formalization in their own supply chains and commit to delivering their products or services to clients who are formally registered or employed. To ensure sustainability and minimize reliance on government, civil society organizations such as think tanks and universities (both at the national and international levels) can organize pledging conferences that seek active participation from companies to formalize their business lines as part of a broader effort to promote stronger social responsibility reputations in the private sector. In Guatemala, local think tank Fundación para el Desarrollo's "Cruzada por la Formalización"—Crusade against Informality—can offer early indicators of success and lessons learned for formalization efforts in the Northern Triangle.

KEEPING UP WITH TALENT: HOW CAN THE PRIVATE SECTOR HELP?

The Challenge: As identified in a previous Atlantic Council report, Central America's demographic bonus represents a limited-time opportunity that the United Nations forecasts will disappear by 2050.[9] While a young national population does not automatically translate into a young and skilled workforce, a young population that contributes to the economy is a prerequisite for creating a skilled workforce for decades to come. In each of the Northern Triangle countries, only about a quarter of the potential labor force has completed upper secondary school, and only about one in ten has completed any type of tertiary education.[10] Thus, the region has limited time to double down on policies that will ensure a full capture of its human capital potential. But research by the World Bank shows that, over the last few years, the more-skilled labor has been most likely to migrate.[11] This trend puts key stakeholders in a difficult position: Why invest in workforce training for higher-quality jobs if workers will take those skills elsewhere?

If the countries and the private sector are unable to align job opportunities with a growing set of skilled workers—and are unable to attract country-wide (much less regional) large-scale and labor-intensive investments—there is little incentive for investment in the national workforce. In this vicious cycle the private sector lacks the tools and ability to increase productivity and improve the region's competitiveness. This human capital paradox where worker skills are quickly outgrowing the job market continues to contribute to the region's brain drain—a loss of much-needed skills and talent for Northern Triangle economies. Finding sustainable solutions to the misalignment of offer and demand in the labor market must be a shared priority across sectors and industries in the three countries.

9 María Eugenia Brizuela de Ávila, Laura Chinchilla Miranda, María Fernanda Bozmoski, and Domingo Sadurní, "Central America Economic Reactivation in a COVID-19 World: Finding Sustainable Opportunities in Uncertain Times," Atlantic Council, September 2020, https://www.atlanticcouncil.org/in-depth-research-reports/issue-brief/central-america-economic-reactivation-in-a-covid-19-world-finding-sustainable-opportunities-in-uncertain-times/.

10 Liliana D. Sousa and Andrés García-Suaza, Remittances and Labor Supply in the Northern Triangle, World Bank, September 2018, http://documents1.worldbank.org/curated/pt/946781540836424906/pdf/131471-NWP-172-Remittances-and-Labor-Supply.pdf.

11 Giselle Del Carmen and Liliana D. Sousa, "Human Capital Outflows: Selection into Migration from the Northern Triangle," World Bank, 2018, https://openknowledge.worldbank.org/bitstream/handle/10986/29368/WPS8334.pdf?sequence=1&isAllowed=y.

Honduran migrants walk toward El Florido border crossing point to return to their country after Guatemalan security forces cleared a road where they were camping after authorities halted their trek to the United States, in Vado Hondo, Guatemala. Picture taken on January 18, 2021. The region has limited time to double down on policies that will ensure a full capture of its human capital potential. But research by the World Bank shows that, over the last few years, the more-skilled labor has been most likely to migrate. Source: REUTERS/Luis Echeverria

How the Private Sector Can Help: In any growth-oriented and innovative economy, training (through active market labor policies mentioned in the previous section or directly from private businesses) and education must be accompanied with compatible and attractive opportunities in the job market. Jobs must evolve with the growing skills of workers, and the market must be nimble enough to adapt to an increasingly sophisticated workforce. Private sector alliances with the government and public universities or educational institutions can go a long way. Specifically, the private sector can commit to guaranteeing jobs for reskilled workers as it is in the best economic interest of businesses to retain employees. Government, educational institutions, and the private sector—including chambers of commerce and business councils—must all be at the table to determine the economy's needs and gaps. In a context of weak labor demand, a low-skilled workforce, and high informality, labor force participation is especially low for women. Hence, any public-private partnership must include a gender lens. For example, support with childcare—on-site or through subsidies—could help more women seize these opportunities. Costa Rica's CEN CINAI program is an example of this. Multilaterals and the international community may also play an important role in this alliance by providing technical assistance and loans and sharing best practices from around the globe.

