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FEATURED Q&A

What Is the Growth Outlook for the Region's Largest Economies?

Q In recent years, many analysts predicted that economic growth in Latin America would take two divergent paths, with faster growth exemplified by Brazil versus Mexico's more sluggish path. However, Mexico grew faster than Brazil in 2011 and is poised to do so again this year. What is the outlook for Latin America's economic growth this year? Are any patterns emerging? Where are the region's two biggest economies headed in the short- to medium-term? What factors have accounted for Mexico's recent successes?

A Alicia Bárcena, executive secretary of the United Nations Economic Commission for Latin America and the Caribbean (ECLAC): "ECLAC estimates that Latin America and the Caribbean will grow by 3.7 percent in 2012, with unfavorable external conditions characterized by a recession in most European countries, a slow and precarious pace of recovery in the United States and slackening though still quite significant growth in China and other emerging economies. In this context, it is not surprising that during most of 2011 and the first months of 2012 growth in Latin America was driven mostly by rising domestic demand. The differing performances of Mexico and Brazil would appear to be the result of several factors that could change in the near future. First, during the first half of 2011 many Latin American economies, including those of Brazil, Chile, Colombia and Peru, but excluding Mexico, faced symptoms of overheating that in many cases led to increases in interest rates to prevent eventual inflationary pressures from rising, affecting the pace of growth of domestic consumption and investment. This contrasts with the greater growth of private and public investment in Mexico, with the latter probably stimulated by Mexico's political cycle. Second, growing risks and recessions during the second half of 2011 in Europe, which receives almost

Continued on page 4

Chávez Accuses Rival of Seeking to Incite Violence

Venezuelan President Hugo Chávez on Sunday accused his rival, Henrique Capriles, of trying to spur violence ahead of the country's presidential election. A scuffle broke out the day before when Capriles led a march through a poor neighborhood. See brief on page 2.

File Photo: Venezuelan Government.

Inside This Issue

FEATURED Q&A: What Is the Growth Outlook for the Region's Largest Economies? ..1

Peña Nieto's Security Advisor Recommending Elite Drug Units 2

Ecuador 'Working Hard' to Return to Credit Markets: Central Bank Chief.....2

Venezuela's Chávez Accuses Rival of Trying to Spur Violence.....2

Workers at Colombia's La Jagua Coal Mine Vote to Strike 3

In Focus: Lugo's Impeachment a Political Process, Not a Coup: Ambassador.....3

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NEWS BRIEFS

Venezuela's Chávez Accuses Rival of Trying to Spur Violence

Venezuelan President Hugo Chávez on Sunday accused his rival, presidential candidate Henrique Capriles, of attempting to incite violence ahead of the country's Oct. 7 election by campaigning in areas that support Chávez, the Associated Press reported. "They are going to try to destabilize the country. I've been saying it and everybody should be alert," Chávez told soldiers during a ceremony in Caracas. On Saturday, a scuffle between supporters of the candidates occurred when Capriles led a march through a poor neighborhood of the capital. "I'm not walking Venezuela's streets to fight with anybody," said Capriles.

Heineken Delays Investments in Brazil After Tax Increase

Heineken will delay investments in Brazil as a result of an increase in beer taxes from 17 percent to 20.8 percent, Reuters reported, citing the Agencia Estado news agency. According to the report, Brazilian brewers have been struggling as a result of the decline in the real and sales have also fallen 1.6 percent in the first six months of 2012.

Mexico to Import Eggs After Bird-Flu Outbreak

Mexican authorities are preparing to import eggs after an outbreak of avian flu in the state of Jalisco, EFE reported Friday. Although the infected birds represent only 1.7 percent of the country's egg-producing poultry, the government is ready to suspend duties on egg imports to prevent a hike in prices. Economy Secretary Bruno Ferrari also warned egg producers against artificially inflating prices, saying his department will act against anyone exploiting the situation.

Political News

Peña Nieto's Security Advisor Recommending Elite Drug Units

Mexican President-elect Enrique Peña Nieto's top security advisor said Friday that he is recommending the government create elite units comprised of police officers and members of the military in part to target the hitmen who carry out killings in the country's brutal drug war, the Associated Press reported. Gen. Óscar Naranjo, who retired in June after five years heading Colombia's national police, told the wire service in an interview that

