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FEATURED Q&A

What Factors Are Driving Currency Trends in the Region?

Q Multinational corporations have been reporting quarterly earnings in recent weeks, many of which cited currency downturns in Latin America for crimping results. Are the worst of the region's currency fluctuations likely behind us, or will multinationals in Latin America and the Caribbean face bigger uncertainty this year and next? What underlying factors are driving these currency trends, and what policy responses should governments be taking?

A Edgardo Sternberg, vice president and emerging markets portfolio manager at Loomis, Sayles & Company in Boston: "With the exception of the Mexican peso and some Central American currencies, major Latin American currencies depreciated significantly against the U.S. dollar in 2013. So far this year, the only currency that has shown a significant recovery has been the Brazilian real. In fact, Argentina engineered a large devaluation early in the year and we may see something similar in Venezuela. Most of the losses last year happened in May-June, August and November, with recoveries in subsequent months. May losses resulted from the Federal Reserve's announcement that it would start reducing the purchases of bonds, while uncertainty on when exactly the tapering would start produced the August selloff. The significant slowdown in China's economy motivated the end-of-year decline. Every selloff was followed by significant recoveries as certainty or less positive news on the U.S. economy and more positive news on China's economy reversed the trend. China's growth has an impact on the demand of resources from Latin America and, thus, on its trade balance. Mexico, Central America and the Caribbean are somewhat insulated from this as they are more related to the vagaries of the U.S. economy. On the other hand, many countries are experiencing economic growth slowdowns, with increasing inflation. To fight inflation and reverse the weakening

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U.S. Congress Considering Sanctions Against Venezuela

The U.S. Senate and House of Representatives are considering sanctions against the government of Venezuelan President Nicolás Maduro over the violent protests that have been happening for three months in the South American country. See story on page 2.

File Photo: Venezuelan Government.

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NEWS BRIEFS

Venezuela's Zulia State to Begin Rationing Electricity

Venezuela's western Zulia state will begin rationing energy to reduce demand on the power grid after Colombia halted natural gas sales to the country last week as a drought reduces water levels at hydroelectric dams, Bloomberg News reported today. The government's announcement comes on the heels of a **Ford Motor Co.** decision to halt production in Venezuela due to difficulty obtaining dollars from the country's government.

Chile Must Invest $58 Billion in Infrastructure: Report

Chile must invest $58 billion in infrastructure between now and 2018 in order to maintain competitiveness, the Chilean Construction Chamber said in a report released Wednesday. The chamber's report proposes that the government pay for 54 percent of that amount and the private sector foot the bill for the remainder. Chile needs improved roads, energy infrastructure, hospitals, railroads and ports, among other projects, the report said.

Mexichem Considering Additional Joint Ventures

Chemical products producer **Mexichem** will pursue more joint ventures as Mexico's energy sector opens up and creates new petrochemical sector growth, Bloomberg News reported Thursday. Returns from existing projects have kept the company above its competitors on the stock market. It has acquired 15 companies since 2007, but there are more opportunities for joint ventures with state oil company **Pemex** and others, analysts told the news service.

Political News

Brazilian Federal Police Begin Strike, May Affect Next Month's World Cup

Federal police officers in Brazil have started a strike over pay and said they may continue the work stoppage during next month's World Cup, BBC News reported Thursday. At least 40 percent of the country's federal police participated in the strike, said Renato Deslandes, a spokesman for the striking officers. Though Thursday's strike was called for only 24 hours in cities that are scheduled to host the World Cup next month, Deslandes said the walkout would continue next month during the soccer tournament. "Federal agents are the only category of workers whose salary has been frozen in the last five years," Deslandes told the BBC. "We are not looking for a real salary increase, but a re-adjustment in accordance with inflation during those five years." Federal police are paid between 7,500 and 12,800 reais ($3,200-$5,800) monthly before taxes, according to Agence France-Presse. Some federal police refused to work Wednesday in cities including Rio de Janeiro Brasília and Fortaleza, among others.

