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## FEATURED Q&A

# What Changes Are Needed in Chile's Pension System?



Demonstrators took to the streets March 31 in Chile to demand changes to the country's pension system. // Photo: @NOMasAFP via Twitter.

**Q** A civilian movement in Chile, “No + AFP,” called for a nationwide demonstration on March 31 to support a project it recently submitted to Congress to overhaul the country's pension system, following a popular legislative initiative process in which some 12,000 people participated, *La Nación* reported. The bill counters President Sebastián Piñera's proposed legislation and seeks to eliminate private-sector pension administrative funds, or AFPs, which manage Chilean workers' capitalization accounts. What are the arguments for and against the use of AFPs? Which parts of Chile's present pension system should the best-possible reform maintain, and which elements should it eliminate? What is the status of Piñera's proposal in Congress, and how much longer is the debate likely to last?

**A** Manuel Agosin, professor and former dean in the School of Economics and Business at University of Chile: “The ‘No + AFP’ movement is a populist reaction to the low pensions that many people are receiving. The movement claims that private companies are stealing people's money and enriching themselves at everybody's expense. This is obviously not true. The reasons behind the low pensions are the many lapses in contributions to workers' pension accounts; the relatively large percentage of the work force that is in the informal sector and therefore don't contribute to the pension accounts (probably between 30 and 40 percent of the work force); the low age of retirement (65 years for men, 60 for women); and the low rate of contribution to the system (10 percent of taxable income, with a ceiling). A return to the pay-as-you-go system that prevailed before 1981 is infeasible. With

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## TODAY'S NEWS

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## U.N. to Provide Training to Mexico's New National Guard

United Nations High Commissioner for Human Rights Michelle Bachelet signed an agreement with Mexican President Andrés Manuel López Obrador to provide human rights training to Mexico's new National Guard.

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## Brazil to Pay Petrobras \$9 Bn to Settle Dispute

The Brazilian government will pay the state oil company to settle a deepwater contract dispute, following years of negotiations.

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## U.S. Secretary of State to Begin Tour of Region

U.S. Secretary of State Mike Pompeo is to leave Thursday on a four-country tour of South America as part of the Trump administration's efforts to push for a political transition in Venezuela.

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Pompeo // File Photo: U.S. State Department.

## POLITICAL NEWS

## U.S. Secretary of State to Begin Latin America Tour

U.S. Secretary of State Mike Pompeo is scheduled to leave Thursday for a four-country tour of Latin America in order to reiterate the Trump administration's push for a political transition in Venezuela, *The Wall Street Journal* reported. During the visit, Pompeo is to visit the capitals of Chile, Paraguay and Peru before heading to Colombia to visit Cúcuta, which lies on the country's border with Venezuela and has been the first stop for many Venezuelans fleeing their home country's political and economic chaos. The visit "reaffirms our commitment to the Western Hemisphere," a senior State Department official told reporters Tuesday, the newspaper reported. Chile, Paraguay and Peru offer models for how countries can transition from dictatorship to democracy, the official said. All four countries on Pompeo's tour have recognized Venezuelan opposition leader Juan Guaidó as Venezuela's legitimate interim president, as has the United States. During his stop in Cúcuta, Pompeo will visit "entities supporting Venezuelan refugees and assess the challenges due to the closed border," the State Department official said. During a Senate Appropriations subcommittee hearing on Tuesday, lawmakers pressed Pompeo, saying the administration should grant temporary protected status to Venezuelans who are living in the United States and whose visas are expiring. The White House has revoked temporary protected status, which allows foreign citizens whose homelands are deemed unstable to remain in the United States, for many Haitians, Salvadorans and Hondurans. Pompeo told senators that the Trump administration is still reviewing proposals to protect Venezuelans who live in the United States. Also on Tuesday, the Organization of American States recognized Gustavo Tarre, the Venezuelan opposition's envoy, as the country's ambassador to the organization, the Associated Press reported. The OAS resolution to recognize Tarre passed with

18 votes in favor, nine opposed, six abstentions and one absence. "It means the usurpation of the Venezuelan seat [at the OAS] has ended," said Tarre. Venezuelan President Nicolás Maduro's foreign ministry issued a statement saying it will consider any decision by Tarre to be "null" and called him a "loud-mouth political usurper." On Monday, the White House formally accepted Guaidó envoy Carlos Vecchio as Venezuela's ambassador to the United States. And last month, the Inter-American Development Bank accepted another diplomat designated by Guaidó, Ricardo Hausmann, as Venezuela's representative to the bank.

