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CONTENTS

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Politics trumps economics in Brazil

Brazilian politics remain volatile, but something important has changed. When former President Luis Inácio 'Lula' da Silva (2003-2010) was briefly arrested for questioning over corruption allegations on 4 March, plunging the government of his protégé, current President Dilma Rousseff, into a new crisis, the Bovespa stock market index and the national currency, the Real, both rallied. The business community appears to have concluded that the government must fall before the economy can rise. Anything that shortens the Rousseff presidency is likely to encourage the markets. Yet resolving the political crisis still looks like being more complex, and taking longer, than many would hope.

Despite some earlier claims that the Brazilian economy might have been stabilising, the outlook remains unremittingly gloomy. Updated figures are showing that the recession in 2015 was deeper than expected. GDP contracted by 3.8%, the sharpest fall in the last 25 years. The consensus of private economists tracked by the Brazilian central bank (BCB) is now pointing to a further GDP contraction of 3.8% in 2016. Looking ahead, the market is expecting a weak return to growth in 2017 with expansion of only 0.5% (a number which could still be revised downwards). The fact that a falling economy might reduce the rate of inflation (currently 10.2% and expected to fall to 7.6% by year-end) is not much consolation.

"There is nothing to celebrate in these GDP figures", Luciano Rostagno of Banco Mizuho do Brasil told the *Wall Street Journal*, adding "There is no reason to expect the economy will rebound. Investment and industrial sector activity are expected to remain weak, and the outlook for private consumption remains bleak on the back of job and credit market conditions". Some analysts highlight a small early-2016 rebound in consumer and investment confidence from record lows, which in other circumstances would perhaps herald the beginnings of a recovery. But they say a rebound is being blocked because private sector companies are overburdened by debt and face difficulties raising credit. "This is a big difference compared to prior crises", says Carlos Kawall of Banco Safra.

The business community seems to have reached the conclusion that the government of President Rousseff, beset by political crisis and corruption allegations, simply lacks the authority and skill needed to steer Brazil out of recession. Emblematic of that view was a statement issued on 7 March by the São Paulo Federation of Industries (FIESP), considered the country's most influential private sector association. "In our unanimous view, this government has lost credibility and trust, and this fact is driving the deterioration of the economy", said FIESP president Paulo Skaf. He added that 1.6m jobs had been lost and companies were going bankrupt. "We can't keep silent while this is happening" Skaf added. FIESP said it would support the anti-government, pro-impeachment demonstrations called for 13 March.

Much will depend on how the political crisis eventually ends. There are at least three potential scenarios, each with different implications for economic policy. The first is that President Rousseff manages to complete her second, four-year presidential term with general elections due in late 2018 and a new government set to take office in January 2019. Until recently, this scenario was considered by many as the most likely, but may no longer be so. Most analysts now concede that if the president does in fact survive, she will be too weak to get to grips with the economy. There has been some recent speculation that the price for survival might be a deal reducing the powers of the presidency and creating a new prime ministerial role. But whatever deals are done, a big disadvantage of this scenario is that the current, deeply divided, federal congress is set to remain in office for almost another three years. This congress, many of whose members face ongoing corruption allegations, has consistently refused to implement measures to reduce the fiscal deficit. So from a business point of view, the "continuity" option looks like three lost years during which there will be no serious attempt to initiate much-needed structural reforms. They are also likely to be three years of recession or of flat growth.

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Scenario two is that the current attempt to impeach President Rousseff, based on her alleged use of "creative accounting" techniques (known as *pedaladas*) in the 2014 budget will eventually succeed. Until recently, this was considered unlikely because of procedural disputes and doubts that the supporters of impeachment would gather the necessary two-thirds majority they need in congress. As a result of the latest revelations, this scenario may now be more likely than it was a month or two ago. However, it too falls somewhat short of delivering the radical economic policy overhaul many in the business community would like to see. If President Rousseff is impeached, Vice President Michel Temer will take her place and serve the remaining portion of her four-year term in office. On the plus side, Temer is from a different political party in the ruling coalition (Partido do Movimento Democrático Brasileiro [PMDB]) and has taken some distance from the president, which would enable him to seek multi-party support as a transitional figure. In this scenario there might be more effective short-term macroeconomic management in the run-up to the 2018 elections. But there are downsides here too: the PMDB is both the largest and most internally divided political party in Brazil. The composition of congress will not change until January 2019, and there is no guarantee that Temer will be able to get the existing congress to support necessary austerity measures.

In a third scenario, a different process - cassação - could remove Rousseff from office if the top electoral court, the Tribunal Superior Eleitoral (TSE), rules that monies from the Petrobras corruption scandal were used to fraudulently manipulate the results of the 2014 general elections. The TSE has the power to declare the 2014 elections null and void and to order a re-run. In the interim President Rousseff would be dismissed. While this scenario offers much more rapid change, and the prospect of electing a new government and a new congress as early as this year, both with a renovated democratic mandate to tackle the country's economic malaise, it too has some downsides. One of the main ones is that the interim presidency during the time it takes to call new elections falls to the speaker of the chamber of deputies – a position currently occupied by Eduardo Cunha (of the PMDB), a controversial figure facing attempts to unseat him over multiple corruption allegations. For *cassação* to work in political terms, Cunha would need to be replaced by a deputy with greater cross-party support.

CUBA

Chipping away at the embargo

Ahead of President Barrack Obama's planned visit to Cuba on 20-22 March, there are signs of further moves to ease the US embargo on bilateral trade.

US congressional sources said that further measures to liberalise bilateral economic relations would be announced ahead of the visit, and that they could involve travel, trade, and banking rules. One possibility was an easing of regulations restricting trips from the US to Cuba by individuals. Easier travel has so far been restricted to group tours or family visits – the change would ease rules governing what is called "people-to-people" travel. Also said to be under consideration was a relaxation of US regulations limiting Cuba's use of US dollars for international transactions.

There are limits to the economic thaw on both sides. On the US side, the upcoming presidential elections are casting a long shadow. President Obama would clearly like his opening to Cuba to endure after he steps down from office next January. To try and increase the chances of that happening, he has invited selected members of Congress from both his own Democratic Party and from the Republican Party (GOP) to accompany him on the trip. Jeff Flake, a Republican senator who supports lifting the trade embargo, has confirmed he will be accompanying Obama. But opinion within the GOP is divided. Donald Trump, the frontrunner in the race for the Republican nomination is on record as saying that he supports Obama's opening to Cuba (a position which contrasts with Trump's high-profile attacks on Mexico). But the two other prominent contenders, Ted Cruz and Marco Rubio, are both Cuban-Americans who feel that the Obama administration is not doing enough in support of human rights on the island, and strongly oppose any lifting of the trade embargo imposed by the US in 1960. They have taken this position despite opinion poll surveys showing that a narrow majority of Cuban-Americans support lifting the embargo. Given the current composition of the US Congress, the embargo can only be lifted with Republican support, and the party has said it will not back such a move during Obama's presidency.

"One point of controversy during the visit will centre on Obama's meeting with selected activists from the Cuban opposition. His Republican critics are demanding better engagement with the opposition and human rights activists, while the Cuban authorities want to minimise those contacts."

On the Cuban side, on 9 March the government signalled that it was ready to make further progress in improving bilateral relations, but that it would not abandon socialist policies. An editorial in *Granma*, the Communist Party newspaper, set the tone by saying, "This will be the first time that a US president visits a Cuba that is in control of its own sovereignty and has a revolution in power, presided by its historic leadership." The newspaper went on to describe the trade liberalisation process as "complex" and as one that can only advance in the terrain of "mutual respect and reciprocity". Cuba says the US must not intervene in its internal affairs, must lift the trade embargo, and must withdraw from the Guantánamo military base. One point of controversy during the visit will centre on Obama's meeting with selected activists from the Cuban opposition. His Republican critics are demanding better engagement with the opposition and human rights activists, while the Cuban authorities want to minimise those contacts.

COLOMBIA

Government tries to head off power cuts

President Juan Manuel Santos announced the resignation of his mines and energy minister Tomás González on 7 March and the appointment of María Lorena Gutiérrez to replace him. The change came amid growing pressure on Colombia's power supplies caused by drought, and fears that power cuts will be unavoidable. The outgoing minister had "assumed responsibility for the delay in savings measures" the president said.

"As a result of the El Niño weather pattern, Colombia has been suffering a severe drought since the last quarter of 2015. Water levels at the country's hydroelectric power generators have been dropping, threatening electricity supply. In normal times, about 70% of Colombia's total power supply comes from hydroelectric generators."

As a result of the El Niño weather pattern, Colombia has been suffering a severe drought since the last quarter of 2015. Water levels at the country's hydroelectric power generators have been dropping, threatening electricity supply. In normal times, about 70% of Colombia's total power supply comes from hydroelectric generators. A fire in February at the 560MW Guatapé hydroelectric plant in Antioquia reduced generating capacity and limited water flowing into other plants. Guatapé will not return to normal output levels until September. There were also technical problems at the 610MW TermoFlores power plant on the Atlantic coast, which was expected to be out of commission for 3-4 weeks. As a result Colombia suffered an 11% fall in electricity supply over 15 days, President Santos said.

