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FEATURED Q&A

What is the Future of Energy Integration in Central America?

Q First proposed in 1987, the Central American Electricity Interconnection System (SIEPAC), a plan to create a more robust regional transmission grid in Central America, is scheduled to become operational this year. In order to allow economies of scale to occur, the aim is to harness the transmission project to create an integrated regional electricity market known as the Mercado Eléctrico Regional (MER). What are the potential benefits and downsides of the MER? What challenges does the integrated market face? What steps do the region's governments and institutions need to take to bring it to fruition?

A Juan Miguel Cayo, senior energy specialist for Latin America and the Caribbean at the World Bank: "SIEPAC was designed to bring the benefits of integration to the six countries and improve their national power systems. Due to the relatively small size of the power system in each of the region's nations, the opening of the regional market was seen as a means for creating a larger market that enhanced competition among power producers and for providing security of supply to all individual countries at the same time. The goal is for the regional market to gradually allow qualified agents to buy or sell electricity no matter where they are located in the Central American region. Additionally, a regional market with clear and uniform rules is expected to

offer incentives for building larger and more efficient power plants, sparking investments that would help reduce the costs of electricity in the region and strengthen the reliability of its electricity systems. However, as the national markets evolve towards integration and increased trade, there are still important barriers remaining that hinder the full implementation of the Regional Electricity Market. Power integration is much more than simply building transmission lines and interconnection facilities. Its success will

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Calderón Defends Strategy in Meeting With Victims' Families

Mexican President Felipe Calderón defended his strategy in fighting drug traffickers during an emotional meeting Thursday with victims' family members, including poet Javier Sicilia. See story on page 2.

Photo: Mexican Government.

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NEWS BRIEFS

Humala Promises to Support Natural Resources Investment

Peruvian President-elect Ollanta Humala said Thursday that he will support investments in natural resources, Bloomberg News reported. "I ratify my willingness to resolve and prevent social conflicts while guaranteeing investment and the sensible exploitation of natural resources with respect for the rights and freedoms of the indigenous population and local community," he said in Lima. Mining investment in the country has slowed amid concerns about Humala's plan to implement a windfall tax on mining companies.

Uruguay Central Bank to Raise Interest Rates: Survey

The Uruguayan central bank will likely raise the benchmark interest rate by 50 basis points to 8 percent today, according to three economists surveyed by Bloomberg News. The bank boosted the rate by 100 basis points on March 23. Policymakers are struggling to contain inflation, which rose to 8.53 percent in May from 8.34 percent the month prior, in the booming economy.

Mexican Lender Su Casita to Complete Debt Swap

Mexican mortgage lender **Hipotecaria Su Casita** received approval from 95 percent of bondholders and will proceed with a debt swap of about 7 billion pesos (\$593 million), the company said Thursday, Dow Jones reported. Holders of the company's 5.36 billion peso-denominated notes will receive 2.32 billion in new seven-year guaranteed notes plus equity of 36.7 percent of the company, while holders of \$136 billion in dollar-denominated notes will receive \$59 billion in new seven-year notes.

Political News

Calderón Defends Drug War Strategy in Meeting With Families

Mexican President Felipe Calderón on Thursday defended his efforts in fighting drug cartels during a emotional meeting with some of the citizens who have become his biggest critics—family members of people killed in the country's brutal drug violence, the Associated Press reported. Poet Javier Sicilia, whose son was killed in drug-related violence in March, opened the televised meeting at Mexico City's Chapultepec Castle. He demanded that Calderón remove soldiers from the streets and apologize to victims of the drug war, which has cost more than 35,000 lives since Calderón took office in December 2006. "Where are the benefits of this strategy?" Sicilia asked. "You don't have anything to show us, and we are not politicians, we are citizens." Sicilia added that Calderón is "obligated to apologize to the nation and in particular to the victims." Pounding the table and pointing his finger, Calderón responded by saying

it would have been irresponsible of him not to act as organized crime groups sought to control the country. "I agree that we must apologize for not protecting the lives of victims, but not for having acted against the criminals," said

“One thing I regret is not having sent [the military] before.”

