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## FEATURED Q&A

### Is the Itaipu Agreement a Good Deal for Brazil & Paraguay?

**Q** Last month, Brazilian President Luiz Inacio Lula da Silva and Paraguayan President Fernando Lugo signed a deal that increases Paraguay's benefits from the shared Itaipu hydroelectric dam and allows Paraguay to sell its excess electricity freely on the Brazilian market, which had been one of Lugo's key campaign promises. Did both countries get a good deal? What was each side forced to give up? What impact will the agreement have on each country's power sector and economy in general? Will it be accepted by each country's legislature, and what is the timeline for approval?

balanced. First, Paraguay will earn an additional \$240 million per year as compensation for the use of energy, close to 1 percent of its GDP. While the basic tariff paid by Eletrobras will remain unchanged at \$43.80 per megawatt hour (MWh), the additional charge will go from \$3.17 to \$9.51 per MWh. Second and potentially even more important, as it could represent up to a \$10 per MWh premium over the Eletrobras purchase price, would be permission for Paraguay to sell part of its energy directly to the Brazilian unregulated

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**A** **Guest Comment: Cláudio Frischtak:** "Brazil and Paraguay have come to an agreement regarding new terms for use of the Paraguayan energy generated by the Itaipu hydroelectric dam that is not consumed domestically (around 4 GWs of firm energy on average, or 90 percent of Paraguay's share). This is a long-simmering issue that became a major sticking point in bilateral relations since President Lugo's election. For Brazil, the key concern was to ensure that the Itaipu Treaty was not challenged in international courts, an action with unpredictable political consequences for the region. For Paraguay, the question was how to obtain significant enough concessions so that Lugo could claim he fulfilled a campaign promise. The outcome can be claimed by both sides as fair and



### Envoy: US Military Plan May Embolden Colombian Forces

Luis Gallegos, Ecuador's ambassador to the United States, told the *Advisor* that the US military deal with Colombia could embolden Colombia to launch an attack inside a neighboring country. See 'In Focus' on page 3.

*File Photo: NDN.*

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## NEWS BRIEFS

**Oscar Arias Has Swine Flu**

Costa Rican President Oscar Arias has been diagnosed with swine flu, government health officials said Tuesday. The Nobel laureate, 68, has been isolated since Monday with the illness, local daily *La Nacion* reported. In a statement, Arias said he has had fever, aches and a sore throat since Sunday, but feels well enough to work from home. Arias also suffers from chronic asthma, which makes him a high-risk patient. One in five of the 28 persons killed in Costa Rica by the H1N1 virus were asthmatics, *La Nacion* reported.

**Mexico's Industrial Output Fell 10.6 Percent in June**

Industrial output in Mexico fell 10.6 percent in June from the same month a year earlier, Dow Jones reported Tuesday, citing the country's National Statistics Institute, Inegi. June's decline marked the third consecutive month of double-digit drops in industrial production. Mexico's manufacturing sector, which is heavily dependent on the United States, was the economy's weakest. Manufacturing output declined 15.2 percent in June from a year earlier.

**Gol Sees Profits Climb in Q2**

Brazilian discount airline **Gol** on Tuesday posted a second-quarter net income of 353.7 million reais (\$US 192 million) compared to a loss of 166.5 million reais the year before as cheaper jet fuel and a merger contributed to lower operating costs. Profit was up 476 percent since the first quarter of 2009, buoyed by a favorable exchange rate for Brazil's currency. The company's EBIT fell 14 percent from the previous quarter to 89.9 million reais due to seasonality, according to a release.

## Political News

**OAS Reaffirms Plan to Send Delegation to Honduras**

The Organization of American States on Tuesday reaffirmed its plan to send a delegation of foreign ministers to Honduras in an effort to end the political crisis that has simmered since the country's June 28 coup, the Associated Press reported. The government of de facto President Roberto Micheletti has said OAS Secretary General Jose Miguel Insulza is welcome to be part of the delegation, but only as an observer. Insulza has called for the reinstatement of ousted President Manuel Zelaya and the de facto government has blasted Insulza as lacking "objectivity, impartiality and professionalism." On Tuesday, the OAS chief said his status on the delegation is unimportant. Resolving the crisis "is too important to lose time with this kind of dispute," Insulza said. The delegation was to arrive Tuesday in Tegucigalpa, but the de facto government over the weekend postponed the visit. The other members of the delegation are the foreign ministers of Argentina, Canada, Costa Rica, the Dominican Republic, Jamaica and Mexico. Insulza said he hopes the de facto government will accept a compromise authored by Costa Rican President Oscar Arias. The plan includes reinstating Zelaya as president and moving up the country's presidential election.