> "You also have to put a lot of importance on these groups of hitmen to control the violence."
>
> *— Gen. Óscar Naranjo*

the elite units should not simply focus on "high-value-targets," such as drug cartel kingpins. "You also have to put a lot of importance on these groups of hitmen to control the violence," said Naranjo. The activities of such elite units are often isolated from those of other law-enforcement agencies, the AP reported, adding that units get more resources the better they perform and that information is often compartmentalized in an effort to guard against leaks. Similar efforts have worked in Colombia and may also be successful in Mexico, said Naranjo. Mexico's drug war has left more than 47,000 people dead since President Felipe Calderón began his military-led offensive against the cartels after taking office in December 2006. During his campaign, Peña Nieto said he wants to increase efforts to protect ordinary citizens from violence. Naranjo has also said Mexico's government should set goals for reducing violence. "In the first 100 days [of Peña Nieto's government] the goal should be set for reducing violence. It could go badly. It could go well. But it should be put in play," Naranjo told the AP. "I think it's possible to tell Mexicans, 'Look, in 100 days we want to cut the violence we have in half. ' " Mexican authorities are aided by the fact that the country's drug violence is relatively concentrated, said Naranjo, adding that the bulk of the violence is in six areas. "It's impossible that in six cities you can't have some control," he said. On Friday, Mexico's electoral authority finished its official count of the July 1 presidential election. It announced that Peña Nieto of the Institutional Revolutionary Party, or PRI, won the election with 38.21 percent of the vote. Andrés Manuel López Obrador of the Democratic Revolution Party garnered 31.59 percent and Josefina Vázquez Mota of the ruling National Action Party won 25.41 percent. López Obrador has vowed to mount a legal challenge of the results, based on the accusation that Peña Nieto's party engaged in vote-buying, which the party denies. On Saturday, tens of thousands of demonstrators marched through Mexico City to protest the allegations that the PRI distributed pre-paid gift cards, groceries and other goods before the election. Protesters carried signs with messages such as "Peña, how much did it cost to become president?" Officials in Mexico City estimated that the crowd of students, union members and leftists numbered about 50,000 by the time it reached the city's central square, the Zócalo, the AP reported.

Economic News

Ecuador 'Working Hard' to Return to Credit Markets: Central Bank Chief

Ecuador's government is making significant efforts to return to international credit markets following its default on $3.2 billion of debt in 2008 and 2009, the country's central bank president told Bloomberg News in an interview Saturday. "We are working very hard on this, and various groups from our economic teams have been visiting investors, investment

Delgado

File Photo: Ecuadorean Government.

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banks and ratings agencies," said Pedro Delgado. "We are in this process and we'll do it when the moment is opportune." Since the default, Ecuador has used Chinese loans and its public pension fund to help finance its budget. In addition, the central bank plans to repatriate $1.1 billion of reserves in order to pay for infrastructure and other projects, President Rafael Correa said on Saturday. The country is also "very advanced" in talks about negotiating a new loan from China, said Delgado. In order to cover fuel import costs when the country's biggest refinery is shut down for repairs later this year, Ecuador has sought a loan of $515 million from the Latin American Reserve Fund.

Company News

Workers at Colombia's La Jagua Coal Mine Vote to Strike

Coal workers at Colombia's La Jagua mine, which is operated by **Glencore**'s **Prodeco** unit, voted Saturday to strike over wages and working conditions, Reuters reported, citing a union official.

> "On Monday, we'll continue negotiating with the company."
>
> *— Ricardo Machado*

In a unanimous vote, workers voted to strike after 40 days of negotiations with Prodeco, said the official, Ricardo Machado. "We were relatively close to a deal but it couldn't be reached. On Monday, we'll continue negotiating with the company," Machado told the wire service in a telephone interview. Workers at the mine now have a 10-day strike period, though they are legally barred from walking off the job in the first two days or last two days of that period. A strike at La Jagua is unlikely to affect prices unless it lasts for several weeks. Workers at the mine held a five-week strike in 2010 before agreeing to a two-year deal with the company. Last year, workers at the Calenturitas mine walked off the job for eight days.

In Focus

Lugo's Impeachment a Political Process, Not a Coup: Ambassador

By Rachel Sadon

WASHINGTON—The impeachment of former President Fernando Lugo was fundamentally a political process, not a coup d'etat, Paraguay's ambassador to the United States, Rigoberto Gauto Vielman, said Friday at the Inter-American Dialogue. "He lost the political support necessary to lead the country," said Gauto, who had been appointed to his position by Lugo but remains in office.

Gauto

File Photo: Paraguayan Government.

Lugo's impeachment last month drew international outcry for what critics called a "parliamentary" or "institutional" coup, occurring just nine months before the country's scheduled presidential election.

Despite the impending election, it was in the political interest of Paraguay's three main political parties to see Lugo out of office, said former U.S. Assistant Secretary of State for Western Hemisphere Affairs Arturo Valenzuela. "They shouldn't have impeached Lugo … but unfortunately this is what politics is in many places. This is not a coup d'etat."

"It is so important to understand how light years away we are from a time when the military called the shots both literally and figuratively," he added.

