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CONTENTS

LEADER	1
Which way for El Salvador's economic policy?	
SPECIAL FOCUS	
Region	3
Economic growth and family remittances to Central America in 2018	
REGIONAL ECONOMY REVIEW	
Cuba	6
Concerns mount on several fronts	
Ecuador	7
IMF confirms progress towards loan deal	
Brazil	8
Central bank holds interest rates again	
Brazil	9
Great Expectations	
Haiti	10
Government declares economic state of emergency	
ECONOMIC HIGHLIGHTS	12
REGIONAL BUSINESS REVIEW	
Brazil	14
Few signs of change after latest mining disaster	
Region	15
How fast will EV take-up happen?	
Venezuela	18
Oil output plunges: what chances (eventual) recovery?	

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Which way for El Salvador's economic policy?

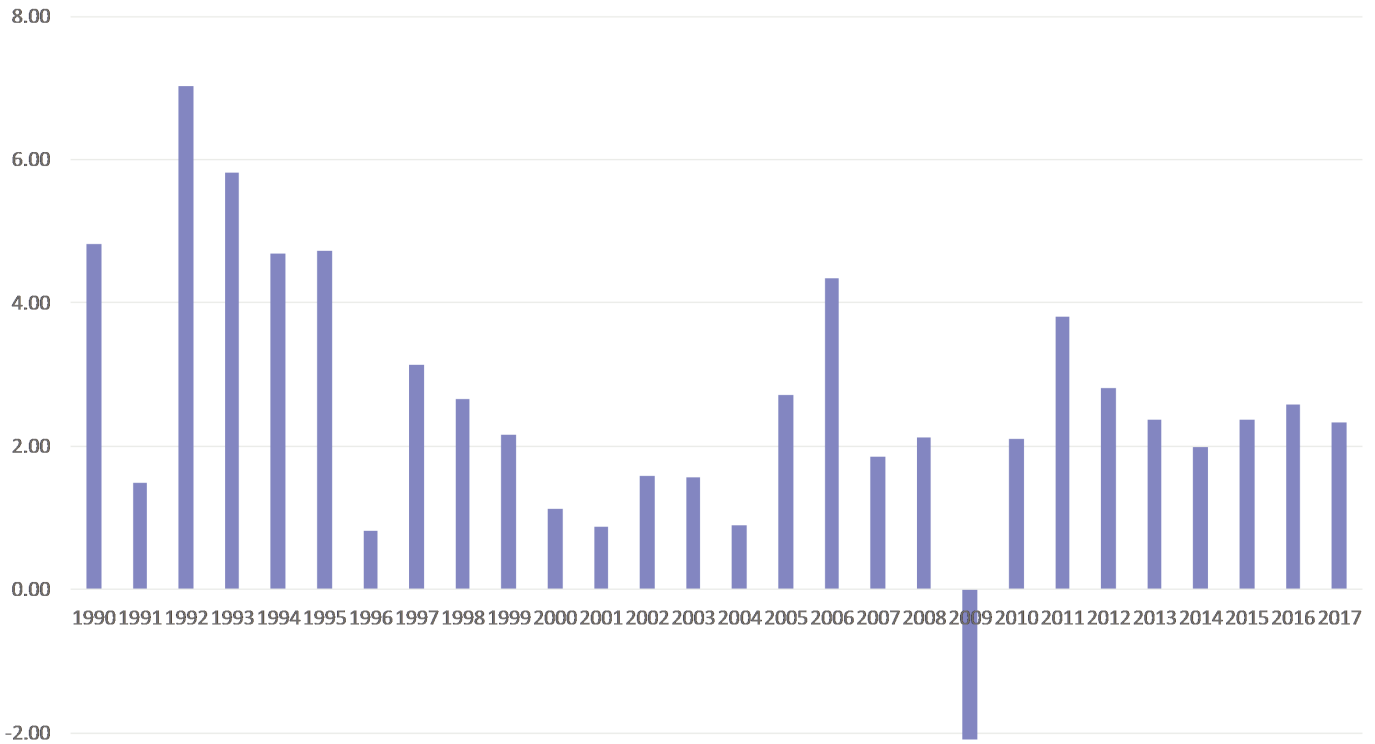
Nayib Bukele won the El Salvador elections on 3 February with a near-landslide (53.1% of the vote, more than his two main rivals combined). The 37-year-old populist has been vague about his economic policies, but promises tough anti-corruption measures, job creation to discourage illegal immigration to the US, and an investment surge to boost growth and reduce poverty. He takes office on 1 June. Does it all add up?

One thing clear at this stage is that Bukele will have limited room for manoeuvre. Almost four out of ten Salvadoreans live in poverty. Despite recent improvements, the homicide rate remains one of the world's highest. Corruption is endemic. Given a chance, many Salvadoreans flee the country and try to get into the United States. One in five Salvadoreans now live outside the country. The dollarised El Salvador economy has suffered from sluggish growth, hovering at around 2% in recent years. Only one in four workers are in formal tax-paying employment. Debt levels are high. The UN's Economic Commission for Latin America and the Caribbean (Eclac) ranks El Salvador as one of the five most heavily indebted economies in the region, with public debt of US\$18.97bn or 49% of GDP at the end of last year.

For over three decades governments of the left (Frente Farabundo Martí para la Liberación Nacional – FMLN) and of the right (Alianza Republicana Nacionalista – Arena) have quarrelled on ideological grounds over the size of the fiscal deficit. They have left the new president with a large deficit this year of around 3.2% of GDP, together with a strict fiscal responsibility law which requires him to narrow it to 0.7% of GDP by 2021 – a daunting correction that is equivalent to 2.5 percentage points of GDP. To complicate matters further, Bukele can at this stage count on only the support of 10 of the 84 members of the legislature. The president-elect will therefore have to do deals with the traditional parties to get legislation approved. A number of changes, including amending the fiscal responsibility law, require a two-thirds super-majority (56 out of the 84 votes).

So far, like the other candidates who were short on detail, Bukele has only sketched out some general policy ideas. He has said that 75% of gang violence reduction will come from "prevention, rehabilitation and reinsertion" with the remaining 25% coming from "enforcement with intelligence". On corruption he has suggested creating a UN and Organisation of American States (OAS) supported anti-corruption body, to be known as Comisión Internacional Contra la Impunidad en El Salvador (CICIES). A strong anti-corruption stance may have been the key to Bukele's success: his main campaign slogan was "There is enough money when no-one is stealing." To combat poverty and boost growth he says he wants to modernise agriculture in northern El Salvador, where some of the deepest

El Salvador's GDP growth



pockets of poverty are located. In the south of the country near the Pacific coast he wants to build a new airport and revive a rail network to help stimulate tourism and local development.

Among other policy comments, Bukele has called for closer relations with the United States and suggested that the previous government's decision last year to establish diplomatic relations with the Peoples' Republic of China could be reviewed. The Trump administration in the US wants to eliminate the Temporary Protected Status (TPS) visa programme, forcing an estimated 200,000 Salvadoreans to return home. Bukele, however, thinks he might be able to negotiate an agreement to prolong TPS, but to stem the northward flow of illegal immigrants by offering jobs and development at home. The president-elect told US ambassador Jean Manes that he felt some kind of "win-win solution" might be possible. He added that the best "border wall" was not a physical structure but the creation of opportunities which would make emigration from El Salvador unnecessary. Some analysts agree that better use of the remittances sent home by expatriate Salvadorean workers could boost development back home. Remittances represent 22% of GDP and have been growing at an annual rate of over 10%. Reducing financial exclusion in El Salvador might allow those remittances to be channelled more efficiently into local development projects.

For the moment the fundamental enigma is how the next government will attract the funding for the major investments it says that are needed – while squaring that with the demands of public sector fiscal austerity. An International Monetary Fund (IMF) mission is due to visit the country next month, following up on the previous Article IV consultation carried out in February-May 2018. On that earlier occasion the Fund said that despite some progress to improve the fiscal accounts, the country was struggling with slow growth and high debt. The Fund recommended a two-point increase in the VAT rate, from 13% to 15%. The outgoing government stopped short of implementing such an unpopular tax increase, kicking the whole issue forward for the next administration to deal with.

REGION

Economic growth and family remittances to Central America in 2018

General trends in 2018

Central American economies continue to struggle with achieving higher rates of economic growth, of above 4%. The sluggish growth continues to limit the ability of these countries to achieve economic development and prevent emigration in the long term. Of particular relevance is the fact that these economies are highly dependent on a small number of economic activities, and remittances is a central, if not the most important, source of income.

