LATIN AMERICA ADVISOR

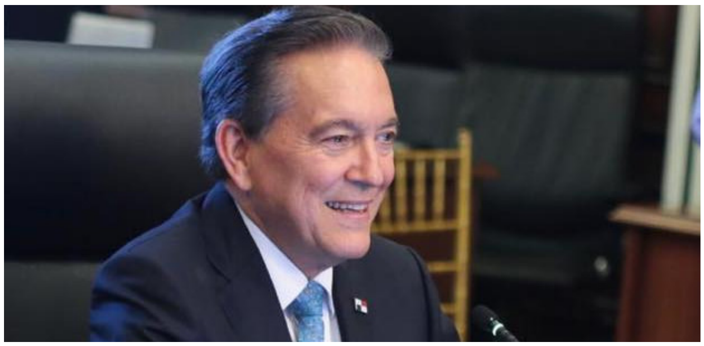
A DAILY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

Thursday, February 20, 2020

FEATURED Q&A

Is Panama's Weaker Economy a Sign of Trouble to Come?



Panamanian President Laurentino Cortizo, who took office last July, is facing economic challenges including a growing deficit and higher government debt levels. // File Photo: Panamanian Government.

Q Panama is facing economic headwinds that include a widening fiscal deficit and higher levels of government debt. Economic growth in the Central American country has also slowed in recent years. Does Panama face growing economic challenges, and what will they entail? What factors will help to support the country's economy in the period ahead? How well is President Laurentino Cortizo, who has been in office less than a year, managing the economy?

A Livia Honsel, associate director for sovereign and international public finance ratings at S&P Global Ratings: "After years of impressive economic growth, which contributed to improved socioeconomic indicators, President Laurentino Cortizo took power last July amid an economic deceleration, a deterioration in fiscal accounts and rising unemployment. President Cortizo's administration has prioritized restoring fiscal discipline and reviving growth. The government has started clearing the large stock of accounts payable, passed a public-private partnership law and is willing to reform the constitution in order to strengthen institutions. Although implementation is key and results will take time, these measures have generated optimism in the business sector. Difficulties could arise in passing legislation in the National Assembly given the tense relationship between President Cortizo and his own party's legislators, which could hurt confidence. Despite slower growth compared with previous years, Panama's economic prospects remain solid. Business-friendly policies, progress in large infrastructure projects and the expansion of copper exports should support

Continued on page 3

TODAY'S NEWS

POLITICAL

Couple Arrested in Murder of Mexican Girl

A man and a woman were arrested in connection with the murder of a seven-year-old girl who was abducted last week after leaving school in Mexico City.

Page 2

ECONOMIC

Argentina's Debt Level Not Sustainable: IMF

Argentina's level of debt is unsustainable, and private creditors must make a "meaningful contribution" to help end the country's financial crisis, the International Monetary Fund said.

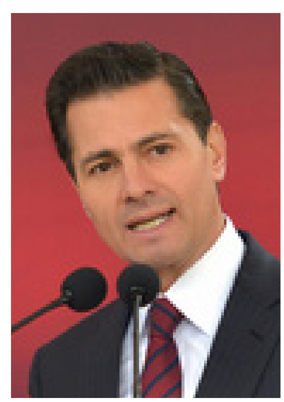
Page 2

POLITICAL

Former Mexican President Peña Nieto Under Investigation

Mexican authorities are investigating former President Enrique Peña Nieto in connection with the corruption case against former Pemex chief Emilio Lozoya, who was arrested last week in Spain.

Page 2



Peña Nieto // File Photo: Mexican Government.

