

BOARD OF ADVISORS

Diego Arria

Director, Columbus Group

Devry Boughner Vorwerk

Corporate VP, Global Corporate Affairs
Cargill

Joyce Chang

Global Head of Research,
JPMorgan Chase & Co.

Marlene Fernández

Corporate Vice President for
Government Relations,
Arcos Dorados

Peter Hakim

President Emeritus,
Inter-American Dialogue

Donna Hrinak

President, Boeing Latin America

Jon Huenemann

Retired VP, U.S. & Int'l Affairs,
Philip Morris International

James R. Jones

Chairman,
Monarch Global Strategies

Craig A. Kelly

Director, Americas International
Gov't Relations, Exxon Mobil

John Maisto

Director, U.S. Education
Finance Group

Nicolás Mariscal

Chairman,
Grupo Marhnos

Thomas F. McLarty III

Chairman,
McLarty Associates

Carlos Paz-Soldan

Partner,
DTB Associates, LLP

Beatrice Rangel

Director,
AMLA Consulting LLC

Jaana Remes

Partner,
McKinsey Global Institute

Ernesto Revilla

Head of Latin American
Economics, Citi

Gustavo Roosen

Chairman of the Board,
Envases Venezolanos

Andrés Rozental

President, Rozental &
Asociados and Senior
Policy Advisor, Chatham House

Shelly Shetty

Head of Sovereign Ratings,
Latin America, Fitch

Roberto Sifon-Arevalo

Managing Director, Americas
Sovereign & Public Finance Ratings,
Standard & Poor's

FEATURED Q&A

Why Does Brazil's Economy Continue to Struggle Along?



Brazilian Economy Minister Paulo Guedes announced this month that the government was cutting its forecast for this year's economic growth. // File Photo: Brazilian Government.

Q Brazil's government is cutting its 2019 growth forecast to 1.5 percent, down from 2.2 percent, Economy Minister Paulo Guedes said May 14, adding that it is asking the country's development bank, BNDES, for additional funding of as much as 240 billion reais (\$60 billion) in order to meet current expenditures without resorting to issuing debt. Moreover, central bank data suggests real activity in March declined for the third consecutive month and by larger than expected, on top of activity declines in January and February. What is behind the government's lowered forecast for economic growth this year, and why does it differ from previous estimates? Which sectors are most likely to take a hit, and why? Is supplementary funding from BNDES enough to help the government meet its budget goals?

A Armando Castelar Pinheiro, coordinator of applied economics at Fundação Getúlio Vargas' Instituto Brasileiro de Economia and former head of the economics department at BNDES: "Three key factors caused the government to lower its growth forecast. One was the weaker-than-expected numbers for the economy in the first quarter, likely a result of tight financial conditions in the last two quarters of 2018. The other is the rise in geopolitical risk, which will further slow the global economy and raise risk aversion, harming emerging markets. Finally, optimism declined about the pace and size of social security reform, lowering consumer and business confidence, leading to a less substantial rise in private domestic demand. Manufacturing and construction are to perform particularly poorly this year—the former due to the combined effect of weak domestic demand and falling

Continued on page 3

TODAY'S NEWS

POLITICAL

Dozens Killed in Brazil, Venezuela Prison Clashes

At least 55 people were killed in a string of clashes at prisons in Brazil's Amazonas State, while at least 29 were killed in a prison in Venezuela's Portuguesa State.

Page 2

BUSINESS

Charges Filed Against Former Pemex CEO

Authorities in Mexico have filed corruption charges against Emilio Lozoya, the former chief executive officer of state oil company Pemex. Lozoya led the company from 2012 to 2016.

Page 3

ECONOMIC

Regulations Holding Back Chilean Mining: Codelco CEO

New environmental regulations and low productivity levels among Chilean workers are holding back the country's mining sector, said Nelson Pizarro, the CEO of state-run copper miner Codelco.

Page 2



Pizarro // File Photo: Codelco.