Family remittances to the region continued to grow in 2018, but inflows exhibited a slower growth of 8.6% compared with the 12% registered in 2017. The slowdown is associated with a reduction in emigration from the region to the United States and increases in intra-regional migration, as well as with political crises, particularly in Nicaragua.

The table below shows central bank data on remittances. The flow of money increased in all countries, but Guatemala exhibited the higher volume and growth. For three countries, El Salvador, Guatemala and Nicaragua, 2018 growth also showed a higher position relative to the Gross Domestic Product (GDP). In each the reasons are different.

In the Salvadoran case, growth is mostly explained by increases in the principal amount sent. In Guatemala, the growth is explained by a mix of continued and growing migration, as well as increases in the principal amount remitted. Nicaragua's growth is predominantly related to the economic crisis plaguing the country during the year; the economy contracted more than 4% in 2018, so remittances represent a higher proportion of GDP.

		Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama
Remittances	2017 (US\$, millions)	564	5,054	8,452	4,333	1,409	442
	2018 (US\$, millions)	581	5,458	9,635	4,550	1,494	455
	Growth in 2017	3%	10%	14%	13%	11%	4%
	Growth in 2018	3%	8%	14%	5%	6%	3%
	As share of GDP in 2017	1%	20%	11%	19%	10%	1%
	As share of GDP 2018	1%	21%	12%	19%	11%	1%
GDP	GDP Growth 2018	3%	2%	3%	4%	-4%	5%
	Remittances as a proportion of GDP growth (2018)	1%	68%	54%	26%	1%	0%

Source: Central banks

The Nicaraguan crisis, migration and remittances

With the political crisis affecting the economy, which registered a contraction in 2018 to the tune of -4.1%, on data from the United Nations Economic Commission for Latin America & Caribbean (Eclac), remittances are of increased importance. Some important points note are that, firstly, annual growth in remittances, though robust, was slower than in the year before, at 6% (against 11% in 2017).

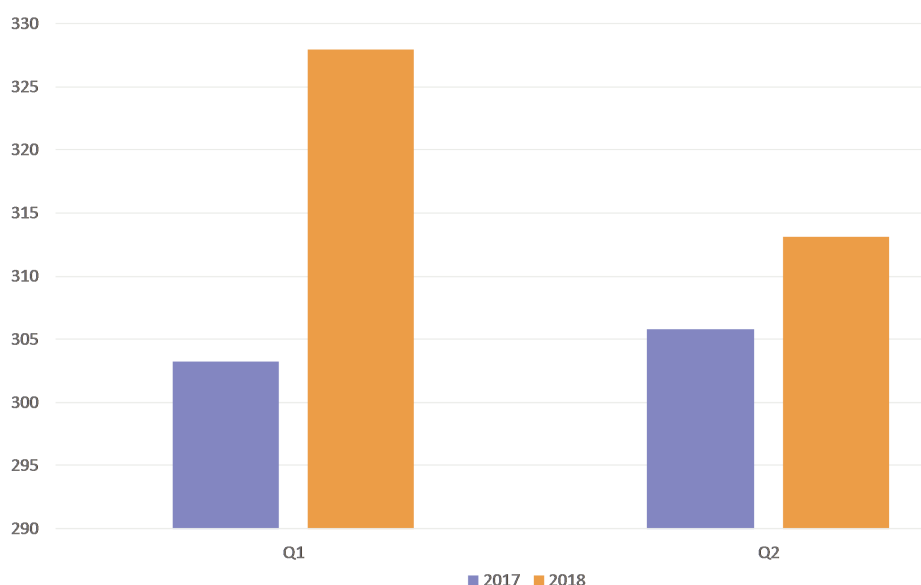
Secondly, during the second quarter, migrants sent more than usual, perhaps in response to the crisis. Remittances from Spain to Nicaragua, for example, showed a higher principal amount sent during the second quarter, just as the crisis was beginning.

Decline of key economic factors of growth in Nicaragua				
	Percent	Value (US\$)	Growth 2017	Growth 2018
GDP		13,852,694,387	4.5%	-4.1%
As share of GDP				
Maquila	5.0%	692,634,719	5.0%	0.0%
Remittances	10.0%	1,385,269,439	11.0%	6.0%
Tourism	5.0%	686,940,000	7.0%	-50.0%
Energy	2.0%	277,053,888		
Exports Merch.	41.0%	5,679,604,699	10.0%	-18.0%
Mining	3.0%	415,580,832		
As share of all of above	60.0%	8,311,616,632		

Source: Central banks, FUNIDES

Thirdly, the slowdown may reflect the outmigration pattern during 2018 where at least 50,000 Nicaraguans are said to have left for Costa Rica, many of whom were remittance recipients. It is possible that in 2019 remittances regain growth, depending on the foreign exchange controls that the Nicaraguan government plans to implement in the second quarter. Currently, these flows are, or have become, the most important support for many enduring the economic crisis.

Total remittance principal sent from Spain to Nicaragua



Guatemala's migration and remittance growth

Guatemala is the only country in the Northern Triangle that has shown greater migration. In a survey of Guatemalans in 2018 in the US, 4% said they arrived in 2018. Migration for Guatemala has shown higher numbers than from El Salvador or Honduras due to a combination of factors affecting the country. Particular drivers of Guatemalan migration include persistently-high levels of extortion and violence, the political crisis over election campaign financing, corruption, and the president's alleged abuses of authority ([for full analysis of these issues see our Guatemala archive](#)).

A look at the remitting profile of Guatemalans shows that this population is sending more than 30% more than in 2017 and previous years. A significant driver of the rise is the increased fear of deportation in recent months, due to the rhetoric emanating from the White House and tougher policies being enacted to reduce the population of immigrants from across the US' southern border. There is a desire among Guatemalans in the US to send as much money back to their home country as possible while opportunity is there for them to do so.

Guatemalans in the US sending home remittances		
Length of stay	Not naturalised (85%)	Naturalised US Citizen
Less than 3 years	\$ 4,991	\$ 2,400
4 to 7 years	\$ 4,075	\$ 2,603
8 to 15 years	\$ 4,450	\$ 7,246
Over 15 years	\$ 4,102	\$ 3,555

Border crossings by year: migration is uneven or down, 85% is irregular



Panama as a remittance sending country

Another important feature of Central American remittances is Panama's participation in the regional remittance sending landscape. Until a few years ago, Panama did not have a large migrant population. However, since the reconstruction process of the Panama Canal and the global economic recession, and more recently the political crises in Colombia, Venezuela, and Nicaragua, immigration and remitting has increased. According to Panama's central bank over US\$800 million were remitted out of Panama in 2018. Of that, Nicaraguan transfers were registered at US\$100 million. The Nicaraguan central bank recorded US\$75 million in person-to-person transfers. Either way, the flow of money as reported in 2017 has increased further with continued migration of Nicaraguans to Panama. The role of Panama as another remittance sending country, like Costa Rica, is opening market opportunities to expand money transfer services to the Latin American and Caribbean region.

Table Remittances sent from Panama: official and estimated amounts

Country	Remitters	Official figures, Balance of Payments	
	Immigrants	Per capita amount sent	Official total amount
Total	348,281	4,332	US\$833,507,100
Colombia	98,253	4,768	US\$258,853,100
China	20,850	15,525	US\$178,837,500
United States	17,988	10,015	US\$99,534,400
Nicaragua	31,775	5,395	US\$94,718,800
Venezuela	79,990	862	US\$38,114,000
Dominican Republic	18,703	2,705	US\$27,955,500
Costa Rica	8,684	4,239	US\$20,337,200
Mexico	6,246	5,350	US\$18,461,200
Other	65,792	2,660	US\$96,695,400

Source: Official transfers: Balanza de Pagos de Panamá Estimated volume based on interviews with migrants. Immigrants: extranjeros según principales países conforme al censo, legalizaciones y pre - registros realizadas del 2010 al 2017 (<https://www.migracion.gob.pa/inicio/estadisticas>).

As long as the crises in Venezuela, Nicaragua and Guatemala continue to drive migration, the overall growth in remittances in Central America may well remain subdued – sustained outmigration patterns will continue to reduce the number of remittance recipients. However, with the anti-immigrant rhetoric in the US set to continue, increased remittances from there may help to bolster overall remittance flows. It is certainly the case that as immigrant populations continue to grow in countries around Central America, the remittances landscape is likely to grow in complexity.