## Economic News

**Mexican Finance Minister: Oil Output May Drop 4.9% Next Year**

Mexico's oil output may fall as much as 4.9 percent next year and continue dropping through 2012, Finance Minister Agustin Carstens told a Mexican Senate committee Tuesday, Bloomberg News reported. Mexico is seeing as much as 300 billion pesos (\$US 23.05 billion) in lost sales each year because of slumping production, Carstens said. The lost sales could create a budget deficit next year for Mexico, which relies heavily on oil revenue. Last year, oil revenues funded 38

percent of Mexico's budget. A Mexican government report released last month said the country's economy, the second-largest in Latin America after Brazil's, may have contracted as much as 10.4 per-



Carstens

*File Photo: Mexican Government.*

cent in the second quarter of this year due to lower levels of exports, remittances and foreign direct investment. On July 30, Mexico's state oil monopoly **Petroleos Mexicanos**, or Pemex, said it was likely to produce 2.65 million barrels daily this year, a lower forecast from the earlier estimate of 2.8 million barrels. Mexico's oil production has fallen as output at Pemex's largest field, Cantarell, dropped twice as quickly as the company had predicted. In related news, US authorities on Tuesday transferred to Mexico \$2.4 million that a US-based oil importer paid after its president acknowledged buying and reselling crude petroleum condensate that had been stolen from Mexico, the Associated Press reported. In May, Donald Schroeder, president of Houston-based **Trammo Petroleum**, pleaded guilty to charges of purchasing and reselling \$2 million of the stolen fuel, Assistant US Attorney Jim McAlister told the AP.

## Company News

**Itau's Recurring Profit Falls 14 Percent in Second Quarter**

Brazil's **Itau Unibanco** reported Tuesday that its recurring profit for the second quarter declined 14 percent year-on-year, a drop that was not as steep as analysts had expected, Reuters reported. Itau Unibanco, which is Latin America's largest financial services company by assets, said its provisions for bad debt

more than doubled. Also, the bank's defaults will likely rise until next month but are then likely to decline next year to levels seen in 2008, CEO Roberto Setubal

“The economy is bouncing back, growing at a much faster rate.”

— Roberto Setubal

told business leaders Tuesday in a speech. "We have data showing that at the margin, it's improving," said Setubal. "The economy is bouncing back, growing at a much faster rate." The bank's recurring net income declined to 2.43 billion reais (\$US 1.31 billion) from 2.84 billion reais during the same period a year ago. The figures exclude the sale of Itau Unibanco's stake in **Visa** and **VisaNet**. Including one-time transactions, the bank's profit declined 8.1 percent to 2.57 billion reais.

### Canada's Agnico-Eagle May Acquire Assets in Mexico, Arctic

Canada's **Agnico-Eagle Mines** may use its increasing revenue to boost dividends and purchase assets in Mexico and Canada, Bloomberg News reported Tuesday, citing Chief Executive Officer Sean Boyd. Agnico may use cash flow generated by the completion of five new mines for the purchase, Boyd told the wire service. The company plans to begin producing gold at its Pinos Altos mine in Mexico in September and also open its Meadowbank mine in the Canadian territory of Nunavut in next year's first quarter. "We've got a great asset in Mexico; that would be a place where we're looking for opportunities in early stages," Boyd was quoted as saying. "And part of our strategy is the Arctic. We've developed a strong skill set up there with Meadowbank, and we look to expand our footprint up there as well." The Toronto-based company is seeking to increase production at Pinos Altos to approximately 175,000 ounces annually. It hopes to produce 350,000 ounces of gold on average over nine years at the Meadowbank mine.

## In Focus

### Envoy Says US Military Plan May Embolden Colombian Forces

By Matthew Schewel

WASHINGTON—A greater US military presence in Colombia would likely increase chances the South American nation would launch a "pre-emptive" attack on a neighboring country, creating a "rupture of the whole inter-American system," Ecuador's ambassador said in an interview with the *Advisor*.

The notion of pre-emptive attack is "a doctrine that the United States has used in other parts of the world and [that] the Colombians accept," Ambassador Luis Gallegos said Friday, citing the March 2008 raid by the Colombian military on a guerrilla camp in Ecuador. Colombian defense minister and presidential hopeful Juan Manuel Santos has made it clear he would not hesitate to repeat such an action, Gallegos said.

Several South American leaders have expressed strong concerns about a new military agreement that would give US troops access to Colombian bases for anti-narcotics flights. At Ecuadorean President Rafael Correa's second inauguration earlier this week, the Union of South American Nations, a regional political group whose revolving presidency Ecuador now holds, agreed to convene a special meeting later this month to address the issue. "I think that the guarantee that everybody has to have is that we will not be attacked again," Gallegos said.