> "Federal agents are the only category of workers whose salary has been frozen in the last five years."
>
> — *Renato Deslandes*

U.S. Lawmakers Move Toward Sanctions Against Venezuela

The U.S. Congress is moving toward imposing sanctions against Venezuela's government, the Associated Press reported. Today, State Department officials are scheduled to brief a Senate committee on the deadly street protests that have been happening in the South American country since early February, and a panel of the House of Representatives is expected to finalize a version of sanctions legislation on Friday. The sanctions under discussion in both chambers center on $15 million in funds to promote the rule of law and democracy in Venezuela. The measures would also prohibit visas for some Venezuelan officials who were involved in crack-downs on protesters.

Economic News

Ecuador Rejects Petition for Yasuní Park Oil Drilling Referendum

Ecuador's National Electoral Council has a rejected a petition to hold a referendum on opening the Yasuní National Park to further oil exploration saying that activists failed to collect enough signatures to force the referendum, BBC News reported Tuesday. YasUnidos, a group of Ecuadorean environmentalists and indigenous groups that collected the signatures, accused the council of bias and "fraud." The council validated 359,781 of the 850,000 signatures collected saying many were repeated, incomplete, written by children or used fictitious names. Signatures of five percent of the population, or 583,323 signatures, are required to force a referendum. "Almost seven out of 10 signatures were thrown in the bin," YasUnidos said on Twitter. "The council talks about irregularities, we talk about fraud." The group said it will take its case to the Inter-American Commission on Human Rights. Limited exploration has been conducted in the park since the 1970s, but Ecuadorean President Rafael Correa late last year announced that he was ending a conservation plan that had sought donations of $3.6 billion to prevent drilling in the park, which covers some 10,000 square kilometers (3,860 miles). Critics expressed concern about the effects drilling would have on one of the world's most biodiverse areas and indigenous groups living there.

Correa

File Photo: Ecuadorean Government.

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Featured Q&A

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trend in their currencies, they may have to increase interest rates as Brazil and others have done, which results in slower growth. This is most likely a no-win situation. Now that the tailwinds have shifted, most governments and policymakers should be realizing that structural reforms are needed. Mexico has been doing them and its currency has, therefore, not been penalized. Unfortunately, with a heavy election calendar in the region, many of these reforms are unlikely. Therefore, views on how currencies move will be determined by the Fed, China and, to a certain extent, inflation. Do not expect a much different 2014. The bright spot? Investors are not as enamored of and invested in emerging markets as they were in early 2013. It may not be as bad as last year."

David Ross, independent emerging market analyst: "Recently, companies including Ford, British American Tobacco and Unilever have blamed emerging market currency volatility for earnings shortfalls. This volatility is likely to continue through the next year due to uncertainty concerning China, the global engine of growth, and the United States, the global printer of money. A slowing China means weaker growth prospects for emerging markets, bringing pressure on their currencies. In contrast, the unknown for the United States is its underlying growth and timing of normalization of monetary policy. With the strong April jobs report, the betting will move toward rate hikes earlier in 2015 rather than later, leading to money flows coming to the United States. In addition to China and the United States, the anticipated continued recovery in Europe will add pressure to emerging market currencies. U.S.-oriented exporting countries receive some benefit from a weaker currency. Even for these countries, however, the ability to absorb extreme currency volatility to continue to attract long-term investment is important; for import-oriented economies, such as those in the Caribbean, absorbing this volatility is imperative. To face the upcoming external shocks, countries across Latin America and the Caribbean should be following policies of building reserves, undertaking fiscal policy adjustments (such as reducing budget deficits, raising consumption taxes and lowering public spending) and expanding upon FDI-friendly reforms. Unfortunately, history demonstrates that most countries fail to prepare before a crisis erupts, requiring a central bank response of dramatic interest rate hikes in an effort to protect the currency and control inflation, usually resulting in recession."

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