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ECLAC lowers regional growth forecast

The UN's Economic Commission for Latin America and the Caribbean (ECLAC) has lowered its GDP growth forecast for the region this year to just 1.1%.

The latest revision is down from the 1.3% the Commission had projected in December 2016. The growth story will vary from country to country, ECLAC notes. The South American economies, geared to primary exports such as oil, minerals and agricultural commodities, will grow below the average, at just 0.6%, down from the 0.9% expected last December. This modest projection still incorporates a rise in demand and prices for the sub region's key export commodities, but it is still also affected by the very slow recovery in Brazil (where growth of 0.4% is now expected this year) and the continuing domestic chaos in Venezuela, where ECLAC now expects the economy to shrink by 7.4% in real terms (down from its previous figure of -4.7%).

By contrast, the Central American economies will expand by 3.6% in 2017 (only marginally down on the 3.7% projected in December). The region will be helped by good growth in the US, its main trading partner, and by resilient domestic demand. ECLAC also foresees modest growth of 1.9% in Mexico, where the effects of trade and immigration disputes with the new US administration led by President Donald Trump continue to generate a degree of uncertainty. Finally, the English and Dutch-speaking Caribbean will sit between the two other sub-regional groups in growth terms, with real average GDP forecast at 1.4%, slightly up on the 1.3% forecast in December.

ECLAC's executive secretary, Alicia Bárcena, has been repeating her mantra that the region could achieve a better economic performance if it pursued economic integration opportunities more pro-actively. Early in April, she noted that intra-regional trade had fallen from 19% of its total trade three or four years ago, to only 16% per now, a trend she attributed to growing Chinese exports to the region. Bárcena warned that falling foreign investment and uncertainty over trade was eroding confidence. Potential adverse changes in US trade policy is particularly worrying, because around 40% of regional exports go to the US, she noted. For Mexico and Central America, the proportion rises to a full 80%.

ECLAC has also long called for increased investment in infrastructure and for a range of measures to boost productivity, employment, innovation and environmental sustainability.

Country / Region	ECLAC GDP % forecast
Latin America and the Caribbean	**1.1**
Argentina	2.0
Bolivia	4.0
Brazil	0.4
Chile	1.5
Colombia	2.4
Ecuador	0.6
Paraguay	3.8
Peru	3.5
Uruguay	2.0
Venezuela	-7.2
South America	**0.6**
Costa Rica	4.1
Cuba	1.0
El Salvador	2.5
Guatemala	3.4
Haiti	1.0
Honduras	3.7
Mexico	1.9
Nicaragua	4.6
Panama	5.2
Dominican Republic	5.3
Central America & Mexico	**2.3**
Central America	**3.6**
Latin America	**1.1**
Antigua & Barbuda	3.0
Bahamas	1.0
Barbados	1.9
Belize	3.7
Dominica	3.2
Grenada	2.4
Guyana	3.8
Jamaica	1.6
Saint Kitts & Nevis	3.4
St Vincent & The Grenadines	2.3
Saint Lucia	2.2
Suriname	0.8
Trinidad & Tobago	0.5
Caribbean	**1.4**
Note: *Central America includes the Spanish-speaking Caribbean*	
Source: *ECLAC, April 2017.*	

IMF a little more downbeat

Publication of the revised ECLAC economic forecasts coincided with the release of the IMF's latest (Spring 2017) World Economic Outlook (WEO). In the last report, released in October 2016, the IMF forecast global growth of 3.4% in 2017, with growth of 1.6% for Latin America and the Caribbean (LAC).

However, in its latest WEO the IMF edged up its global growth forecast to 3.5% while cutting its LAC forecast by half a percentage point to 1.1%. This reduction can be traced mainly to worse-than-expected performances in Venezuela and Mexico. The IMF is also more pessimistic than ECLAC about Brazil's performance this year (expecting growth of only 0.2%), albeit it is more upbeat about the performance of Latin America's largest economy in 2018 (expecting real GDP growth to rebound to 1.7% next year).

At a press conference, Oya Celasun, chief of the IMF economic studies division, said that the ongoing investigations into corruption in Brazil were a factor contributing to political uncertainty, but noted that the government led by President Michel Temer was pushing forward with its reform programme. Success in pension and other reforms "should set the stage for returning fiscal finances to a much healthier setting and also putting a strong foundation for return to stronger growth" Celasun said.

REGIONAL ECONOMY REVIEW

MEXICO

NAFTA prospects still uncertain

NAFTA is definitely off. No, NAFTA is most probably on. Actually, and most likely, NAFTA will be renegotiated, but the timetable is far from clear. In fact, within the last month different officials have expressed almost all these positions on the future of the North American Free Trade Agreement (NAFTA). The balance of probabilities does indeed now point to renegotiation, but the path ahead is still lengthy and highly uncertain.

The latest US flip-flop on NAFTA happened over a few days leading up to 27 April. On that day, President Donald Trump told the *Reuters* news agency that he had been "psyched" to terminate the free trade agreement with Canada and Mexico – particularly on hearing about problems in US-Canada dairy trade – but had then been persuaded by subsequent telephone calls with Prime Minister Justin Trudeau of Canada and President Enrique Peña Nieto of Mexico to opt instead for renegotiation. "I'm not looking to hurt Canada and I'm not looking to hurt Mexico. They are two countries I really like" Trump was quoted as saying, adding, "So they asked to renegotiate, and I said yes". Asked what the aims of renegotiation might be from Washington's point of view, Trump gave an answer apparently at variance with the protectionist rhetoric that had dominated most of his speeches during last year's election campaign, stating: "Open markets. Open borders for trade…Fairness, no government subsidies so that it makes it impossible for our people to compete".

The mechanics of any renegotiation in the US requires the office of the US Trade Representative (USTR) to send a formal notice to Congress triggering a 90-day domestic consultation period before talks can begin. This is unlikely to happen until the Senate confirms Trump's proposed appointment for

head of USTR, Robert Lighthizer (the upper house was due to consider the nomination in mid-May). Analysts suggests that formal talks will not start until August, at the earliest. Moreover, it is possible that they could start later, and stretch out longer, thereby coming into collision with the political calendars of the three member countries. Ideally, Mexico would like any renegotiation wrapped up before the end of this year, since its presidential election race will ramp up from early 2018 (ahead of polls in July). It is hard to see such a quick renegotiation happening. US mid-term congressional elections, on the other hand, are also due later in November 2018, while Canada goes to elections in October 2019.

Both Canada and Mexico have been trying to frame any upcoming NAFTA renegotiation in a way that would enable favourable outcomes for their national interests. In the last few weeks, Canada has seen an intensification of trade disputes with the US in soft lumber, dairy products, and aerospace. Trudeau said he had told Trump that ending NAFTA would cause "a lot of short-term and medium-term pain." As a result of that conversation, he reported, "we agreed we could sit down and get to work on looking at ways to improve NAFTA".

In turn, Mexico's economy minister, Idelfonso Guajardo, floated the idea that the three governments could re-use some of the work already done during the negotiations for the 12-country Trans Pacific Partnership (TPP) agreement, from which the Trump administration withdrew right at the beginning of this year, effectively scuppering the TPP. His argument was that the TPP texts incorporate a more modern and up to date approach across several areas, such as e-commerce and intellectual property, which could be used to modernise the 23-year old NAFTA text. Mexico and the US should see themselves not as economic rivals, Guajardo argued, but as partners who need to work together to compete with low-cost Chinese manufacturers, and need to adapt to the changes posed by new trends such as the digital economy and robotisation. "We are fed up with complaints that Mexico is stealing jobs from US manufacturing. We are part of the solution that has maintained competitiveness for the US versus China" Guajardo said.

Signs of economic resilience

There have been further indications that Mexico's economy is showing resilience. Over 80% of Mexico's exports are shipped to the US so it is highly dependent on the relationship with its northern neighbour. Fears that uncertainty over NAFTA and wider problems in the relationship with the US would rapidly tip the country into recession appear nevertheless to have been premature.

