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FEATURED Q&A

Why Is Peru's Economy Losing Steam So Quickly?



Peruvian President Martín Vizcarra is facing a slowing economy. // File Photo: Peruvian Government.

Q Peru's government on Aug. 23 cut its projections for growth this year to 3 percent and next year to 4 percent. The government had previously expected growth rates of 4.2 percent and 4.5 percent, respectively. What are the most important domestic and international factors weighing on Peru's economy? To what extent is political uncertainty in Peru leading businesses to delay investment decisions? Which sectors in the country are doing the best, and which are doing the worst?

A Alfredo Thorne, former Peruvian finance minister and principal director at Thorne & Associates: "After averaging per capita growth of 4.6 percent between 2001 and 2014, Peru's real GDP has slowed to 1.8 percent between 2014 and 2018, and consensus estimates are only 0.7 percent for this year's growth. Analysts ask if Peru's economic miracle is coming to an end. Certainly, the trade war between Peru's two main trading partners—the United States and China—has hit the economy. Also, the export growth rate, as well as terms of trade, have turned negative after being the drivers of economic growth. Yet this was unsurprising given Peru's dependence on commodity exports and trade openness, reaching more than 50 percent of overall real GDP. The upshot is that the more traditional engines of growth—capital and total factor productivity growth—are failing to deliver rapid growth rates. Some blame politics. For once, since the Lava Jato scandal broke in late 2016, Peru has engaged in a fight against corruption. At that time, Brazilian construction firms involved in corruption controlled about 80 percent of public works and PPP concessions. Since then, civil servants

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Ex-FEMA Officials Charged With Fraud in Puerto Rico Case

Two former officials of the U.S. Federal Emergency Management Agency were among those arrested on fraud charges in connection with recovery efforts after Hurricane Maria struck Puerto Rico in 2017.

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Colombia's top administrative court maintained a suspension on the use of hydraulic fracturing.

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POLITICAL

Brazil's Homicide Rate Falls for First Time Since 2015

Brazil's homicide rate fell 10 percent last year, its first decline since 2015, according to a research group. Justice Minister Sérgio Moro said the government is working to bring the country's murder rate down.

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Moro // File Photo: Brazilian Government.

POLITICAL NEWS

Brazil's Homicide Rate Falls 10 Percent: Research Group

Brazil's homicide rate declined by 10 percent last year, as compared to 2017, according to the Brazilian Forum on Public Safety research group, news magazine *Veja* reported Tuesday. The country registered 57,341 violent deaths in 2018, making Brazil one of the countries with the highest levels of violence in the world. However, it was a drop from 2017, when Brazil recorded a record high 63,880 violent deaths.

“Our expectation is that this trend continues and that's what we're working towards.”

— Sérgio Moro

Last year was the first since 2015 that the country's homicide rate declined, and it was the sharpest annual decline since 2007, the organization said, *The Wall Street Journal* reported. Brazilian Justice Minister Sérgio Moro told the newspaper that the number of murders this year in Brazil fell by 20 percent for the first half of this year, as compared to the same period last year. “Our expectation is that this trend continues and that's what we're working towards,” said Moro, who has headed the Brazilian government's efforts at fighting crime since President Jair Bolsonaro took office in January. While still high, Brazil's murder rate of 27.5 per 100,000 inhabitants now places it lower than Mexico, the newspaper reported. The decline is largely due to a truce in a turf war between Brazil's largest drug gangs, according to crime experts. Additionally, states have worked to isolate and transfer imprisoned drug kingpins, who often run drug trafficking networks from inside prisons. Researchers also add that Brazil's federal police force has weakened criminal gangs by targeting their

money laundering activities. However, Brazil is also facing a growing number of killings by police, which Bolsonaro has supported, *The Wall Street Journal* reported. In 2018, police officers in Brazil were responsible for 6,220 deaths, a 20 percent rise from 2017, according to data compiled by the Brazilian Forum on Public Safety. [Editor's note: See related [Q&A](#) in the May 15 issue of the Advisor.]