CUBA

Concerns mount on several fronts

2018 was a difficult year for the Cuban economy, with a floundering Venezuelan economy causing headaches as preferential oil exports dried up, and agricultural output hampered by damage from Hurricane Irma in late 2017. Prospects for 2019 look weaker still, not least on the back of a tougher policy stance from US President Donald Trump, which looks set to hurt investment and tourism.

A toughening of the US government stance towards Cuba has been on the cards for several months. Back in November 2018, the US National Security Advisor John Bolton voiced support for a harder approach in response to alleged acoustic attacks on US embassy staff, referring to Cuba as one of the Latin American “Troika of Tyranny”, alongside Venezuela and Nicaragua. He indicated that the US was seriously considering introducing new measures against the Cuban government. In mid-January, the US authorities provided more details of this potential new stance, stating that it might allow Americans to sue foreign companies over confiscated property in Cuba.

A focus on Title III

In order for this to happen, the US government would have to allow Title III of the Helms-Burton Act to come into force. Since the legislation’s inception, successive US administrations have passed waivers on this Title, for six-month periods at a time. However, as the expiry date on the latest waiver extension approached, the US government announced that the next waiver period would only last for a duration of 45 days, from 1 February until 18 March. During this period, the US authorities will make a decision about whether to continue granting waivers, or whether to allow the legislation to come into full effect.

There is a large number of cases (several thousand) relating to claims of confiscation of US assets in Cuba following the Cuban Revolution in 1959 and the issue has long been a thorny one between US and Cuban governments. If the US government now allows American claimants to pursue these cases, it could open up a significant amount of international litigation, particularly against foreign companies operating in Cuba’s tourism industry, since a large number currently operate on land that was held by US companies or individuals prior to the revolution (including hotel chains, as well as airport and port operators).

This would affect the Cuban economy in a number of ways. The most immediate would be through a likely suspension of investment plans on the part of foreign companies active in Cuba, since the possibility of facing legal action over current holdings will deter firms from further expansion in Cuba. Potential US claims would be likely to struggle in international courts, not least as it would be difficult to prove ownership with such a significant time lapse, but the legal uncertainty is likely to prove sufficient for foreign companies to hold back from channelling further investment into Cuba.

Given that the domestic economy is floundering in Cuba, with fiscal difficulties making hikes in public investment difficult, the authorities are hoping that an injection of foreign investment will help lift overall GDP growth from 1.2% in 2018 to 1.5% this year. Indeed, in the country’s Portfolio of Foreign

Investment Opportunities, many of the 176 projects identified by Cuba include tourist facilities. This would be unlikely to materialise if President Trump goes ahead with the lifting of the waiver on Title III of Helms-Burton.

Debt will not be fully serviced

Investment is not the only area of the Cuban economy likely to come under pressure this year. The Cuban government has admitted that it will not be able to service all of its debt in 2019, citing the ongoing impact from Hurricane Irma (which has squeezed the public purse as a result of higher government spending) and US sanctions (which complicates accessing fresh external finance). The first casualty of the year appears to have been Brazil's development bank, BNDES, which in January declared Cuba in default on a US\$600m loan that has not been serviced for over six months.

This reflects ongoing shortages of foreign exchange, in the context of reduced oil shipments from Venezuela (which forces the Cuban authorities to purchase oil on the open market from other suppliers). With the situation in Venezuela unlikely to improve anytime soon, there is little prospect of an increase in oil shipments in 2019, which will sustain pressure on Cuba. The government has not given any indication of which debt it is likely to service and which liabilities might slip into default, but Paris Club obligations are likely to be prioritised.

ECUADOR

IMF confirms progress towards loan deal

Following a series of talks between the International Monetary Fund (IMF) and the Ecuadorian authorities, a formal loan deal looks likely in the coming months. Although this will provide support for ongoing fiscal consolidation, financing needs will remain large, explaining the late-January issuance of US\$1bn in fresh (and fairly costly) debt.

That President Lenin Moreno is seeking a new loan agreement with the IMF comes as little surprise and had been heavily alluded to in recent months. The president met with Fund officials at the World Economic Forum (WEF) meeting in Davos in mid-January and on 13 February the IMF published a statement confirming that it was engaged in a close dialogue with Ecuador over an IMF-supported financial arrangement. It said that an IMF team is currently in Quito to further this dialogue, heavily implying that a final deal is approaching.

A surprise bond issue

This would help provide assurance to investors that the government remains on the right policy track and that it will continue to address several structural economic weaknesses, including pressing difficulties on the public finances. Financing needs for 2019 are large, which the finance ministry estimates at US\$8bn. It had been thought that the Ecuadorian government would hold off from tapping international capital markets for fresh debt until an IMF arrangement was signed, in the hope that it would reduce the interest rate on new issuance, but in late January the government surprised markets with a new, US\$1bn bond issue. Although it managed to reduce the coupon from an initial 11% to 10.75% after preliminary orders were three-times oversubscribed, the rate still marked an all-time high since Ecuador returned to the international capital markets in 2014.

The finance ministry stated that this issuance would cover 12.5% of the country's projected US\$8.1bn financing needs for this year. It provided more

information about how it plans to meet the remainder: the government is pencilling in US\$1.6bn from China, US\$1.6bn from multilateral lenders (comprising US\$860m from the development bank CAF, US\$420m from the World Bank, and US\$320m from the IDB), US\$1.5bn from oil-swap loan deals, and US\$1.4bn in commercial bank borrowing. Interestingly, it has not included any credit from the IMF in its calculations, although if this is secured it would reduce the obligation to agree new oil-swap loan deals (which compromise the country's longer-term export earnings), as well as potentially taking the pressure off the authorities to agree new credit from the Chinese.

Oil prices remain a concern

One potential area of concern is oil prices, as the government calculated its 2019 budget on the assumption that Ecuadorian crude would average US\$58.3/barrel. Oil prices are currently trading at just below this level and have proved relatively weak so far this year. If oil prices remain weak, or even fall further (futures prices remain fairly low, suggesting a rapid rebound is unlikely) then the Ecuadorian government might face even higher financing needs. More aggressive fiscal consolidation could keep this under control, but may take its toll on the government's popularity.

BRAZIL

Central bank holds interest rates again

Brazil's central bank held its benchmark interest rate unchanged on 6 February and signalled that congress needs to pass austerity measures before borrowing costs can fall. The bank board, led by its president, Ilan Goldfajn, kept the Selic rate at 6.50 percent for a seventh straight meeting. This was likely the last rate decision under Goldfajn, as the senate is expected to approve President Jair Bolsonaro's nominated successor later this month.

In the statement accompanying the decision, the members of Copom – the bank's monetary policy board – considered that “inflationary risks have moderated” since their last meeting, but they stressed that the “frustration of expectations regarding the continuation of reforms” could trigger price pressures. In the minutes to the decision, published a week later, Copom members pointed out that “an acceleration in the pace of the economic recovery will depend on the decrease in uncertainties regarding the approval and implementation of reforms – notably those of fiscal nature – and adjustment in Brazil's economy”.

The newly elected speakers of both houses in congress have expressed support for a proposal to cut pension spending that are the heart of Brazil's budget woes.

Brazil's pension expenditures are already high compared with other countries, and a rapidly aging population makes the current system a ticking time bomb. Brazil spends the equivalent of 13 percent of gross domestic product on social security, well above the average of eight percent for G-20 nations, according to a government report published in December. Yet it is far from clear if and when the government can muster the necessary majority in congress to approve the constitutional amendment.

Chief of Staff Onyx Lorenzoni said in early-February that the economy could see sustainable growth of three percent if the government's reform agenda is passed. Still, a lower-house lawmaker later said getting the necessary votes will not be easy, as the administration needs to build a coalition of support in a fractious congress.

Fiscal crisis

Six states have declared a fiscal crisis, citing a lack of control by previous governments. Minas Gerais, Rio Grande do Sul, Goias, Alagoas, Mato Grosso do Sul, and Para have asked the STF for authorisation to reduce salaries and/or the work week of state employees to reduce the latter to 60% of state expenditures.

Economists recently switched their forecasts from an increase to a hold of the Selic rate as inflation came in below expectations and the labour market weakened. In addition, emerging market jitters had eased, and investors had become more optimistic with the Bolsonaro administration's market-friendly discourse. Swap futures also show traders are already pricing in a mild bias toward a cut.