The president added that new emergency regulations would apply penalties for over-use of electricity, together with benefits for households and companies achieving energy savings. "As President I would have preferred that we take these measures sooner", Santos commented, adding, "What is at stake is the credibility of the government, but most of all, Colombians' confidence in the electrical system". A further factor in the departure of González was the beginning of a formal investigation by the attorney general's office into conflict of interest allegations, concerning his suspected links to a company that won government contracts.

On taking office, new minister Gutiérrez noted that despite earlier exhortations to save energy, Colombia's electricity consumption actually rose 9% year-on-year in February, bringing closer the possibility of power cuts. "Saving energy is no longer an option, it is a duty" Gutiérrez said. The country would have to make 5%-10% energy savings if it was to avoid electricity rationing, she warned. She has urged consumers in high temperature areas of the country not to set their air-conditioning thermostats below 22 degrees centigrade, and ordered that all government buildings turn off their main lights after 6pm. Gutiérrez, previously minister of the presidency, is considered to be part of the Santos inner circle.

The drought and water shortages have also affected the agricultural sector and led to sharp rises in the prices of some foodstuffs. There have been reports of displacements of people in the province of Bolívar, as local communities move in search of better access to drinking water and food supplies. The government says it is authorising CREG, the power and gas regulator, to introduce a new "carrot and stick" policy that will reward energy savings and penalise over-use.

According to officials, the government will match any savings made, relative to average use, and double the charge for over-use. As a result, if a household's average electricity bill is COP100,000 and a family uses COP90,000 worth, then the bill charged will be a lower COIP80,000. Similarly, were the same household to use COP110,000, the bill charted will be a higher COP120,000.

In theory, Colombia's power sector should have been better prepared for the recurring El Niño drought (the El Niño weather pattern occurs on average once every five years). Given the country's high dependence on hydroelectricity, in earlier years the government had introduced a regulatory and energy pricing system, which encourages companies to maintain a proportion of thermal generating capacity. But delays in planned natural gas imports from Venezuela have had a negative impact on the evolving energy balance. National power demand in January was the equivalent of 10.2GW with hydroelectric plants meeting only around 50% of the total, and the remaining thermal plants, which have 4.4GW capacity, struggling to make the balance.

In an attempt to avoid power cuts, Colombia is also importing electricity from Ecuador. Further investment in new generating capacity and system resilience is needed. The Inter-American Development bank (IDB) has recently provided a US$9.3m loan to promote private investment in renewable energy, noting that "About 60% of Colombia's territory is not connected to the electricity grid, and roughly 1.8m of its people rely on limited and scattered power services."

DOMINICAN REPUBLIC

Benefiting from the tailwinds

The Dominican Republic remains one of the strongest economies in the region, thanks to a combination of factors including the steady recovery in the US, lower energy (and food prices) and sound fiscal and monetary policies. There is still considerable room for improvement to the country's physical – and institutional – infrastructure.

"The Dominican Republic remains in something of an economic 'sweet spot', with inflation remaining low in spite of the country being one of the fastest growing emerging markets globally. The IMF's latest figures and forecasts point to a slight slowing in real growth in the US$68bn economy, from 7.0% in 2015 to 5.4% in 2017."

The Dominican Republic remains in something of an economic 'sweet spot', with inflation remaining low in spite of the country being one of the fastest growing emerging markets globally. The IMF's latest figures and forecasts point to a slight slowing in real growth in the US$68bn economy, from 7.0% in 2015 to 5.4% in 2017. Inflation, which has been suppressed by the fall in fuel and food prices over the last year or so, is expected to pick up, but only to 4.3% in 2016 . The central bank is targeting inflation of 3%-5%.

The Dominican Republic's economy - as the IMF sees it

	2013	2014	2015	2016
Real GDP growth %	4.8	7.3	7.0	5.4
Nominal GDP US$bn	61.3	64.1	67.6	
Average CPI inflation %	4.8	3.0	0.8	4.3
USD/DOP exchange rate - end of period	42.7	44.3	45.4	
Consol. Public Sector deficit % GDP	-5.0	-4.5	-1.3	-5.0
Consol. Public Sector debt % GDP	48.3	48.1	48.5	
Government revenues and grants % GDP	14.6	15.1	18.0	14.6
Government primary spending % GDP	15.1	15.2	14.6	
Growth in credit to the private sector %	15.0	19.5	12.2	9.1
Current account deficit % GDP	-4.1	-3.2	-2.0	-2.2
Gross International Reserves US$bn	4.701	4.862	5.258	5.645

Source: *IMF Press Release 16/84, 1 March 2016*

There have been numerous tailwinds. The general strength of the US economy has boosted growth in inbound tourism and remittances. This, in turn, has boosted consumption in the Dominican Republic at a time that private sector investment has been robust. Aside from restricting inflation, the fall in fuel prices has also placed downwards pressure on import costs and boosted disposable incomes. Bank credit to the private sector has been growing slightly faster than nominal GDP.

This is in the context of a declining current account deficit (it fell to 1.3% of GDP in 2015), broadly stable international reserves and moderate currency depreciation over the last three years.

Public finances are also basically in good shape, with the government running a primary surplus and an overall public sector deficit of about 1.3% of GDP in 2015 (albeit it is expected to grow to 5.0% of GDP over the coming year).

The main challenges relate to deficiencies in the Dominican Republic's infrastructure and institutions. The IMF noted that "addressing long-standing problems in the electricity sector remains key to improving growth prospects. Needed measures include significant upgrades to the public distribution networks, a move toward cost recovery pricing and reducing regulatory uncertainty". The Fund believes that these initiatives would boost investment even further.

The *Global Competitiveness Report 2015-2016* published by the World Economic Forum (WEF) confirms that the power supply – or lack of it – remains a critical problem. The Dominican Republic was assessed as being the 98th most competitive economy of the 140 assessed globally. The country's ratings across the 12 major 'pillars' considered by the WEF are broadly similar except in relation to the macroeconomic environment (57), market size (70), business sophistication (76) and technological readiness (84). However, the country is ranked 123 for the quality of its electricity supply.

The WEF also found that corruption and governance remain a significant challenge. The country is rated 134 for diversion of public funds and only marginally better for public trust in politicians, judicial independence, favouritism by government officials and the ethical behaviour of firms. In spite of government revenues and spending amounting to less than one fifth of GDP, high tax rates were the factor identified by the companies that the WEF surveyed as being the most problematic for doing business in the Dominican Republic.

"The weakness in the education system has contributed to the unequal distribution of income and wealth. The Dominican Republic's impressive macro-economic outcomes have yet to produce growth that is truly inclusive."

Corruption and the inadequate training of the workforce were the second and third most important problems. The overall implication is that the government is not efficient at collecting tax revenues from what is a fairly small base and is not spending the money wisely – although it is generally spending less than it is collecting. One consequence of this is that the country's education system has been deficient. The weakness in the education system has contributed to the unequal distribution of income and wealth. The Dominican Republic's impressive macro-economic outcomes have yet to produce growth that is truly inclusive.

JAMAICA

Sticking with the program

The newly-elected Jamaica Labour Party (JLP) government under Prime Minister Andrew Holness may find it hard to meet its pledge to create about 200,000 new jobs over the next five-to-seven years. In the meantime, the government will continue to follow the economic reform program that was agreed with the IMF as a part of the four-year Extended Fund Facility initiated in May 2013.

The latest (October) review of the country's labour force, published by the Statistical Institute of Jamaica (SIJ) at the end of January, contained good news. The total labour force came to just under 1.33m, or 1.1% more than one year previously. The male labour force grew by 0.9% to 723,100, while the female labour force increased by 1.5% to 602,100. The number of employed men rose by 1.6% to 655,700, while the number of employed women increased by 2.6% to 490,900. In terms of occupations, the biggest growth (of 4.6% to 262,100) was in the number of people classified by the SIJ as 'professionals, senior officials and technicians.' The growth of employment is being driven by the services sector. The number of people working in hotels and restaurants increased by 13,700 (or 16.8%), while the number of people working in real estate and business activities grew by 10,000 (or 15.5%).

This means that the overall unemployment rate fell by 0.7 percentage points (pp) to 13.5%. For men, the rate dropped by 0.6pp to 9.9%; for women, by 0.9pp to 18.5%. Over the year to the end of October, the unemployment rate for youths aged 14-24 years dropped by 3.3pp to 32.7%.

Collectively, these numbers mean that the labour market is developing broadly in the way desired by the new government, which achieved a very slim victory over the People's National Party (PNP) of former Prime Minister Portia Simpson-Miller in the general election of 25 February 2016. The JLP campaigned on an ambitious pledge generate new jobs over the next half decade or so. According to its election manifesto, the JLP is looking to create 10,000 jobs from urban renewal in Kingston; 30,000-40,000 in Business Process Outsourcing (BPO); 15,000-25,000 in the construction of transport infrastructure; a similar number – after completion of the projects – in logistics and tourism; 20,000 in manufacturing and agribusiness; 30,000 from further expansion of the hotel industry; 20,000 from new small businesses; 50,000 in the development of the Sun Coast (from Port Royal to Morant Point) and another 30,000 permanent jobs on the Sun Coast in maintenance, housekeeping, landscaping and management services. Crucially, these jobs should be suitable for the young and relatively unskilled, where unemployment rates are still very high.

"On 4 March 2016, the IMF confirmed that the new government would pursue the primary surplus target of 7.0% of GDP in the coming fiscal year and introduce tax reforms to boost efficiency and equity. In order to enable the government to focus on setting up a new administration, the IMF will combine the 11th and 12th reviews under the program: these will take place in May."