Admittedly, there is a lot to worry about, and both the economy ministry and the Mexican central bank (Banxico) have been cutting their forecasts for this year's real GDP growth, now down in both cases to a conservative 1.3%-2.3% range. Yet private banks such as Santander, JP Morgan, BBVA and Citibanamex have been edging their growth predictions upwards. A factor in this has been the better-than-expected Q1 GDP results.

The authorities released first-quarter GDP data in late April, revealing that the economy grew by 0.6% on a seasonally-adjusted basis from the fourth quarter of 2016. On a year-on-year basis, GDP growth stood at 2.5%. The results defied prior expectations and reinforced the perception that, for the moment at least, the election of Donald Trump in the US has not had a particularly negative impact on economic performance in Mexico.

GDP growth during the first quarter was driven by primary sector activity (mainly agriculture) and by the services sector. Primary activity rose by 0.7% from the fourth quarter of 2016, while services registered growth of 1%, with both results marking an acceleration from the pace of growth recorded the previous quarter. On a year-on-year basis, primary activity was up by a stellar 6.5%, compared to 3.8% for services activity. By contrast, secondary activity (which includes manufacturing, mining, construction and utilities) stagnated for a third consecutive quarter. On a year-on-year basis, secondary activity was down by 1.3%.

Although some observers have pointed to the weak result for secondary activity as evidence of negative follow-through from the US election, the reality is that falling mining output and disappointing results for construction and utilities are the main reason that secondary output is stagnating.

Although the detailed sub-sector breakdown has not yet been published, the monthly industrial production index results substantiate this, with mining output falling by around 10% year on year in January and February. Utilities also contracted during the same period, with construction faring slightly better but only just in positive territory.

The other component of the industrial production index (and of secondary sector activity) is manufacturing, which is dominated by US exports and therefore highly vulnerable to developments in the US. This component of the industrial production index rose by an average 3.6% during January and February, marking an acceleration from rates of 1-2% during the second half of last year. It is now possible that official projections for GDP growth, which have been edging downwards, might actually reverse and be upwardly revised.

Inflation remains the weak spot

The main area of concern for the Mexican authorities remains the level of inflation. After remaining at 2-3% for most of 2016, inflation soared in early 2017, with the latest monthly data showing a rate of 5.4% in March. Inflation rose further in the first half of April, to 5.6% year on year.

Inflation continues to be driven by the impact of currency depreciation in 2016, particularly in November and December, when the peso plunged from Ps19:US$1 to Ps22:US$1. Importers have been significantly affected, with producer price inflation rising by an average of 11.5% year on year in the first quarter of 2017, with retailers subsequently passing on much of the increase to consumers.

Although the Mexican monetary authorities have been quick to respond by raising interest rates, most recently to 6.5% at the end of March, they have been hoping that the re-appreciation of the Mexican peso since mid-January would help reduce levels of inflation. Yet these hopes may be dashed by a partial reversal of these currency trends, with the peso weakening once again since mid-April, from a level of Ps18.5:US$1 to over Ps19:US$1 in early May.

The governor of the Banco de México (Banxico, the central bank) has recently indicated that monetary tightening may in fact continue, despite the previous widely-held belief that the current tightening cycle may have reached its peak (or be close to doing so).

The fact that GDP growth appears firmer than initially-feared may give the Mexican authorities some room for manoeuvre, since it had been feared that in the context of extremely weak domestic demand, further interest-rate hikes would choke off demand, potentially even pushing the economy into recession.

Demand-side GDP data for the first quarter of 2017 will not be published until later in May, but if the data show that private consumption was firm, at least one more interest rate hike is likely to be on the cards. Banxico's monetary policy committee are next meeting in mid-May, with their decision on interest rates announced on 18 May.

On the basis of the first quarter results, Pedro Balcão, Santander's head of Mexico research and strategy, is the most optimistic, predicting overall real GDP growth of 2.2% this year and proclaiming that, on the strength of President Trump's switch to favour renegotiations, "NAFTA is no longer a risk". Carlos Serrano, chief economist at BBVA Bancomer, has increased his 2017 growth forecast to 1.6% (up from 1.0% previously). And finally, JP Morgan now is predicting growth of 2.0%, up from 1.3% previously.

There are indeed a number of reasons for (relative) optimism. Whatever the outcome, the renegotiation of NAFTA looks like being a long-haul process, so the direct impact on trade for this year, at least, will be relatively small. As the London-based consultancy Capital Economics notes: "All in all, despite the plunge in a number of business and confidence surveys in the early months of this year, the economy is continuing to grow at a decent pace."

Meanwhile, exports have been doing well also. Helped by a weak peso for much of last year, exports rose by 14.1% in the 12 months to March 2017. Remittances sent home by expatriate Mexican workers have also remained buoyant – in March, they were up by 15.1% year-on-year to US$2.12bn (in 2016, remittances hit an all-time record of US$26.97bn, up 9% on 2015).

Much may yet happen to influence business and investor sentiment, of course. In sharp contrast to Balcão's view, Valeria Moy, head of the Mexican think tank ¿Cómo Vamos? recently stressed, "Of course it is too early to eliminate the NAFTA risk. There is no way that I would do that."

Sugar dispute rumbles on

The dispute over Mexican sugar exports to the US shows no sign of early resolution. Under the terms of an agreement reached in 2014, the US set new prices and quotas for imports of Mexican sugar. The deal was seen as broadly favourable to Mexico, giving it around one-third of the total US import market of 12m tons.

But starting last year, US sugar producers and refiners began demanding that the Commerce Department renegotiate the deal in their favour. So far, talks on a new agreement have failed to prosper. The US said it would re-impose anti-dumping and anti-subsidies duties on Mexican sugar effective from 1 May, but later postponed that deadline to 5 June to allow for more time to reach a solution. However, the new US Commerce Secretary, Wilbur Ross, has stated that talks are "at an impasse". "While I regret that such measures were needed, it is my hope that Mexico and the US can reach a fair agreement before June", Ross added.

For its part, the Mexican economy ministry has blamed the deadlock on "excessive demands" by US sugar producers and refiners, complaining that they were seeking to eliminate "all competition" from Mexican sugar. There were also reports that Mexican sugar producers might demand a dumping investigation into imports of US high-fructose corn syrup as a retaliatory measure, seeking to use a WTO ruling announced in April in favour of Mexican tuna exporters as a precedent. That WTO arbitration decision authorised Mexico to impose US$163.2m in annual trade sanctions against the US in a dispute over tuna fish labelling; the US was deemed to have

sought an unfair trade advantage using 'dolphin friendly' labelling rules. Juan Cortina, president of the Mexican sugar and alcohol industry association, said it would be asking the government to start a dumping investigation against fructose.

ARGENTINA

More than lemons

President Mauricio Macri met his US opposite, Donald Trump, at the White House on 27 April. The meeting had one immediate positive result for the Argentine economy: the lifting of a 16-year old ban on imports of Argentine lemons into the US. The Buenos Aires government hopes for additional benefits in the near term.

President Trump often comes across as a mercantilist – someone who judges the value of bilateral relations purely on the basis of whether the US has a surplus or a deficit in trade with partner countries. That explains Trump's hostility to Mexico. The US has an annual deficit in its trade with Mexico of around US$60bn, and in March the deficit hit US$7.03bn, 30% more than a year previously and the highest level since October 2007.

By the same criteria, this might put Argentina into Trump's 'good books'. In 2016, the US posted a US$2.5bn trade surplus with Argentina, on exports of US$6.98bn and imports of US$4.48bn. From Macri's point of view, the aim of his White House visit was to expand that trading relationship, and perhaps nudge towards more of a balanced exchange.

In the 15 years before his government came to power (in December 2015), Argentina was partially cut off from global markets, not only because of its quarrels with creditors, but also because of the protectionist trade policies implemented by the left-wing *Kirchnerista* administrations of Nestor Kirchner (2003-2007) and his wife and presidential successor, Cristina Fernández (2007-2015). Rebuilding bridges with the US, the country's third largest trade partner (behind Brazil and China), is therefore an important objective for Macri. The US is also the largest single investor in Argentina, holding assets with a book value of around US$27bn. Most critically, Macri's strategy to lift Argentina's economic growth rate depends on boosting trade and inward investment.

