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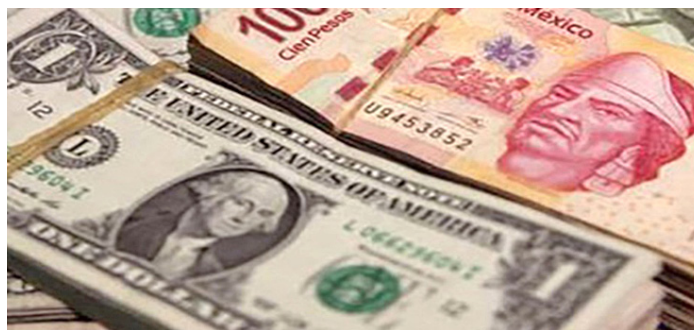
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## FEATURED Q&A

# How Will Currency Fluctuations Affect Economic Recovery?



Some Latin American currencies have slumped against the U.S. dollar this year. // File Photo: Mexican Government.

**Q** JPMorgan on April 13 recommended that investors sell emerging-market currencies, a reversal from early in the year when it had forecast strength in the currencies of emerging markets. Among the currencies that have been battered is the Brazilian real, which has slumped 9 percent against the U.S. dollar this year. What are the major reasons for the weakness in emerging-market currencies in Latin America, and what will those fluctuations mean for the region's economic recovery? Where in the region will currencies be the weakest this year, and where will they see relative strength?

**A** Geoffrey Dennis, independent emerging markets commentator and former head of global emerging markets strategy at UBS: "Two factors explain the weakness of Latin American currencies in 2021—a rising U.S. dollar and domestic political/macro developments mainly tied to the devastating impact on the region of Covid-19. The dollar/euro rate has unexpectedly risen by 2.2 percent this year, and regional currency performance versus the dollar varies from flat for the Mexican peso to a drop of 7 percent for the Brazilian real (and -9.5 percent for the Argentine peso). While every country has suffered badly from the pandemic, deaths per 100,000 people have been highest in Brazil, Peru and Mexico, according to Johns Hopkins University data. Political risks abound. Governability is in question in Bolsonaro's Brazil, Peru faces a second-round election with neither candidate having a high approval rating, and Chile faces a constitutional conference and an election in 2021. The standout performance of the Mexican peso

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## TODAY'S NEWS

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## Bolsonaro Cuts Environment Budget After Vowing Increase

Brazilian President Jair Bolsonaro approved cuts to the country's environmental budget one day after he vowed to raise spending to protect the environment.

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### ECONOMIC

## Guyana, India Eying Long-Term Oil Deal: Report

India has reportedly approached Guyana about a potential long-term deal to buy oil. The countries could soon enter talks about a long-term agreement for Guyana to supply the commodity to India.

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### POLITICAL

## Mexico Extends Term of Supreme Court Chief

Mexico's Congress approved controversial legislation, which President Andrés Manuel López Obrador supports, to extend the term of the country's Supreme Court chief, Arturo Zaldívar.

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Zaldívar // File Photo: Mexican Supreme Court.

## POLITICAL NEWS

## Mexican Congress Extends Term of Supreme Court Chief

Mexico's Congress on Friday approved legislation to extend the term of the chief of the country's Supreme Court, Arturo Zaldívar, the Financial Times reported. The measure has the support of President Andrés Manuel López Obrador. Zaldívar said he was caught by surprise when the measure was added last week to a package of judicial reform legislation. The Supreme Court itself would resolve any legal challenges to the legislation, said Zaldívar. Mexico's Chamber of Deputies gave its final approval to the measure following approval the week before in the Senate. Opponents of López Obrador see the legislation as a move by the president to interfere in the country's judiciary, The Wall Street Journal reported. The measure extends the term of Zaldívar, who is seen as close to López Obrador, by two years. It also extends the term of the entire Judicial Council, which manages Mexico's federal courts and has the power to investigate judges for wrongdoing and fire them. The broader package of judicial reforms has been touted as an effort to improve the judiciary's efficiency and reduce corruption. The country's courts are widely seen as ineffective, and government statistics show that most crime in the country goes unpunished. However, some political analysts and legal scholars see some of the reform provisions as an attempt by López Obrador to concentrate power, The Wall Street Journal reported. "The legislative power, with López Obrador's blessing, is clearly violating the autonomy of the judicial power...destroying the separation of powers and breaking the constitutional order," María Marván, a legal scholar at Mexico's National Autonomous University, told the newspaper. "It's a disgrace." According to Mexico's constitution, the Supreme Court's justices select their leader every four years with no possibility of re-election. López Obrador has said the changes are constitutional, and a spokesman for the president said he has never

intended to interfere in the judiciary. When asked if he would remain in his position if the Supreme Court ruled the measure constitutional, Zaldívar told Radio Fórmula, "We would talk again then." Meantime, he added, "I am serving as chief justice of the court for the period for which I was elected." If Zaldívar's term is extended for two years, it would end in 2024, when López Obrador's presidency also ends, the Financial Times reported. Also last week, López Obrador and his staff released several allegations against judges, accusing some of them of working with his opponents, the Associated Press reported. Among the judges targeted were one who issued an injunction against the president's attempt to limit private gas-fired and renewable energy plants as well as one who ruled against a government plan to fingerprint users of cellphones, the wire service reported.