## U.N. to Provide Training to Mexico's New National Guard

The United Nations High Commissioner for Human Rights on Tuesday signed an agreement with Mexico's government for the U.N. agency to provide human rights training to President Andrés Manuel López Obrador's newly created National Guard, *El Universal* reported. High



Bachelet and López Obrador signed the agreement on Tuesday in Mexico City. // Photo: Mexican Government.

Commissioner Michelle Bachelet, a former two-time president of Chile, said her office would offer technical assistance to ensure that the new security force respects human rights. "Experience shows us that you can't have security without full respect for human rights, and you can't enjoy human rights without security," Bachelet said, the Associated Press reported. The agreement goes beyond training, she added, saying it will also incorporate elements such as a mechanism for citizen preservation, transparency and accountability. Meanwhile, López Obrador announced that he will name

## NEWS BRIEFS

## Venezuela Removes Eight Metric Tons of Gold From Central Bank: Report

Venezuelan President Nicolás Maduro's government has removed eight metric tons of gold from the central bank's vault and is seeking to sell it abroad in order to raise hard currency, Reuters reported Tuesday, citing a lawmaker and a government source. Amid tightening U.S. sanctions, Maduro has increasingly turned to selling gold reserves in order to raise foreign currency. Venezuela's gold reserves have fallen by eight metric tons since the beginning of the year, the government source said.

## Ecuador Tells Assange He Can't Stay at Embassy Indefinitely

Ecuador on Tuesday reminded WikiLeaks founder Julian Assange, who has been under political asylum at the Andean country's London embassy since 2012, that he can't stay there indefinitely, the Associated Press reported. Foreign Minister José Valencia said a permanent stay was not a viable option for anyone. The comments come as tensions between Ecuador and Assange rise, following the government's accusations that Assange has spread allegations of offshore corruption related to President Lenín Moreno, as well as leaked personal photos of the president online.

## Argentine Gov't Issues \$1.58 Bn in Treasury Notes

Argentina issued two series of treasury notes, denominated in dollars and pesos, on Tuesday worth some \$1.58 billion, the economy ministry said in a statement, Reuters reported. It included \$700 million in so-called "Letes" notes, due in 217 days at a nominal annual interest rate of 4.5 percent, as well as peso-dominated "Lecap" notes for an equivalent of \$875 million, which are due in 110 days at a 55 percent interest rate.

the force's commander on Thursday. The National Guard will consist of military police from Mexico's army and navy, as well as some federal police, he added. López Obrador has vowed to end the country's war on drugs, saying, "We are going to carry out this change to guarantee security without violating human rights," the AP reported. [Editor's note: See related [Q&A](#) in the Dec 3. issue of the Advisor.]

## BUSINESS NEWS

# Brazilian Gov't to Pay Petrobras \$9 Billion to Settle Dispute

Brazilian state-owned oil company Petrobras will receive \$9.06 billion to settle a deep-water contract dispute with the government after years of negotiations, Folha de S.Paulo reported Tuesday, citing a statement by the National Energy Policy Council, or CNPE. The settlement paves the way for other oil companies to access enormous crude deposits in the pre-salt area by allowing the auction of blocks to develop oil reserves beyond the five billion barrels that Petrobras is allowed to produce under a 2010 transfer-of-rights contract, Energy Minister Bento Albuquerque told reporters on Tuesday, Bloomberg News reported. The government will pay the compensation in one settlement after the Oct. 28 auction is held, and winners in the tender will have to pay Petrobras for investments the company has already made in the areas, he added. Details including the value of the signing bonuses and the criteria for participation in the auction will be announced on April 17. "Today we removed the legal uncertainty for one of the main contracts in the country," Waldery Rodrigues Júnior, an official at the Brazilian economy ministry, said at the same press briefing, Bloomberg News reported. The additional volumes up for bidding can reach as much as 15 billion barrels of crude oil. The government has said the auction could raise as much as 100 billion reais (roughly \$25.9 billion) and help alleviate the country's budget deficit.

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the increase in life expectancy, this would imply growing public deficits in short order, or a reduction in benefits and/or increases in contributions. The government's proposal is to increase the rate of contribution to the current system to 14 percent, with the extra 4 percent coming from employers. Furthermore, the project calls for a substantial increase in the non-contributory pensions of people who are unable to generate a minimum pension for themselves. It is going to be a long slog. The opposition is in no mood to give the government a victory, but they are offering no alternative."

