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Is Mercosur asleep on the job?

During the decade of the commodity boom (roughly the ten years to 2012) the governments of Argentina and Brazil (the two dominant members of the Mercosur trade bloc, whose other members are Paraguay and Uruguay [and Venezuela – suspended since 2016]) neglected the customs union and bickered between themselves over protective tariffs. When there was a political swing to the centre-right in Argentina (late 2015) and Brazil (mid 2016) there was a lot of talk of reviving Mercosur and making a new commitment to open trade and regional integration. But has anything really happened?

Mercosur was founded in 1991 and is now 27 years old. But talk over the last two years of giving it a new lease on life hasn't really produced results – at least so far. According to Mario Braga and Cecilia Arregui, writing for website *The Brazilian Report*, one of the problems it has always faced is that its four key members are very different-sized economies. Guillermo Valles Galmés, a Uruguayan delegate to the World Trade Organization (WTO) has described Mercosur as "An elephant, a mouse, and two ants": Brazil is the elephant – the largest economy in Latin America – Argentina is the mouse, and Paraguay and Uruguay are the two ants. Brazil's GDP is three times larger than Argentina's, 34 times larger than Uruguay's, and 65 times larger than Paraguay's. This means that most internal trade is between Brazil and Argentina. The nature of those two economies is that trade tends to be something of a win-lose affair. José Augusto de Castro, head of Brazil's foreign trade association, admits, "The three smaller economies are funding Brazil and gradually becoming more dependent on its economy."

Trade within Mercosur did rise strongly in the 1990s, but after reaching a peak of 23.1% of total bloc exports in 1998 fell back significantly and remains well below that level. Other trade blocs do much more internal business: trade within the 21 members of the Asia-Pacific Economic Cooperation group (Apec) currently accounts for 69.7% of their total exports. Both Argentina and Brazil suffered major financial crises in the late 1990s and early noughties, which did not help. In response to those troubles, the two main Mercosur members slapped a range of tariff and non-tariff protectionist barriers on their internal trade (typically requiring and then delaying the issue of bilateral import licence).

With the benefit of hindsight, it seems Mercosur missed some key opportunities. One was to enlarge, bringing in new members with more varied patterns of trade. But the insistence on a customs union – requiring complex negotiations on accession – and the existing members' reluctance to dilute their power discouraged applicants. Bolivia remains an associate member, Venezuela joined for political rather than economic reasons, and was later suspended on the same grounds. Many other countries like Chile and Peru opted instead for simpler and more open free trade agreements (FTAs). Mercosur itself signed few trade deals – only nine in 27 years, and of those

nine only three were full FTAs (with Israel, Egypt, and the Palestinian National Authority). It has been very difficult to get internal consensus on FTAs. Uruguay's attempts to strengthen trade relations with the US and China were largely boycotted within the bloc.

Nicolás Albertoni, a Uruguayan economist at the University of Southern Califonia (USC), says that trade bloccs with various economies at similar stages of development – such as the European Union – are more likely to be successful than those with very different economies like Mercosur. In addition, the EU continues to invest heavily in reducing internal economic imbalances among its members, which Mercosur does not. The EU's cohesion and regional development funds total EUR358bn in 2014-2020: in contrast Mercosur had a structural convergence fund (FOCEM) worth only US$1bn in 2007-2015. Investment in infrastructure lags behind in Brazil itself and across Mercosur as a group.

What is the way forward? Expanding Mercosur is no longer feasible, with the bloc's neighbours more interested in FTA's or looser associations like those exemplified by the Pacific Alliance (Chile, Peru, Colombia, and Mexico). Abandoning Mercosur would be seen as politically too much of a backward step. Albertoni suggests "flexibilisation" is the only real way forward, which would include finding a way to allow members to strike their own FTAs with other countries. Many believes the decades-long talks on the EU-Mercosur free trade agreement, if they are finally completed, could also generate some much-needed dynamism.