Last year, when Colombian forces crossed unannounced into Ecuadorean territory and attacked an encampment of the Revolutionary Armed Forces of Colombia, or FARC, Ecuador cut diplomatic ties with its northern neighbor, claiming the raid violated its sovereignty. Gallegos said Ecuador is doing everything it can to improve bilateral relations, but that Colombia's war with the FARC remains largely an internal problem fueled by US drug consumption.

"The central problem is that you're producing 1,000 tons of cocaine and you're selling it to the American market ... and you're trying to blame the guy next door for one camp, while how many camps are there in Colombia?" Gallegos said. Colombian officials who accuse Correa of supporting the FARC are in fact doing so to gain political leverage in the US, he added. "We're put in a corner by the strategy by the Colombians to promote their free trade agreement and their Plan Colombia in the United States," he told the *Advisor*. "It's an intelligent strategy. It appeals to your sense of antiterrorism."

But critics of Ecuador's government say new evidence, including the apparent diary of slain guerrilla leader Raul Reyes, confirm that Correa aides took campaign contributions from the FARC. Gallegos said the president had been quite clear that "he does not know anyone from the FARC and that he did not receive money." But the ambassador agreed that if an investigation by Ecuador's prosecutor yields indications of wrongdoing, those involved should be punished.

Gallegos rejected claims that Correa is merely a follower of Venezuelan President Hugo Chavez, an outspoken US critic, and instead sought to portray Ecuador as a country that shares mutual interests with various countries in the hemisphere. He said the US and Ecuador are currently engaged in a "constructive" dialogue encompassing trade, migration and security issues, which was bolstered by a positive encounter between Correa and President Barack Obama at the Summit of the Americas. "We will agree on many things and we will disagree on others, and we will agree to disagree, because that is the nature of ... the foreign relations of countries," he said. [Editor's note: our interview with Amb. Gallegos will continue in this week's issue of the Dialogue's *Energy Advisor*.]

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

energy market. Both these changes will have to be approved by each country's congress. Finally, a new 500 kilovolt transmission line from Itaipu to Asuncion will be built at a cost of \$450 million and paid for by the binational company, and donated to Paraguay. It is likely that both congresses will end up approving the deal this year, in advance of Brazil's elections in 2010."

**A Guest Comment: Diego Abente Brun:** "Among the most important items of the Itaipu agreement is the threefold increase in the price Brazil pays for the energy sold by Paraguay. It also permits ANDE, the Paraguayan electricity company, to gradually dispose of its own surplus energy freely, selling directly in the Brazilian market (and not only to Eletrobras as until now) and to third countries after 2023. There are still some unresolved issues, such as whether certain provisions of the agreement should be approved by the Brazilian Congress, where it faces opposition from some quarters, and whether the resources to pay the additional bill will come from some sort of financial engineering of the Itaipu debt with Eletrobras, which Paraguay also questions and both parties have agreed to revise. The agreement is a momentous political triumph for President Lugo. Renegotiating the Itaipu treaty was a centerpiece of his campaign and this agreement gives him a badly needed influx of political capital after numerous personal issues and political setbacks were weakening his presidency. Besides, with a minimum 3 percent decrease in the GDP expected for this year as a result of the international crisis and a severe drought, the additional resources which amount to roughly 1.5 percent of GDP come at a particularly welcome time for Paraguay. For Lula, it is also a triumph. He has dispelled the criticisms of Brazilian heavy-handed attitudes toward its poorer neighbors, put to rest growing accusations of Brazilian imperialism, and allowed Brazil to hold the higher ground in its quest for greater leadership. Lula has shown that he

is not only a highly successful and popular president but also a sagacious statesman."

**A Guest Comment: Rubens Barbosa:** "Both countries greeted the agreement as 'historic.' It was a great victory for President Lugo, but it is questionable if Brazil got a good deal in the long run. The current government in Brazil is still trying to find the right attitude in relation to our smaller neighbors. Under the deal, Brazil allowed the Paraguayan energy company to sell power directly into Brazil's open market and assumed the financial cost of increasing the bonus for the cession of energy to Brazil. Brazil will build a transmission line worth \$450 million to bring power from Itaipu to the capital, Asuncion. The effect will be positive for Paraguay's economy if there is foreign investment to follow it up. In the case of Brazil, there will be an increase in the price of power for industrial and residential consumers, with a small but sure inflationary byproduct. The agreement will have to be submitted to both congresses. I don't foresee any problem with the deal getting approved in Paraguay, but I anticipate a strong opposition to its approval in the Brazilian Congress. The elimination of the US inflation factor and the direct selling of energy to the Brazilian market go against the letter of the Itaipu Treaty. The possibility of selling energy to a third country after 2023 also goes against the provisions of the treaty. It is likely that the changes to be negotiated with the Congress will take some time to be approved."

**Cláudio Frischtak** is president of *Inter.B Consultoria Internacional de Negocios*.

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