**A Kathleen C. Barclay, former president of the American Chamber of Commerce in Chile:**

"Chile's pension system is composed of private defined contributions managed by an administrator (AFP), as well as a solidarity pillar that is fiscally financed for the government to provide minimum pensions for those unable to save. The AFP system on its own was never designed to fully finance all pension needs in Chile. The AFP system has been a success, delivering annual returns of more than 8 percent per year since its inception in 1981, versus 6.3 percent for the MSCI world index. For those who have saved consistently, pensions in excess of 70 percent of final annual earnings can be expected. The system has enhanced domestic savings, thereby fueling the development of a long-term capital market critical to generating Chile's high growth rates. Changing demographics in Chile, including an aging population—where life expectancy has increased by just under 10 years—as well as a large percentage of the working population that has not contributed to the system (independent workers and many small businesses) or that have spent many years out of the work force (for example, women raising families) are factors contributing to inadequate pensions for many Chileans. Further pressure on the system arises from an overall decline in expected yields

from financial investments. The solutions for Chile are clear: significantly increased levels of savings; extension of the retirement age; incorporation of all workers into the defined contribution system; and strengthening of

**“ The AFP system on its own was never designed to fully finance all pension needs in Chile.”**

— Kathleen C. Barclay

the solidarity pillar within the context of Chile's commitment to fiscal discipline. President Piñera's proposal moves pension legislation in the right direction on all fronts and is much needed to introduce necessary reforms. Looking to the future, it will be important for future governments to remain vigilant to make ongoing reforms that will certainly be necessary. It is expected that the discussion will continue over the next several months."

**A Fernando Larraín, director general of AFP Association in Chile:** "Chile's mixed pension system needs to address certain

issues that have not been resolved in the last 40 years in order to be able to provide better pensions. For example, the contribution rate (10 percent) is the same as at the beginning of the system, while life expectancy in Chile has grown rapidly and interest rates have gone down. The bill proposes a change in the contribution rate, raising it to 14 percent. Given the changes in health care and quality of life, the retirement age should also be revised upwards, as has been done in most other countries. The legislation does not change retirement age but establishes certain incentives to delay it. Another problem of the pension system is the gaps. Roughly 30 percent of those who received a pension in 2018 contributed for less than

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10 years. The proposal does not structurally solve the lack of steady contributions for informal workers. It does incorporate insurance, but it's insufficient. The three pillars of the system (solidarity, contributory and voluntary) must be strengthened to improve the system. The proposed bill mainly seeks to strengthen the first pillar. The proposed

“Chile’s mixed pension system needs to address certain issues that have not been resolved in the last 40 years.”

— Fernando Larraín

solution to the political challenges of AFPs—for other actors to manage the additional 4 percent contribution—is not well resolved. It complicates the system for affiliates and may end up being more expensive, including a potential double commission payment, among others. The proposal is currently in the Chamber of Deputies’ labor commission, which is inviting guests to offer their viewpoints on the bill. After this process, the commission will vote on the ‘idea of legislation’ for the project to move forward. If approved, the proposal will go back to the finance and labor commissions for technical work. Then, there will be a vote in the Chamber, after which it will go on to the Senate, where discussion will once again begin. If

both chambers approve it, then the project passes. If only one chamber approves it, a joint commission would have to be created.”

**A** Marco Kremerman, economist at Fundación Sol in Santiago: “The AFP system based on the paradigm of individual accounts as the central element of the contributory pillar of the Chilean pension system failed. At present, 50 percent of old-age pensions are less than 151,000 Chilean pesos (\$225), which is equivalent to 50 percent of the minimum wage, and only half of the 124,000 people who retired last year were able to self-finance pensions of under 48,000 Chilean pesos (\$72) with their savings and AFP returns. The median replacement rate is less than 20 percent of the last salary, a number that reaches 40 percent with state subsidies, far from the 80 percent that was promised when the system was created almost 40 years ago. Given the ostensible fall in the rate of return observed in the last decade, increasing the contribution rate in a scheme of individual accounts does not ensure better pensions for current retirees. Even increasing individual savings from 10 percent to 18 percent will only compensate for the drop in profitability that retirees of the future will experience. In this context, President Piñera’s proposal to strengthen the AFPs’ business and not advance a system that salvages the principles of social security will only have marginal effects on the improvement of pensions, and it will not reverse the current pension crisis.”

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