POLITICAL NEWS

Dozens Killed in Clashes at Prisons in Brazil, Venezuela

Dozens of inmates have been killed over the last few days in violent prison clashes in Brazil and Venezuela. In the northern Brazilian state of Amazonas, at least 55 people were killed in clashes that began Sunday among rival drug gangs in several prisons, The New York Times reported. Drug smuggling routes in northern Brazil have become increasingly profitable, and drug factions have fought for control, the newspaper reported. The violence broke out during visiting hours at the Anísio Jobim penitentiary in Manaus, where 15 inmates were killed, prison officials said. Some of the prisoners were stabbed to death with sharpened toothbrushes, and others were asphyxiated. The prison has seen previous outbreaks of violence. In January of 2017, 56 inmates were killed in clashes there, and violence spread to prisons in other Brazilian states, leaving more than 120 people dead. Following the first incidents of violence at the Anísio Jobim penitentiary on Sunday, bloodshed spread to three other prisons in Amazonas State, where at least 40 inmates were killed. "Infighting among inmates" led to the deaths, Marcos Vinicius, the head of the state's corrections system, told The New York Times. He added that no prison guards had been hurt or taken hostage. On Monday, Brazil's Justice Ministry said it was sending a task force to Amazonas to provide support to local officials. The state's governor, Wilson Lama, expressed hope that the federal reinforcements would "help us in this time of crisis to confront a problem that is a national one: the problems in our prisons." Brazil's prisons are designed to hold about 400,000 people. However, the country's prison population has grown from about 451,000 in 2008 to approximately 841,000 last year, according to data collected by staff members at Brazil's Senate. The prison population is likely to grow if legislators approve measures backed by President Jair Bolsonaro to increase penalties for some crimes. On Saturday, au-

thorities in Venezuela said at least 29 inmates were killed after violence broke out in a jail inside a police station in Portuguesa State, BBC News reported. The state's public security chief, Oscar Valero, said at least 19 people officers were injured. The clashes began Friday when authorities attempted to stop what he called a "massive" escape from the jail. The facility, located in Acarigua, contains approximately 540 inmates, though it was designed to hold only 250. Inmates detonated grenades during the incident, and police faced a "hail of gunfire" when they responded to the attempted breakout, Valero told reporters.

ECONOMIC NEWS

Regulations Holding Back Chilean Mining: Codelco CEO

New environmental regulations and low productivity levels among Chilean workers are holding back the country's mining sector, the chief executive officer of state-run mining company Codelco said Friday, La Tercera reported. In a presentation, Nelson Pizarro said hurdles including water shortages, falling grades of ore and higher energy costs have long presented problems for Chilean miners, and regulatory hurdles are only adding to those problems. "Every day we have to take two steps backward to confront another new environmental regulation, which has created an insufferable level of uncertainty," said Pizarro. The CEO's comments came as Codelco's Chuquicamata mine is undergoing a \$5 billion overhaul in an effort to extend the open-pit mine's lifespan, Reuters reported. Difficult labor negotiations have plagued the mine's operations, and unions have threatened strikes. On Saturday, unionized workers at the mine rejected Codelco's final contract offer and said they would take a strike vote today and tomorrow, Mining.com reported. At the same time, Pizarro criticized Chilean mine workers, saying they are only half as productive as their counterparts in Peru. "I think the development of policies in Chile

NEWS BRIEFS

At Least Two Killed as Strong Earthquake Strikes Northern Peru

Peru's government has declared a state of emergency in parts of the Loreto and Cajamarca regions after a magnitude 8.0 earthquake struck Alto Amazonas province on Sunday morning, state news agency Andina reported. The quake killed at least two people and left dozens injured. School classes have been suspended until an inspection of infrastructure is completed. Staff have reported cracks and damage to 64 schools in several provinces.

Venezuelan Government, Opposition to Continue Talks in Norway

Representatives of Venezuela's government and opposition have agreed to return to Norway for talks on how to address their political impasse, The Washington Post reported Saturday. The meeting, scheduled for next week in Oslo, was confirmed by Norway's foreign ministry. The parties held talks there earlier this month, but the opposition says there were no face-to-face meetings. Tensions escalated in April after opposition leader Juan Guaidó called on the military to oust President Nicolás Maduro.

Two Senior Officials Step Down From Mexican Government

Mexican President Andrés Manuel López Obrador accepted the resignation of a second senior official over the weekend, revealing signs of discord in his six-month-old administration, the Financial Times reported. Josefa González-Blanco resigned as environment minister on Saturday after she admitted to asking Aeroméxico to delay a plane so that she could board. Days earlier, Germán Martínez quit as head of the state social security service, IMSS, over what he called finance ministry "interference."

... has made it so that the hours worked [by Chilean workers] are only little more than half of the formal workday," he said. Over the next two years, output at the Chuquicamata mine is expected to drop by about 40 percent, Reuters reported last week. [Editor's note: See [Q&A](#) on productivity in Latin America in the May 16 issue of the Advisor.]