No white smoke in Brussels

The EU and Mercosur said on 27 April that they had concluded another negotiating round on their long-proposed free trade agreement, making some progress on automobile trade, but also referring to various sticking points. Sources in the European Commission said that the talks had been "useful" but that the two sides remained some way apart over the treatment of agricultural products such as Mercosur beef exports to the EU and EU dairy product exports to Mercosur. The EU wants the FTA to cover maritime issues and access to public procurement. It is also calling for protection of regionally produced specialised food and drink products, such as champagne and Parma ham. A Mercosur source told *Reuters* news agency that the talks had ended early with Argentina and Uruguay leaving the negotiating table in protest at what they said was the inability of Brazil and the EU representatives to reach agreement.

Brazil-Chile FTA

Brazilian President Michel Temer, who was playing host to the visiting and newly sworn-in Chilean President Sebastían Piñera, said on 27 April that the two countries were interested in exploring a possible bilateral free trade agreement. Bilateral trade is significant, totalling over US$9bn in 2017. Further details of what was being proposed were not given. Under the current terms of the Mercosur agreement, Brazil would have to secure the support of the other three active members for doing a trade deal with Chile.

REGIONAL ECONOMY REVIEW

DOMINICAN REPUBLIC

IMF call to rebuild the buffers

An International Monetary Fund (IMF) mission to the Dominican Republic published its Article IV consultation findings on 23 April. The report was positive, predicting that after a relative slowdown in 2017, the economy will pick up pace again. The country is poised to continue as one of the

fastest-growing in Latin America, although the IMF warns that the government should focus on rebuilding its buffers against external shocks.

In 2014-2016 the Dominican Republic's economy boomed with average GDP growth of 7.1%. This breakneck pace was, however, described by the Fund mission as "above potential"; there was subsequently a slowdown in the first three quarters of 2017, driven by a cyclical correction in domestic demand, uncertainty over reforms, and disruption caused by the close passage of two category five hurricanes in September 2017. Despite this, a shift to a more expansive monetary policy from mid-2017 onwards seems to have had the desired effect, with lower interest rates on lending and stronger credit growth triggering an economic recovery in the last quarter of 2017 that looked like continuing into 2018. Employment and wages continued to improve. After GDP expansion of 4.4% in 2017, the pace is predicted to rise to 5.5% this year and then to moderate to a medium-term potential rate of around 5% in subsequent years. The Fund expects inflation to remain within the central bank's four (+/- one) percent target band.

The main risks to the economy are external. They include higher international oil prices (the country is dependent on oil imports); weaker than expected demand for the country's exports; and the possibility of tighter-than-expected global financial conditions. According to the IMF Executive Board, "the key challenge will be to build resilience to these risks by rebuilding policy buffers, reinvigorating structural reforms, and further reducing poverty and inequality". Despite acknowledging that there has already been some progress in improving the debt profile and fine tuning tax and customs administration, the mission calls for additional action to strengthen the fiscal position. It notes that public debt has continued to increase. Further reform must "reverse the upwards debt dynamic" while protecting against negative impacts on growth, poverty and inequality. Just under one-third of the population of 10.17m (30.5%) lives below the poverty line. It is suggested that the government should widen the tax base, streamline tax incentives and exemptions, rationalise inefficient spending, and increase public investment and social spending. There is also a suggestion that the Dominican Republic might benefit from setting up a medium-term fiscal framework, "anchoring" decision making and aligning it with sustainable objectives.

Switching from Taipei to Beijing

On 1 May the Dominican Republic formally ended 77 years of diplomatic relations with Taiwan, switching instead to recognise the Peoples' Republic of China (PRC) in Beijing. The move was condemned by Taiwan, with foreign minister Joseph Wu suggesting that the PRC had used "financial incentives" to persuade the Dominican Republic to change sides. It seems to represent another step in a long and slow process by which the PRC uses its trading advantages to improve its diplomatic position in Central America and the Caribbean. Panama switched diplomatic relations to Beijing in June last year and since then has been discussing a range of new initiatives, including investment in ports and rail infrastructure and a potential trade agreement.