Lemon exports may be a small but significant place to start. Argentina is the world's top lemon producer, and the US is one of the top consumers. The US banned imports of Argentine lemons back in in 2001 on health grounds, maintaining that Argentina's controls on pests and crop diseases were insufficient. At the tail end of the Barrack Obama administration (2009-2017), the Department of Commerce finally agreed to lift the ban, but the measure was placed on hold when Trump took office in January. Trump, however, announced a formal lifting of the ban shortly ahead of Macri's visit.

It will become effective as of 26 May. Initially, Argentine lemon imports will be allowed only into the north-eastern US, affording a degree of protection to Californian lemon growers, who have opposed the move, citing fears of lower prices. In Argentina, the agri-industry minister, Ricardo Buryaile, welcomed the news as very positive for the regional economy in the north-east of the country. Argentina's total lemon exports last year (excluding the US) were worth US$467m. Sales of lemon juice to the US, which was not affected by the ban, totalled US$61m.

Beyond lemons, the Macri government wants to see increased trade and investment with the US across the board, in addition to US support for the country taking a higher profile in global economic affairs. Buenos Aires is also seeking the removal of restrictions on its bio-diesel exports to the US. A joint statement issued after the Macri-Trump meeting said that the US president had "welcomed Argentina's growing leadership role on the world stage", particularly in relation to trade and investment. Argentina will host a World Trade Organisation (WTO) ministerial conference in December; it will also hold the G20 presidency in 2018. Argentina is also taking initial steps to seek membership of the Organisation of Economic Cooperation and Development (OECD) – Macri said Trump had agreed to support eventual Argentine membership.

Argentina to benefit from Mexico pivot?

Mexico has begun preparing itself for possible problems in its trading relationship with the US and one of its defensive strategies could be very beneficial for Argentina.

The Mexican deputy trade minister, Juan Carlos Baker, visited Buenos Aires in April and said that the two countries could sign a partial trade deal before the end of the year. Baker said that Mexico was looking to diversify its imports of grains and foodstuffs. It imports close to US$4bn a year of maize and soya from the US, he noted, but would consider buying some of that from Argentina instead. Argentine farm exporters could find "attractive conditions" in Mexico, he said.

At the same time, Baker also suggested that Mexican manufactured exports could be of interest to Argentina. According to the Argentine daily *La Nación*, any arrangement would probably fall short of a full trade deal because Argentina's existing commitments require it to negotiate formal trade deals not as part of the regional trade group, the Southern Common Market (Mercosur, also comprising Brazil, Paraguay and Uruguay).

Baker suggested that an "economic complementation agreement" might be the best way to proceed, along the lines of the three-way automotive agreement currently in force between Mexico, Argentina and Brazil. Baker commented, "It would be almost as ambitious as a free trade agreement. Mexico, Argentina, and Brazil are the three largest economies in Latin America. Trade between Mexico and Argentina is minimal – just US$2.3bn – and Mexico has a surplus."

BRAZIL

Temer continues push for reform

In April, the administration led by President Michel Temer continued with its push to get an array of economic reforms approved in the federal congress. Despite some progress, resistance is rising and the critical battle for pension reform – due to be put to a vote in May – has been getting harder.

The Temer administration has chosen to make a stand on four areas: fiscal reform, tax reform, labour reform and pension reform. Its reasoning is that action to control the fiscal deficit and reduce private sector operating costs will boost business sentiment and stimulate Brazil's still-tentative economic recovery. So far, the path to reform has been both helped and hindered by a rather unique political situation: while weakened by allegations of corruption, the Temer administration has continued to be able to count upon a large centre-right majority in the ever-unwieldly federal congress. By contrast, in Brazil at large, the reform programme is unpopular and widely resisted.

The first major step in the reform campaign came in December 2016, when a constitutional amendment was approved placing a 20-year cap on public spending. Annual expenditure growth is now limited to the previous year's rate of inflation.

In March, the government also began a phased reform of the tax system, beginning with an effort to simplify and streamline the notoriously complex PIS/Cofins payroll taxes. The taxes – formally the Programa de Integração Social (PIS) and the Contribuição Social para o Financiamento da Seguridade Social (Cofins) – account for about 20% of federal revenues. In late March, a new law (approved with a 231-188 vote in the lower chamber of deputies) gave Brazilian companies much wider scope to outsource jobs through contractors. The thinking is that this process, known as *tercerização*, will make it easier to take on or lay off temporary workers, supporting greater flexibility and encouraging companies to hire staff more quickly during the up-turns in the business cycle. However, the labour union movement and the leftist political opposition regard tercerização with great suspicion, seeing it as a device to reduce wages and erode employment security.

In late April, the chamber of deputies approved a package of labour reforms in a 296-177 vote. For the first time, this reform makes major changes to a compendium of labour laws formalised in the 1940s (during the height of *trabalhismo*, the labour-based political movement) and known as the Consolidação das Leis do Trabalho (CLT). Importantly, the changes to the CLT have now abolished mandatory payment of trade union dues. They also allow work shifts of up to 12 hours (instead of eight); the reduction of lunch breaks to half an hour (instead of one hour); and will permit collective labour agreements to override national labour code provisions in certain circumstances. Again, the rationale is to give employers greater flexibility, but critics see it as an attack on historic social conquests.

The main battle, however, is pension reform. Brazil has traditionally had a generous state pension system that allows early retirement and is expensive to run. There is no obligatory minimum retirement age. Many Brazilian workers are able to retire in their early fifties, and some professional groups, particularly civil servants, enjoy extremely generous pension privileges.

Military pensions are notoriously high, and in some cases army pensions can be "inherited" – i.e. passed on to the next generation. The International Monetary Fund (IMF) calculates Brazil's total pension costs at 11.3% of GDP, compared to an average of 7.8% in the Organisation for Economic Cooperation and Development (OECD). Brazil's average retirement age is 57.5, compared to just over 64 in the OECD. As the Brazilian population begins to age, and the ratio of pensioners-to-workers increases, unfunded pension liabilities will grow exponentially. The IMF calculates that without reform, Brazil's pension costs will surge to 18% of GDP in 2021, rising to 26% by 2050.

The Temer administration's attempt to head off this unsustainable rise in costs is known as constitutional amendment 287 (PEC287). In its original form, the draft PEC 287 established a single retirement age of 65 for both sexes, and required workers to make pension contributions for a minimum of 25 years to qualify for a full pension, based on a proportion of the final-salary. These proposals have proven deeply unpopular. The labour movement, through the Central Única dos Trabalhadores (CUT), held Brazil's first general strike in just over 20 years on 28 April, mainly in protest at the pension changes.

According to a survey published by the daily *Follha de São Paulo* in early May, 71% of people oppose the pension reform, 64% think the labour reform will only benefit employers, and opinions are divided over the benefits of *tercerização* (34% think it will boost employment while 31% think it will not). The first cracks also began to appear in the government's congressional majority: on 24 April, the Partido Socialista Brasileiro (PSB), a member of the ruling coalition, said it would vote against the pension reform.

In response to these political challenges, the government has diluted some of the original proposals. For instance, it has reduced the obligatory retirement age for women to 62 (male retirement remained at 65 in the draft). It has made more generous provisions for the transition between the old and new systems. It has also allowed for earlier retirement and reduced contribution period benefits for rural workers, and in response to protests, it has also extended earlier retirement provisions to the police.

There is a split between those who believe that these concessions are just enough to secure the necessary three-fifths approval in the lower house (308 votes) and those who argue that the concessions go too far, to the detriment of the planned fiscal savings. The government is in the former camp. The 10-year saving from the pension reform initially was calculated at BR800bn (US$254bn). Finance Minister Henrique Meirelles says that the diluted version of PEC287 would reduce those savings by a 'manageable' 25%.