Since at least 1996, when the country's current monetary policy board was created, no incoming bank governor has ever cut the benchmark Selic in his first meeting. Roberto Campos Neto, nominated to replace Goldfajn, may be no exception. He is expected to receive senate confirmation and assume his post before the bank's next monetary policy meeting in March.

Who is Campos Neto?

Campos Neto is the grandson of Roberto Campos, a controversial economist, diplomat, writer, and politician who enjoyed sprinkling his conversation with dry witticisms, helped mould Brazil's economic liberalism in the 1950s and 1960s, and as Brazil's planning minister signed the decree that created the central bank in 1964.

The central bank presidency will be Campos Neto's first public-service role. In his private sector experience, he has accumulated a deep understanding of international investors. Much of that experience comes from his work at Santander Americas' treasury business, which had offices in the US, Mexico, Chile, Peru, Brazil, and Argentina. Campos Neto also oversaw the market-making business at the bank, a job that introduced him to dozens of fund managers and company executives looking to invest in Brazil.

BRAZIL

Great Expectations

A gap is opening up between Brazilians' economic expectations and current conditions, including the job market and family finances. That means they may be in for a reality check, particularly if President Jair Bolsonaro fails to deliver the reforms needed to boost the country's anemic recovery.

Shortly after Bolsonaro's election victory in October, consumer optimism jumped to a six-year high, according to an index from the Getulio Vargas Foundation. While consumer expectations are a traditional driver of growth, troubling signs for the recovery abound.

Unemployment stopped falling in the fourth quarter of 2018, after months of steady decline. Most of the new jobs being created are in the informal sector. Retail sales dropped 2.2 percent in December from the prior month, falling the most since January 2016. Car production in the first month of the year plunged 10 percent from the year before. Itau Unibanco SA cut its 2019 GDP forecast for Brazil by a half percentage point to two percent.

Even with the benchmark interest rate at an all-time low, Latin America's largest economy is still held back by a stubbornly-high unemployment rate of 11.6 percent. Formal jobs in the construction sector, one of the country's top employers, have fallen some 40 percent since 2014 to 2 million.

"There's a certain wave of optimism that goes beyond economics and has a subjective component, disconnected from real life," said Aloisio Campelo Jr., public statistics superintendent for FGV's economics institute. "After such a big crisis there is perhaps some wishful thinking on the part of the consumer."

Embraer Jets

On 7 February, Embraer Defense announced that it had sold 12 Super Tucano A-29 jet prop fighter planes to Nigeria for US\$ 250m. These planes will be produced at the Embraer installation in Jacksonville, Florida. Nigeria plans to use these planes against the Boko Haram Islamic rebels in Northern Nigeria.

Infrastructure

On 7 February, Infrastructure Minister Tarcísio Freitas announced that the government plans to establish a new transportation infrastructure agency that would combine the current land transportation agency with the organisation responsible for ports and rivers. He said that this would result in simplification and integration.

As an example Freitas cited Santos, the largest port in Latin America, which is regulated by the port agency but has all of its cargo inspected by the land agency. The minister said that this model is working successfully in Canada and Italy. The new combined agency would be called ANT-National Transportation Agency. The National Agency for Civil Aviation would not be included.

This proposal would have to be approved by congress and the new ANT would have fewer staff with transfers of some to other government units. Many of the current directors of the current two regulatory agencies were nominated by leaders of some political parties. In theory, the director-general and directors of the new ANT would not be indicated by politicians but rather selected for their technical experience in the transportation sector and clean records

Eletrobras

Brazil's government expects to privatise Eletrobras in 2020, Deputy Energy Minister Marisete Pereira said in an interview with *Folha de Sao Paulo*. The administration is re-evaluating the capitalisation model to be used with Eletrobras, which is likely to prevent the transaction from happening this year.

While capitalisation is a priority for the ministry the model to be used is still being discussed, she said. The current thinking within the administration is to allow government to hold a so-called golden share in the utility, which would grant the state certain powers even as a minority stakeholder. Given the uncertainty over whether the transaction will take place in 2019, the economic team has decided to remove an estimated revenue of 12b reais from the federal budget this year, *Folha* reported.

HAITI

Government declares economic state of emergency

As violent protests continue to rock Haiti, the government has responded with a number of measures designed to address public gripes. On 5 February, President Jovenel Moïse declared an economic state of emergency, outlining a series of measures to tackle the ailing economy. On 16 February, Prime Minister Jean-Henry Céant unveiled nine emergency measures that he hopes will raise living standards.

With the president now two years into his five-year term, problems are mounting. The public is tiring of a lack of progress on boosting the ailing economy, particularly given Moïse' campaign pledges to improve basic physical infrastructure (including paving roads and tackling electricity shortages), provide food security, boost economic growth, and reduce corruption. The public perception is that not only has the government failed to fulfil these campaign pledges, but that in many cases conditions have worsened in recent months.

Weakening gourde lifts inflation

The local currency, the gourde, depreciated steadily over the course of 2018, but the currency incurred particularly sharp losses in the last quarter of the

year, weakening from HTG67:US\$1 in late September to over HTG77:US\$1 at the end of the year. Currency depreciation continued in early 2018, with the gourde trading at close to HTG83:US\$1 in mid-February. This bout of weakening is essentially explained by the monetisation of the fiscal deficit, which reached a record HTG34bn in the October 2017-September 2018 financial year. A lack of financing options has meant that the bulk of the deficit was financed by borrowing from the central bank (BRH), which in turn has raised the amount of liquidity in the domestic economy.

This has increased inflationary pressures: the latest data from the BRH shows that consumer price inflation came in at 15.1% in December, up from 13.2% at the beginning of the year. Given that local-currency depreciation has picked up pace in recent months and that the impact typically takes several months to feed through to consumer prices, many fear that inflation is likely to rise further in the coming months.

Government targets fiscal consolidation

The measures unveiled by the government in early February aim to tackle public disquiet in a number of ways. The cabinet has passed two resolutions: the first is targeted at improving conditions for vulnerable Haitians and is aimed at cutting the price of staple goods (through lifting subsidies), strengthening social welfare programmes and improving access to credit for small and medium-sized enterprises (SMEs).

The second resolution is focused specifically on the public finances and is aimed at cutting the fiscal deficit. The measures are mainly concentrated on the expenditure side, with the authorities seeking to trim spending. Public-sector workers are no longer entitled to new vehicles; they are prohibited from hiring vehicles until the end of the 2018/19 financial year; sharp cutbacks have been introduced to reduce overseas travel for public officials; and some benefits for all public-sector workers have been scaled back. In addition, salaries for senior public officials are set to be “streamlined”, which in practice is likely to involve a cloaked attempt to reduce spending on public-sector wages.

The prime minister’s unveiling of nine emergency measures on 16 February in many cases covered the same ground as the earlier announcements from the president. However, there were a few measures, including efforts to reduce smuggling of goods out of Haiti (which the government hopes will lift revenue), an admission that the government will consider raising the minimum wage, and renewed efforts to secure development aid from overseas creditors.

Economy unlikely to pick up

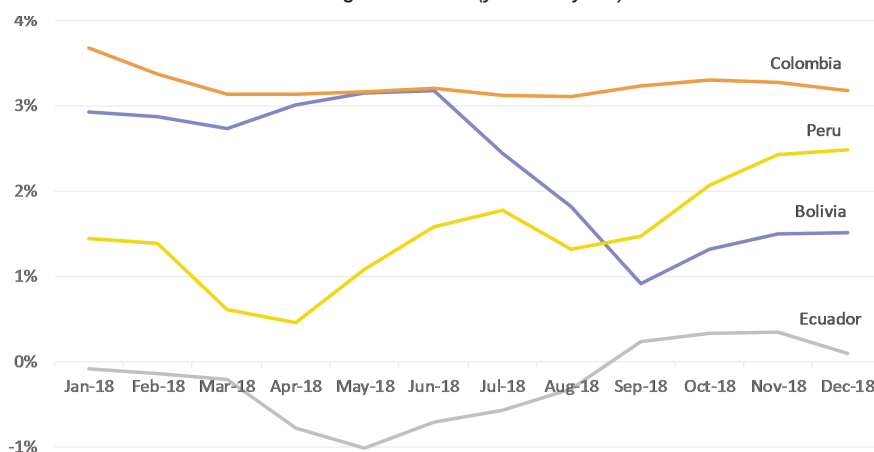
The government diagnosis of the problem is correct, in that targeting fiscal consolidation will reduce the extent of deficit monetisation, which in turn will ease pressure on the local currency and gourde. Cutting current expenditure would also, in theory, free up funding for capital infrastructure projects. However, it is highly questionable whether the government’s new measures will either materialise, or – if they do – whether they will have a material impact on the economy in the short term. Many of the fiscal measures have either already been attempted, or have been under discussion, with weak implementation capacity preventing a significant improvement in the public finances. Gripes with the extremely weak state of electricity provision will continue, given that it takes several years to tackle the structural problems behind this issue. As such, public disquiet with the weak economy will continue, with related social unrest also set to persist.