Ex-FEMA Officials Charged With Fraud in Puerto Rico Case

U.S. authorities on Tuesday arrested two former officials of the Federal Emergency Management Agency, or FEMA, on fraud charges in connection with the recovery efforts in Puerto Rico after Hurricane Maria pummeled the U.S. territory in 2017, *CNBC News* reported. Ahsha Tribble, FEMA's former deputy administrator for the region that includes Puerto Rico, was arrested for allegedly taking bribes from the president of a company that received \$1.8 billion in federal contracts to repair the island's electrical grid. Tribble is accused of pressuring other FEMA employees and the Puerto Rico Electric Power Authority, or PREPA, to use a company called Cobra Acquisitions to work on power restoration, according to a statement from the Justice Department, *Time Magazine* reported. Donald Keith Ellison, then-president of Cobra Acquisitions, was also arrested as part of the investigation. Tribble allegedly received perks including hotel accommodation, first-class airfare, a credit card and personal helicopter flights from the company, as well as a job at Cobra Acquisitions for a friend who previously worked at FEMA, Jovanda Patterson, who was also arrested and is facing charges. “These defendants were supposed to come to Puerto Rico to help during the recovery after the devastation suffered from Hurricane Maria,” U.S. Attorney Rosa Emilia Rodríguez-Vélez said in a statement. “Instead, they decided to take advantage of the precarious conditions of our electric power grid and engaged in a bribery and honest services wire fraud scheme in order to enrich themselves illegally,” she added.

NEWS BRIEFS

Venezuela Begins Military Exercises Along Colombian Border

Venezuelan President Nicolás Maduro's government on Tuesday began extended military exercises along the country's border with Colombia, the Associated Press reported. Tensions between the South American nations recently rose as both governments accused each other of harboring hostile armed groups within their respective territories. “The moment has come to defend our sovereignty and national peace by deploying our defense resources in full force,” Maduro said. Tanks, missile launchers and aircraft sat at the an international airport near the border, where some 150,000 military personnel will conduct drills through Sept. 28.

Squatters Find Bones at Site Believed to be Home of Ex-Paraguayan Dictator

Forensic experts plan to carry out tests on bones that squatters found at the site of a home believed to have belonged to late Paraguayan dictator Alfredo Stroessner, *BBC News* reported Tuesday. The bones were found at the property near the city of Ciudad del Este. During Stroessner's 1954-1989 rule, 459 people were killed or disappeared. Stroessner died in 2006.

Brazil's Banrisul to Hold Secondary Share Offering

Brazilian state-controlled lender Banco do Estado de Rio Grande do Sul said Tuesday it would hold a secondary share offering of 96 million common shares, according to a securities filing, *Reuters* reported. Banrisul, as the bank is known, had said last month that its controlling shareholder, the state of Rio Grande do Sul, was looking to sell a stake in the company but maintain its controlling stake. The lender added that it will price the share offering on Sept. 17.

‘Safe Third Country’ Deal With U.S. Unneeded: Ebrard

Mexican Foreign Minister Marcelo Ebrard on Tuesday portrayed a “safe third country” deal with the United States as unnecessary and politically untenable, CBS News reported. Ebrard’s comments in Washington followed an announcement on Monday by acting U.S. Customs and Border Protection head Mark Morgan, who said the number of migrants apprehended or turned away by U.S. authorities fell for a third consecutive month in August. “The Mexican strategy has produced important results,” said Ebrard. A safe third country deal would require migrants passing through that country to request asylum there rather than continuing to the United States.

ECONOMIC NEWS

Colombian Court Maintains Suspension of Fracking Activities

In a ruling Tuesday, Colombia’s top administrative court maintained a temporary suspension on the use of hydraulic fracturing, or fracking, techniques to extract oil and gas, El Tiempo reported. The Council of State’s decision continues a moratorium on the regulation for development of non-conventional oil deposits that has been in place since November, as part of an ongoing lawsuit that an environmental lawyer filed against the energy ministry, Reuters reported. “The measure that proposed giving an open road to the exercise of fracking has been defeated while it is decided whether its regulation is legal or not,” the court, which is responsible for ruling on administrative matters, said in a statement. There is no law against fracking in Colombia, but state-run oil company Ecopetrol has been pushing for the use of the practice, and the government says

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afraid of wrongdoing have delayed approval of public works projects, and politics have turned for the worse. From 2001-2014, the economy delivered rapid growth, more than 10 million were pulled out of poverty, the income of the middle class boomed and political confrontation had limited effects on the economy. Amid the Lava Jato graft scandal, with Peru’s last five former presidents being investigated, politics have taken the front seat, and the economy’s ability to benefit the lower and middle classes has been undermined. Social conflict has stalled large mining and PPP projects and, afraid of losing popularity, the government has edged in favor of populism—benefiting small rent-seeking minorities that block large projects. The upshot is that the essence of Peru’s model of economic reform and rapid growth extending to the society at large is being challenged.”

