

# Inter-American Dialogue

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Subscribers may pose questions to the Board of Advisors for the Featured Q&A by contacting the Editor at [rsimpson@thedialogue.org](mailto:rsimpson@thedialogue.org)

### Featured Q&A With Our Board of Advisors

**Q** Brazilian President Luiz Inacio "Lula" da Silva last week authorized a modest 20-real increase in the monthly minimum wage, a positive signal of Lula's fiscal discipline for most investors while a disappointment to labor groups that had sought a larger increase. How much more do you foresee Lula raising the minimum wage over the remainder of his term? Do you see him coming close to his campaign promise of doubling the minimum wage in the four years of his presidency? How much more of an increase can Brazil sustain over the next two years?

**A** Board Comment: Michael Gavin: "While political pressure to maintain the purchasing power of the minimum wage will likely put a floor on future adjustments, there is little or no room for substantial increases in the minimum wage beyond this. The fiscal consequences of a big upward adjustment cannot be borne when the social security deficit is as large and is growing as rapidly as is now the case. Moreover, higher minimum wages would further discourage formal-sector employment—already overtaxed by a high and inefficient tax regime, a burdensome regulatory structure, and weaknesses in public infrastructure. Room for further increases in the minimum wage must be 'earned' through productivity growth and fiscal adjustment—neither of which is going to happen overnight."

**A** Guest Comment: Albert Fishlow: "Lula's decision to fix the new minimum wage at 260 reais was not an easy one for him: it has provoked negative reaction not merely within the unions, but also within the Congress. That number affords only a small real increase since last year, and makes clear that Brazil remains committed to Finance Minister Antonio Palocci's strategy of macroeconomic realism. There is no way Brazil is going to have minimum wage of 400 reais in two years—unless there is a totally unexpected return to infla-

*Continued on page 4*

### PHOTO OF THE DAY



US President George W. Bush's special envoy for Latin America, Otto Reich, will resign his post, effective June 1, to return to the private sector. See related story on page 2.

Source: BBC

### Inside This Issue

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## NEWS BRIEFS

**Caracas Inflation Slows to 1.3 Percent in April**

Consumer prices in the Caracas, Venezuela metropolitan area rose 1.3 percent in April, down from 2.1 percent in March and 1.7 percent in April 2003. For the first four months of the year, inflation stood at 7.8 percent. Core inflation in April was 2.0 percent, versus 3.6 percent in March. Roughly a fifth of Venezuela's population of 25 million live in Caracas.

Source: Central Bank.

**Mexico to Allow Pensioners to Invest in Foreign Securities**

Mexican pension fund regulator Consar said Monday it would allow pensioners to expand their investment options to include foreign corporate and government securities. Pensioners will be able to indirectly invest up to 20 percent of their assets in foreign securities. Consar said allowing pensioners to diversify their investment portfolios would result in increased returns. The new investment options should become available in 6-7 months. Mexican pension funds were managing \$37 billion at the end of last year.

Source: Consar, Reuters.

**Banco Itau, MoneyGram Launching Money Transfer Service**

Brazil's **Banco Itau** said Monday it had joined with **Viad Corp.**'s **MoneyGram** to launch money transfer services. The service is aimed at some 4 million Brazilians who live abroad and send an estimated \$4.6 billion to family members back home in Brazil annually. Customers will be able to send money from any of 56,000 MoneyGram points of service in 155 countries to any of Itau's 3,000 branches in Brazil.

Source: Reuters.

## Political News

**Otto Reich To Resign as Special Envoy to Latin America**

Otto Reich has announced his planned resignation from his position as the White House's special envoy for the Western Hemisphere, effective June 1, *El Nuevo Herald* reported Monday. The news comes as President George W. Bush receives a controversial policy proposal by the Commission for a Free Cuba, of which the hard-line Cuban-American Reich is a member. The proposal recommends limiting Cuban-American travel to the island and significantly reducing remittances. According to *El Nuevo Herald*, Reich sent

that we have downgraded the post of ambassador," Luis Ernesto Derbez told local radio. On Sunday, Mexico said it was recalling its ambassador and expelled Cuba's envoy to Mexico after Cuban President Fidel Castro gave a speech on Saturday criticizing Mexico's support last month for a United Nations censure of Cuba for human rights violations. Castro said Mexico's world prestige had "turned to ashes" as a result of its support for the UN censure. Derbez said Mexico was caught off guard by Castro's remarks. "It was a surprise for us. We understand that we have had differences about certain issues in particular but we have had these differences for three years," he said, although adding that "the diplomatic

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News of Reich's resignation comes as President George W. Bush receives a controversial policy proposal by the Commission for a Free Cuba.