BUSINESS NEWS

Mexican Authorities File Charges Against Former Pemex CEO

Investigators in Mexico said today they have filed corruption charges against the former head of state oil company Pemex, Emilio Lozoya, The Wall Street Journal reported. The case against Lozoya, who served as CEO of Pemex from 2012 to 2016, marks the first high-profile corruption investigation launched by the administration of President Andrés Manuel López Obrador, whose term began in January. Last week, Mexico's Secretariat of Public Administration (SFP) slapped Lozoya with a 10-year ban on holding public office for providing "false information" about his assets, El Financiero reported. Meanwhile, Mexico's Finance Ministry announced Sunday it had frozen Lozoya's bank accounts, as well as those of steelmaker Altos Hornos de México, or AHMSA, said Santiago Nieto, head of the finance ministry's financial-intelligence unit, in an interview with The Wall Street Journal. AHMSA, one of the country's largest steelmakers, is being investigated for alleged payments of some \$10 million in bribes brokered by Brazilian construction giant Odebrecht in AHMSA's 2014 sale of a fertilizer plant to Pemex, according to the report. In a statement, Ahmsa denied any responsibility for wrongful acts and called the government's action "unprecedented, arbitrary and a violation" of its rights, Reuters reported. The company "denied all responsibility regarding the improper acts" attributed to the firm.

FEATURED Q&A / Continued from page 1

exports, on account of Argentina's recession and the slowdown in international trade more generally. Construction is suffering from the drop in public investment and the large inventory of empty houses. The money from BNDES will be used to redeem government debt, thus preventing a sharper rise. It will not be used to directly finance the deficit. The government expects BNDES to pay around 126 billion reais, slightly less than 2 percent of GDP. The overall public sector deficit ranges around 7 percent of GDP."

A Paulo Vieira da Cunha, partner at Verbank Consulting in New York: "Most likely, GDP contracted in the first quarter (-0.2 percent quarter-over-quarter seasonally adjusted) with a negative carryover for the second quarter, sparking worries that the economy may dip again into a recession. The cause? The anticipated recovery in investments did not come; on the contrary, it is likely to have contracted, again, in the first quarter. Five years after the start of the recession, no sector has returned to its previous peak. Like many, I expected that the 2018 electoral outcome together with the formation of the new economic team and its policy commitments would boost animal spirits. Temer's team adjusted the macroeconomy, and firms and families deleveraged. Then came a bumbling and politically inept president, uncertainties about the social security reform and a more adverse external scenario. Now everyone waits for the reform—after waiting for years, what's a few more months? The question is whether this is the fillip to reanimate investors. If growth is to resume on a sustainable basis, it must be led by investment. Few still think this will be the case, even if there are additional cuts to interest rates and even if the full effects of previous cuts suddenly become more apparent. Among other things, the 2019 budget is underfunded, which has made the government unusually beholden to Congress. It must approve a special debt increase if programs such as Bolsa Família are

not to run out of money. The government will try other subterfuges, but ultimately, it must return to Congress. The way things stand politically, it will be a mess as we approach the 2020 midterm elections—on top of all

“If growth is to resume on a sustainable basis, it must be led by investment.”

— Paulo Vieira da Cunha

the other known structural impediments to growth. So, while there is hope for the public/private partnerships in infrastructure, the now historical low growth (a decade of average growth little above 1 percent annually with declining per-capita incomes) seems to indicate a more permanent drop in the country's capacity to grow."

A Gabrielle Trebat, director for Brazil and the Southern Cone at McLarty Associates: "Prospects for Brazil's economic recovery continue to lag amid ongoing uncertainty with regard to the pace and ambition of much-needed economic reforms. Despite the early optimism that pension reform could be approved in the first half of 2019, political realities have set in, and the timeline for approval has slipped to later this year. The ongoing uncertainty and resulting delay in tackling other needed reforms, including tax and trade liberalization, has left companies hesitant to implement ambitious new investment plans that could catalyze growth and reduce unemployment from its current level of around 12 percent. The situation is affecting all sectors, but, notably, manufacturing and services have taken a hit, while the mining sector continues to feel the fallout of the Brumadinho mining disaster earlier this year. That said, there is reason for continued optimism. Interest rates remain low at 6.5 percent, inflation has stabilized at

Continued on page 4

FEATURED Q&A / Continued from page 3

4.5 percent—well within the central bank's target band—and oil production is healthy, which should help alleviate the fiscal crunch. Tremendous pressure is on BNDES to return \$100 million to the national treasury not only to shore up the fiscal accounts and address budget short gaps, but also as part of an effort to return BNDES to its original mission of promoting economic development and reduce its role in supporting corporate giants that have generously benefited from low-cost BNDES financing at great expense to the federal budget."