Dominican Republic: key economic variables

	2016	2017	2018	2019	2020
Real GDP %	6.6	4.6	5.5	5	5
Contribution to growth					
Consumption	3.7	3.3	3.4	3.3	3.4
Investment	2.7	-0.6	1.8	2	1.9
Net exports	0.2	1.9	0.3	-0.3	-0.4
Nominal GDP (US$bn)	71.6	74.9	na	na	na
Unemployment (%, period average)	5.5	5.4	5.1	5.1	5.1
Consumer price inflation (eop)	1.7	4.2	3.7	3.8	4
Consolidated public sector balance (% of GDP)	-4.1	-4.6	-4.3	-4.4	-4.4
Central government balance (% of GDP)	-2.8	-3.2	-2.8	-3	-3.1
Consolidated public sector debt (% of GDP)	50	52.7	52.6	53.7	54.4
Current account balance (% OF GDP)	-1.1	-0.2	-1	-1.4	-1.7
Of which:					
Trade balance (% of GDP)	-10.5	-10.1	-10.7	-10.8	-10.7
Services balance (% iof GDP)	6.9	7	7.1	7.4	7.4
Income balance (% of GDP)	2.5	2.8	2.6	1.9	1.6
Foreign Direct Investment (FDI), net, % GDP	-3.4	-4.8	-3.3	-3.3	-3.3
NIR - Net international reserves, US$bn	6.047	6.78	7.428	8.028	8.578
NIR in months odf imports	3.4	3.5	3.6	3.7	3.8

Source: *IMF*

The mission also calls for greater transparency in public procurement, improved public sector financial management, and action to bring economic statistics up to international standards. There is a call for greater exchange rate flexibility, seen as valuable because it can provide an automatic adjustment mechanism in response to external shocks. The country's external position is described as moderately strong, and the mission suggests this offers an important opportunity to continue building reserve buffers, which have strengthened since the Dominican Republic's last major financial crisis (in 2002-2004). Finally, the IMF says "Growth and socially-oriented structural reforms will be important to enhancing the economy's growth potential and addressing remaining social challenges." There are specific mentions of the need for reform in the electricity sector, to reduce high transportation costs, and to ensure adequate retirement pensions

BRAZIL

Growth without the feel good factor?

President Michel Temer, along with other centrist would-be candidates in Brazil's October elections, have always worked with a key hypothesis: if the market-friendly policies pursued since 2016 can deliver an economic recovery, the electorate is likely to shun political extremes and vote for more of the same. But the calculation may not work: there is reason to believe that the recovery is taking shape without delivering a 'feel good' factor. Brazilians are so far not feeling a change for the better in their pockets.

Brazil is growing again, but it is doing so unevenly, and in a way that leaves important segments of the population behind. Overall, real incomes are still falling, and pockets of poverty are holding out and even deepening. A batch or recently released data offers some clues as to why 2018 is looking like a recovery without joy – something that could have big electoral implications.

Take the metropolitan region of São Paulo state, traditionally one of the key engines of the Brazilian economy. Using official statistics from IBGE (Instituto Brasileiro de Geografía e Estadísticas), private sector consultancy LC Consultores says that the number of people living in extreme poverty in the 36 municipalities that make up the metropolitan area has increased by 180,000 or 35% since 2016, to reach 700,193 people. The study uses the World Bank's definition of extreme poverty – those earning less than US$1.90 a day. The extreme poor represent 3.3% of the total population in the metropolitan area. Cosmo Donato, an LC Consultores analyst, points out that poverty has increased even though unemployment dropped 0.7 percentage points to 14.2% in the year to the last quarter of 2017. "We are talking about people who often cannot even enter informality. It is a structural problem," Donato told business newspaper *Valor*, adding, "They are people with low skills and productivity, and who have been employed in the past because of the labour market's overheating. It is data that does not improve along with the labour market's cyclical recovery: it will require social policies." There is also continuing evidence that poverty is skewed by race. The number of blacks or mixed race Brazilians living in extreme poverty grew by 61% in 2017, compared with a 13.6% increase for whites in the same situation.