The nature of Lugo's removal from office—balancing on the legitimacy of a 24-hour trial—has hampered a cohesive regional response. Most of the countries in the region, including Paraguay's most important trade partners, have recalled their ambassadors and Paraguay has been suspended from Mercosur. But the regional trade bloc has not imposed economic sanctions and the United States has remained neutral in the conflict. The Organization of American States is expected to release a report today detailing its response.

"We hope that once the dust settles, everyone will respect that the internal affairs of Paraguay are a Paraguayan concern only and that soon we will be working together again with our partners in the region," said Gauto.

But the country's suspension from Mercosur and strained relations with its neighbors may make that impossible until elections are held next April. One of the most vociferous critics of Lugo's impeachment, Venezuela, has said it would cut off oil exports to the country, which amount to 30 percent of its fuel, Venezuelan daily newspaper *El Universal* reported.

Paraguay, in turn, accuses Venezuela of meddling in the impeachment process. Paraguayan officials have alleged that Venezuela's foreign minister, Nicolás Maduro, asked the military to step in and stop the impeachment. In response, Paraguay has opened an investigation into a meeting held between Maduro and military leaders. Maduro has denied the accusation.

Gauto was also sharply critical of Mercosur's decision to suspend Paraguay and invite Venezuela to join the bloc, accusing it of violating the terms of the Treaty of Asunción, which established Mercosur in 1991, and not respecting due process—the same criticism that has been made of Lugo's short impeachment process.

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Featured Q&A

Continued from page 1

one quarter of Brazil's exports, contrasts with the moderate—albeit weak—recovery during that time in the United States, which receives approximately 80 percent of Mexico's exports. Finally, a drought negatively affected Brazil's agriculture, reducing its production and exports of sorghum. This contrasts to the relatively dynamic growth of Mexico's agricultural sector during the first months of 2012. Challenges ahead for both economies relate to their ability to take advantage of their internal markets and to increase integration with other economies in the region. This would compensate for lower external economic activity and would allow them to take advantage of the more favorable economic performance that many countries in the region are posting."

Luis Oganes, managing director and head of Latin America Research at J.P. Morgan Chase & Co. in New York: "The disappointing activity data in Brazil still stand in stark contrast to Mexico's resilience. Last week's release in Brazil of weak industrial production growth numbers for May and auto production for June have led us to revise down our GDP growth forecast for the second quarter to 2.4 percent quarter-on-quarter sequential growth in seasonally adjusted annual rate terms, down from the 4.1 percent previously expected. While the first signals of final demand recovery are beginning to emerge, the perception that global manufacturing will remain sluggish in the third quarter also limits the upside in Brazil so we preserve the same recovery profile for the year's second half. As such, the second-quarter change resulted in a downward revision to the full-year 2012 GDP forecast to 1.7 percent year-over-year from 2.1 percent. In turn, while the U.S. Institute for Supply Management's manufacturing index has decelerated sharply in the last two months, the Mexico Manufacturing Purchasing Managers' Index (PMI) for June was the highest of the past five years. That said, any divergence between Mexico and U.S. PMIs has historically proven to be short-lived so we do expect Mexico's manufacturing growth to slow to 4 percent year-over-year in the second quarter (from 5.4 percent in the first quarter) and to stabilize around 3.5 percent over the year's second half. This is consistent with our full-year 2012 GDP growth forecast of 3.6 percent year-over-year. Brazil's sluggishness is proving to be a drag on Argentina where the drivers of activity weakness have clearly rotated from the domestic to the external sector in the second quarter, but not on other countries like Chile, where last week's release of strong May economic activity data suggest that the economy also keeps defying the downward pull of global growth gravity and supports our constructive 5 percent growth projection for 2012 despite the abundance of external tail risks."

Rogelio Ramírez de la O, president of Ecanal in Mexico City: "Mexico's growth in 2011 and 2012 is greater than Brazil's, but it would be wrong to see a new pattern in this. The temporary superiority of Mexico is cyclical. It is linked to resilient U.S. manufacturing growth and to low growth in past years. In other words, it would be difficult for Mexico to slow down as much as Brazil has slowed down, having posted poorer growth relative to Brazil's. Just to refresh the memory, Mexico recorded average annual growth of 2 percent per year between 2001 and 2011, while Brazil experienced average annual growth of 3.6 percent and Latin America as a whole saw 3.4 percent, according to ECLAC. Over the medium term, Mexico can improve upon its record if macro policy is changed toward strengthening domestic supply, given that a large part of demand is dominated by U.S. trends, while U.S. growth will probably not be high as deleveraging continues. In contrast, Brazil and most other Latin American countries have policies in place with a better balance of external and domestic demand drivers. Mexico can only improve, but not without a policy change."

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