— Felipe Calderón

Calderón. "One thing I regret is not having sent [the military] before." Criminals, not the government, are causing the violence, said Calderón. "Francisco was killed by criminals, not federal forces," he said, referring to Sicilia's son. Authorities have made several arrests in connection with the March 28 murder of Juan Francisco Sicilia. Since his son's death, Javier Sicilia has organized marches and protests in locations including Mexico City, Cuernavaca in the violent northern border city of Ciudad Juárez. Sicilia's movement also said it will soon send a protest

Featured Q&A

Continued from page 1

depend on several conditions: political, institutional, regulatory and physical. At present, these conditions are not fully in place. Political conditions are not clear and decisive actions still need to be taken; institutions are weak; regulatory conditions are not completed yet and important obstacles remain; and there is weak power supply. While Central America should pursue its power integration, each country needs to focus on strengthening its domestic market, while simultaneously working to strengthen the supranational institutions and removing obstacles at both the regulatory and commercial levels, to promote the materialization of a truly enhanced power market. The consolidation of the regional regulatory and institutional framework and the creation of a strong regional power market will not succeed if it will be based on weak, inefficient and

vulnerable national power sectors. Achieving a strong integrated market based on weak national markets is a mirage."

A Jorge Asturias, subregional coordinator for Central America for the Latin American Energy Organization (OLADE): "The regional electricity market is a seventh market superimposed on the six national markets, which will operate based on the following premises: a) regional electricity trade can take place in a regional contract market and a spot market; b) all MER agents with the exception of the transmission companies can purchase and sell electricity freely and will have open access to the transmission system; c) MER generation agents can install power plants in any of the member countries and sell energy at

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caravan to the Mexico-Guatemala border. At the end of the meeting, Calderón and Sicilia awkwardly hugged and Calderón promised to meet with peace activists again in three months.

Former Top Bolivian Antidrug Official Pleads Guilty in U.S.

A former head of Bolivia's counternarcotics police and a co-defendant both pleaded guilty to cocaine trafficking charges in U.S. federal court in Miami, the Associated Press reported. René Sanabria, 58, had also headed an elite



Sanabria

File Photo: Agencia de Noticias Fides.

drug intelligence unit in Bolivia's Interior Ministry. He and codefendant Marcelo Foronda, 43, each faced life in prison. However, their decisions to plead guilty and cooperate with U.S. authorities mean they will likely face 10 years or less in prison

when they are sentenced in September, according to one of Foronda's lawyers. During a sting conducted by the U.S. Drug Enforcement Administration, Sanabria and Foronda agreed to help transport thousands of dollars worth of drugs to the United States, according to U.S. authorities. The incident was an embarrassment for Bolivian President Evo Morales who in 2008 barred the DEA from operating in Bolivia, accusing the agency of helping his political adversaries.

Company News

Brazil's Caixa Planning to Sell \$2 Bn in Mortgage-Backed Securities

Brazilian state-run mortgage lender **Caixa Econômica Federal** is planning to sell as much as \$2 billion in mortgage-backed securities as part of an effort to ensure the mortgage sector's growth and also modernize it, bank president Jorge Fontes Hereda said Wednesday, Reuters reported. The transaction would effectively allow the lender to offload a por-

The Dialogue Continues

What Factors Are Contributing to Unrest in Chile?

Q Scores of people were arrested and millions of dollars in property was damaged in Chile's capital city last week after an estimated 80,000 people took to the streets to demand lower tuition and protest a perceived government 'privatization' of the education system, the latest in a series of demonstrations against government policies. The administration of President Sebastián Piñera has also faced heavy criticism over a hydroelectric project in Patagonia. A poll taken last month found that President Piñera's approval fell to a new low of 36 percent in May, Reuters reported. What factors are contributing to unrest in Chile? How are the protests affecting Piñera's ability to govern effectively? Is the administration likely to face a serious political crisis?