For São Paulo state as a whole, extreme poverty rose by 23.9% in 2017 to reach 1.39m people, or 3% of the state total. Nationally, extreme poverty rose by 11.2% to 14.83m people, or 7% of the total population. Last year São Paulo state's GDP rose by 1% after a 3.9% contraction in 2016 (according to Banco Santander estimates). São Paulo's growth was therefore in line with the national average of 1%, but was still insufficient to reduce poverty. Poverty increased even though the distribution of income became more equal. The Gini index fell from 0.541 in 2016 to 0.534 in 2017 (zero represents perfect equality and 1.0 represents maximum inequality). However what seems to have happened is that the income of the rich fell, while that of the poor did not improve.

Anyone looking at the relative performance of Brazil's regional economies would see trends that raise concerns for the electoral strategists attached to the centrist parties. At a national level the recovery is slow. But two key regions, the Southeast (home to 44% of Brazil's voters and widely seen as a middle class stronghold) and the Northeast (a much poorer area, with another 27% of the voters, traditionally favouring parties of the left) are lagging behind. In the 12 months to February, according to the Banco do Brasil economic activity index, the national economy grew by 1.7%. However, the Southeast grew by only 0.6% while the Northeast also lagged, with growth of 1.2%. The remaining three regions – the North, the South, and the Centrewest, all grew faster than the national average. These three regions are home to 29% of the voters.

The Southeast, which includes São Paulo and Rio, could be critical to the election outcome. While traditionally (and correctly) seen as affluent compared with the rest of the country, it now seems to be having an ill-starred recovery that may make its voting preferences volatile and difficult to predict. *Valor* calculates that the average real income of the highest earning 10% of the population in the Southeast fell by an inflation-adjusted 8% last year. This reflected the economic crisis in Rio de Janeiro, the poor performance of manufacturing, and lower returns in financial markets caused by the drop in interest rates. While the government can rightly point to lower inflation as one of its voter-pleasing achievements, many may choose instead to focus on lower incomes and the still-difficult labour market.

Another set of statistics from IBGE will further challenge the centrist electoral strategists. These show that on average, Brazilians' incomes fell by 0.5% last year. The figure reflects income from wages, pensions, rent, and social welfare programmes. Among Brazilians who said they had received any type of income last year, the monthly average was BRL2,112 (US$624), down from BRL2,124 (US$627) in 2016. If the calculation is limited to those actually in employment, the fall in income was larger, at 1.3%. Fundação Getúlio Vargas (FGV) economist Fernando de Holanda Barbosa Filho said "The figures show that Brazil was coming from a very bad situation and it continued very bad. The recovery at the end of 2017 has not had an effect on incomes yet." As with the Sao Paulo research, this IBGE data suggests that both the very rich and the very poor have lost income, although the latter have proportionately lost much more than the former. The top 1% of earners – around 900,000 people – saw their monthly income fall by 2.9% on year-ago levels to BRL 27,213. At the same time, the bottom 5%, around 4.5m people, saw their income slashed by 38.2% to BRL47 a month.

CUBA

Which way for Díaz-Canel?

In April Cuba's national assembly voted in Miguel Díaz-Canel as the country's new president, replacing Raúl Castro, who had been in office since 2006. For the first time in six decades the presidency has gone to someone whose surname is not Castro. What does this mean for economic policy? Díaz-Canel faces conflicting pressures to liberalise – and not to liberalise – the Cuban economy. It is likely that not much will change in the short term, but the new president can be expected to try to resume reform efforts that ran out of steam during Raúl's tenure.