Likewise, recent trends in supply chain reconfiguration may offer a window to disrupt and break away from conventional educational models that may be too lengthy and unrealistic for a region where many citizens are looking for a way to make a living as soon as possible. In this respect, governments at the national and local levels can work to offer vocational training earlier in life, with programs that prepare men and women for labor-intensive positions or help them create their own businesses. These institutions may have agreements in place with companies to churn out workers who reach different specialization levels for jobs in customer service, information technology, or other industries. If a harmonized regional framework existed, the region could build an extensive, large-scale value chain that could greatly foster the Northern Triangle's competitiveness.

PREPARING THE NORTHERN TRIANGLE FOR THE 21ST CENTURY ECONOMY: HOW CAN THE PRIVATE SECTOR HELP?

The Challenge: National and international investors, the private sector, and multilaterals have long seen the infrastructure (energy and transport, specifically) and digital sectors in the Northern Triangle as having the largest potential for generating regional economic opportunities through increased connectivity, access to new and scalable markets, and improved overall competitiveness. The development of transport infrastructure is critical to connect isolated towns and provide them with access to the global market, especially in Guatemala –most recently ranked at the bottom of the World Bank's 2018 Logistics Performance Index.[12] Given the existing bilateral trade agreements, increasing commercial integration, and close cultural ties among Northern Triangle countries, efforts that enhance regional connectivity are not beyond reach. But investment in large-scale infrastructure has been significantly limited in the Northern Triangle, both at the national and intraregional levels. In Guatemala alone, the International Monetary Fund calculated that the country must raise infrastructure expenditure to at least 15 percent to reduce poverty and increase economic opportunities.[13]

A worker walks past newly installed solar panels at the Honduran Solar Energy Company SA (COHESSA) and Solar Power SA (Soupy) solar power plant in Nacaome, Honduras. Picture taken on May 12, 2015. The Biden administration's regional plan intends to focus on large-scale energy projects, but private business leaders in this sector must work together toward a shared regional vision, overcome short-term political agendas, and commit to the highest transparency standards.
Source: REUTERS/Jorge Cabrera

From politics and policy to mismanagement and corruption, there are many reasons infrastructure investment has been limited, including insufficient fiscal revenue due to tax evasion and informality. According to the World Bank's Doing Business 2020 report, the three Northern Triangle countries rank lower than 90 of 190 countries studied worldwide.[14] Among thirty-two of their Latin American neighbors, Guatemala, Honduras, and El Salvador received a significantly lower collective ranking on contract enforcement at 30, 27, and 21, respectively. Dealing with construction permits and protecting minority investors are also top challenges for the three countries, especially for Honduras, which performed the lowest overall among Northern Triangle countries. Taken together, these indicators reflect a business environment in need of improved regulatory frameworks, safeguards against graft, and stronger transparency requirements. By taking serious steps in generating a more business-friendly environment, the Northern Triangle will not only be more attractive for investment in infrastructure, but also ensure the full and efficient execution of critical projects in this sector.

How the Private Sector Can Help: The Northern Triangle private sector can position itself as an indispensable partner to the Biden administration for transformative infrastructure projects in the region. Leveraging existing projects in energy and infrastructure funded by the US International Development Finance Corporation in the three countries—including $1 billion commitments in Honduras and Guatemala—would be an important step in this process. But any new partnerships under the Biden administration's regional strategy will require that capable partners not only demonstrate their commitment to abiding by the rule of law, but also take actions to implement anti-corruption measures, integrate climate-mitigating strategies beginning at project inception, and prioritize efforts that directly benefit Indigenous communities as well as rural populations most likely to migrate. One first step to consider for interested private sector companies in each Northern Triangle country is collectively organizing a road show (both virtual and in-person) to Washington, DC, to publicly demonstrate their commitments to guaranteeing transparency and fighting

12 Maria Fernanda Bozmoski and Pablo Reynoso. "Transport infrastructure in southern Mexico and Guatemala: A step toward development," New Atlanticist, October 25, 2019, https://www.atlanticcouncil.org/blogs/new-atlanticist/transport-infrastructure-in-southern-mexico-and-guatemala-a-step-toward-development.

13 International Monetary Fund, "Guatemala: More Investment and Social Spending Needed," International Monetary Fund, June 8, 2018, https://www.imf.org/en/News/Articles/2018/05/30/NA060118-Guatemala-More-Investment-and-Social-Spending-Needed.

14 World Bank Group, "Doing Business 2020," World Bank, 2020, http://documents1.worldbank.org/curated/en/688761571934946384/pdf/Doing-Business-2020-Comparing-Business-Regulation-in-190-Economies.pdf

corruption in infrastructure projects. With increased visibility, this could, at the very least, pave the way to build confidence between US-based and international investors and in-region businesses operating in the infrastructure sector.