But some private sector economists calculate the loss at 40%, and argue that a second pensions reform will thus be necessary within a decade. "This reform is better than nothing: a half step forward, but short of the full decisive leap that we need to get the fiscal accounts in shape" Goldman Sachs economist Alberto Ramos told the *Financial Times*. Pedro Castanheira Schneider, an analyst at Itaú BBA, pointed out another potential problem. If more concessions are made on pension reform, annual pension spending will continue to increase, and that could mean that this and future governments will struggle to stay in line with the new spending cap, which also has constitutional standing. If pension spend growth exceeds the cost of living, the government could be forced to make offsetting cuts elsewhere to stay in line with the overall spending freeze.

On 3 May, the amended PEC287 draft was approved in a preliminary 23-14 vote by a lower house committee, with government spokesman Alexandre Parola stating that "Brazilian society recognises the urgent need for reforming the social security system". Despite this, government officials admitted that they were still uncertain as to whether they could muster the necessary three-fifths majority support later in the month, when a full vote was expected. Thereafter, a coalition of trade union bodies announced a round of demonstrations, including a planned 'occupation' of the capital Brasilia, in an attempt to persuade federal deputies to vote against the reform.

COLOMBIA

Turning a corner

It has been bad, but it is getting better, is the message coming from Colombian policy makers. Officials hope that cuts in the benchmark interest rate will keep the economy on target for GDP growth of 2.5% this year.

On 10 April, Economy Minister Mauricio Cárdenas acknowledged that the first quarter "had not been easy" for the local economy, as it continued to suffer from problems carried over from last year including higher inflation, tighter monetary policy and the resultant negative knock-on effects on consumption levels and demand. Inflation in calendar 2016 was 5.75%, significantly above the central bank's 2-4% target range. Cárdenas argued that the worst was now over. He noted that inflation had peaked (in the 12 months to March it eased to 4.69%, with a further fall to 4.66% in April). Since December furthermore, the central bank has been able to switch to an easing stance in monetary policy. The fourth generation (4G) road-building programme will also inject some stimulus into the domestic economy.

External factors were beginning to look up also, Cárdenas added. The gradual recovery in international oil prices is looking auspicious for a hydrocarbons exporter like Colombia. After a period of weakness, the Colombian peso has become relatively stable against the US dollar. Finally, the peace process is helping to revive interest in Colombia and international tourism to the country is growing.

President Juan Manuel Santos took up the theme in early May. As he put it, Colombia is finally emerging from the difficulties posed by the slump in international oil prices, global turbulence, and the recent disruptions caused by the El Niño weather pattern. The president added a new cause for optimism – the discovery of significant deep water gas reserves in the Gorgon field, operated jointly by Ecopetrol and Anadarko. This, Santos emphasised, is the most significant hydrocarbons discovery in Colombia in almost three decades, amounting to an entirely new gas province. The president noted that along with foreign investment of over US$39bn in the last seven years, Colombia is therefore well-positioned to resume a strong growth path.

It is clear, however, that the economy was weak in the first quarter. Real GDP grew by only 0.8% in quarter on quarter terms, a sharp slowdown compared to the 1.6% q-on-q rate registered in the fourth quarter of 2016. This sharper-than-expected slowdown may reflect the impact of a three-percentage point rise in the VAT rate (to 19%) from 1 January – part of the Santos government's fiscal reform package (designed to prevent the fiscal deficit from widening too much in the post-conflict era). As a result, retail sales and consumer confidence took a hit. And while the oil sector is beginning to recover from its long downturn, manufacturing remained slow.

Cárdenas still argues that GDP will grow by 2.5% overall this year, with the economy strengthening in the second half. Making that happen may require some further aggressive interest rate cuts. On 28 April, the central bank announced a 50bps cut in the benchmark rate to 6.50%. Market analysts, who had been predicting a 25bps cut, were taken by surprise. In a statement, the bank said it had observed "increasing weakness in economic activity, and the risk of an excessive slowdown". While the bank gave no clue as to the direction of further moves, analysts now believe that some more 50bps cuts are in prospect.

PERU

Future proofing

The government led by President Pedro Pablo Kuczynski has unveiled a US$9bn plan to rebuild and replenish infrastructure and resurrect the economy after the recent flooding emergency, which caused devastation across half the country.

On 25 April, the national congress – which is controlled by the right-wing *Fujimorista* opposition, Fuerza Popular (FP), approved the government's 'Reconstruction with Change' programme (Reconstrucción con Cambio, RCC), by 90 votes to 18, after some changes.

Congress approved the plan having added several clauses to prevent against the risk of corruption, including an insistence on tighter anti-corruption and resolution clauses in reconstruction works contracts. It also opted to increase oversight, both by itself and the comptroller general's office. The head of the RCC must publish a progress report every quarter, and also present an annual report to congress once a year over the planned three-year life span of the scheme. While congressional approval of the RCC and its legal framework is a positive, the actual financial details, including budgeting details, have yet to be finalised, meaning another tough round of executive-legislative negotiations ahead before anything can get underway.

The RCC plan, which has an estimated price tag of US$9bn (or 4.5% of GDP), will be administered by a new National Reconstruction Authority, to be led by a cabinet-level official (yet to be named). Of this US$9bn, approximately one-third will be destined for immediate repair needs (corresponding to the government's US$3bn estimate of the immediate flood damage), with two-thirds to be put towards strengthening (and even relocating) infrastructure, so as to better 'future proof' Peru against the increasing ravages of climate change in the country. In many ways, the RCC dovetails with Kuczynski's pledge in his 2016 election campaign to overhaul Peru's national infrastructure, a pledge thrown off balance by the explosion of the Odebrecht scandal in the country late last year, when it emerged that the Brazilian construction giant had made some US$29bn in illicit payments to officials in three different governments in Peru in the period 2001-2015 to secure major works contracts.

The reconstruction task is immense. According to the national institute for civil defence, over 2,000 schools need to be repaired or rebuilt, while almost 40,000 homes have been designated unfit for habitation and/or unsafe. Elsewhere, over 225 bridges also collapsed, wreaking havoc to national transport. The government has made clear that re-building will not be permitted in zones deemed unsafe, or where risk cannot be mitigated; this condition will apply equally to private and public construction work.

Rebuilding with jobs

On 10 April, President Kuczynski and Labour Minister Alfonso Grados unveiled 'Trabaja Perú', a separate US$19.9m plan to create temporary jobs assisting with the reconstruction efforts in the 11 regions affected by the floods crisis. Grados said the scheme should create 20,650 temporary posts

Rebound from 2018

Inevitably, Peru's economic growth will take a hit this year because of the floods crisis. Economy Minister Alfredo Thorne now admits that real GDP growth in 2017 will be 3% (at most), but he and the rest of the government remain confident that the economy will bounce back, better than before, from 2018 onwards. Thorne is looking for a rebound of over 4% next year. The IMF is now expecting growth of 3.5% this year, from 4.3% previously, but expects growth of 3.7% in 2018, while the World Bank has cut its 2017 forecast to 3.5%, from 4.2% previously.

Thorne has been at pains to emphasise that public investment will rise by up to 15% this year and next year, driven by the reconstruction work, as well as other planned works including for the 2019 Pan American Games (in Lima),

Line 2 of the Lima metro, stage 2 of the Majes Siguas irrigation project and stage 3 of the Chavimochic irrigation scheme.

Kuczynski confident on Chinchero

Kuczynski reiterated on 3 May that the new Chinchero airport, to serve the southern city of Cusco, is going to go ahead, albeit in the same breath he admitted that "we have to see in what form". "We have to see what the comptroller's report says," Kuczynski acknowledged, in reference to a pending report about the contract.

Kuczynski had been due to turn the first stone on the US$500m project back in January, but it was all put on hold after a congressional investigative commission said that a financing addendum to the contract by the new government was prejudicial to the state, and requested that the works be suspended indefinitely. "I want Chinchero, don't doubt it. But we have to wait…if everything goes well we can start moving earth in a few weeks," Kuczynski reassured a Cusco audience.