One way of looking at Cuba is as a long and unfinished struggle between conservatives wanting to maintain a tightly controlled state-run economy and reformists or modernisers who want a greater role for the private sector. Sometimes the same person can straddle a combination of both positions. What is clear is that starting in 2011 Raúl Castro made a big effort to liberalise the economy, and that it gradually got bogged down, blocked, or even

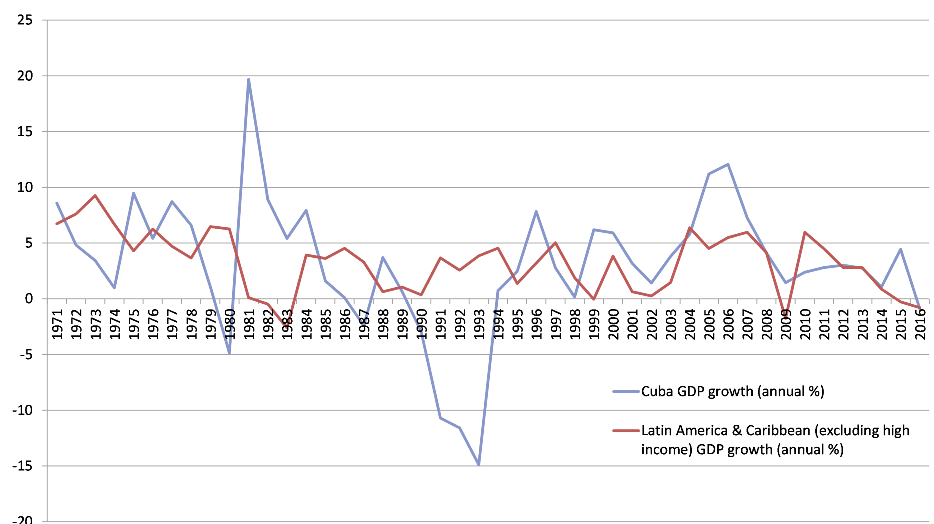
reversed. As army commander, Raúl had already brought market-oriented management techniques to military enterprises, sending officers to business schools abroad. In 2011 he announced no fewer than 314 detailed reforms. State enterprises were to make a profit or close. Rules were to be relaxed to allow the population to be self-employed or set up small businesses. Foreign companies were to be encouraged to invest in Cuba, with a goal of attracting US$2.5bn a year in foreign direct investment (FDI). The overall goal was to introduce a model of socialism that combines market efficiency and productivity with the social benefits of free healthcare and education.

It hasn't gone terribly well, for a variety of reasons. Bureaucracy and political resistance to change have played a part. Five years after the 313 reforms were announced, only 21% had actually been implemented. Subsidies for state enterprises still absorb about 20% of the state budget. External factors have also played a part. The rapprochement between Raúl and US President Barrack Obama has now gone into reverse under Donald Trump, Obama's successor. This is important because it was hoped that US investors and tourists would help revive the island economy. The crisis in Venezuela has also been bad news: the Caracas government has been forced to reduce the subsidised oil it ships to Cuba under the Petrocaribe programme.

The economy is suffering. In April Cuban state-TV acknowledged that "economic tensions" caused by a shortfall of foreign currency export earnings in the first quarter of 2018 were continuing. The broadcast gave no hard figures but spoke of "difficulties in fuel supply" even though it said the government's investment programme had been 90% fulfilled in Q118. It also referred to shortages of imported supplies, delays in investment, and a deficit in certain types of skilled labour. Separately, the tourism ministry said that tourist arrivals fell 7% in the first quarter, due mainly to a fall in US tourism. The destruction of facilities by Hurricane Irma, which hit the island in September 2017, was also a factor. According to government data, average economic growth over the last decade has been only 2.4%. Also according to official data, in 2016 the economy contracted by 0.9% (largely due to the Venezuelan crisis). Speaking last December, economy minister Ricardo Cabrisas said growth had recovered to 1.6% in 2017 in spite of it being "a period characterised by major challenges to productive activities and services". The government's estimate of growth last year was higher than that made by the UN's Economic Commission for Latin America and the Caribbean, which put it at only 0.5%. Cabrisas said that the priorities for 2018 would be infrastructure investment, increased foreign exchanger revenues, and promotion of the Mariel Special Development Zone (a deep-sea port and industrial park).