A **Maria Velez de Berliner, president of Latin Intelligence Corporation:** "Education in technology and the hard sciences underpins future growth and competitiveness in any country. Chile will not be exempt. While destruction of private property and incivility are condemnable, some of the students' academic demands are sensible; particularly those related to scholarships at the secondary and university levels, and public technical education rather than having it concentrated on private institutions. Given the relationship of education to competitiveness, tuition increases of about 7 percent, student loans at 7

percent, coupled with increases in food and fuel costs, make education something of a luxury for those not in the highest 10 percent, who receive 41.6 percent of income. Piñera is far from a governability crisis caused by students' protests. He has some options. The proposed changes in the military budget that eliminate Codelco's 10 percent of export revenue contribution to the armed forces (\$6 billion in 2010) would give the government the option to raise public education expenditures above the current 4 percent of GDP, thus mitigating students' unrest. Patagonia's hydroelectric plants present Piñera with a more complex and politically risky dilemma. Nature makes Chile energy insufficient for its industrial demands. Its dependency on energy imports is costly and needs to decrease. Therefore, to keep growth on track, Chile will require increasing supplies of endogenously-produced energy. But is Patagonia, a region prone to earthquakes, the best location for these plants? The flooding of about 14,600 acres of land is a decision that will haunt Piñera's and subsequent governments, if it is implemented. Those protesting in Patagonia will not remain quiet. Their voices, particularly those of the Mapuches, whose lands will be flooded, have the potential for deleterious political and economic consequences."

Editor's note: The above is a continuation of a Q&A published in Wednesday's issue of the Advisor.

tion of its balance sheet and continue its lending growth at a pace of more than 50 percent annually. The move also could provide foreign investors another way to participate in Brazil's real estate boom. Caixa, which controls approximately three quarters of Brazil's mortgage market, is still discussing the terms of the

transaction with Brazil's finance ministry and central bank. It plans to offer the securities in this year's second half, Hereda told Reuters. Caixa has been instrumental in President Dilma Rousseff's plan to construct at least 2 million homes by 2014, a main item on her agenda.

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the regional level; d) the MER is a market with its own rules, independent of the national markets, which makes energy transactions using the regional transmission grid (RTR) and the national networks. The points of connection between the MER and national markets are the nodes of the RTR. The design and regulations of the regional market provide a regulatory framework that allows and promotes long-term firm power trade among Central American countries and facilitates the development of regional generation plants. However, the market regulations have several obstacles to achieving this goal; for example, the existence of vertically integrated state-owned companies in Costa Rica and Honduras that may limit generators from other countries from accessing their domestic markets. The operation of long-term firm regional contracts is not compatible with the application of rules that give priority to the domestic demand in the case of energy shortages. (Two countries maintain explicit norms that give priority to domestic demand.) The application of price controls and generalized subsidies in some countries could reduce the opportunities for long-term contracts and short-term transactions in the regional market. It is important to establish a proper coordination mechanism between bilateral agreements like the electric interconnection between Guatemala-México or Panama-Colombia and the MER regulations. The application of the MER will be strengthened by a second protocol signed in 2007 and ratified by five countries (it is waiting for the ratification of the National Congress in Costa Rica)."

A **Angel Baide, independent energy consultant:** "The benefits of the MER are those of greater competition, which will produce lower prices for consumers. The downsides are only for governments and state-owned companies, mainly in Costa Rica and Honduras, which will lose their dominance of the power sector. They now have to step back and let private

agents take advantage of the institutional and regulatory infrastructure created by SIEPAC. It seems governments were reluctant partners in SIEPAC. The original design presents the MER as 'a seventh market, superposed to the six national markets.' But, the MER makes sense only if it is to become the single electricity market for the region. Also, the treaty defines 'regional' transactions as those where the parties are in different countries. However, the goal being that of a single integrated market, all transactions are the same, they are all regional! The

“The downsides are only for governments and state-owned companies, mainly in Costa Rica and Honduras.”

— *Angel Baide*

narrow definition has led to problems now that project costs begin to be charged to regional transactions, because there are too few of them, leading to high unit costs which discourage trading. The MER operation rules reflect the best standards. However, there is no obligation for national system operators to use this fine machine. They can keep the national markets segregated, and avoid global optimization. Governments must introduce rules obliging each national system operator to elevate each day to the regional system operator all buy and sell bids received in the national market. Only in this manner will there be an integrated regional dispatch optimizing the use of generation and transmission resources in the region."

The Advisor welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.

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