The JLP's job creation target may be difficult to attain, however. A government that won office by 32 seats in the House of Representatives to 31 seats will be vulnerable to attack in the event of any deterioration in the local labour market – even if it is only temporary.

Nevertheless, the program is not impossible – and particularly as other trends are favourable. For instance, Jamaica has been a major beneficiary of the slump in the global price of oil. According to the SIJ, the merchandise trade deficit for the first 11 months of 2015 was US$3.15bn, or 12.2% less than in the previous corresponding period. Thanks mainly to a reduction in the bill for imports of fuel (and food), imports for the period were US$4.6bn, or 12.9% lower than in the first 11 months of 2014. Merchandise exports from January to November last year were US$1.15bn, or 14.8% lower than in the previous corresponding period. Consumer price inflation was -0.4% in the month of January and +3.7% over the preceding 12 months.

Late last year, we highlighted that Jamaica's economy was at an early stage of a virtuous circle of stronger growth, lower inflation and reduced financial risk. In November 2015, the IMF was sufficiently pleased with the fiscal discipline being implemented by the PNP administration and other reforms (such as the new Banking Services Act, the broadening of the mandate of the Bank of Jamaica – the central bank – in relation to financial stability and changes to the operation of the country's money markets) that it lowered the target for the government's primary surplus to 7.25% of GDP for the current (March 2016) fiscal year and to 7.0% for the next fiscal year.

Prime Minister Andrew Holness and his new economy team remain committed to the reform program. On 4 March 2016, the IMF confirmed that the new government would pursue the primary surplus target of 7.0% of GDP in the coming fiscal year and introduce tax reforms to boost efficiency and equity. In order to enable the government to focus on setting up a new administration, the IMF will combine the 11th and 12th reviews under the program: these will take place in May.

TRINIDAD & TOBAGO

Downgrade, yes; crisis, no

On 4 March 2016, Moody's Investor Services placed the Baa2 sovereign rating of Trinidad & Tobago on review for a downgrade. However, a full-blown financial crisis in 2016 is unlikely.

Moody's assessment is based on the structural shock to the finances of the government of Trinidad & Tobago resulting from the fall in prices of oil and gas, which together account for nearly two-thirds of total exports and about 30% of GDP. They also account for about 36% of government revenues (having generated half of revenues as recently as 2013). In December 2015, ratings agency Standard & Poor's (S&P) had maintained its investment grade A/A-1 long- and short-term ratings for the sovereign, but revised its outlook from stable to negative.

"The current budget (for the year to September 2016) does recognise that the economic environment is much tougher than in much of 2015 (let alone 2014 and 2013). Overall spending in the year to September 2015 amounted around TT$61.8bn (about US$9.7bn). In the current year, spending – after one-off payments of back-pay to public sector workers – should be reduced by about TT$3.8bn."

Looking forward, Moody's is fairly bearish about the prospects for the energy sector. The ratings agency looks for the price of oil (as per the Brent benchmark) to be US$33/barrel this year before rising to US$38/barrel in 2017. Moody's expects that the price of oil will increase gradually to US$48/barrel by 2019. Moody's is looking for a gas price (as per the Henry Hub benchmark) of US$2.25/ million Btu in 2016 and US$2.50/ million Btu in 2017.

Moody's notes that, "assuming no policy response and other factors being equal, the depressed energy prices for the coming years would imply a further reduction of 22% in government revenues (to 23% of GDP from 30.6% of GDP), an increase in the fiscal deficit and a rise of 15 percentage points in Trinidad & Tobago's debt burden over a four year period. (2013-2016)."

The current budget (for the year to September 2016) does recognise that the economic environment is much tougher than in much of 2015 (let alone 2014 and 2013). Overall spending in the year to September 2015 amounted around TT$61.8bn (about US$9.7bn). In the current year, spending – after one-off payments of back-pay to public sector workers – should be reduced by about TT$3.8bn.

Measures to boost revenues include changes to the Value Added Tax (VAT) system. The overall VAT rate is being reduced from 15.0% to 12.5% and the threshold for VAT registration has (since the beginning of 2016) been increased from TT$360,000 to TT$500,000. However, the base for VAT has been broadened, and collection has been made more rigorous. The government expects to boost overall VAT revenues in the current fiscal year by TT$4.0bn.

Other tax changes should boost revenues by another TT$1.2bn. These include: the reduction of the fuel subsidy (which had kept the retail prices of gasoline and diesel at artificially low levels); increased efficiency in the collection of tax; the introduction of a new property tax system; rises in the Green Fund and Business Levies; and a new tax for the gaming industry.

However, these figures pale into insignificance relative to what the government hopes to generate from one-off items. The budget envisages TT$13.4bn in revenues from: an Initial Public Offering (IPO) of Trinidad & Tobago NGL Limited; a partial repayment from insurance-based conglomerate CLICO – which had been rescued by the government in the wake of the global financial crisis; dividends from the National Gas Company (NGC); and a capital repayment from Trinidad Generation Unlimited.

In other words, the government has assumed that new revenue measures and one-off items will assist the budget to the tune of 3.2% of GDP and 8.2% respectively, with the result that the deficit falls from 4.2% of GDP in 2015 to 1.8% of GDP this year. This is in the context of the government having access to the Heritage & Stabilisation Fund (HSF), whose assets amount to around US$5.6bn (or 22% of 2016 GDP). In an address to the nation on 29 December 2015, Prime Minister Keith Rowley noted that the government plans to draw down around US$1.0bn from the HSF this year and, perhaps, another US$0.5bn in 2017.

In explaining its decision to place the government of Trinidad & Tobago on review for a downgrade, Moody's identified a number of factors that could actually result in a lowering of the rating. One was a "marked worsening in the fiscal balance for which there was no clear reversal". A second was pressure on the exchange rate regime. The third was deterioration in the local or regional political environment that disrupts energy production or investment. A fourth was signs of financial stress at state-owned oil company Petrotrin and the NGC.

Considering all of these factors together, it is nearly certain that Moody's will downgrade the sovereign at some stage in 2016. Considering the factors individually, though, we conclude that a full-blown crisis is unlikely.

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• Thanks to the combination of higher tax revenues, lower spending, one-off items and access to around TT$6.4bn in funds from the HSF, it appears unlikely that the government would really find itself in a situation where the deficit is irredeemably large. Even if the government is only able to raise half the amount that it is looking for in the current year from one-off transactions, the gap should be filled by money extracted from the HSF.

• Nor is there evidence of a foreign exchange crisis. The Central Bank of Trinidad & Tobago (CBTT) has allowed the currency to depreciate from around TT$6.35/US$, the prevailing level for much of 2015, to TT$6.55/US$ currently. However, this is in the context of a currency that had been appreciating in real terms for years previously because the level of inflation in Trinidad & Tobago had been higher than in the country's trading partners. Foreign exchange reserves at the CBTT have run down from US$11.3bn in March 2015 to US$10.3bn (or about 11.8 months of export cover) at the end of 2015.

• Although the industrial relations environment in Trinidad & Tobago has often been difficult, in that workers have demanded and received wage increases that are quite independent of any improvement in productivity, there is no sign of an exacerbation in industrial tensions. Over the medium-term, any agreement with the government of Venezuela that permits the development of the Loran-Manatee gas field should actually boost production and exports. Meanwhile, there is no sign of financial problems at the state-owned energy companies that would be beyond the capability of the government to deal with.

In October 2015, we suggested that the government had not found a fiscal policy that is truly sustainable over the long-term. We did concede, however, that it had bought itself time in which it could build consensus with key stakeholders in order to make hard decisions. In short, we considered that a full-blown crisis was far from inevitable. This remains our view.

URUGUAY

The bastion of stability in a volatile region

Uruguay's economy has been fairly shockproof to date and looks to remain relatively insulated from the problems in neighbouring Brazil.

In its latest Article IV Consultation on Uruguay, the IMF described the country as being a "bastion of stability in a volatile region". The country has enjoyed over a decade of steady growth. Per capita GDP (of around US$16,600 in 2016) is one of the highest in Latin America, while the incidence of inequality and poverty are among the lowest. Growth has fallen over recent years, but has remained resilient in spite of the economic problems in neighbouring Argentina and Brazil. The problems in Argentina have been more challenging, because Argentina accounts for more than half of Uruguay's tourism receipts and imports specialised manufactures that do not have obvious alternative markets. About one fifth of Uruguay's merchandise exports go to Brazil: although these exports exceed the merchandise exports to Argentina by four times, they are dominated by commodities, for which alternative markets are easier to find.

"The country has enjoyed over a decade of steady growth. Per capita GDP (of around US$16,600 in 2016) is one of the highest in Latin America, while the incidence of inequality and poverty are among the lowest. Growth has fallen over recent years, but has remained resilient in spite of the economic problems in neighbouring Argentina and Brazil."