Cuban growth has disappointed over the last decade

GDP % change Cuba and LAC



Source: World Bank

Various analysts have looked into Díaz-Canel's background for clues as to what he might do. There are few definitive indicators. He served three years in the army, was a Communist party leader in Villa Clara and Holguín provinces, and later became minister for higher education. He is not known for dramatic, Castro-style speeches, and is described as more effective in smaller meetings. At 58, he is the first prominent Cuban leader who was born after the revolution. He has tried to show he has the common touch. During the 'special period' – the economic slump of the 1990s – he went to work on a bicycle, rather than in the standard air-conditioned car used by party leaders. Some say he is a social liberal, citing his defence of a gay club in Santa Clara. He has been photographed with his wife (for example, when voting in the March elections) – unusual for a top Cuban leader. He was one of the first Communist party leaders to use a laptop, and has defended wider Internet access and independent bloggers – although there is also a video of him addressing a party meeting and threatening to close down critical websites.

Diego Moya-Ocampos, an IHT Markit analyst, says "What we can expect from Miguel Díaz-Canel is policy continuity and gradual economic reform, but no democratic political opening or Cuba's moving to a more pluralistic political system," adding "Canel is Raúl Castro's boy, and change will continue to be steered by Raúl Castro, who'll remain the head of the Communist Party."

One of the major challenges the new president will face is to unify the currency, currently split between a convertible peso (CUC – pegged one-to-one to the US dollar) and a domestic peso (CUP – with an exchange rate of 24 to the CUC). The system subsidises inefficient state enterprises, leads to a massive misallocation of resources, and reduces Cuba's ability to compete internationally. As president, Raúl Castro repeatedly said the official aim was to re-unify the currency, although he never actually did so, perhaps because the political costs could be very high (forcing a shake up in the dominant state sector of the economy and possibly triggering expressions of public discontent with the regime). So one important indicator of future economic policy in Cuba will be the speed with which Díaz-Canel engages with the currency reunification issue. More generally, William LeoGrande of the American University in Washington has commented: "If Díaz-Canel can deliver on the economy – the top priority for most Cubans – he'll be judged a success. If not, we will face a rising tide of discontent from a population impatient for change."

PARAGUAY

Abdo Benítez offers more of the same

The Paraguayan economy has been growing at a strong average rate of around 6% from 2013-2017. The Central Bank is forecasting 4.5% expansion this year, based on strong soya and beef exports (Paraguay is the world's fourth-largest soya exporter). Initial indications are that the victory of conservative Mario Abdo Benítez in the presidential elections held on 22 April will signal continuity in both economic policies and results (he is due to take office on 15 August)

The presidential race was closer than expected, raising some doubts over Abdo Benítez' chances of having a working majority in congress for his five-year term in office. With 99% of the votes counted the candidate of the traditional and conservative Partido Colorado won with 46.44% of the valid votes, against 42.74% for Efraín Alegre of the Liberal party-supported centre-left Alianza Ganar coalition. The margin of victory, at 3.7 percentage points, was narrower than the opinion polls had suggested. Definitive results in the gubernatorial and congressional elections have yet to be released. However the first assessment that the ruling party would be weak in congress was subsequently revised. It now looks as if the Colorados will have 17 of 45 seats in the senate (down two – a smaller reduction than predicted) leaving the door open for the

next government to make alliances with smaller parties. "The traditional parties are maintaining their hegemony," political analyst Sebastián Acha told *Reuters* news agency, adding, "We can't talk of a turn to the left as some predicted. Abdo's Partido Colorado will have an important block in the senate and looks like getting a big majority in the chamber of deputies."