By contrast, even the MEF admits that private investment will remain crippled for a second year running, with forecast growth of just 0.5% in 2017. In 2018, the government is crossing its fingers that private investment will finally crank back into action, with forecast growth of 5%. This is still very far below what it needs to be, however, to propel the Peruvian economy forward sustainably – the public sector cannot prop up growth indefinitely.

Fiscal impact to be limited

Luckily for Kuczynski and Thorne, successive governments have been good at fiscal management in Peru, meaning that there are funds to call upon for its public spending plans. Thorne has submitted to congress a modified fiscal deficit schedule whereby the deficit is now programmed to be 3% in 2017 (from 2.5% previously), 3.5% in 2018 (from 2.3%), 2.9% in 2019 (from 2%) and finally 2.1% in 2020 (from 1.5%). Some of Peru's regional neighbours would be more than happy would this moderate deficit programme, which should not affect Peru's international credit ratings.

Thorne revealed that the government is currently preparing a tax reform (with a view to implementation by year end, for a revenue effect as of 2018-2019). The main focus is to expand the currently-narrow base of contributors. The Kuczynski government's plans for formalisation of the labour force go hand-in-hand with this. Of the 16m jobs in the country, 11m are informal. Labour Minister Alfonso Grados is also working on a labour reform, as part of which he is seeking to streamline the number of labour regimes in the country in support of this formalisation effort. In conjunction with this, the government is also considering reforms to the civil service law (known as the Ley Servir). And marking International Labour Day on 1 May, President Kuczynski also proposed changes to the country's pension and health systems to incorporate more of the informal sector. According to the national statistics institute (Inei), 65% of workers have no access to any kind of welfare provision, with only 35% affiliated to some kind of provider (whether private or public).

Confidence is returning

According to the latest omnibus Peru Pulse (Pulso Perú) survey by Datum, released in early May, confidence is finally returning to consumers, after a long period of very weak confidence. Sentiment is still subdued in the North of the country, the worst affected by the floods, but is strengthening in Lima and Callao. Consumers are more confident that the economy is no longer stagnant, and they are supportive of the government's public investment plans, aimed at stimulating activity. They also sense that private investment is slowly picking up, while they themselves are more willing to spend, albeit not on big-

ticket items (cars, holidays, houses) as yet. The Datum survey coincided with a rise in the latest national consumer confidence index (prepared by GFK) and a recovery in business expectations in the recent central bank surveys.

Copper lifeline

For this year, the expansive mining sector will provide a crucial stay to the Peruvian economy. Peru is currently benefitting from a new copper boom, with prices up in line with revived Chinese demand. Peru's copper output was up by 5.9% year on year in February on latest data from the national statistics institute (Inei). By region, Apurímac, home to the massive Las Bambas mine, registered the strongest output growth, at 225.2%, Las Bambas, operated by the Chinese-Australian MMG consortium, produced 73,644 fine metric tonnes (FMT) of copper in February. According to Energy and Mines Minister Gonzalo Tamayo, copper exports now make up just over half (51.3%) of total mining exports.

Largely thanks to the copper sector, as well as rising prices for other commodities, the economy and finance ministry has lifted its trade surplus forecast for the year to US$3.7bn (from the US$776m projected in August 2016), an increase of 375%. It has also increased its forecast for 2018 to US$3.43bn.

VENEZUELA

Default concerns ease...for now

In the midst of significant social unrest, the government led by President Nicolás Maduro made three large scheduled bond repayments on time on 12 April, relatively unnoticed. These latest payments reinforce the perception that the left-wing regime intends to continue to service its external debt commitments, come what may. Yet the continued deterioration in the country's underlying economic conditions, combined with few sources of fresh credit, suggest that a default risk is still high.

Three bond payments were due on debt issued by the state oil company Petróleos de Venezuela (Pdvsa). The largest repayment was US$2.1bn, due on the Pdvsa 2017 bond (comprising both principal and interest repayments), while US$81m was due in interest payments on the Pdvsa 2027 bond, plus US$41m in interest payments on the Pdvsa 2037 bond.

Rather unusually, the Maduro government made little fanfare about the repayments, failing to publicise the transfers, with news of the payments instead coming from investors, who indicated that they had received the funds ahead of the deadline.

Where did the cash come from?

This latest payment eased immediate concerns of an external debt default, as it had been unclear whether the Caracas government had sufficient cash to make the payments.

In fact, it remains very unclear where the government actually found the money, since foreign reserves only fell slightly (by around US$370m) just before the payments, suggesting that these were only tapped for a small part of the total sum repaid. Moreover, reserve levels had been relatively stable during March and early April, implying that the government had not been gradually drawing down on reserves in the run-up to the repayment deadline (as might be expected).

The extremely opaque nature of the Venezuelan public finances means that the administration may have alternative sources of savings. Oil prices remain low by recent historical comparison, but with Venezuela's export price averaging close to US$45/barrel in the first quarter of 2017, prices are over 80% higher than in the first quarter of 2016. Rather than increase import spending, the government may well have put aside part of these additional earnings in anticipation of the 12 April repayment.

It is also possible that part of the funds from the sale of an unusual bond issue at the end of 2016 may have been stashed by the government in an off-budget account, with the specific intention of using the money to repay the large April debt payments. When the bond issue came to light in January, there was speculation that the issue – made available only to Venezuelan state-owned banks – represented securities for China, following rumours that Beijing had potentially extended further credit to the Venezuelan government, but had demanded something concrete in return, given the still-substantial risk of default. It is in China's interest for Venezuela to remain current on its debt repayment schedule, because if Venezuela was to default, there would be a high risk that the current government would collapse. A successor opposition-led administration might not honour the large debts racked up by presidents Hugo Chávez (1999-2013) and Nicolás Maduro (2013-).

CDS spreads remain high

Although the immediate risk of default has passed, markets remain highly concerned about the government's creditworthiness. Notably, the 5-year Credit Default Swap (CDS) spread – an indication of default risk, as the CDS market provides insurance to investors against default – has not fallen since the 12 April repayment.

CDS spreads stood at around 3,700 basis points in early May, similar to early April and higher than in most of January-March. This indicates that markets still adjudge an extremely high risk of default within the next five years. By comparison, CDS spreads on other high-risk sovereigns are much lower, with Greece's 5-year CDS spread standing at just 670bps.

The fact that market risk surrounding Venezuelan repayment capacity remains elevated reflects several factors. Firstly, there are ongoing concerns that the government may run out of ways to put together sufficient cash to make future repayments. The May-September repayment schedule is relatively light, but a total of US$3.5bn falls due in October and November, mainly comprising capital and interest repayments on the Pdvsa 2020 bond and the final tranche of the Pdvsa 2017 bond. The authorities already restructured bonds falling due in 2017 in order to reduce repayments, so it would be very difficult to repeat this in the near term.

Foreign reserves are likely to have been tapped to some extent in the run-up to the April repayment, but with reserves levels continuing to fall, this option may not be available later in the year. At US$10.1bn in early May, reserves are perilously close to dipping below the psychologically-important US$10bn mark. With much of this held in gold (the exact amount is unclear, given holes in official data), liquid reserves, put at no more than a third of the total, may be close to depletion.

Secondly, market risk remains elevated because of the highly volatile political situation. Anti-government protests have raged for over a month, with the death toll approaching 40. The protests have been given additional impetus by President Maduro's surprise announcement of a constituent

assembly, which the opposition fears will erode its already-weak position even more. The fear is that Venezuela could end up a one-party state.

Although the military leadership is continuing to prop up the Maduro government for the time being, the ongoing unrest means an elevated risk of a change of administration. This affects default risk in several ways, with the most obvious being the possibility that an opposition-led government would either seek a voluntary debt restructuring or, more likely, be forced into default owing to a lack of available funds.