ECONOMIC HIGHLIGHTS

ANDEAN COUNTRIES

Andean Countries: Inflation rate (%)

Percentage variation (year-on-year)



Source: Local central banks. No reliable data available for Venezuela.

Andean Countries: GDP growth (%)

Quarterly figures are year-on-year growth

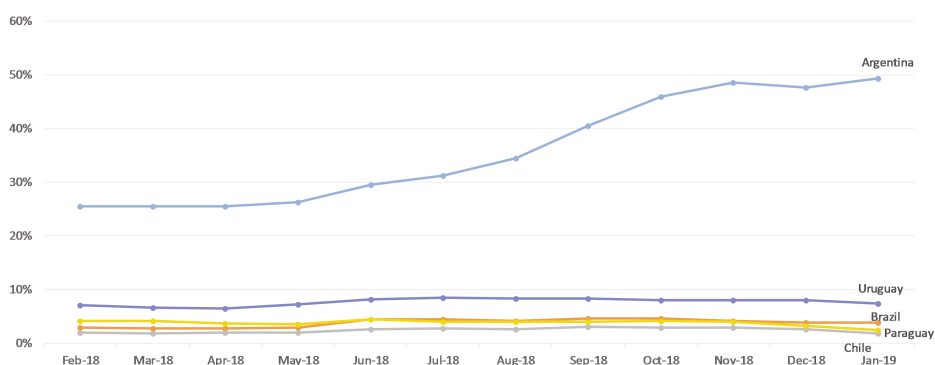
GDP	end 2017*	2018 forecast**	Q4 2017	Q1 2018	Q2 2018	Q3 2018
Bolivia	4.2%	4.3%	Not available yet	Not available yet	Not available yet	Not available yet
Colombia	1.8%	2.7%	1.6%	2.2%	2.8%	2.7%
Ecuador	3.0%	1.0%	3.0%	1.9%	0.9%	Not available yet
Peru	2.5%	3.9%	2.2%	3.2%	5.4%	5.3%
Venezuela	-13.0%	-15.0%	No data	No data	No data	No data

*Figures from the United Nations Economic Commission for Latin America & Caribbean (Eclac) August 2018. **Figures from Eclac Oct 2018.

Quarterly growth based on figures from the local central banks. Bolivia has ceased providing quarterly y-o-y GDP data.

Brazil & Southern Cone: Inflation rate (%)

Percentage variation (year-on-year)



BRAZIL & SOUTHERN CONE

Country	GDP growth rate, quarterly annualised figure*					
	End 2017**	2018 forecast**	Q4 2017	Q1 2018	Q2 2018	Q3 2018
Argentina	1.30%	2.20%	3.90%	3.60%	-4.20%	-3.50%
Brazil	0.90%	2.00%	0.99%	1.29%	1.03%	1.27%
Chile	1.50%	2.80%	3.30%	4.10%	5.30%	2.80%
Paraguay	4.00%	4.50%	4.50%	4.10%	6.20%	1.10%
Uruguay	3%	3.20%	2.00%	2.20%	2.50%	2.10%

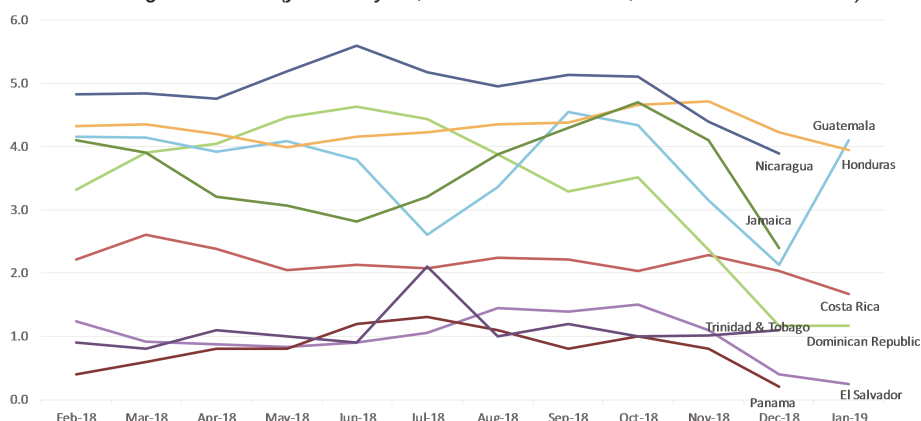
* Figures from local Central Banks

** Figures from United Nations Economic Commission for Latin America and the Caribbean

ECONOMIC HIGHLIGHTS

CENTRAL AMERICA & CARIBBEAN

Central America & Caribbean: Inflation Rate
Percentage variation (year-on-year, selected countries, latest available data)



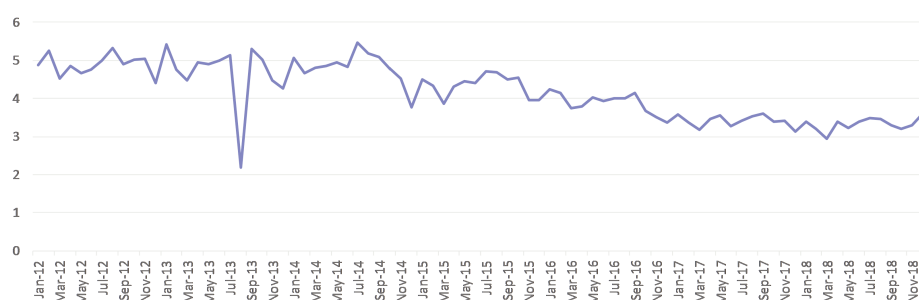
Central America & Caribbean, selected countries: GDP growth (%)

GDP	end 2017*	2018 forecast*	Q4 2017	Q1 2018	Q2 2018	Q3 2018
Costa Rica	3.9%	3.3%	3.2%	3%	3.3%	2.1%
Dominican Republic	4.9%	5.4%	6.5%	6.4%	7.1%	7.3%
El Salvador	2.4%	2.4%	2.41%	3.4%	2.5%	2.1%
Guatemala	3.2%	2.9%	2.9%	2%	2%	3.5%
Honduras	3.9%	3.9%	3.6%	3.1%	3.3%	3.1%
Nicaragua	4.9%	0.5%	4.3%	2.3%	3.9%	-4.8%
Panama	5.3%	5.2%	4.9%	4.2%	4.2%	3.6%
Jamaica	1.2%	1.3%	range: 1.0%-2.0%	range: 1.0%-2.0%	2.2%	Not yet available
Trinidad & Tobago	-2.3%	1.5%	-1.2%	3.1	Not yet available	Not yet available

*Figures from the United Nations Economic Commission for Latin America & Caribbean December 2018

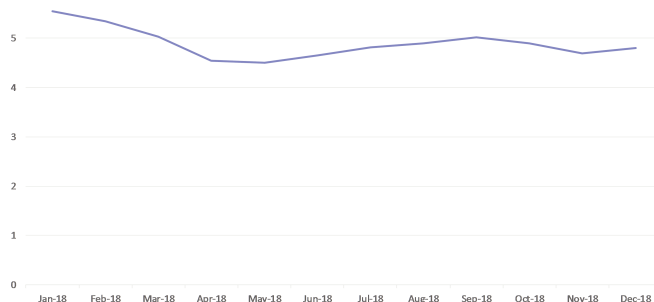
Quarterly growth based on figures from the local central banks, year-on-year growth

Mexico's unemployment rate
Economically active population

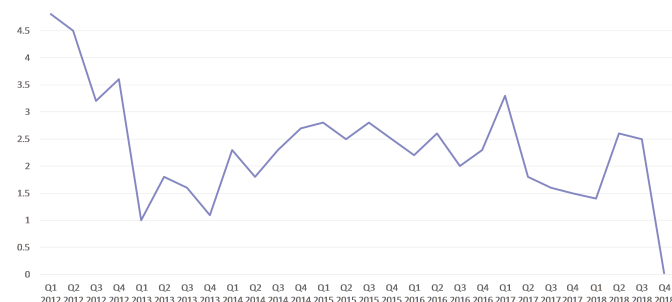


MEXICO & NAFTA

Mexico's inflation rate
Percentage variation (year-on-year)



Mexico's GDP
Percentage variation (year-on-year)



Source (all Mexico Highlights data): National Statistics Institute (Inegi)

BRAZIL

Few signs of change after latest mining disaster

Over 165 people have died, while scores remaining missing, presumed dead, after the collapse of a tailings dam operated by Vale near Brumadinho, Minas Gerais. The accident comes just three years after another dam, also part operated by Vale, burst near the town of Mariana, killing 19 people and resulting in the worst environmental disaster in Brazil's history. Efforts to ban upstream dams and force mining companies to improve the safety of dangerous dams in the wake of the first tragedy failed to gain traction in congress.