POLITICAL NEWS

Mexican Authorities Investigating Peña Nieto in Graft Case

Mexican authorities are investigating former President Enrique Peña Nieto in connection with the corruption case against Emilio Lozoya, the former head of state-run oil company Pemex, The Wall Street Journal reported Wednesday, citing a senior Mexican judicial official. Lozoya was arrested last week in Spain, and Mexico has requested his extradition. He is accused of pocketing millions of dollars' worth of bribes from Brazilian construction conglomerate Odebrecht and Mexican steel manufacturer Altos Hornos de México. Mexican government investigators allege that Odebrecht paid Lozoya $9 million in order to secure contracts when he was a top official of Peña Nieto's campaign for president in 2012 and after he was named head of Pemex. Authorities also allege that Lozoya received $3.5 million from Altos Hornos to ensure the sale of a fertilizer plant, Agronitrogenados, to Pemex for far more than it was worth. "The attorney general's office has evidence that the corruption of Lozoya in Agronitrogenados and Odebrecht reaches to the highest level," the unnamed Mexican judicial official told The Wall Street Journal, referring to Peña Nieto. "The extradition and [any possible] confession of Lozoya are elements that together with ongoing investigations will decide if the former president is charged in the future." Peña Nieto could not be immediately reached for comment, but he has denied wrongdoing in the past. The chairman of Altos Hornos, Alonso Ancira, whom Spanish authorities arrested last May, also has denied wrongdoing. Ancira is currently fighting extradition to Mexico. Before fleeing Mexico last May, Lozoya denied wrongdoing. After Lozoya was arrested in Spain last week, his lawyer, Javier Coello Trejo, told a Mexican television station that Lozoya "didn't act on his own." As Pemex's chief executive, Lozoya reported directly to Peña Nieto. Coello Trejo said he was unsure whether Lozoya would fight extradition back to Mexico.

Couple Arrested in Murder of 7-Year-Old Mexican Girl

Mexican authorities on Wednesday arrested a couple as part of the investigation into the murder of a seven-year-old girl last week that has sparked protests and calls for action, BBC News reported. Fátima Aldrighett disappeared after leaving school in Mexico City on Feb. 11. Her body was found with signs of abuse in a plastic bag four days later. Police detained a man and a woman after discovering items at a house linking them to the child's disappearance. They are suspected of kidnapping, torturing and killing Aldrighett. The girl's murder has renewed a wave of protests by women's rights activists, who have clashed with police over the last week and set fires in the capital's central square, The Wall Street Journal reported. They also spray-painted the walls of the National Palace, including with the names of women recently killed and phrases such as "AMLO Get Out," in reference to President Andrés Manuel López Obrador. The president sparked anger during a daily morning press conference last week when asked about Aldrighett's murder. "Look, I don't want to talk anymore about femicide," he said. "Because this issue has been very much manipulated in the media." On Tuesday, the lower chamber of Mexico's Congress passed legislation that would raise prison sentences for crimes of femicide and sexual abuse of minors. The bill will now go to the Senate.

ECONOMIC NEWS

Argentina's Debt Level Unsustainable: Int'l Monetary Fund

Argentina's debt is unsustainable, and private creditors need to make a "meaningful contribution" to help end the South American country's financial crisis, the International Monetary Fund

NEWS BRIEFS

Brazil's Petrobras Posts Record Profit of $9.19 Billion for 2019

Brazilian state oil company Petrobras posted a record profit last year of 40.1 billion reais ($9.19 billion), the firm said in a securities filing on Wednesday. Petrobras' strategy of doubling down on deepwater production and exiting noncore activities seems to be paying off, Reuters reported. However, Petrobras underperformed analysts' expectations in the fourth quarter, when net income amounted to 8.15 billion reais, significantly below the estimated income of 9.09 billion reais, according to analysts at Brazilian investment bank BTG Pactual.

Colombia Launches $63.9 Million Fund to Help Coffee Farmers

Colombia, the world's number-one producer of washed arabica coffee, launched a fund worth 218 billion pesos ($63.9 million) on Wednesday in a bid to stabilize coffee prices and protect farmers from volatile markets. Colombia's coffee output last year was its highest in 27 years, totaling 14.8 million 60-kilogram bags. The fund will allow coffee growers to cover production costs and avoid losses in case of unexpectedly lower prices. [Editor's note: See related **Q&A** in the April 26 issue of the Advisor.]