However, even if the Maduro government does not collapse, ongoing unrest raises the risk of an accidental default. With the government's focus elsewhere, there is a possibility, for example, of administrative errors resulting in a missed deadline. There is also a possibility that the military places ever-greater (financial) demands on the government in return for its support. These demands could eat up any extra money earned from higher oil prices, reducing the government's capacity to repay debt.

Currency reform is unlikely to bring any change

The government's preoccupation with social unrest has affected economic policy plans. Most notably, a new round of currency reform – initially unveiled in late March – have not yet materialised. At that time, the government announced a new programme of regular central bank foreign exchange auctions through the secondary 'Dicom' system, which is essentially the conduit through which private-sector firms and individuals can purchase US dollars. Although the authorities said that these auctions would begin straight away, there has been no progress in this respect, with the official silence only broken in early May, when Finance Minister Ramón Lobo stated that the technical platform to manage the auctions was now ready.

The government has not made clear the amount of US dollars to be made available per auction, or with what regularity the auctions will be held. More importantly, the authorities have failed to say if the Dicom exchange rate – which is heavily managed – will be devalued with the new auctions. The rate currently stands at around BsF720:US$1, much weaker than the fixed 'Dipro' rate of BsF10:US$1 (used for public-sector imports), but stronger than the black-market exchange rate, now trading at over BsF5,000:US$1, according to websites that publish the (illegal) rate.

In any case, the description of the new system as an auction is likely to be somewhat of a misnomer, since it implies a relatively open and democratic process, with market participants able to bid for foreign exchange and the price determined by the level of interest and availability. What is more likely to occur instead is that the central bank will provide an unspecified amount of foreign exchange, likely to be relatively little given heavy liquidity constraints, with the authorities distributing it to chosen recipients at an undisclosed price. That is how the previous 'Sicad' currency system functioned during the Maduro government's last (failed) experiment with foreign currency auctions in 2015.

Imports – throttled

As the Maduro government scrabbles to make debt repayments, some of the most vulnerable Venezuelans have been pictured in the media scrabbling through rubbish bins, in search of food scraps and other essentials.

The local economic consultancy Ecoanalítica now projects total imports of just US$15.3bn in 2017. In 2012, at the height of Chavismo (which coincided

with peak oil), Venezuelan imports soared to US$66bn, on central bank data, of which 80% (US$52.6bn) corresponded to non-oil imports. At that point, Venezuela was importing some 80% of its food needs. By 2015, imports had fallen to US$27.9bn (but 80% was still made up of non-oil items). Official BCV import data for 2016 has not been made available.

According to Ecoanalítica, and based on BCV data, Venezuela's total external debt was US$24bn in 2004. In 2016, the consultancy estimates, external debt was valued at US$103.7bn (inclusive of bond issues by the sovereign and Pdvsa, as well as financing from China). In other words, the country's external debt rose by factor of four in the space of 12 years.

When oil prices were above US$80/b, it was not a problem to service public debt, including the principal plus interest. But once oil prices began to creep down from late 2013 (before collapsing from mid-2014), the debt burden complicated.

Pdvsa was in double trouble, because not only were oil prices falling, so too was its production. On data from the Organisation of Oil Exporting Countries (OPEC, of which Venezuela is a founding member), Venezuela's oil production, which had been stagnant at about 2.9m b/d between 2003 and 2013, dropped by 400,000 barrels in the space of 15 months to just 2.2m barrels/day by October-November 2016 (when OPEC was in talks with members and other producers about global output cuts to put a floor under prices).

Of that total production, 1.6m barrels generates income for Pdvsa, Ecoanalítica calculates, with the remainder set aside for internal consumption and debt payments. Currently, Pdvsa is paying interest only on its loans with strategic partner China, with capital repayments deferred in light of Venezuela's economic difficulties. In late 2016, China also agreed to allow Venezuela to defer payments pending on US$2.8bn in separate bond debt.

Of its actual earnings, Pdvsa keeps some for its operational needs (including debt), with the rest transferred into the central bank's international reserves, again used for debt servicing and for imports. At just over US$10.1bn, reserves are now at a 15-year low.

In October-November next, the government and Pdvsa have combined bond debt payments of US$3.5bn falling due. The Venezuelan economist Francisco Rodríguez of Torino Capital calculates that the Caracas government has money in various funds worth about US$4.5bn, plus gold reserves of another US$7.6bn. However, neither assets are readily liquid, he notes. Access to international capital (and even multilateral financing) is also now more difficult because of the problems between the Maduro executive and the opposition-controlled national assembly, which warns that there might not be any future legal claim on external debt contracted by the government without its assent.

Given this tight situation, another Venezuelan economist, Alejandro Grisanti, head of research and strategy on Latin America for investment bank Barclays (and the founder and former director of Ecoanalítica), estimates that the Maduro government has to make savings of some US$500m-US$600m a month in order to meet the October-November debt crunch, meaning no chance of any increase in imports. Complicating matters, as of mid-May, Brent crude prices were still failing to breach US$50/b, and OPEC was moving to roll over output cuts, potentially all the way to 2018, in a bid to neutralise the effect of rising inventories (notably in the US) and continued increases in non-OPEC output, as compliance with the late-2016 global oil agreement weakened.

Ecoanalítica now expects imports of just US$15.3m in 2017, a drop of 15% on 2016. Taking the peak non-oil import figure of US$52.6bn in 2012, that would amount to a drop of 71% in Venezuela's imports in five years (with next to no substitution by domestic supplies either).

As things stand, there will be no reprieve for ordinary Venezuelans any time soon. The question is how much longer the country can physically withstand this immense chokehold being imposed – at the cost of people's very lives – by the Maduro regime.

REGIONAL BUSINESS REVIEW

PANAMA

One year on from the Papers

April saw the first anniversary of the so-called 'Panama Papers' scandal – the leak of around 11.5m confidential documents from the offices of Mossack Fonseca, a Panama-based offshore law firm, which revealed a vast network of shell companies being used for money-laundering and tax evasion purposes. One year on, the scandal is still having an impact on Panama.

The Mossack Fonseca scandal had a significant negative impact on Panama's reputation. As a result of the leak, around 150 investigations were begun in 79 countries, looking at a wide range of illicit financial transactions. The prime minister of Iceland was forced to resign, and a wide range of political leaders (including the-then UK prime minister David Cameron and Argentina's President Mauricio Macri) had to answer embarrassing questions about shell companies linked to their families. By late 2016, Europol said it had found 3,469 probable matches to criminal organisations when comparing the content of the leaked documents to their own files.

From an early stage, but with little success, the government of President Juan Carlos Varela tried to stop the international media from using the term 'Panama Papers' as shorthand for the scandal. This, it argued, unfairly singled out Panama as responsible for a whole range of tax evasion activities that in reality were conducted on a global scale and were a global, not a specifically Panamanian problem. But in reality, Panama had little option other than take responsibility and begin to reform its offshore sector, tightening regulatory oversight and allowing greater transparency. The country joined the OECD's multilateral convention on mutual administrative assistance in tax matters. This commits Panama to sharing tax data. Panama also began a slow process of tightening up rules requiring the identification of the ultimate owners of companies. The country still operates a system of bearer shares, whereby beneficial owners of Panama-registered companies can conceal their identities, although this too is due to be gradually phased out.

In some aspects, Panama may have actually increased the reputational damage it suffered. At one point, it threatened retaliatory trade measures against countries that might blacklist it as a tax haven. It appointed an international committee of experts to investigate ways of reforming its offshore financial sector, only to see its two most prominent members, the Nobel-prize winning US economist Joseph Stiglitz and the Swiss anti-corruption expert Mark Pieth, resign angrily when it emerged that the government would not commit to publishing their findings in full. When finally published, the official report called for Panama to align itself with UN transparency standards, adopt

tougher anti-corruption legislation and do more to identify the ultimate owners of 'legal and financial instruments'. Stiglitz and Pieth published their own separate unofficial recommendations calling for the establishment of a searchable public registry that would allow the identification of all directors and actual owners of Panama-registered offshore companies. Lobby group Transparency International agreed with this stance, saying that without a registry, criminals would continue to win the fight against corruption.