In the immediate aftermath of January's tragedy, Vale, the largest iron-ore producer in the world, saw its share price drop almost 25 percent. It rebounded a little after Chief Executive Officer Fabio Schvartsman said Vale would stop using all upstream dams over the next three years, shutting a group of older mines in the process and cutting the company's annual iron production by some 40 million tons. Brazilian police arrested three Vale employees and two contractors as part of the investigation into the disaster. The company says it does not know why the dam failed but is the "most interested party" in finding out. Vale says it is cooperating with the investigation and has turned over the results of an ongoing internal probe of the dam failure.

After the 2015 collapse, an investigation ordered by the dam's co-owners, Vale and Australia's BHP Group Ltd., concluded that misguided efforts to raise the height of the dam and fix structural defects hindered drainage, causing parts of the earthen structure to liquefy and collapse. Yet since then the governor of Minas Gerais imposed a process to speed up environmental licensing of mines, dams, and other industrial projects. Vale benefited by getting quick approval to expand the mining complex that included B1, which was built in the 1970s and is similar in design to the dam that failed in 2015. Vale says it hadn't been dumping mine waste behind the dam for about two and a half years and was in the process of decommissioning it.

Instead of hiring more dam inspectors, as state and federal investigations urged, the Brazilian federal government slashed budgets. In Minas Gerais, just four federal inspectors police more than 400 dams – unchanged from 2015. State regulators say they cannot guarantee the safety of at least 12 dams. That has left Vale and other mining companies to largely self-regulate, by hiring private inspectors to file reports with government regulators, often based on data the company produces. Lawyers for Samarco, the Vale subsidiary that owns the Mariana mine, used appeals and other legal maneuvers to fight fines levied for the 2015 dam collapse. So far, Samarco has not paid any of the 350 million reais (US\$95m) of fines imposed for that disaster, according to Ibama, the government's top environmental regulator.

Vale has denied a series of news reports alleging that the company knew of potential problems at the dam before it burst. Vale executives on February 12

Vale evacuated 200 people as a precautionary measure in an area near one of its dams in Minas Gerais state, Brazil, the company said in an emailed statement on 16 February. The people near the B3/B4 dam in the Mar Azul mine, about 25 kilometers (16 miles) from the state capital, were evacuated to a community center on Saturday night and will be accommodated in hotels.

made public third-party audits affirming the dam's stability, and provided data and internal email communications as evidence that the monitoring equipment was functioning normally.

President Jair Bolsonaro visited the scene of the tragedy in the immediate aftermath but the administration appears unwilling to criticise Vale too harshly. Bolsonaro's chief of staff, Onyx Lorenzoni, said the government cannot interfere in Vale's management. Infrastructure Minister Tarcisio Gomes de Freitas warned of the "demonisation" of Vale. The new government has promised to open the Amazon to mining and take aim at environmental regulation. Despite public outrage at the latest disaster, there seems little sign that the Bolsonaro administration will change tack.

REGION

How fast will EV take-up happen?

There are strong arguments in favour of converting Latin America to use electric vehicles (EVs), rather than petrol-burning ones. But there are also obstacles to take-up. Here we look at where, and how, the transition may begin to happen.

On the face of it, there are compelling reasons to convert Latin America to EVs. The region is massively dependent on the private motor car. Around 5m new cars were registered in 2017, a number that will rise to 8m by 2025. These cars burn expensive fuel and emit carbon into the atmosphere. If Latin America is to meet the Paris Agreement target of limiting global warming to less than two degrees Celsius, reducing emissions from the transport sector is a good place to start. It is calculated that the region's car fleet is responsible for 37% of total transport emissions while public transport, including buses, accounts for nearly 10%. According to the UN Environment Programme (UNEP), by switching to EVs the region could cut CO₂ emissions by more than 1.5bn tonnes and save US\$85bn between 2016 and 2050.

This contribution could be particularly relevant in the region's polluted cities, home to roughly 80% of the population. The mayors of 50 cities, including Buenos Aires, Mexico City, Rio de Janeiro, and Santiago have pledged to achieve zero carbon emissions by 2050. Turning to EVs would build on a natural Latin American advantage: the region already has one of the cleanest energy matrices in the world with 50% of installed capacity coming from renewable sources (such as hydro, wind, and solar) well above the global average of 15%. The region also has one of the world's highest per-capita bus use rates. Electric-powered buses could make a big contribution to cleaner cities.

And yet EV take-up in Latin America is lagging behind the trailblazers in the US, Europe, and China. According to the International Energy Agency (IEA) the global stock of both BEVs (battery electric vehicles) and PHEVs (plug-in hybrid electric vehicles) rose from around 2m in 2016 to just over 3m in 2017. Yet by one estimate, the EV stock in four Latin American countries – Brazil, Chile, Colombia, and Mexico in 2017 was only around 2,500 vehicles (about 0.01% of the global total). According to a study published by the

FIGURE 1: GLOBAL ELECTRIC CAR STOCK

Source: International Energy Agency (IEA), *Global EV Outlook 2018*. Notes: BEV = battery electric vehicle, PHEV = plug-in hybrid electric vehicle

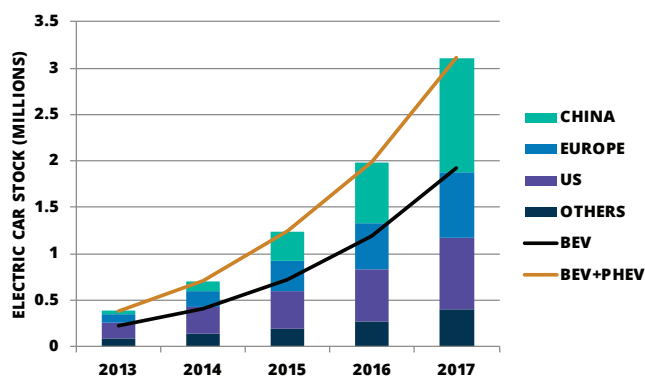
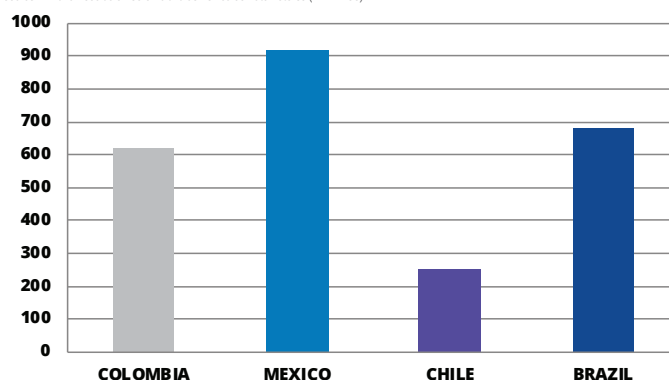


FIGURE 4: EV STOCK BY COUNTRY, 2017

Source: IEA and Asociación Colombiana de Vehículos Automotores (ANDEMOS)



Source: *Charging Ahead: The Growth of Electric Car and Bus Markets in Latin American Cities*, Guy Edwards, Lisa Viscidi, and Carlos Mojica, September 2018

InterAmerican Development Bank (IADB) annual sales of EVs in the six largest markets (Argentina, Brazil, Chile, Colombia, Mexico, and Peru) could range between 52,000 and 220,000 units by 2023, depending on a variety of factors. If correct, this would represent a disappointing market penetration rate of between 0.3% and 2.5%.