Uruguay's economy - as the IMF sees it

	2013	2014	2015	2016	2017
Real GDP Growth %	5.1	3.5	1.5	1.4	2.6
Unemployment %	6.0	6.5	7.9	7.6	7.5
CPI Inflation %	8.6	8.9	8.7	8.2	7.7
Central government revenue % GDP	29.5	29.0	28.9	28.9	29.0
Non-interest spending % GDP	29.1	29.3	28.7	29.0	28.8
Primary balance % GDP	0.4	-0.6	0.0	-0.4	-0.1
Overall balance % GDP	-2.3	-3.5	-3.6	-3.4	-3.0
Gross public sector debt % GDP	60.2	61.3	61.9	63.1	64.0
Net public sector debt % GDP	35.9	34.9	36.6	38.6	39.9
Current account % GDP	-4.9	-4.3	-3.8	-4.0	-3.8
FDI % GDP	5.3	4.8	4.5	4.4	4.4
Reserves (months of imports)	13.2	14.6	14.6	15.2	14.7

Source: *IMF Article IV Consultation, February 2016*

Both government revenues and spending have remained slightly under 30% of GDP (which is expected to amount to about US$57bn in 2016) in recent years and, in the view of the IMF, will continue to do so. Revenues and spending have generally been balanced. The overall fiscal deficit has increased, but is expected to stabilise at a little over 3% of GDP. The current account deficit has been running at around 4% of GDP, but has been covered by inwards Foreign Direct Investment (FDI). Although the Banco Central del Uruguay (BCU, central bank) has allowed foreign currency reserves to fall in absolute terms by US$2.6bn since June last year, reserves continue to equate to around 14 months of imports.

Arguably the main challenge is inflation. The rise in CPI inflation to above 10% has had political implications for the ruling left-wing Frente Amplio (FA) coalition. Inflation has consistently been above the BCU's 3%-7% target range over recent years. This is in spite of the fall in global prices of food and energy through 2014 and 2015 and in spite of the central bank's fairly tight monetary stance.

Various factors have contributed to the stubbornly high level of inflation over the last two years. One is the depreciation of the peso, which fell by 22% against the US dollar in 2015, having slipped by 16% in 2014. (Since the beginning of 2016, the peso has dropped by a further 10% or so). Another has been the lack of the pass-through to consumers of lower fuel prices by Administración Nacional de Combustibles, Alcoholes y Portland (ANCAP), the state-owned fuel company. The government has been working to improve ANCAP's financial situation.

Domestic demand has remained strong. Because of the indexation of wages, prices of non-tradable goods and services have risen. The government considers that its fairly tight monetary and fiscal policies, together with the new guidelines for wages and prices should contribute to a moderation in inflationary pressures. The IMF, for its part, argues that the government can and should do more.

Overall, though, Uruguay should remain unaffected by the general volatility in global financial markets, the imbalances in the global economy and the economic slowdown (or worse) in much of Latin America. The floating exchange rate should, on its own, provide some protection against external shocks. As an importer of fuel and an exporter of food, the overall impact on Uruguay of the price fall in both has been limited.

"Overall, though, Uruguay should remain unaffected by the general volatility in global financial markets, the imbalances in the global economy and the economic slowdown (or worse) in much of Latin America."

The IMF assesses the banking system to have adequate capitalisation: in addition, the banks (and the BCU) collectively have foreign currency assets that exceed foreign currency deposits (which account for about 80% of total deposits). Nor have the banks been aggressive in their lending practices. At a little under 30% of GDP, credit to the private sector is, by that measure, less than half what it is in Chile and Brazil. Credit growth to firms (in US$) and to households (in real Uruguayan pesos) has been running in single digits.

The government itself is in good financial shape, too. Liquid assets amount to around 6% of GDP and are sufficient to cover debt service to the end of this year. At 15.5 years, average maturity of public sector debt is high – meaning that refinancings of maturing securities in the short- to medium-term are correspondingly low. The government also has access to contingent credit lines (including those made available by the Inter-American Development Bank and the World Bank) that equate to about 4% of GDP.

Dealing with the problems of ANCAP

The state-owned monopoly oil refiner ANCAP had total assets of US$2.3bn in 2014, and was the largest corporation in Uruguay. In spite of the fall in global oil prices, the company has been incurring losses since 2011. Losses of US$323m in 2014 reduced ANCAP's net worth to US$424m.

Asof the end of October 2015, ANCAP had debt of just over US$1.4bn. Most of this amount was denominated in US dollars and half was owed to banks. Slightly under half of the debt is at variable rates and most is short-term.

The government will use a loan from Corporación Andina de Fomento (CAF – the Latin American Development Bank) to restructure the finances of ANCAP. Debt owed to the government (which mainly arose from the opportunity for ANCAP to repay what it owed to Venezuela's state oil company Petróleos de Venezuela [Pdvsa]) on terms that greatly favoured ANCAP) will be forgiven. The government will seek to reduce ANCAP's borrowings in US dollars and to extend the maturity of its debt.

Working out the economics of crime

There is a big crime problem in Latin America and The Caribbean, but relatively little has been done to compile accurate statistics or understand its economic background. A recent paper published by the London School of Economics (LSE) offers a useful summary of the relevant metrics and key issues.

In their paper, Laura Jaitman (Inter-American Development Bank) and Stephen Machin (University College London) make a convincing case as to why crime is important in the region from an economic viewpoint. One in four citizens in the region say that insecurity is the main problem they face, and rate it as more important than either unemployment or the state of the economy. The region has 9% of the world's population but 33% of the world's murders. The region's average murder rate of 20 violent deaths per year per 100,000 inhabitants is three times higher than the world average. Six out of ten robberies are violent. The authors estimate that "crime imposes significant costs on the economy, absorbing at least 3% of the region's economic output at a conservative estimate". The cost of crime is therefore comparable to the region's annual spending on infrastructure. It can also be argued that without the cost of crime to weigh down its economies, Latin America would not be in recession in 2016.

"What is clear is that Latin America seems to be an exception to the global trend for crime rates to fall. The authors note that, "it is the only region where violence remains high and, since 2005, has been intensifying". There is a global pattern whereby countries with higher per capita income have lower crime rates. But Latin America is an outlier here too: actual homicide rates in Latin American and Caribbean countries are higher than would be expected given their per capita income."

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One explanatory approach is a school of thought known as 'crime economics', which says that potential criminals make a rational assessment of the costs and benefits of committing crimes, relative to the costs and benefits of legal activities. The suggestion is that for a range of institutional and practical reasons the calculation in the region is skewed towards the benefits of crime. The costs of crime are reduced because of the inefficiency of local police and criminal justice systems, which means that only 10% of crimes are resolved (equivalent to a 90% impunity rate). The benefits of legal activity are reduced because of factors such as poor quality education or limited job opportunities. If this theory is correct, it follows that what is required is a "portfolio" of government policy interventions "to increase the payoff to legal activities, together with crime control strategies that deter crime and violence".

The authors suggest that there are many promising initiatives that could be taken to reduce the incentives for crime. They include improved education and skills, community policing, electronic monitoring, community work programmes, behavioural therapies, and drug courts. There is an additional problem, however: crime prevention strategies should be evidence-based, and there is very little evidence because of incomplete statistics. Without this, "Citizen security interventions are often driven by politics, dogma, and emotion", the paper warns.

REGION

Informal economy still an obstacle to growth

A long-standing feature of Latin American and Caribbean economies has been a high level of informality, defined as the proportion of the labour force that works outside the tax and benefits system. Despite some reductions during the commodity boom decade, it is estimated that nearly half the

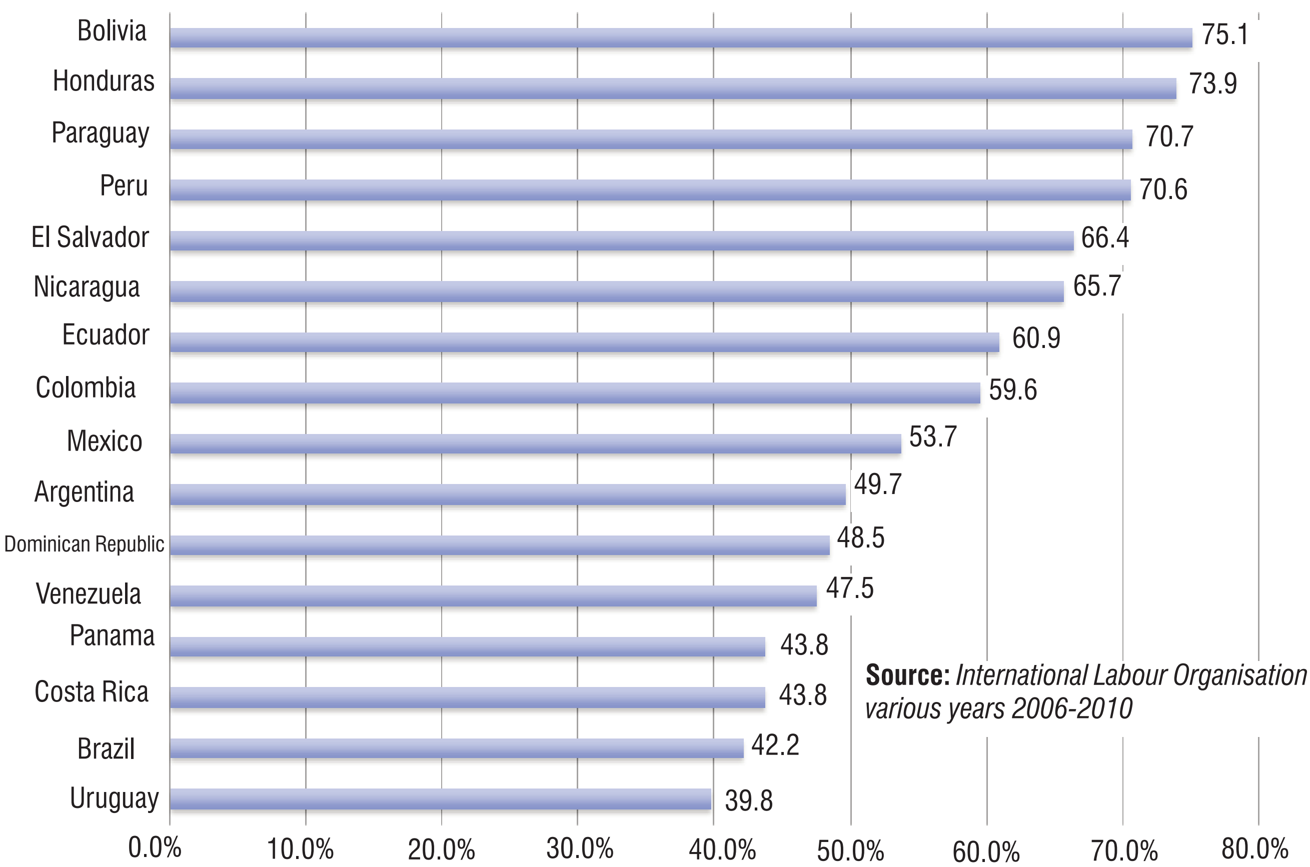
region's workforce remains informal, and the proportion may be edging up as a result of the current recession. Here we examine the impact of informality on living standards, productivity, economic growth, and corruption.