The scandal had important knock-on effects with Panama itself. Ramón Fonseca Mora and Jürgen Mossack, partners in the Mossack Fonseca law firm, were arrested (and later released to house arrest) on separate charges linking them to money laundering investigations under 'Lava Jato', the giant Brazilian corruption case. Fonseca, a former close friend and one-time minister in Varela's government, then told journalists that the Panamanian president had received campaign donations from Odebrecht, the Brazilian construction company at the centre of a major international bribery scheme. Fonseca also accused Panamanian government officials of manipulating the judiciary. The president has denied these charges, but they cast doubt over the integrity of his anti-corruption campaign. According to opinion polls, 81% of Panamanian voters believe that the Varela government is not sufficiently transparent. The country's main business lobby, Cámara de Comercio, Industrias, y Agricultura de Panamá (CCIAP), has called for tougher anti-corruption legislation.

There is also the economic fall-out to consider, although this has been less damaging than was initially feared. Jorge Hernán Rubio, a manager at Mossack Fonseca, in April said that the business of setting up and running offshore companies had fallen by 40% in Panama. He insisted that the business had simply moved to other offshore jurisdictions. Jürgen Mossack told journalists that in, "jurisdictions such as Delaware, Nevada, and others located in the United States, where virtually no due diligence is required…incorporations are thriving".

Offshore company management is only a small part of Panama's diversified economy, and the other parts do not seem to have suffered much contagion. Foreign Direct Investment (FDI) rose by 15.9% to US$5.21bn last year according to the economy and finance ministry, while 25 new companies opted to open regional headquarters in Panama (the latest of these, the Shanghai Gorgeous group, says it will invest US$1.8bn in the country). Revenues from the newly enlarged Panama Canal are up – rising by 16.5% in the first quarter. The IMF, meanwhile, expects real annual GDP growth to accelerate from 5.2% in 2016 to 5.8% this year.

REGION

Cooperation against corruption

Regional governments are seeking to work together to tackle the blight of corruption.

On 8 May, the Ecuadorean national Carlos 'Charlie' Pareja Cordero, wanted in connection with corruption at the state oil company Petroecuador, was detained in Lima, Peru.

It will be up to the Peruvian judiciary to decide on Quito's extradition request, but Ecuador's outgoing President Rafael Correa, who leaves office

on 24 May, appeared keen to deliver a scalp before he leaves. His final year in office, as well as the campaign for the February 2017 general election, was badly scarred by the emergence of corruption scandals implicating members of his decade-old left-wing administration. At least 80 individuals with public sector links are now under investigation.

Coincidentally, Correa's successor-elect, Lenín Moreno, was due to meet Peru's President Pedro Pablo Kuczynski the very next day (9 May) in Lima. Officially, the agenda was centred on bilateral border development and integration, but Moreno was expected to press for Pareja to be handed over to face justice in Ecuador. The Kuczynski government is also battling major corruption scandals in Peru, which, like Ecuador and Colombia, has been severely affected by the recent Odebrecht case, in which the Brazilian construction giant has admitted to paying billion-dollar bribes to governments all over the region (and further afield), over the course of at least two decades, in order to secure lucrative public infrastructure contracts.

A new crop of politically centre-right and economically-liberal regional governments – led by Kuczynski, Argentina's Mauricio Macri and Brazil's Michel Temer, are very keen to demonstrate their commitment to routing the corruption that appears to have badly infected their left-wing predecessors.

Brazil's former left-wing presidents Lula da Silva (2003-2010) and Dilma Rousseff (2010-2016), Argentina's former radical leftist President Cristina Fernández (2007-2015) and three nominally leftist former Peruvian presidents (Alejandro Toledo [2001-2006], Alan García [2006-2011, who was also president in 1985-1990] and Ollanta Humala [2011-2016] are all now under a cloud of suspicion for apparently unfettered embezzlement and malfeasance on their watch.

Kuczynski, elected in a tight run-off in early June 2016, centred his campaign on a strong anti-corruption message. Colombia's also-centrist President Juan Manuel Santos, who is seeking to see his ruling coalition re-elected for another term in 2018 (under a new candidate, Santos cannot run again), has also been seeking to burnish his anti-corruption credentials, after his administration too was tainted by the Odebrecht (and other) scandals.

As such, the current trend is for stronger and more proactive regional cooperation against the blight of corruption, now proven beyond all doubt to be have eaten into Latin America's economic and social development. According to Global Financial Integrity (GFI), a non-profit research and advisory organisation based in Washington DC, illicit financial flows out of Latin America run at an annual 3% of GDP, approximately. This is definitely a conservative estimate, because it is based on an analysis of official trade and balance of payments statistics, which will not capture most illicit funds (typically, these are laundered through complex offshore arrangements).

Evidencing this new regional cooperation, Colombia's attorney general, Néstor Humberto Martínez, on 4 May handed over to his Ecuadorean counterpart, Galo Chiriboga, 700,000 files from seven computers seized from Odebrecht's offices in Guayaquil and Quito on 23 December and 11 January last. A few weeks later, in early February, the Ecuadorean authorities requested formal assistance from Colombia to process some 12m files found on the computers. Ecuador's attorney general will now incorporate those files into its investigation into Odebrecht's operations in Ecuador, where the company allegedly paid out US$33.5m in bribes in the past decade – coinciding with the tenure of the Correa administration.

The Pareja family syndicate

Still on the run (purportedly in Europe) is the former hydrocarbons minister and former head of Petroecuador, Carlos Pareja Yannuzzelli, who happens to be a relative of 'Charlie' Pareja Cordero. Pareja Yannuzzelli is accused of taking bribes in exchange for Petroecuador state contracts, with some US$1m in suspicious funds deposited in offshore accounts in Panama during his short stint as hydrocarbons minister (November 2015- April 2016). On 16 May, an Ecuadorean judge is due to decide whether 'Charlie' Pareja Cordero and seven others detained in relation to the case should face trial for money laundering. The seven others include Charlie's son Carlos Dassum, his son-in-law and father-in-law, his personal secretary, and also the son and daughter of Pareja Yannuzzelli.

Having fled Ecuador in September 2016, Pareja Yannuzzelli has since been a thorn in the side of the Quito government, alleging in a 'Twitter war' that the recent former vice president Jorge Glas (2013-2016) – who will hold that position again in the Moreno administration – was well aware of the goings-on at the state oil company. Glas subsequently took a low profile in the election campaign.

Via his so-called 'CapayaLeaks', Pareja Yannuzzelli also alleged that Attorney General Chiriboga had alerted him in advance after the Petroecuador corruption scandal emerged via the Panama Papers leak in March-April 2016. Chiriboga, accused by critics of deliberately delaying both the Petroecuador and Odebrecht corruption investigations ahead of the February general election, is stepping down from his post, handing over to Carlos Baca Mancheno.

ECUADOR

Unilateral recrafting of international investment treaties

Under Article 422 of the 2008 constitution (introduced by President Rafael Correa), Ecuador is prohibited from entering into instruments whereby "the State yields sovereign jurisdiction in the international arbitration of disputes with private individuals or corporations".

Ecuador had signed 29 BITs in all before President Correa and his left-wing party, Alianza Pais (AP), won election in 2007 pledging a 'Citizen's Revolution'. Two of these treaties were signed but never took force, leaving 27 in effect.

The new government wasted little time in signalling its disdain for these treaties, which Correa said threatened national sovereignty. In early 2008, Ecuador unilaterally terminated nine BITs (with Cuba, the Dominican Republic, El Salvador, Honduras, Guatemala, Nicaragua, Paraguay, Uruguay and Romania), followed by another (with Finland) in 2010. In 2009, the Correa government served notice of its intention to withdraw from the International Centre for Settlement of Investment Disputes (ICSID) at the World Bank. This took effect as of 2010, albeit the ICSID retained jurisdiction under treaties in place up to then.