## Bolsonaro Cuts Environment Budget After Vowing Raise

Brazilian President Jair Bolsonaro on Friday signed off on a 24 percent cut to the country's environmental budget, a move that came one day after he vowed to increase government spending to fight deforestation, Reuters reported. On Thursday, at a virtual climate summit organized by U.S. President Joe Biden, Bolsonaro vowed to double by 2030 Brazil's budget for environmental enforcement and fighting illegal deforestation. However, the next day, Bolsonaro approved the federal budget, which included 2 billion reais (\$365.3 million) for the country's Environment Ministry and agencies it oversees, a cut from the 2.6 billion reais approved last year, Reuters reported. Bolsonaro also vetoed \$240 million worth of environmental budget provisions, including proposed spending for environmental enforcement. The Economy Ministry, to which Bolsonaro's office referred questions, said the environment budget as approved by Bolsonaro was in line with what the president had originally proposed. At the end of the two-day U.S. climate summit, Biden urged participants to make good on their pledg-

## NEWS BRIEFS

## Castillo Solidly Leads Fujimori in Peru: Poll

A new poll released Sunday shows that far-left candidate Pedro Castillo has expanded his lead in Peru's presidential campaign, Reuters reported. Castillo holds almost double the level of support of center-right opponent Keiko Fujimori, with 41.5 percent support as compared to 21.5 percent for pro-market Fujimori, according to a poll by the Peruvian Studies Institute (IEP) commissioned by La República. Castillo leads Fujimori "in almost all areas of the country and social groups" ahead of the June 6 runoff vote according to the poll, which surveyed of 1,367 people between April 17-21 with a margin of error of 2.65 percent.

## Venezuelan Forces Have Abused Local Residents Along Border: Report

Venezuelan security forces have committed "egregious abuses" against local residents during a weeks-long operation launched against armed groups on the border with Colombia, Human Rights Watch said in a report released today. The operation, which began in March, led to the execution of at least four peasants, among other documented abuses. "The egregious abuses against Apure residents are not isolated incidents by rogue agents, but consistent with the Venezuelan security forces' systematic practices," said José Miguel Vivanco, Americas director at Human Rights Watch.

## Chile's Congress OKs Pension Withdrawal Bill

Chile's Congress on Friday gave its final approval to a measure that will allow private pension account holders to make a third emergency withdrawal to counter the adverse economic effects of the Covid-19 pandemic, Reuters reported. The lower house approved the measure on a vote of 119-13 with three abstentions. The Senate gave its approval earlier in the week.

es to fight global warming. “The commitments we’ve made must become real,” said Biden, the Associated Press reported. “Commitment without doing anything is a lot of hot air, no pun intended.” Biden is seeking \$2.3 trillion from Congress for electric vehicle charging stations, a new national electric grid and other environmental initiatives.

## ECONOMIC NEWS

## Guyana Reportedly Eying Long-Term Oil Deal With India

India has approached Guyana’s government about a possible long-term deal to buy the South American country’s oil, Reuters reported Sunday. Natural Resources Minister Vickram Bharrat said India is looking to buy a 1 million-barrel cargo that Guyana’s government is testing in its refineries. If the crude is compatible with India’s needs, the countries



Bharrat // File Photo: Guyanese Government.

could begin talks on a long-term arrangement, according to the report. Prices for crude are on the rise globally after last year’s pandemic-led commodities rout, compelling the South Asian giant to diversify its sources of fuel, according to the report. Moody’s Investors Service today changed its outlook for the global energy industry to positive from stable, citing a sustained uptick in commodity prices on the back of a recovering global economy that is set to “bolster a turnaround” in energy industry fundamentals over the coming 12 to 18 months. India’s oil demand has risen by 25 percent in the last seven years, more than any other country, and the nation of 1.36 billion

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this year is explained by the AMLO government’s refusal to launch a major Covid relief package that would damage fiscal stability and due to the low beta of the Mexican peso/U.S. dollar rate compared to other regional currencies. I expect the dollar’s recent pullback to be extended over the rest of 2021 (between 1.25-1.30 euros), as U.S. trade/budget deficits balloon and the Fed remains very accommodating. Flows to Latin America should rise, providing some support to regional currencies. The Mexican peso will continue to trade narrowly, the Brazilian real and the Andean currencies should rally, although the Argentine peso—a special case—will continue to fall. If correct, the weaker dollar will provide some breathing space for regional interest rates and, at the margin, support economic recovery.”