Estimating the size of the informal labour force is quite complex, and has involved overcoming a number of statistical issues. However, according to a working paper published by WIEGO (Women in Informal Employment Globalising and Organising) and using International Labour Organisation (ILO) data, informal employment now accounts for 51% of non-agricultural employment in the region. For comparison, the proportion in other areas of the world ranges from a low of around 10% in Eastern Europe and Central Asia (given the legacy of centrally planned economies, where informal employment was considered illegal), to 33% in China (based on a survey of six cities), and up to 82% in South Asia.

More women than men are informally employed in Latin America. According to WIEGO, 54% of the region's female workers and 48% of male workers are informally employed. The overall rate affecting both genders also varies sharply between countries. According to the ILO, the rate varies between a low of 39.8% in Uruguay and a high of 75.1% in Bolivia. While good economic growth in the region during the commodity boom years may have led to a slight reduction in the share of informal employment, it is hard to detect a clear trend and there are signs that informality may be increasing again. Writing for the Americas Society/Council of the Americas (AS/COA) in April 2015, Elizabeth González said that the regional informality rate had fallen from 50.1% in 2009 to 46.8% in 2013, which she described as a "slow but sure" reduction. However, as we have seen, WIEGO estimates that the number is now back up to 51% and comments that,"contrary to predictions, the informal economy has not only persisted, but has also emerged in new forms and in unexpected places".

A lot of informal workers in Latin America

Share of informal jobs in total employment (%)



Source: *International Labour Organisation (ILO); various years 2006-2010*

"Countries with higher informality rates tend to have more unequal distributions of income and greater poverty. While it is possible for certain informal occupations to pay comparatively well – some taxi drivers, domestic servants, or street sellers can in certain circumstances have good earnings – the reality is that they lack the protection for the bad times that are enjoyed by formal workers – everything from health insurance through to unemployment support or pensions."

Informality matters for a number of reasons. One is that informality and poverty tend to be positively correlated. A recent paper by the Organisation for Economic Cooperation and Development (OECD), *Promoting productivity for inclusive growth in Latin America*, notes that there is a broad correlation between the degree of labour force informality and inequality in the distribution of income. Countries with higher informality rates tend to have more unequal distributions of income and greater poverty. While it is possible for certain informal occupations to pay comparatively well – some taxi drivers, domestic servants, or street sellers can in certain circumstances have good earnings – the reality is that they lack the protection for the bad times that are enjoyed by formal workers – everything from health insurance through to unemployment support or pensions.

Informal workers as a whole earn less money, have greater instability of employment, and are more exposed to working in unsafe or dangerous environments. "To cite just one example", the OECD report states, "individuals with fewer skills are often confined to operate in low-productivity, precarious jobs, frequently in the informal economy."

The 'invisible' nature of informal workers – meaning that their details are not known or captured by social services – has also been an obstacle for government-backed poverty reduction programmes. The more successful programmes have had to find ways to deal with this problem. Brazil's *Bolsa Família* programme – an example of a conditional cash transfer (CCT) approach, has made payments to mothers in poor households, on condition that they can demonstrate things like their children's school and health clinic attendance. It is significant that this programme involves building at least a minimal database of information about the beneficiaries. Other government programmes which, for whatever reason, fail to capture the details of the intended beneficiaries, have tended to be less effective. Some have become politicised and are no more than electorally motivated giveaways. Others may be well-run programmes but by their very nature are restricted only to formal workers (such as health insurance or pension programmes).

The formal/informal split also leads to major inefficiencies and distortions in the functioning of labour markets. Typically, informal workers have very low earnings and little or no protection, while formal workers have higher wages, coupled with employment law protection and trade union representation. According to research by the IMF, skilled workers in Colombia earn on average four times the wages of unskilled workers, the largest wage gap in the region. This situation creates inflexibilities in the way companies respond to the business cycle. Because the cost of laying off formal workers is high, companies tend to be slow to adjust employment levels to business conditions. A recent report by UBS notes that in Latin America "firms tend to hire only gradually in the upswing of the cycle, while the decision to lay off in the downswing is usually delayed until the point where large scale firings are made necessary" – a situation said to be typical of the current stage of the labour market in Brazil. Rigid formal labour markets also tend to trigger higher inflation at an earlier stage of an upswing in the business cycle.

ILO regional director José Manuel Salazar said in December 2015, "The cumulative effects of the economic downturn that began three or four years ago and deepened during 2015, can be described as a crisis in slow motion". Latin America's unemployment rate increased to 6.7% in 2015, the first upwards move in five years. "There are signs", Salazar added, "that there may be increasing informality, which according to the latest available data has reached 130 million workers". Another reflection of the problems of informality has been highlighted by the World Bank, which estimates that there are now more than 20m 'ni-nis' in Latin America, a descriptive tag derived from the Spanish phrase 'ni estudia ni trabaja' – people aged 15-24 neither in full time education nor in formal work. The report said that typically, male ni-nis often drop out of school, become unemployed "and are only lucky enough to find unstable jobs in the informal sector, usually never going back to school".

A further by-product of high levels of informality is that Latin America has inefficient and often regressive tax collection systems. With high rates of tax evasion, governments have tended to focus on the taxes that are easier to collect – meaning a high reliance on sales taxes like Value Added Tax (VAT), considered regressive since it has a greater proportional impact on the poor than on the rich. There also tends to be over-reliance on energy or mining royalties in hydrocarbons and minerals-producing countries. In general, as direct taxes are only levied on those in formal employment, the rates tend to be higher than if they were spread across a wider section of the work force. But even then, income tax is widely avoided or diluted.

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In Mexico, for example, a member of the middle class in formal employment can expect to pay a 35% income tax rate, while a poorer but also formal employee will pay 20%. However, the real gap between the two rates is much smaller. The middle class tax payer benefits from a wide range of tax exemptions (among other things for medical bills, mortgage interest and children's education) meaning that his or her effective tax rate is closer to 20%. Seen from the point of view of the informal worker, there is little incentive to become a taxpayer, particularly taking into account the low levels of trust in the government. Some efforts have been made in Mexico to offer incentives to informal workers to become formal and pay taxes, but they have not yet been sufficient to encourage much movement. Policy analysts suggest that some form of gently tapered tax system, whereby low earners start at very low rates – and receive clear social benefits for doing so – might be required.

Informality also tends to combine with financial exclusion. In Mexico, it is only possible to open a bank account if the applicant can produce details of a formal employer, salary levels and taxes paid. Not surprisingly, as more than half the population is informal, only 39% have bank accounts (World Bank data, 2014). The data also shows that under one third of adults had a debit card (27%), less than a fifth had a credit card (18%), and just under one-tenth (8%) had a mortgage. In Peru, only 29% have bank accounts (2014). Equifax, a ratings agency, has calculated that 10.7m Peruvians have access to credit from the financial system. This is less than half the population. Here too efforts are being made to support greater inclusion, for example, through the development of micro-credit institutions and some finance houses that are prepared to lend to people in the informal sector. There are also attempts to use new technology, such as mobile banking, to reach the unbanked. Peru has developed an electronic payment system known as the 'billetera electrónica', which may widen the availability of basic financial products.

A report by the Instituto Mexicano de la Competitividad (IMCO) notes another phenomenon partly caused by a high informality rate. Around 98% of all financial transactions in the country are conducted in cash, compared to a global average of 38%. Cash-reliant countries tend to have larger informal or "shadow" economies (39% of GDP on average) compared to less cash-reliant countries (20% of GDP on average). Cash and corruption tend to go hand in hand. Low cash-reliant countries tend to perform better in the Corruption Perceptions Index (a ranking prepared annually by the NGO Transparency International) than high cash-reliant ones. Cash also facilitates illegal activities. Cities where social security payments are made electronically have up to 10% fewer robberies and muggings than those that pay out in cash. Finally, electronic payments are more efficient and IMCO suggests that properly managed, they could boost growth by between 0.4 and 0.5 of a percentage point of GDP.