A **Beatrice Rangel, member of the Advisor board and director of AMLA Consulting in Miami Beach:** “Peru is perhaps the single most important success story after Chile and Costa Rica in terms of development. Its GDP has been growing steadily for the past 15 years, poverty has been reduced from 40 percent to 26 percent of the population and the reach of public services has grown tenfold over the last decade, thanks to neighborhood associations that have turned former shantytowns into thriving middle class localities. But there are limits to growth when you neglect infrastructure. While the country has had several blue-chip infrastructure plans, they all collapsed in 2017 when the Odebrecht scandal turned infrastructure

regulations are needed, a position that has sparked debate among lawmakers, activists, officials and citizens, Reuters reported. Ecopetrol has said it is considering spending \$500 million on exploring unconventional deposits over the next three years, but an environmental licensing authority suspended the evaluation of

into the moral equivalent of a corruption harbingering. The current slowdown has to do with a lack of appropriate infrastructure in terms of roads, highways, train ports and airports. According to the World Economic Forum’s 2018 competitiveness index, Peru has the

“There are limits to growth when you neglect infrastructure.”

— Beatrice Rangel

worst roads in South America after Paraguay and Bolivia and ranks among the poorest for overall infrastructure on the continent. Peru’s infrastructure gap is about \$160 billion. Thus, former growth engines such as mining and fishing have stumbled with the competitive gap as enhanced production demands a much better infrastructure. Its lack makes Peruvian minerals and fisheries less competitive in the world. This has affected the growth rate, as has the slowdown in China—Peru’s single most important trading partner after the United States. Fortunately for the country, the government is facing the infrastructure challenge head on with the establishment of several goals to be met over the next 10-20 years. The great news is the Peruvian state has chosen to act as a facilitator, leaving to private initiative through public-private partnerships or direct investment to come up with a solution to growth limitations. Infrastructure development will thus be geared toward wealth creation, on which Latin America needs to focus.”

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the company’s request to start a pilot project pending the court’s decision on regulations, Reuters reported. ConocoPhillips and Canacol also had their requests for fracking licenses shelved. Colombia’s energy ministry has said fracking could boost the country’s oil and gas reserves by nearly threefold.

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A **Roberto Abusada, president of the Peruvian Economy Institute:** “Successive downward revisions of Peru’s 2019 and 2020 growth rate forecasts are the result of deteriorating domestic and international events. The trade war unleashed by the United States and lower growth prospects of the world economy have weighed on economic performance in Latin America and other emerging economies. In Peru, the protracted political conflict between Congress and the executive branch has hurt business and consumer confidence. It further deteriorated when President Martín Vizcarra announced that he would ask Congress to bring the 2021 general election

“**In Peru, the protracted political conflict between Congress and the executive branch has hurt business and consumer confidence.**”

— Roberto Abusada

forward to April 2020. Private investment has stalled despite very high mining investment derived from the ongoing construction of three large mining projects. Serious managerial deficiencies within both central and subnational governments have ruined the possibility of carrying out countercyclical public investment policies, which declined by 4.6 percent during the first half of the year with respect to a similar period last year. In the first six months of the year, the economy has grown by only 1.7 percent year-on-year, with a particularly sluggish second quarter growth rate of 1.2 percent. While the second half is bound to improve, most analysts believe that 2019 growth will be at or below 2.5 percent, a rate that is lower than the country’s potential output growth, calculated at 3.5 percent. Supply shocks that occurred in the first half in the mining and the fishing industries will be reversed during the second

half. Nonprimary sectors are doing relatively well, led by construction and services. In recent years, the country’s growth potential has been severely hampered by the lack of economic reforms, social conflicts around mining projects and burgeoning bureaucratic red tape.”

A **Francisco Durand, professor of political science at the Catholic University of Peru:** “Peru’s economy is going through a slow growth period, more pronounced now than previously expected, mostly because of the deterioration of the terms of trade given China’s slowdown and its ongoing trade war with the United States. However, business leaders see ‘political noise’ as the major culprit, including the presidential proposal to call for early elections. Business confederation CONFIEP insists on prioritizing private investment rather than insisting on political reforms and corruption investigations, which implicate major foreign and national construction companies. In addition, the APRA and Popular Force parties are considering impeaching President Vizcarra and blocking reforms, generating a stalemate between the two branches of government. The cancellation of the Tía María mining project after weeks of social protest in the south has widened the gap between business leaders and Vizcarra, who is now seen as a ‘leftist,’ adding another element of complexity to the ongoing political crisis. Another political factor is public opinion. Most Peruvians support the president’s initiatives to close Congress and confront the ‘judicial-political mafias’ that are trying to block corruption investigations. In spite of the ‘political noise’ that bothers investors, Peru’s growth rates, moderate as they are, are higher than those of the biggest countries in the region, given Peru’s diversified export basket and a still dynamic internal market. And the political crisis, serious as it is, is being dealt with respecting the rules of the game, without violating the Constitution.”

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