**A** Manuel Agosin, professor in the school of economics and business at the University of Chile: “The Latin American currencies have generally depreciated this year, owing to the upsurge in Covid-19 infections and deaths. Brazil has been particularly affected, and so has Peru. The latter has also been affected by political instability and the prospect of a very uncertain presidential election, where far-left candidate Pedro Castillo is facing Keiko Fujimori, the daughter of imprisoned ex-President Alberto Fujimori and herself under indictment for corruption. Neither candidate garnered 20 percent of the vote in the first round. However, Peru’s central bank is practicing a leaning-against-the-wind exchange rate policy which has kept the sol from a larger depreciation. However, the Peronist government in Argentina has returned to exchange controls. This hasn’t been able to stem the depreciation of the peso in the so-called ‘blue’ (black) market. Chile is the

people wants to use its purchasing power as leverage to keep prices low, Reuters reported. Meanwhile, state-owned Guyana Oil Company Limited, or GUYOIL, has been under a cloud of

exception in the region. High copper prices and advances in Covid-19 vaccinations have tended to appreciate the domestic currency against the dollar. In Colombia, depreciation has been modest, owing to high commodity prices (oil and copper). The Chilean currency

“The Latin American currencies have generally depreciated this year, owing to the upsurge in Covid-19 infections and deaths.”

— Manuel Agosin

should continue to appreciate from its level of slightly below 700 pesos to the U.S. dollar to perhaps about 650 pesos to the dollar by the end of the year. Brazil should continue to experience depreciation. Colombia’s currency might also appreciate before the end of the year. Given the exchange controls in Argentina, which are unlikely to be lifted, it is difficult to forecast what will happen to its currency. The black-market rate for the dollar will continue to rise, perhaps more than inflation. The course of the exchange rate in Peru will depend on the results of the election. Paradoxically, should Fujimori win, the sol will appreciate. But Castillo is the front runner, and should he win, the sol would inevitably lose ground.”

**A** Welber Barral, senior consultant at BMJ Consultores Asociados and former Brazilian foreign trade secretary: “The impact of the pandemic has been substantial in the region, and some important economies (Argentina and others) have suffered a de-

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corruption allegations in recent weeks, with its general manager abruptly resigning last Tuesday amid complaints of kickbacks, Stabroek News reported.

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crease of more than 10 percent in their GDP. While the pace of the recovery is still uncertain, the positive prospects of the U.S. economy for 2021 have been directing investments to the U.S. dollar. Also, major projects in Latin America have been suspended, affecting the flow of direct investment to the region. And although prices for commodities are generally at a higher level, this factor has not been sufficient to sustain national currencies nor to avoid high volatility in the currency markets. The relative strength of individual countries' currencies against the dollar requires an analysis of particular factors in each country. The Mexican peso, for instance, has increased in value this year, in spite of the slow vaccination and last year's fall in Mexico's GDP. The Brazilian real is over-devalued, mostly because of internal political uncertainty and the delay in crucial reforms. This trend could be reversed if the basic interest rate increases (as predicted by now). The Argentine peso is at risk of weakening even more if an agreement with the IMF is postponed until the elections and inflation is not abated. We have seen that high volatility and devaluated currencies affect the level of imports, leading to the reduction of trade level and to surplus in many national accounts. However, it also provokes inflation, which is particularly adverse in a period of reduced income for many families in Latin America."

**A Daniel Velandia O., director and chief economist for research at Credicorp Capital in Bogotá:** "Concerns that a strong economic recovery in the United States may lead to an earlier-than-expected withdrawal of the monetary stimulus from the Federal Reserve have put upward pressures on global interest rates while encouraging the demand for dollars globally, negatively affecting the currencies of emerging markets. Considering that Latin America continues to be one of

the hardest-hit regions by the pandemic, the effect has been particularly strong there. Of course, the impact has been differentiated among countries with idiosyncratic factors playing a role. In the case of the Argentine peso, the lack of a credible economic plan to implement the required adjustments after

“**The Colombian peso is very volatile due to the country's relatively large twin deficits.**”

— Daniel Velandia O.

the default last year, keeps the currency under pressure. In fact, it seems that the Fernández administration has decided to postpone a much-needed agreement with the IMF until after the October legislative elections. In the case of Brazil, the absence of measures to stabilize public debt has reduced the confidence among investors; more recently, the possibility of Lula being able to run in the 2022 elections has further elevated the political risks. The Colombian peso is very volatile due to the country's relatively large twin deficits and the fact that it is at the cusp of losing the investment-grade status; the government has presented a new tax reform for 2 percent of GDP, but the market remains somewhat skeptical as it may be watered down in Congress considering that Colombia is in a pre-electoral year. Conversely, the Chilean peso is enjoying high copper prices, a fast vaccination rollout and the expectation of a solid economic recovery. Thus, this latter currency is likely to be an outperformer in the region this year. For the rest of currencies to be able to follow it, favorable catalysts will be needed."

*The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at [gkuleta@thedialogue.org](mailto:gkuleta@thedialogue.org).*

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