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an e-mail to friends and colleagues on Sunday stating that he "has to return to the private sector because of personal financial situations." Reich's departure may also be related to his hard stance on Venezuelan President Hugo Chavez, according to the newspaper. An unnamed source cited by *El Nuevo Herald* said powerful economic interests are pushing for less hostile relations with Chavez's populist government. "With Reich in the position of the president's special envoy to Latin America, it was going to be very difficult, because he's not seen well by the Chavistas," the source was quoted as saying. Reich was named special envoy in January 2003 after the Senate refused to confirm him as assistant secretary of state for the Western Hemisphere.

**Mexico Still Open to Dialogue with Cuba - Foreign Minister**

Mexico's foreign minister said Monday that despite his country's withdrawal of its ambassador to Cuba and accusations of Cuban interference in Mexican politics, Mexico was still open to dialogue with Cuba, Reuters reported. "There is no rupture. All the channels are open, all the relationship is normal. The only exception is

channels are open." Peru also recalled its ambassador to Cuba after Castro attacked Peru's president in Saturday's speech. Relations between Cuba and Mexico—once friendly—have been at an all-time low during Mexican President Vicente Fox's term in office. Mexican Interior Minister Santiago Creel has also said two members of the Cuban Communist Party's central committee had been "carrying out activities incompatible with their status" in Mexico, and suggested their meetings with Mexico City government officials last month were an attempt to meddle in Mexican politics.

**Week-Long National Strike in Bolivia off to a Weak Start**

The first day of a planned week-long national strike in Bolivia to protest government policies caused only minor disruptions in the South American country on Monday, *The Miami Herald* reported. Participants in the strike, which include members of Bolivia's Workers Union and Aymara Indians, fell short of their goal of shutting down the capital, La Paz, leading Bolivia's Foreign Minister Juan Ignacio Siles to declare the strike a failure. "The public's response has been a clear rejec-

tion," Siles stated. "A strike only creates uncertainty and a lack of confidence in the country's future." President Carlos Mesa, who took over last October after violent protests forced former President Gonzalo Sanchez de Lozada to resign, helped diffuse the strike's impact by declaring the country would observe the May Day holiday on Monday, instead of Saturday.

## Economic News

### IMF Not Worried About Brazil's Compliance with Fiscal Targets

A senior International Monetary Fund (IMF) official said Monday he believed Brazil would comply with 2004 fiscal targets despite recent investor nervousness about the country's economic outlook, Reuters reported. "I have no doubts about compliance with fiscal goals," said Philip Gerson, head of the IMF's Atlantic Division, during a visit to Brazil to review the South American country's compliance with its \$14.8 billion loan agreement with the Fund. "Our opinion is that things are going well in Brazil, and Brazil is making important progress and is going to continue to do so." Brazil's agreement with the IMF requires it to post a primary budget surplus of 4.25 percent of gross domestic product in 2004. In the first quarter, Brazil exceeded that target by 6 billion reais (\$US 2 billion). A number of investment banks, including **J.P. Morgan** and **Citigroup**, have lowered their recommendations for Brazilian debt due to increased fiscal uncertainty. Brazilian President Luiz Inacio "Lula" da Silva has come under growing pressure to increase spending and lower interest rates at a faster pace to stimulate the economy. Gerson said, however, he was not worried about Brazil's inflation target of 5.5 percent for this year. Brazil has missed its inflation target the past three years.