Perhaps one of the most important downsides of a high rate of informality is that it is also associated with low levels of economic productivity, arguably one of Latin America's main economic problems in the early part of the 21st Century. Having half the working population outside the tax and benefits system also means that an economy is likely to be working in very small enterprises, using low levels of capital, technology, and innovation, and consequently having very low output per employee. The OECD has noted that although Latin Americans work longer hours than the average in OECD countries, this is more than offset by a huge gap in productivity levels. OECD general secretary Angel Gurría has argued that Latin American governments need to pursue "a more inclusive concept of productivity growth", which would include better education and skills for young people, the creation of higher quality jobs, reducing barriers to entrepreneurship, trade and investment, encouraging innovation and modernising infrastructure.

REGIONAL BUSINESS REVIEW

REGION

Caribbean tourism needs more flights

For the many governments of Caribbean countries and territories looking to boost in-bound tourism, the US is by far the largest market. Geography dictates that US tourists can get to these destinations either by sea (often as cruise passengers who do not necessarily stay overnight) or by air (in which case, the tourists are often more valuable because they stay several days).

This begs a question as to what a government of a Caribbean tourist destination should focus on in negotiations with international airlines Researchers at the IMF have looked at the relative importance of four factors: the number of flights; the average number of seats on planes; the number of airlines and the number of US departure cities with non-stop flights .

The IMF found that the various tourist destinations vary markedly in terms of the four factors. In 2014, there were three destinations to which there were more than 20,000 direct flights from the US. At 25,684, the number of direct flights to the Dominican Republic was slightly greater than the 25,360 that went to Cancún. Receiving 20,920 direct flights that year, The Bahamas was in third place. At the other extreme, there was only slightly more than one flight a day to Dominica (388 for the whole year) and Grenada (440).

US- Caribbean Airlift Availability 2014

	No.Flights	No. Passengers	Ave. Plane Size	No. US Cities	No. Airlines	Vacancy Rate
Antigua & B.	1,028	119,732	153	4	4	24
Aruba	4,822	646,257	159	10	9	16
The Bahamas	20,920	1,286,118	86	18	18	28
Barbados	1,306	197,440	178	3	4	15
Belize	2,287	248,496	147	7	4	26
Bermuda	2,920	283,687	139	6	5	30
Cancun	25,360	3,426,071	160	33	14	16
Cayman Is.	4,005	400,035	139	11	6	28
Dominica	388	9,608	36	1	1	32
Dom. Rep.	25,684	3,019,154	150	20	17	22
Grenada	440	54,427	154	2	3	19
Jamaica	13,327	1,591,018	151	16	12	21
St Kitts & N.	1,621	84,198	74	5	6	30
St Lucia	1,163	160,070	162	5	5	15

Source: *US Department of Transportation, cited in IMF Working Paper WP/16/33*

Because the average number of seats on plane varies, and because arriving passengers are not necessarily inbound tourists (as they may be in transit to other destinations or returning emigrés), the number of flights is not a perfect proxy for tourist arrivals. Cancún, for instance, is something of a special case, because the number of US tourists has basically remained flat even as the number of passengers flying in has risen. Many US air passengers have flown on to Cuba or to other destinations in Mexico. The Dominican Republic, Jamaica and the Bahamas are the next three most important destinations after Cancún in terms of the number of passengers.

At a little over 100,000 in 2014, the total number of direct flights from the US to the Caribbean has yet to exceed the peak of nearly 120,000 that was achieved in each of 2004, 2005 and 2006. Miami and the three main New York airports accounted for about half of the flights in 2014. Atlanta and Fort Lauderdale – both of which have been becoming more important in terms of this factor over recent years – together about another 15%. Other important points of departures quantified by the IMF's researchers were Houston, Fort Lauderdale, Charlotte and San Juan. Collectively, these cities are the points of origin of about 15% of the direct flights to the Caribbean. Other cities account for the remaining 20%. San Juan is the origin of about one quarter of the flights to the Caribbean destinations that it was a decade ago: its relative importance declined even more rapidly once American Airlines moved its Caribbean hub from San Juan to Miami in 2008.

> "The key conclusion of the IMF working paper is that the Caribbean tourism destinations should benefit more from an increase in the *frequency* of flights than from any of the other factors (numbers of seats per aircraft, points of origin for direct flights or of airlines)."

Of the Caribbean destinations, there are only four that can be reached directly from more than 10 US cities: Cancún (from 33 cities), Dominican Republic (20), The Bahamas (18) and Jamaica (16). Interestingly, the airlines flying from the US to Cancún are fewer in number than those flying to the Bahamas or the Dominican Republic.

The key conclusion of the IMF working paper is that the Caribbean tourism destinations should benefit more from an increase in the *frequency* of flights than from any of the other factors (numbers of seats per aircraft, points of origin for direct flights or of airlines). There are three exceptions. Antigua & Barbuda would benefit more from larger aircraft (with greater numbers of seats). Belize needs direct flights from a greater number of US cities. St Kitts & Nevis, by contrast, would benefit from being serviced by a greater number of aircraft.

External Shocks

The IMF paper also looked at the impact of external shocks on tourism in each of the various destinations.

They found that countries that are frequently exposed to severe natural disasters – such as Antigua & Barbuda, The Bahamas, Grenada and St Kitts & Nevis – tend to suffer a large fall in the number of tourists afterwards. The immediate fall in the number of visitors typically ranges between 30% and 50%, and the total number of arrivals over the year following the disaster is usually down by over 90%. In these situations, the number of arrivals normally begins to recover from 10-12 months after the disaster.

Conversely, small natural disasters generally do not have a significant impact on the number of tourist arrivals – and especially if such disasters are common. This is the case for several of the larger destinations, such as Jamaica and the Dominican Republic, as well as Barbados.

A significant change in the region in recent months has been the easing of restrictions on trade and travel between the US and Cuba. Accordingly, the IMF paper also looked at the impact of changes in the numbers of direct flights from the US to Cuba since 1990 on the numbers of flights to the other destinations. There conclusion is that – except perhaps for Belize – the other destinations are unlikely to suffer a reduction in the number of flights as travel between the US and Cuba is liberalised further. The airlines' response may be to take advantage of the opportunity by transferring planes from domestic US and/or Central American routes. Alternatively, they may schedule more flights to Cuba and the rest of the Caribbean without increasing their fleets.

Corporate Radar

> “Marcelo Odebrecht, former president of Odebrecht SA, Latin America’s largest construction and civil engineering company, has been sentenced to 19 years imprisonment by a Brazilian federal court. The sentence was for his part in the bribery, money laundering and organised crime charges brought against the company, which was found to be a participant in the lava jato (‘carwash’) scandal that engulfed the state-run oil company Petrobras.”

Marcelo Odebrecht sentenced: Marcelo Odebrecht, former president of Odebrecht SA, Latin America’s largest construction and civil engineering company, has been sentenced to 19 years imprisonment by a Brazilian federal court. The sentence was for his part in the bribery, money laundering and organised crime charges brought against the company, which was found to be a participant in the lava jato (‘carwash’) scandal that engulfed the state-run oil company Petrobras. Marcelo, 47, is the grandson of the late Norberto Odebrecht, the founder of the company, known across Latin America for its involvement in large-scale building projects. Odebrecht’s lawyer, Nabor Bulhoes, said the sentence was “a serious error by the judiciary” and that his client would appeal against it. Curitiba-based judge Sérgio Moro, who has been at the centre of investigations into the multiple lava jato cases, concluded that Odebrecht and other companies formed a cartel, agreeing among themselves who would win different Petrobras contracts and manipulating contract prices to their benefit. Odebrecht operates in 28 countries and currently has a staff of 168,000 employees. Its revenue in 214 was US$28.5bn. It has been involved in a range of international projects including building the Port of Mariel in Cuba, the Magdalena river waterway in Colombia, the Panama City metro system, and the Gasoducto del Sur in Peru.

Businesswomen big in beer: Carlos Slim is Mexico’s best-known billionaire, with a business empire based on telecoms group América Móvil and regular appearances in the ranking of the top five richest people in the world. But two Mexican women, both with interests in breweries, may be gaining a little more attention. Eva Gonda Rivera, with assets of US$6.6bn, is now reportedly Mexico’s richest woman. Since the 2008 death of her husband, Eugenio Garza Laguera, she and her daughters control 50% of the B shares in Femsa, Latin America’s largest Coca-Cola and soft drink bottling company, which among other interests also owns Mexico’s Oxxo convenience store chain. Femsa acquired a 20% stake in Heineken in 2010 in exchange for the sale of its Cuauhtémoc Moctezuma brewery, a transaction valued at US$7.347bn. Eva is a graduate of the Instituto Tecnológico de Monterrey. The other prominent businesswoman is María Asunción Aramburuzabala, known as Mariasun, with assets valued at US$5bn. She is the granddaughter of a Spanish immigrant who arrived in Mexico in the 1920s and founded the Grupo Modelo brewery, acquired by Anheuser-Busch InBev for US$20.1bn in June 2012. As part of the deal María acquired shares in Anheuser-Busch InBev (now the world’s biggest brewery) as well as a seat on the board. An accountancy graduate from ITAM, along with her mother and sister María has also set up Tresalia Capital, which has interests in real estate through subsidiary Abilia and in technology through KIO Networks.