A second step would be to identify regional infrastructure efforts with the best potential to impact the most people—and especially the most vulnerable populations in the three countries. One such ongoing initiative is the Central American Electrical Interconnection System, an ambitious program set out by Central American countries (including Panama) to develop their power infrastructure and create an energy-integrated market that could be more efficient and attractive for new investments. The project envisioned the creation of the Regional Electricity Market (MER in Spanish), which was completed in 2014. However, several deficiencies have emerged since, including a lack of clarity in the sector's development strategy.[15] The Biden administration's regional plan intends to focus on large-scale energy projects, but private business leaders in this sector must work together toward a shared regional vision, overcome short-term political agendas, commit to the highest transparency standards, and develop dispute-resolving mechanisms that provide predictability and certainty to all parties involved.

The same applies for a regional digitization policy that has gained renewed urgency in the context of the coronavirus pandemic. The private sector is positioned to lead—with public sector and multilateral collaboration—in the development of an innovative digital agenda that promotes the region's competitiveness and helps fight corruption.[16] This is a challenge, since most rural areas in the Northern Triangle do not have access to information technologies or the internet. Digitization, however, would also help micro, small, and medium-sized businesses and the agricultural sector (which provides more than 60 percent of employment) by presenting them with commercial opportunities beyond their immediate markets through the use of e-commerce and online applications. Broad digitization can also broaden the access to loans and financing through financial technology (fintech) applications, cryptocurrency, and other innovative forms of alternative finance.

IN SUMMARY: WORKING TOWARD A SHARED VISION FOR SUSTAINABLE ECONOMIC OPPORTUNITIES IN THE NORTHERN TRIANGLE

Reducing informality, strengthening human capital, and generating confidence that can draw regional infrastructure investment are only three key areas where the Northern Triangle private sector can lead and—always in collaboration with governments and civil society—help create economic opportunities and improve living conditions in the region. To do so, the Biden administration can be a catalytic partner that can galvanize support from a broad spectrum of regional and international players, from multilateral regional institutions and international financial organisms to in-region civil society leaders and youth organizations. Below are two concluding opportunities for US government engagement with the Northern Triangle private sector:

- **Develop a shared vision for economic advancement.** This is not a new task for President Biden. This is as important today as it was back in 2014 when, as vice president, he led the Plan for the Alliance for Prosperity in the Northern Triangle. In this new global context, the Biden administration must apply lessons learned from that program, plan for contingencies, and ensure sustainability by building long-term trust with the regional private sector. Importantly, a shared vision must include a common understanding of what success looks like and how strategic engagement can work toward that goal. Beyond the business perspective, the administration must leverage its convening power to include voices and participation from civil society groups in the Northern Triangle, with a special focus on integrating the economic development visions of Indigenous peoples in the region (44 percent of Guatemalans self-identify as Indigenous).

- **Establish clear anti-corruption and transparency standards for economic opportunity partnerships.** Corruption manifested in all its forms has hindered progress in the region for too long; the fight to reduce it must include advancing on parallel efforts that can address US national

15 Maria Andrea Higueros Trujillo, "Integrating the Power Sector in Central America: Myths and Realities," Italian Institute for International Political Studies, October 23, 2019, https://www.ispionline.it/en/pubblicazione/integrating-power-sector-central-america-myths-and-realities-24234.

16 Matthew Rooney, "Fighting Coronavirus with Digitization in Central America," The Bush Institute, April 8, 2020, https://www.bushcenter.org/publications/articles/2020/04/fighting-coronavirus-with-digitization-in-central-america.html.

security interests. The Biden administration should establish and clearly communicate the anti-graft standards that it will require from potential private sector partners in economic opportunity efforts. The administration's Central America plan is rightfully prioritizing the fight against corruption transversely across its regional engagements. But to ensure viability and sustainability, the administration must ensure that this conversation includes buy-in, not only from the private sector, but also from civil society organizations that have been on the ground and have a more nuanced perspective for how to understand corruption in the region and how to fight it. Clear anti-corruption and transparency standards are an important consideration for potential foreign investors; without certainty or rules, it will be hard to attract any significant or transformative levels of foreign direct investment.

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Northern Triangle Advisory Group members have provided critical insight and ideas as part of the drafting of this issue brief. Findings and recommendations of this brief, however, do not necessarily reflect the personal opinions of the individuals listed below or the organizations to which they are affiliated.

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