A **Lisa M. Schineller, managing director and lead analyst of sovereign and international public finance ratings at S&P Global Ratings:** "Robust recovery from its deep recession continues to prove elusive in Brazil. Last year, real GDP growth forecasts were sequentially lowered, and the same is occurring again in 2019. S&P Global Ratings has assumed a slow rather than 'V-shaped' recovery since the 2015-2016 recession, and modest growth dynamics are one of the prominent weaknesses in Brazil's sovereign creditworthiness (BB-/Stable). Neither the consumer, the government nor exports are poised to generate robust growth. Consumption remains constrained by both high unemployment and high underemployment, with the latter almost double the 12 percent unemployment rate. Recent weakness in retail sales has led to lower growth expectations this year. Fiscal policy has been and needs to remain contractionary to generate lower primary (noninterest) deficits. Global and regional economic conditions hurt exports. Finally, the tragic mining disaster this year has hit investment in the sector. Despite historically low real interest rates, weak corporate credit growth and substantial excess

capacity in the economy and manufacturing sector in particular is holding back investment, absent signs that domestic demand is likely to accelerate. Policy uncertainties ahead of last year's presidential elections generated a wait-and-see attitude among

“ Robust recovery from its deep recession continues to prove elusive in Brazil.”

— Lisa M. Schineller

investors. Ongoing uncertainty seems to reflect questions on the timing, breadth, depth and pace of fiscal correction—led by passage of pension reform and on the capacity of the Bolsonaro administration to deliver on its market-oriented policy agenda that includes a broad infrastructure agenda dependent on private investment. While pension reform is a key component of fiscal correction in Brazil, it's also only a first step. Additional politically tough measures to tackle payroll and other earmarked nondiscretionary spending would be needed to satisfy the constitutional spending rule and generate a swing of four percentage points of GDP in the primary balance. Progress toward stabilizing debt dynamics appears key for bolstering private sector confidence. Funds from BNDES, while providing space to satisfy some constitutional financing constraints (the so-called golden rule) in the near term, are not a substitute for structural fiscal measures to do just that."

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org.

LATIN AMERICA ADVISOR

is published every business day by the Inter-American Dialogue, Copyright © 2019

Erik Brand

Publisher
ebrand@thedialogue.org

Gene Kuleta

Editor
gkuleta@thedialogue.org

Anastasia Chacón González

Reporter
achacon@thedialogue.org



Michael Shifter, President

Genaro Arriagada, Nonresident Senior Fellow

Sergio Bitar, Nonresident Senior Fellow

Joan Caivano, Director, Special Projects

Michael Camilleri, Director, Peter D. Bell Rule of Law Program

Kevin Casas-Zamora, Nonresident Senior Fellow

Ariel Fiszbein, Director, Education Program

Peter Hakim, President Emeritus

Claudio Loser, Senior Fellow

Nora Lustig, Nonresident Senior Fellow

Margaret Myers, Director, Asia and Latin America Program

Manuel Orozco, Director, Migration, Remittances & Development

Jeffrey Puryear, Senior Fellow

Tamar Solnik, Director, Finance & Administration

Lisa Viscidi, Director, Energy Program

Denisse Yanovich, Director of Development and External Relations

Latin America Advisor is published every business day, except for major U.S. holidays, by the Inter-American Dialogue at 1155 15th Street NW, Suite 800 Washington, DC 20005

www.thedialogue.org

ISSN 2163-7962

Subscription inquiries are welcomed at ebrand@thedialogue.org

The opinions expressed by the members of the Board of Advisors and by guest commentators do not necessarily represent those of the publisher. The analysis is the sole view of each commentator and does not necessarily represent the views of their respective employers or firms. The information in this report has been obtained from reliable sources, but neither its accuracy and completeness, nor the opinions based thereon, are guaranteed. If you have any questions relating to the contents of this publication, contact the editorial offices of the Inter-American Dialogue. Contents of this report may not be reproduced, stored in a retrieval system, or transmitted without prior written permission from the publisher.