American Airlines in on-off Caracas connection: In early March, American Airlines said it would again interrupt its New York-Caracas flights, ceasing the service in April. The airline said the decision, coming only three months after the service was resumed, was a response to low demand. It came amid signs of tough negotiations between the company and the Venezuelan government over the right to repatriate its Venezuelan earnings. The dispute had already led to an 80% reduction in scheduled services in 2014. In January, American said it was writing off US$592m worth of revenues that it has been unable to repatriate from the country. Total unpaid debts to all international airlines serving Venezuela have been estimated at US$3.7bn. American said, however, that it plans to maintain its Caracas-Miami service.

Pemex suffering 'liquidity, not solvency problems': There have been further signs of financial stress at Pemex, Mexico's state-owned oil company. At the end of February, it reported fourth quarter losses of US$9.3bn, an increase of 44% year-on-year, which brought losses for calendar 2015 as a whole to a gigantic US$32bn (using quarterly average exchange rates). Pemex has now lost money for 13 consecutive quarters; in 2015 crude oil output was also down for the 11th consecutive year. Jose Antonio González Anaya, the newly appointed director general, on 8 March told representatives in the Chamber of Deputies that spending cuts of MXN100bn (US$5.6bn) would be made in various areas. Pemex mangers would cut costs and improve efficiencies, including reducing travel and other non-essential expenditure, and restructuring the company's E&P (exploration and production) division: this would make savings of MXN29bn (US$1.6bn). Another important area was a postponement and rescheduling of the capital expenditure programme, including exploration, and designed to save MXN65bn (US$3.6bn). González Anaya told members of the lower house energy commission that "Pemex is facing a liquidity problem, not a solvency problem, and through these adjustments what we are seeking to do is reposition and reshape Pemex as a state-owned productive enterprise, within a new legal and financial framework created by the energy reforms approved by Congress."

REGION

Colombia and Uruguay lead energy transition

World energy markets are going through a major upheaval. The volatility of hydrocarbons prices, coupled with concern over the environmental impact of burning fossil fuels, is highlighting the need for countries to deliver secure, affordable, and sustainable energy. It seems that in the race to do that, some big economies (the US, Japan, Germany) are lagging behind. According to a report by the World Economic Forum (WEF), some smaller ones (Norway, Switzerland) are ahead. Latin America has two star performers in the 'top ten' ranking: Colombia and Uruguay.

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In March, the World Economic Forum (WEF), in partnership with consultancy Accenture, published *The Global Energy Architecture Performance Index Report 2016*, which ranks a total of 126 countries in terms of their ability to deliver "secure, affordable, and sustainable energy". It does so by applying the concept of an "energy triangle". This consists of a given country's ability to deliver first, economic growth and development; second, environmental sustainability; and third, energy security and access. The 2016 report notes that the world's largest economies are not doing particularly well "as their transitions take longer to unfold due to the complexity of their energy systems".

With the exception of France (4th) none of the world's 12th largest economies are in the top ten of the ranking. Germany is ranked 24th; the report notes that despite building impressive capacity in renewables, its energy transmission has been marked by sharp increases in electricity prices. The US is ranked 48th, scoring high on energy security and access, thanks to increasing use of gas instead of coal for power generation. Japan is ranked 50th, still suffering the effects of the Fukushima nuclear accident, which left an aftermath of high-cost energy imports and increased carbon emissions.

The top performers include Switzerland (1st) and Norway (2nd). The report says both are "demonstrating a well-balanced energy system within the 'energy triangle'".

One of the main headlines is that two Latin American countries have entered the top-10: Colombia (8th) and Uruguay (10th), which have become the only two non-OECD countries at the top of the list. Both are singled out for having approved energy reforms and for strengthening energy's contribution to growth and development. Although Colombia has been suffering short-term electricity generation problems due to a current drought, the report notes the country could reach a six-fold increase in its current hydropower capacity.

Uruguay is commended for increasing the share of renewable energy in the mix. Fuel imports as a proportion of GDP have fallen from 9.1% in 2008 to 3.0% in 2014. The share of alternative and nuclear energy use in Uruguay has also increased from 34% in 2008 to 47% in 2013. Uruguay's wind power capacity is expected to reach 1,400MW in 2017, leading the WEF to describe it as the "green power leader in South America".

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Paraguay (21st in the ranking) is also singled out for achieving fully decarbonised electricity generation, which gave it above-average environmental sustainability scores. Brazil (25th) is the top performer among the BRIC nations. The WEF says that Brazil "benefits from a diversified energy mix with a considerable share of low-carbon energy, and a growing domestic oil and gas sector providing revenues and reducing the need for energy imports". On the downside, Brazil's energy mix has recently become less diverse, with the share of alternative and nuclear energy use falling by 6% over the last seven years. The report also noted that the slump in oil prices is forcing or accelerating fiscal and subsidy reforms in countries like Mexico (49th), which have been over-reliant on oil revenues. Mexico is gradually phasing out its petrol subsidy. Average fuel consumption by cars in Mexico has decreased by 8% since 2008.

The report recognises that countries face a challenging energy outlook. Roberto Bocca, head of energy industries for the WEF, noted that "Changes in energy prices and production, a slowdown in the growth of emerging economies and geopolitical instability have effectively reshuffled energy demand and supply scenarios", requiring greater collaboration between stakeholders. The report also highlights the need for a new electric utility business model, capable of managing diverse energy sources and maximising reliable supply. Other important developments include the emergence of intelligent power grids (requiring greater protection against cyber-attack) and an increased emphasis on energy security.

MINING

Maduro government on a major push to resurrect mining

Venezuela's socialist government has hit on a new key sector – mining.

On 29 February Venezuela's planning minister, Ricardo Menéndez, held a meeting in Beijing with the president and the vice-president of China's National Development and Reform Commission, Xu Shaoshi and Ning Jizhe, respectively, to discuss the prospect of Chinese cooperation in various economic sectors as part of the Caracas government's plans to revitalise domestic productive economic activity.

In an official statement, Menéndez said that he had discussed Chinese participation in sectors including pharmaceutical, industrial, petrochemical, hydrocarbons and mining. Menéndez said that attracting Chinese investment was part of the "government's strategy for the country's economic reconstruction". He celebrated that China planned to "invest in the development of these sectors in Venezuela, which is highly important to consolidating the union between our countries, along with China's direct participation in things like the Arco Minero and the Orinoco belt". Venezuela later hosted a forum, on 2 March, under the banner of 'The 14 engines of Productive Economy', in which investment opportunities were presented to over 50 Chinese companies.

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The Orinoco belt is the 55,314km2 area in northern Venezuela under which much of the country's oil reserves – the world's largest after Saudi Arabia – are located and where Chinese oil firms have a growing presence. The 'Arco Minero' ('mining arch'), meanwhile, is an 111,000km2 area in central Venezuela that goes from the country's border with Guyana in the east to its border with Colombia in the west. The Venezuelan government has long held that this region contains high quantities of gold, coltan, diamonds, bauxite, iron ore and other minerals, all of which the government is once again looking to exploit as part of an urgent bid to find new sources of growth (and foreign exchange earnings) after the country's GDP contracted by 5.7% in 2015 on the back of the fall in international oil prices (*see box below*). The fact that mining prices too have come off their previous record highs does not seen to be an issue for the now severely cash-strapped Maduro administration, albeit it could be a disincentive for Chinese or other companies looking to invest large sums in Venezuela's already-fragile and highly unpredictable domestic economic environment.

To this end, the Maduro administration recently signed a US$5bn settlement deal with the Canadian-US company, Gold Reserve Corporation, to end a seven-year expropriation dispute. As part of the deal, Gold Reserve will invest/loan US$2bn to revive and develop the Brisas mine (in Bolívar state) at the centre of the dispute, as well as the adjacent Cristinas gold-copper project, recovering a 40%-45% share in the overall project, with 55% to be held by the Venezuelan government. According to a 29 February company press release, once developed, the combined Brisas-Cristinas Project "is anticipated to be the largest gold mine in South America and one of the largest in the world".

Camimpeg

There is also much speculation as to the purpose of a new state company that appears to increase the Venezuelan military's involvement in both the oil and mining sectors. The 10 February daily *gazette* announced details of a new military company, Cia Anónima Militar de Industrías Mineras, Petrolíferas y de Gas (Camimpeg), authorised to take part in a variety of oil services and mining activities.

Camimpeg will report to the defence ministry, which will appoint the company's board and president. Eulogio Del Pino, who doubles as Venezuela's energy minister and president of the state oil company Petróleos de Venezuela (Pdvsa), said that Camimpeg would provide Pdvsa with various oil services, including the maintenance of wells and drilling rigs, transport and the commercialisation of chemicals and, apparently, provide support for security. "It will help Pdvsa in all the necessary areas. For instance in border areas, we're going to increase our security, in operational issues where our soldiers are perfectly prepared," he was quoted as saying by newswire *Reuters*.