Much to Correa's chagrin, several cases lumbered on. In 2012, the ICSID issued its largest-ever award in a high-profile case between Ecuador and the US oil company Occidental Petroleum (Oxy). In a ruling that made international headlines, Oxy was awarded US$1.77bn for the expropriation of its assets (Oxy in fact had requested a multiple of that, US$17bn, and the final amount was eventually reduced to US$1bn [in November 2015] on appeal).

According to the United Nations Conference on Trade and Development (UNCTAD), Ecuador is in fact the third-most common 'Respondent State' in investment treaty cases filed at the ICSID (behind Argentina and Venezuela), with 23 cases taken against it as of 2016.

In May 2013, President Correa set up a 'Citizen's Commission' (CAITISA in the Spanish acronym), to review the 17 BITs remaining in effect. The commission included Ecuadorean government officials, along with experts and academics from other countries including Argentina, itself also at regular odds with international investors. Around that same time, Correa had demanded that Ecuador's BIT with the US, signed in 1993 and in effect since 1997, be annulled. This reflected the ongoing tensions between the Quito government and US oil firms including Chevron.

In 2015, a report prepared by the office of Ecuador's attorney general claimed that the country had been subject to total arbitration demands for US$17.7bn, of which US$11.7bn was still pending resolution. Correa has continually railed against multinationals for their litigious behaviour against developing countries.

Exactly four years after he first called for the CAITISA, Correa on 8 May took delivery of the final report, which makes clear that Ecuador should denounce its remaining BITs and renegotiate them. On 3 May, just days before the final report was made public, the outgoing assembly denounced 12 further treaties with Argentina, Bolivia, Canada, Chile, China, Italy, The Netherlands, Peru, Spain, Switzerland, Venezuela and, notably, the US.

The timing of all this, just weeks before Correa leaves office, has been criticised by his political opponents as deeply cynical. It is worth noting that the CAITISA was initially scheduled to complete its work in less than year. In January 2016, a version of its findings was leaked, in which its recommendations and advice to quit the BITs was already patently clear. At that time, however, the Correa government was in urgent talks with the European Union (EU) to join the existing EU-Colombia/Peru Free Trade Agreement. An adhesion agreement was finalised in 2016 and formally took effect as of 1 January 2017. Among the 12 BITs denounced in early May were those with Italy, The Netherlands, Spain and Switzerland. Brussels was scathing in its response, saying that Ecuador was sending "a very negative message" just months after it had secured the EU-Andean deal.

The plan now, according to AP Deputy María Augusta Calle, head of the assembly's international relations commission, is to renegotiate all the treaties, but on "equal conditions". She is clear has that Ecuador intends to withdraw from all of its remaining BITs. Echoing Correa, Calle said the agreements as constituted posed "a risk to the country", and denied that they had resulted in significant investment, noting that Ecuador receives less than 1% of foreign investment in the region.

This is indeed the case, but the reality is that foreign investors have been deterred by the interventionist, unpredictable and largely business-hostile policies of the Correa administration over the past decade. FDI in Ecuador has been no more than 1% of GDP under the Correa administration, in marked contrast to the strong inflows into neighbouring Peru and Colombia. The AP will remain in office for another four-year term under President-elect Lenín Moreno, but with a reduced majority. This last-minute move by the outgoing AP bench threatens to undercut Moreno, who has pledged more a pragmatic economic policy stance. And certainly, it will not help to improve investor perceptions of Ecuador, ironically just weeks after finance ministry officials were in London and New York in search of additional lending for this year.

Corporate Radar

Pemex makes a profit: Mexico's state oil company Pemex reported a net profit of MX$87.94bn (US$4.69bn) in the first quarter, citing lower financial costs and a recovery in the international prices of crude oil and other fuels. This was the second consecutive quarter in the black, after years of losses. The company's finance director, Juan Pablo Newman, said that it was the first time in six years that the company had reported net profits for two consecutive quarters. Revenues surged by 54.9% to MX$348.5bn (US$18.33bn), lifted by exports, which were up by 85.8% in value terms, despite a 3.6% fall in volume.

Crude output averaged 2.018m barrels per day (bpd), down by 9.5% on a year-on-year basis. Gas production was down 15.6% to 4.36bn cubic feet per day. Company officials stressed that as Pemex finances improve they will be seeking to reverse the declining production trend. The firm is focusing on private sector partnerships and farm-outs in up to 52 selected areas, along the lines of the Trion block agreement reached last year with Australia's BHP Billiton.

A further three Pemex-owned fields – Ogarrio and Cárdenas-Mora (both onshore) and Ayin Batsil (offshore, shallow waters) are due for competitive auction in October.

Meanwhile, however, efforts by Pemex to attract up to US$5bn worth of investment to modernise its two refineries are being less successful. Sources say that attempts to attract private sector partners to overhaul the Salina Cruz and Tula refineries are not going well. Pemex "categorically rejects" the idea that it is struggling to find investors.

Movement on UPM plant in Uruguay: Plans for Finnish pulp and paper company UPM to build a second plant in Uruguay, as part of a project that could be worth US$5bn in total, appear to be moving ahead. On 3 May, after months of talks with the Uruguayan government, UPM said it was going ahead with the plant in Paso de los Toros, following agreement on 16 of 17 points on the agenda. These reportedly include government commitments to build the necessary road, rail, and port infrastructure (according to some reports worth up to US$1bn). But UPM's request that it be exempt from capital asset taxes appears not to have been accepted.

Construction of the pulp plant is due to start next year, with cellulose paste exports starting in 2020. Total capacity at the plant will be 2m tonnes/year; it will employ a staff of 8,000.

Days earlier, during a visit to Montevideo, Spain's prime minister, Mariano Rajoy, said that a consortium of Spanish and Uruguayan companies (which he did not name) had won a US$200m contract to upgrade the highway linking Paso de los Toros to Montevideo.

Brookfield warning on Brazilian recovery: The emerging recovery in the Brazilian economy is generally seen as a good thing by corporates, but Canada-based Brookfield Infrastructure Partners has a slightly different view. Presenting Q117 results, in which its Brazilian operations figured prominently, Chief Executive San Pollock said the recovery meant that the

window of opportunity for "really high" rates of return was beginning to close "pretty quickly".

In the last two power line transmission auctions in which Brookfield had taken part the cost of capital had fallen, making them much more competitive. In the auction of 31 transmission lines in April, some had received more than 10 competing offers, while in comparable auctions 6-9 months earlier, Brookfield had been the only bidder for some lines.

Recent asset acquisitions in Brazil had been made at prices that were now beginning to move up. Brookfield has invested in the natural gas pipeline Nova Transportadora do Sudeste (NTS) and recently acquired the water and wastewater business Odebrecht Ambiental.

Along with Abertis of Spain, it also has a stake in the toll road operator Arteris, which in April won a US$381m 30-year concession to run the Rodovia dos Calçados highway in São Paulo. Pollack said that as the window of opportunity for high rates of return in Brazil began to close, so the company was examining opportunities in Mexico more closely.

YPF faces possible legal entanglement in US: For over a decade, Argentina faced complicated legal proceedings in US courts, as creditors sued it in the wake of the 2001/2002 foreign debt default. President Mauricio Macri's government finally settled the dispute last year. But a new legal entanglement could be looming.

This concerns the highly-polluted Passaic River in New Jersey, currently undergoing one of the most expensive environmental clean-ups in US history. Hundreds of companies that operated in the area accused of dumping metals, pesticides and toxins.

Attention has focused on one, Maxus Energy, which produced Agent Orange, a toxic defoliant used during the Vietnam war. Maxus was acquired by Yacimientos Petrolíferos Fiscales (YPF), Argentina's state oil company, in 1995, but was declared bankrupt last year. Two New Jersey democrats, Senator Bob Smith and Representative Tim Eustace, are now claiming that the bankruptcy was contrived by the parent company to avoid contributing to the US$1.4bn river clean-up cost. In a recent article they claimed, "Unbeknownst to most Americans, YPF is trying to stick the US government with its share of cleaning up one of America's most polluted rivers, while at the same time raising billions of dollars on Wall Street."

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