Brazil's Caixa to Issue Bonds in Order to Prepay Debt to Government

Brazilian state-run bank Caixa Econômica Federal plans to issue foreign bonds in order to prepay 9 billion reais ($2.06 billion) in debt to the government, Caixa's chief executive, Pedro Guimarães, said Wednesday, Reuters reported. Also on Wednesday, Caixa reported record net income of 21 billion reais ($4.79 billion) for 2019.

said Wednesday in a statement, The Wall Street Journal reported. The statement followed a meeting in Buenos Aires between Julie Kozack, the IMF's deputy director of Western Hemisphere affairs, and Argentina's finance minister and central bank chief.

BUSINESS NEWS

Venezuela's Maduro Creates Commission to Reform PDVSA

Venezuelan President Nicolás Maduro on Wednesday declared an "energy emergency," announcing the creation of a commission to rehabilitate state oil company PDVSA in a bid to bolster the country's crumbling oil industry, Bloomberg News. Economy Vice President Tareck El Aissami will chair the commission, which has the goal of increasing crude production, Maduro said. Other members of the commission include former Energy Minister Asdrúbal Chávez as commission vice president, Defense Minister Vladimir Padrino and armed forces Strategic Operational Commander Remigio Ceballos. "I won't accept more excuses," Maduro said at an event with PDVSA workers that was broadcast on state television. "Either we produce, or we produce. Venezuela has to be an oil power," he added. He said the goal is for Venezuela to raise crude output to two million barrels per day this year, more than double the current levels, Reuters reported. The announcement came one day after the United States slapped sanctions on Rosneft Trading, a subsidiary of Russian state oil company Rosneft that has become a major intermediary for Venezuelan crude since the administration of U.S. President Donald Trump blacklisted PDVSA last year. "The sanctions, the blockade—I will not accept any more excuses," Maduro said, Reuters reported. "I am signing a decree to declare an energy emergency in the hydrocarbons industry in order to adapt necessary and urgent measures to guarantee national energy security and protect the industry from imperialist aggression."

FEATURED Q&A / Continued from page 1

growth momentum in the next couple of years. Long-term growth will also depend on improving the quality of education of the work force, further diversifying the economy—particularly through the development of the tourism sector, improving fiscal management and strengthening the country's large financial system. Panama will also need to address water shortages resulting from climate change combined with heavier traffic, which can affect revenues from the Panama Canal, which are crucial for the country's economy and fiscal revenues. The canal has recently started charging an additional fee to discourage traffic during periods of low water levels and is considering medium-term solutions."

A **Carlos Morales, director for Latin America sovereigns at Fitch Ratings:** "Panama's economic growth slowdown over the past years is mostly due to completion of infrastructure projects and a softer real estate market affecting construction, a key growth driver, and a slump in retail commerce. The Minera Panamá copper mine, anticipated to yield three times Panama's goods exports ($2 billion at peak capacity), began production and accounted for a significant portion of growth in 2019. However, mining activity's economic and fiscal spillover effects have so far been limited. Fitch projects real GDP growth will improve to 4 percent in 2020 and 2021, below the 5 percent five-year average but above regional peers. Growth is set to improve as mining operations ramp up to peak capacity. Copper production could contribute one percentage point to growth, according to authorities. The construction sector will continue to be a drag given indications of oversupply. The government projects to lower on-budget capital investment, below historical averages, are also constraining economic growth. Private-public partnerships could complement government infrastructure projects under a recently approved law; however, these might experience delays as the framework is implemented. Medium-term risks include water scarcity, which could affect the Panama Canal. Lower economic activity could exert pressure on the fiscal consolidation efforts. Government debt rose substantially in 2019 as the new administration cleared accumulated arrears from previous governments. The fiscal deficit rose above historical averages as revenues contracted through the year. Government revenues have persistently fallen short of economic activity, posing another constraint to the government's capacity to reduce the fiscal deficit and stabilize the debt burden."