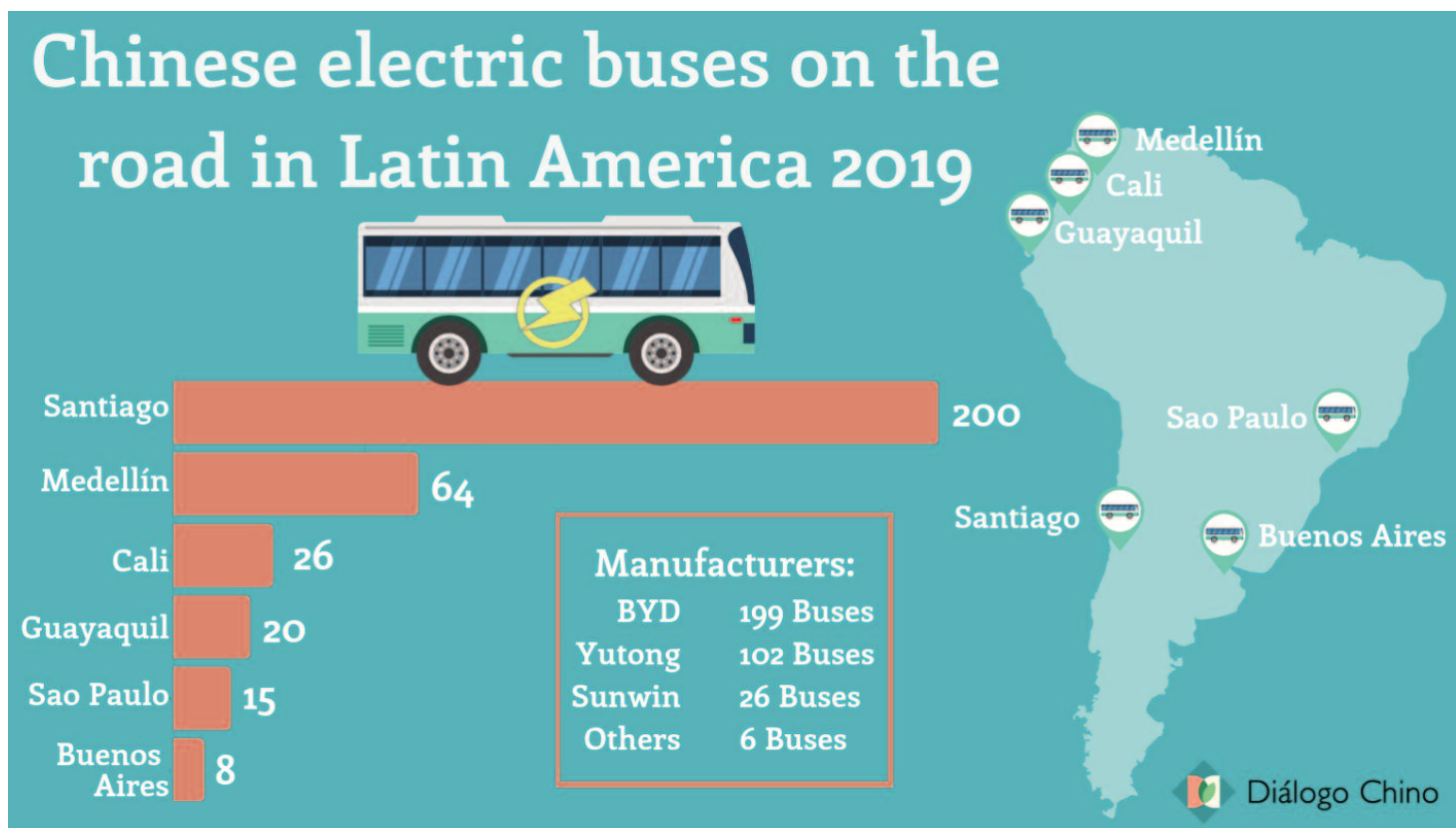
There is clearly a range of obstacles to EV take up. One big problem is charging infrastructure. According to a report by consultancy Arthur D. Little, Latin America suffers from the classic chicken-and-egg problem: “not many electric vehicles are available since the public charging infrastructure is very limited and, in turn, the public charging infrastructure is scarce because there are two few EVs”. The report also highlights relative lack of knowledge about the technology, after-sales service, and other related issues. It comes to the conclusion that for the moment at least, top-of-the range EVs will be bought by the Latin American elites mainly as a status symbol.

An important issue is that while many EVs are cheaper to run than their petrol-burning equivalents, the up-front costs are significantly higher both for cars and buses. In Brazil the Nissan Leaf EV sells for BRL179,000 (US\$48,000) – equivalent to five times the average annual salary. In addition, there are few attractive financial packages to help spread the cost of EV purchases. Many city administrations that issue public tenders to buy fleets of buses are obliged to select the cheapest by capital value, irrespective of the lower running costs that EV buses can offer. Added to this, fossil fuels are still subsidised in many countries (by the equivalent of 1% of regional GDP in 2011-2013). As mentioned, the charging infrastructure is often inadequate and, pending improved battery technology, many EVs lack the autonomy or battery capacity to venture far from cities. According to the Arthur D Little report unstable power supply means the capacity of the few charging points in the region can vary between 3.6kW to 22kW, meaning that charging a 90kW battery can take anywhere between five and 24 hours.

What does seem to be happening, however, is that a number of players in the automobile and transport industry are coming up with different localised ways of tackling and overcoming these challenges. Taken together a variety of initiatives could build up a kind of critical mass. One approach is to focus on buses, because they are heavily used in cities, follow fixed routes, and therefore can be kept within range of fixed charging points.

One country in the forefront of electric bus adoption is Chile. Since December 100 electric buses built by BYD of China have been added to the fleet operating in Santiago. Transantiago, the capital's rapid bus transport system, added a further 100 made by another Chinese manufacturer, Yutong. The adoption of electric buses has received financial support from President Sebastián Piñera who has made "electromobility" a key part of the 2018-2022 energy plan. Enel of Italy is installing 100 charging points around the city. Darío Hidalgo, a researcher on sustainable cities at the World Resources Institute says, "The case of Santiago is very interesting because there is an alliance between private operators, manufacturers, and energy distributors." Energy minister Susana Jiménez says the government wants EVs to account for 40% of Chile's private fleet and 100% of public transportation in the roads by 2050.

Colombian cities are also adopting electric buses. Here, Medellín and Cali are in the forefront, with Medellín starting out with an order of 64 units from BYD and Cali following with a first batch of 26 built by Sunwin Bus Corp, also of China. Both cities are a step ahead of the capital Bogotá because Chinese companies do not yet supply the kind of articulated buses required by Bogotá's Transmilenio rapid bus system. Electric bus pilot schemes are also being introduced in Sao Paulo, Buenos Aires, San José and Montevideo.



There is also scope to introduce EVs via fleet purchase deals. The economics of EVs works particularly well with city-based vehicles that are used for long periods every day. There is therefore interest in EVs from ride-hailing and car-sharing services including Meleva and ZacCar (Brazil), Laudrive and Carrot (Mexico), and Awto (Chile).

A number of governments are taking small incremental measures that could create momentum. In 2017 the Colombian government eliminated import tariffs for up to 1,500 EVs a year. The duty-free quota will rise to 3,000 in July. In

Mexico US-based EV manufacturer Tesla has been installing accessible chargers through deals with shopping centres and hotels. Mexico now has around 1,500 public chargers, most provided under the terms of this Tesla-led partnership.

In January Costa Rica introduced a new law providing incentives for EV uptake. Since 2017 EVs have been exempt from import and other taxes. President Carlos Alvarado has promised that by 2021 his government will introduce a plan to establish a fossil-fuel free transport system. The postal service, Correos de Costa Rica, has begun operating electric motorcycles.

Big challenges still remain, however. For the moment EVs – both cars and buses – are coming in as highly priced imports. So far there are no major plans to manufacture EVs within the region – a key step if, in the long term, the local automobile industry is to keep up with the digital revolution and retain value added. It is also possible that while gathering pace, the growth in EV use will still be insufficient to help reduce global warming. Matías Asun, national director in Chile of Greenpeace, the environmental lobby group, said that at the present rate of take-up, the country would have to take dramatic action to meet its 2050 targets. He said, “Our question to the government is this: from what year will it no longer allow combustion engines to be sold in Chile?”

VENEZUELA

Oil output plunges: what chances (eventual) recovery?