However, commentators put forward various other theories. Aside from the continuing complaints about the creeping militarisation of the Venezuelan government under President Maduro, these include a suggestion that the new company could be used as a vehicle to shield Pdvsa assets from being seized in the event of a debt default. Russ Dallen, of a Miami-based consultancy, Latinvest, made the point to *Bloomberg* that "the state can take away the rights to the oil, gas and resources of Pdvsa at any time, leaving it largely worthless to creditors and protecting Venezuela's ongoing cash generation from oil sales from Pdvsa creditors." He added that the new company "could also help the government maintain operations if unpaid bills to joint-venture partners and oil service providers start to impact output". And, in another scenario, "it could also be used as a bargaining chip in any deal with China".

Others suggested that the new company is simply part of the government efforts to resurrect a mining sector in the country. Del Pino revealed in late January that Venezuela was moving to certify its precious metal resources and was interested in producing diamonds. A subsequent Pdvsa press release noted that Del Pino and the central bank president, Nelson Merentes, had met with Ahmed Bin Sulayem, chairman of the Kimberley Process, an organisation that monitors the sale of conflict diamonds, as part of its certification efforts.

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Tumeremo massacre underlines operating risks in remote mining belt

In the midst of these efforts by the Maduro government to open up the mining sector, some two dozen informal miners in Bolívar state, which lies at the centre of the Arco Minero, were murdered and abducted in early March, with relatives accusing local security forces of involvement.

Relatives reported that an armed gang attacked the informal miners on 4 March in a bid to take control of the Atenas gold mine, located near the town of Tumeremo. They claimed that 28 miners had been captured. Initially, some local reports suggested that the victims had been killed and the bodies violently dismembered by a gang using chainsaws. Controversially, some of the relatives suggested the complicity of local military forces, arguing that corrupt local officers were seeking spoils from the mine. The long-serving governor of Bolívar state, Francisco Rangel, of the ruling Partido Socialista Unido de Venezuela (PSUV), initially denied that anything was amiss, and on *Twitter* accused the political opposition of making things up for political gain. The allegations of the families were "absolutely false", he insisted. He was later obliged to backtrack.

The incident quickly prompted comparisons with Mexico's infamous Iguala case, in which protesting students were kidnapped by a gang in cahoots with the local security forces. Moreover, local critics have alleged that this is not the first such incident to take place under Rangel's watch in Bolívar (he has been governor since 2004). As the news made local and international headlines, the government scrambled the air force in search of the victims, with Defence Minister Vladimir Padrino López pledging that it would not rest until the victims were located.

The attorney general, Luisa Ortega Díaz, two weeks later confirmed that authorities had found the remains of 17 people in a common grave. Several of the corpses, which included two females, were identified as some of the missing. Officials said the people found in the common grave had been shot to death.

Ortega said the grave had been found in Nuevo Callao, "deep in the jungle" near the border with Guyana. She said authorities believed that 21 and not 28 miners had been taken, albeit the families of the missing continue to insist otherwise. Ortega announced an arrest warrant for the leader of a local criminal gang identified as Jamilton Andrés 'El Topo' Ulloa Suárez, reportedly an Ecuadorean native, and said that authorities had already arrested one of his close accomplices, Rosa Saida Gil Salazar.

The Venezuelan opposition has called Rangel's resignation over the case.

“Inevitably, the country posted a huge current account deficit of US$18.2bn, on preliminary figures, as oil exports (96% of the export basket) collapsed. More notably, imports fell by almost 19% last year, which explains the goods shortages in the heavily import-dependent country. Meanwhile, the government spent US$10.9bn last year on external debt servicing, the bank data revealed.”

A grim picture

On 18 February, the central bank (BCV) released economic data to end 2015. According to the bank, the country registered an overall real annual GDP contraction of 5.7% in 2015 (following a contraction of 3.9% in 2014), with inflation of 181%.

The GDP figures are grim. Domestic demand contracted by 10.1% year-on-year, led by fixed investment (-17.6%), private consumption (-7.8%) and even government consumption (-2.4%). Import demand fell by 18.7%.

Local private economists immediately challenged the inflation figures in particular, suggesting that they were underestimated.

Even the Spanish telecoms giant Movistar was moved to comment, issuing a statement complaining that fixed-price services were out of sync with the reality of inflation in the country, adding that this made investment in Venezuela “unviable”. “An average monthly Movistar plan costs 476 bolivars. Much less than a kilo of ham,” it noted dryly.

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Meanwhile the opposition Mesa de la Unidad Democrática (MUD) has reacted angrily to President Maduro’s latest devaluation-led economic adjustment package. Noting that the measures (including devaluation and the first rise in local gasoline prices in almost two decades) would do nothing to resolve the structural economic problems on the ground, the moderate Henrique Capriles Radonski accused Maduro “of putting his hand in people’s pockets”. Under the new dual exchange rate system, which took effect as of 10 March, a new Divisa Protegida (Dipro), fixed at BF10/US$1, will be used for all essential imports, including food and medicines. A second Divisa Complementaria (Dicom) will float, starting at BF206/US$1, and thereafter should be determined by the market, according to Miguel Pérez Abad, the new economic policy czar.

Crucially, Pdvsa will be able to sell dollars at the Dicom rate, which will help boost its parlous financial position, and perhaps settle the nerves of investors wondering about a potential Pdvsa ‘credit event’ in the fourth quarter. Addressing this fear, Abad stressed that Venezuela did not have a solvency problem but a cash-flow problem.

In the absence of official data, private sector economists put the fiscal deficit at upwards of 25% of GDP. While devaluation will help that position, the politically-sensitive rise in fuel prices on the position of Pdvsa may ultimately be negligible, as according to President Maduro the revenues from the fuel price increase are to be put into yet another new off-budget fund controlled directly (and unaccountably) by the executive – the Fondo Nacional de Misiones (the national missions fund).

Reaction to the new FX system has been muted to date, as the sharp difference between the upper and lower rates, and the continued dollar scarcity, means continued distortions. The illegal black market rate was still trading at over BF1,200/US$1 on 21 March.

Like Venezuela, Ecuador is also struggling

On 25 February Ecuador’s President Rafael Correa said that the government had reduced its 2016 budget oil price assumption to US$25 per barrel (/b), a US$10 cut on the original price.

With Ecuadorean crude oil prices hovering just north of US$30/b, an adjustment by the left-wing Correa government to its US$29.8bn 2016 ‘austerity budget’, built on an oil-price forecast of US$35/b, was inevitable. While Ecuador is only a small producer, its oil earnings typically have accounted for over 50% of export earnings, 30% of fiscal revenues, and 15% of GDP. As such, after Venezuela it is the most badly affected country in Latin America by the oil-price shock.

President Correa admitted that the loss in oil revenues last year cost the country

"With still no sign of a global agreement on an oil production freeze, Ecuador's level of international reserves is something to be watched, as a key indicator of its liquidity position. According to the BCE, international reserves stood at just U$2.8bn on 18 March."

about 7% of GDP (so in excess of US$7bn). And with the domestic economy stagnant, the treasury's US$15.5bn in tax revenue projections for 2016 looked over-optimistic from the outset. In January alone, on preliminary figures, tax revenues fell by 20% year-on-year, while oil income was down 12% year-on-year. Ecuador's position as an (increasingly uncompetitive) dollarised country doesn't help matters, making its liquidity crisis all the more acute.

The US$10 cut oil-price forecast could translate into a 15% cut in the budget, private economists suggest. Patricio Rivera, the coordinating minister for economic policy, stressed that a bigger effort needed to be made "to look for margins of priority". He emphasised an aim to ring-fence public sector jobs. The rate of urban unemployment was reported at 5.65% in December 2015 but this masks a rise in underemployment and part-time employment, which has prompted new labour reform efforts by the government, to effectively relax temporarily the country's strict labour laws in an effort to help companies keep people in work.

Correa said the cuts would be "surgical", and would not affect the general population. This throws the onus of any adjustment onto capital expenditure, potentially including planned investments by the state-owned oil company, Petroamazonas, or even the divestment/privatisation of state assets. The government has already reworked legal frameworks to try to attract more private sector investment into the oil sector, as well as into the nascent mining sector; additional efforts to build bridges with private investors may be forthcoming.

The central bank (BCE) has now cut its real annual GDP growth forecast for 2016 to just 0.4%, from 1% previously, albeit the BCE president, Diego Martínez, was at pains to stress that this still constituted positive growth. Ecuador registered a similar result in 2015.

With still no sign of a global agreement on an oil production freeze, Ecuador's level of international reserves is something to be watched, as a key indicator of its liquidity position. According to the BCE, international reserves stood at just U$2.8bn on 18 March.

Taxation for Inclusive Growth

The Executive Secretary of the United Nations (UN) Economic Commission for Latin America and the Caribbean (ECLAC), Alicia Bárcena, and the Executive Director of Oxfam International, Winnie Byanyima, in February presented a new report on the high levels of inequality in Latin America, entitled '*Time to Tax for Inclusive Growth*'. Despite a 10% decrease in inequality between 2003 and 2013 in the subcontinent, from 54.2 to 48.6 on the Gini Index (0 representing perfect equality and 100 perfect inequality), the report highlighted that it is the "most unequal region in the world"; the wealthiest 10% of the population own a substantial 71% the wealth.

Bárcena and Byanyima stressed the urgent need for reform of "poorly designed tax systems" and the prevention of tax avoidance and evasion, which costs Latin America "billions of dollars" that should be invested in confronting inequalities in the distribution of the region's economic growth. Tax evasion cost Latin America US$190bn in 2014 alone.

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