A **Renzo Merino, assistant vice president and analyst in the Sovereign Risk Group at Moody's Investors Service:** "After expanding at almost 6 percent on average from 2014-2017, Panama's economic growth slowed to 3.4 percent in 2018-2019. The economy's dual tracks appear to be facing important headwinds. The external, service-oriented sector, where the canal plays an important role, is exposed to slower global trade and the effect of climate change on water resources. Meanwhile, the domestic, investment-led economy is highly dependent on the construction industry. Over the past two decades, the construction sector has grown to represent 20 percent of GDP and is a key source of employment. But as large-scale infrastructure projects conclude and the real estate market reshuffles following a period of strong supply, the construction sector is underperforming. Moody's expects growth to recover in 2020, with future trend growth likely closer to 4 percent. Growth will remain dependent on investment prospects. This will lead to fiscal challenges as revenues will not grow as fast as in the past, potentially requiring the government to rein in capital expenditures to reduce the deficit. The Cortizo administration has expressed interest in fostering public-private partnerships to compensate for

Continued on page 4

FEATURED Q&A / Continued from page 3

lower public investment. Panama's role as a regional trade and financial hub underpin its economic potential, making it an attractive destination for foreign direct investment. Further developing the logistics sector will not only require greater fixed capital but also ensuring a continued supply of skilled labor. Additionally, income inequality remains a lingering issue. More inclusive growth will be key to containing potential social tensions, as seen elsewhere in the region, that could further weigh on growth and fiscal dynamics."

A **Joaquín Jácome Diez, senior partner at Jácome & Jácome in Panama City and former trade minister of Panama:** "Panama's economy has been among Latin America's top performers over the last decade. With an average growth of 6 percent, Panama is one of the region's biggest FDI recipients per capita. Poverty levels are diminishing significantly, but income distribution is the worst in the hemisphere after Haiti. President Cortizo not only received a weakened economy with growth of 3 percent in 2019 and a projection of 4 percent for 2020, but also a fiscal deficit of more than 2 percent. His administration was forced to modify the fiscal social responsibility law in order to allow a deficit of 3.5 percent for 2019 until 2022. The national debt is hovering around $30 billion, 46 percent of the country's GDP. Besides reactivating a sluggish economy, the new administration must modify the constitution and make structural changes in some sectors so that Panama can remain competitive and keep attracting FDI. It has to address the most sensitive issues for Panamanians: social security and pension reform, which requires national consensus in order to avoid social instability. Public investment, tourism, mineral exports and logistics are among the areas expected to help the economy recover its leadership in the hemisphere, but the impact of the coronavirus on the economy remains uncertain. The executive branch has taken several actions to turn around the economic situation. However, the perception that certain factions of the ruling party are more concerned with their political agendas (recovering lost time after 10 years out of power) helps neither the country nor President Cortizo's administration."

A **Marco Gandásegui Jr., professor of sociology at the University of Panama and research associate at the Center of Latin American Studies (CELA):** "The IMF and the World Bank backed Panama's spending spree in the early 21st century. The country was enjoying an economic boom after the Panama Canal was transferred in 1999. After the boom years passed, the Panamanian economy went into a tailspin, and government spending lost its earlier thrust. Following the IMF's advice, the governments after the 1989 invasion abandoned industry and agrobusiness. At present, the economy's main income are tolls from the Panama Canal and financial activities. The isthmus has the two largest Latin American port complexes and a copper mine, which export more than $3 billion a year with little impact on Panama's economy. The main economic challenge at present is how to deal with China's Silk Road offers. The Chinese are interested in converting Panama and its canal into its Latin American hub. Panama's government and weak private sector are also very interested. However, the United States has blocked negotiations between Panama and Beijing. The cash flow from the canal (between $2 billion and $2.5 billion dollars annually) is increasingly subject to corruption by traditional rentiers who control the country's political system. President Cortizo faces all kinds of political and financial problems. Corruption is his main quagmire. Political parties have lost their wings, and many fear a collapse of governance. The government's ability to balance its budget is in peril. The canal's cash flow has stagnated, and there are no signs a new tax regime can replace the old one put in place 25 years ago."

LATIN AMERICA ADVISOR
is published every business day by the Inter-American Dialogue, Copyright © 2020

Erik Brand
Publisher
ebrand@thedialogue.org

Gene Kuleta
Editor
gkuleta@thedialogue.org

Anastasia Chacón González
Reporter & Associate Editor
achacon@thedialogue.org

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