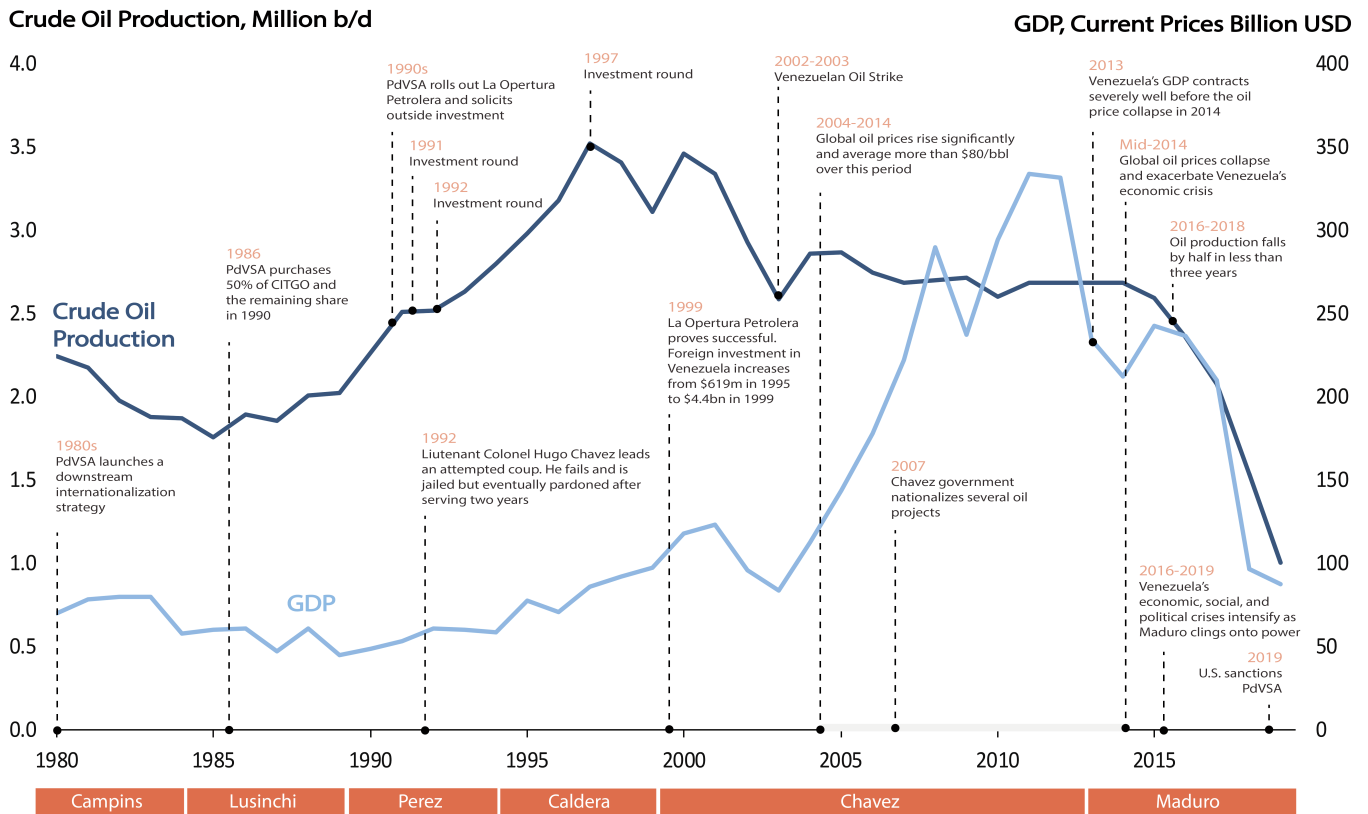
Amidst Venezuela’s political and economic crisis there are two questions to be asked about oil production. First, on the way down, how sharply will it continue to fall over the next few months? Second: will it ever go up again, and what will be required for that to happen?

The chavista brand of socialism has not been kind to Venezuela’s oil industry, the country’s main source of foreign currency. Oil production peaked in 1997 at around 3.5m barrels per day (bpd), two years before Hugo Chávez (1999-2013) was elected. Since then it has been on a relentless downward curve. By last December crude production was estimated at 1.25m bpd, having fallen by two-thirds since the 1990s and by half in the preceding three years.

Multiple factors triggered this collapse. From 2002-2003, after an opposition-led oil strike and an attempted coup, almost half of the staff at the state-owned oil company Pdvsa was sacked. Since then the technical quality of management has been disastrously poor. From 2005-2007 the government renegotiated oil contracts with foreign companies imposing tougher terms and expropriating some oil fields. From 2008-2009 a number of oil service companies were also expropriated and transferred to Pdvsa, which proved to be a poor home for them since it was suffering from entrenched corruption and terrible management. In 2013 Chávez died and was replaced by Nicolás Maduro. The successive chavista governments frequently raided Pdvsa’s cash balances to fund general spending.

The US-based Centre for Strategic and International Studies (CSIS) has presented a dramatic visualisation of the fate of oil production and the wider

Venezuelan Oil Production and GDP Timeline



Source: CSIS using EIA and IMF data

CSIS | CENTER FOR STRATEGIC & INTERNATIONAL STUDIES

Venezuelan economy (*see below*). This shows that since 2015 oil output and GDP have been in a kind of lockstep death plunge, both falling by more than half in absolute terms.

Oil production will fall further before it improves. On 23 January the US government announced a new set of sanctions. They ensure that any payments for Venezuelan oil exports to the US must be diverted into blocked accounts held for the benefit of the parallel opposition government of Juan Guaidó which is now recognised by Washington. It is estimated that Venezuelan oil exports to the US have been running at around 515,000bpd, worth approximately US\$11.5bn a year. In addition, the new sanctions are preventing US companies from exporting around 120,000bpd worth of light diluents to Venezuela (these are normally mixed with Venezuelan heavy crude from the Orinoco Belt to make it exportable).

Inevitably the sanctions will hit production further. Venezuela has begun to cut shipments to the US. It is seeking to source diluents from, and to direct cash-generating crude sales to, other markets (mainly India). The country exports to Asia (around 570,000bpd) and to Europe and the Caribbean (320,000bpd), but a significant portion of these exports does not generate cash as they are payment in kind for earlier financial loans. China could potentially increase its cash imports from Venezuela. But CSIS concludes, "Reduced cash flows as a result of sanctions will gradually have an impact...and will create difficulties for PdVSA in paying workers, purchasing equipment and diluents, and carrying out maintenance on the few remaining operational upgraders and refineries. These dynamics majorly skew the production outlook further to the downside for the coming year." Energy research company Rystad

believes production could fall from 1.34m bpd at the end of 2018 to as low as 680,000bpd in 2020.

Looking further ahead, would a future post-crisis government be able to get the oil flowing again? Venezuela has the world's largest proven hydrocarbon reserves, so in principle recovery must be possible. Iraq, which suffered an invasion in 2003 and years of conflict, managed to get its oil moving again. However, it will take time and a lot of money to change things in Venezuela. Guaidó says he intends to name Gustavo Baquero, a former international oil executive, as head of Pdvsa, and will seek to introduce a hydrocarbons law to allow majority private ownership of new projects, with competitive fiscal terms and an independent regulator conducting licensing rounds. Optimists have argued that under a future government with investment flowing back in, a post-crisis Venezuela might be able to raise production by 150,000bpd a year. At that rate it would take over a decade to get production back up to 3m bpd, near where it was in the 1990s.

Even that might err on the side of optimism, however. Pdvsa is in a disastrous state and is saddled with a reported US\$34.6bn worth of debt. It will need a root and branch overhaul. Some of the mature fields operated by Pdvsa have been damaged by the way gas or water injection for secondary recovery was closed down. The entire logistics chain including pipelines, ports, and tankers is in disrepair. Starting new production from the Orinoco Belt will require the construction of expensive upgraders to blend the heavy oil it produces with imported light crude.

One estimate by oil experts is that to rebuild the oil industry, investment of the order of US\$20bn a year will be required for many years. Even that does not dispel some uncertainties. There are doubts over long-term demand for Venezuelan heavy crudes, with the US refinery network increasingly geared to handle lighter crudes. The global growth of renewable energy sources and the shift towards electric vehicles is not going to stop the world needing oil, but it may dampen long-term demand and prices in a way that is unhelpful to the eventual reconstruction of the Venezuelan economy.

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