### Chile May Seek Arbitration Over Gas Shipments from Argentina

Chilean Vice President Jose Miguel Insulza said Monday a regional natural gas crisis is not a willful Argentine action against Chile, but is a result of shortages in

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Discussion on

The Caribbean Community in  
the Western Hemisphere

with

Ambassador Albert Ramdin  
Advisor to the Secretary General of the OAS

Ambassador Richard Bernal  
Director General of the Caribbean  
Regional Negotiating Machinery

Wednesday, May 5, 2004  
9:00 a.m. – 10:30 a.m.  
Inter-American Dialogue  
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Argentina, Chile's *El Mercurio* reported. However, Chile would not rule out international arbitration if Argentina does cut the gas flow to its South American neighbor. "One might seek arbitration, but only once the gas is cut. It is necessary to remain calm, because all people want to do is warm their houses, and so far there is no emergency," Insulza said. "We're going to continue conversing [with Argentina], because the problem isn't of good or bad will, but of shortage. To break relations seems absurd to me, because of [our] closeness." The vice president said treaties must be respected and be the base of any

negotiation. Chilean President Ricardo Lagos has insisted that Argentina respect contracts to supply natural gas to Chile, but has admitted that continued cuts are likely. The Argentina government has denied violating any treaties and insists it must comply with a law that requires it to meet internal demand first before exporting natural gas. Last month, Argentina announced it would cut natural gas shipments to Chile by 20 percent. Chile depends on Argentina for some 37 percent of its electricity generation needs. Chilean Foreign Minister Soledad Alvear announced yesterday that a bilateral com-

**Featured Q&A***Continued from page 1*

tion, devaluation, statism, protection, and all the other deficiencies of the period before the Real Plan."

**A Board Comment: Roger Scher:** "With this move on the minimum wage, it is clear that the Lula government is currently moving with great caution toward its policy objectives. The politicians setting

“The politicians setting economic policy in Brazil right now understand that they have little room to mess around with fiscal and monetary policies ...”

– Roger Scher

economic policy in Brazil right now understand that they have little room to mess around with fiscal and monetary policies, which must remain at the current settings in order to inspire confi-

mission will meet this week to discuss the energy crisis.

### Ecuador: Multilateral Creditors Must Consider Political Risks

Ecuador's finance minister said Monday that multilateral lenders should weigh whether well-meaning economic reforms pose political risks for economically precarious Andean countries like Ecuador, Reuters reported. "We don't want an extension of the problems that already exist in Bolivia, that are coming alive again in Bolivia, that exist in Peru and could exist in Ecuador, and then Colombia, and we all know what is happening in Venezuela," Mauricio Pozo told reporters. "In this sense I think that it would be no good for anyone to have a larger regional problem. This is why we believe that the economic program should be one that can be fulfilled—I don't want to sign one I can't fulfill—

dence in debt sustainability and the inflation outlook, underpinning greater investment and economic growth. Nevertheless, the outlook for additional economic reforms—in the areas of public finances and microeconomic reforms—is not very positive right now. In order to underpin better growth prospects, Brazil should pursue the following policy agenda: second-stage social security reform, revenue-earmarking reform, bankruptcy legislation, central bank autonomy, additional tax reform, privatization, and a stable, market-friendly regulatory environment."

**Michael Gavin** is a member of the Advisor board and Head of Latin American Economic Research at UBS.

**Albert Fishlow** is Director of the Brazil Center at Columbia University.

**Roger Scher** is a member of the Advisor board and Head of Latin American Sovereign Ratings at Fitch Ratings.

and shouldn't forget about the political and social elements that any economic program with multilateral organizations has," he added. Officials from embattled President Lucio Gutierrez's administration met with the International Monetary Fund (IMF) last week to negotiate a new stand-by loan to rejuvenate investor confidence after its \$205 million loan agreement with the IMF expired earlier this month. The unpopular Gutierrez faces calls for his resignation from Indian groups and politicians over a campaign financing scandal and his pursuit of IMF-backed economic policies. Pozo said Inter-American Development Bank President Enrique Iglesias has called for a meeting of multilateral lenders on the plight of Ecuador, which has delayed payments on almost \$50 million in debt owed the Fund this year to guarantee government salaries and promote social development projects.

**Latin America Advisor**

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**Latin America Advisor** is published every business day by the Inter-American Dialogue  
1211 Connecticut Avenue, Suite 510  
Washington, DC 20036  
Phone: 202-822-9002 Fax: 202-822-9553

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