The president-elect may also have side-stepped a long-standing political dispute which could distract attention from economic policy: the vexed issue of presidential re-election, currently prohibited by the constitution. The Colorados, the party that supported the long-dictatorship of General Alfredo Stroessner (1953-1989) are frequently suspected of wanting to stay in office, and not always by fair means. Last year when supporters of incumbent President Horacio Cartes tried to push through a reform law that would allow him to stand again, there were violent demonstrations and part of congress in Asunción was burn down by protestors. Abdo Benítez is from a rival faction of the Colorados, and although his father was General Stroessner's right hand man, he can claim his own democratic credentials are good. After the election he suggested there might be a constitutional reform referendum in 2019 on the re-election question, but that an affirmative result would apply to future presidents, not to himself. By insisting he will only serve one term, he may have defused the issue.

The president-elect's core economic policy seems to be to keep the export-fuelled growth going, while maintaining a low tax environment and seeking to encourage inward investment. During the campaign he also spoke of fighting corruption and reforming the judiciary. The big question is whether his macroeconomic policies will be enough to reduce still-high levels of poverty and social exclusion. Over one in four Paraguayans lives below the poverty line. About one-third of the country's 15 to 19 year-olds do not receive proper schooling. On all key social indicators Paraguay lags behind its fellow Mercosur trade bloc members, Argentina, Brazil, and Uruguay. Political scientist José María Costa told Spanish newspaper *El País* "The election result shows the fundamental need for a political dialogue, particularly since we face big challenges such as reducing poverty, increasing social spending, and strengthening our institutions."

Last year the Paraguayan congress approved a bill that would have imposed a 10% soya export tax. However, Cartes used his presidential veto to stop it becoming law, a move which was also supported by Abdo Benítez. Had the centre-left Alegre won the election, many expected higher taxes would be back on the agenda, but that now looks unlikely.

Ratings agency Fitch kept a positive outlook on Paraguay after the election, arguing that it expects Abdo Benítez to maintain the fiscal discipline that characterised the Cartes administration. Moody's took a similar line, noting that Paraguay has a long history of fiscal conservatism that "supports our view that the country will maintain a low debt burden". The country began accessing global debt markets in 2013 and since then has placed around US$3.5bn in bonds. According to *Bloomberg* these have paid an average yield of 4.97%, more competitive than the 5.92% yield achieved on average in all emerging markets.

Unlike some neighbouring countries where there is an ageing population, Paraguay's demographics are still young. The total population is 6.9m. In the next five years it is calculated that around 500,000 people, mainly millennials, will arrive in the country's urban areas, requiring jobs, education, and housing. Daniel Correa, an economic adviser to Abdo Benítez (and former deputy finance minister) points out that roughly half the population is aged 24 or younger. He told *Bloomberg*, "Paraguay needs democratic leadership that can meet the demands of these millennials. That demographic bonus could be an asset or could turn into a liability."

Booming economy, protests on the streets

As a general rule of thumb, strong economic growth tends to create greater political stability and support for the government in power. But this is not always the case, and Nicaragua, with widespread street protests in April against the regime of Daniel Ortega, is showing itself to be a significant exception to the rule.

According to the IMF, Nicaraguan GDP is set to grow by 4.7% this year and by 4.5% in 2019. If achieved, this rate of expansion will make it the second-fastest growing economy in Central America (after Panama in first place). But it is clear that Nicaragua has much weaker institutions than Panama. In Nicaragua, "The multiple citizen demonstrations sparked by a government attempt to make regressive changes to the pension system, and the unfortunate violent response by the Nicaraguan state, show there is an unstable political balance in the country," says Jonathan Menkos, director of Instituto Centroamericano de Estudios Fiscales (Icefi), a think-tank. Menkos says that Nicaragua's growth has been based on a tacit understanding between the party in power – Frente Sandinista de Liberación Nacional (FSLN) – and the local business community. By playing down the negatives (authoritarianism, corruption, weak institutions) this alliance has attracted significant inward investment flows, particularly into agriculture and services. Despite his criticism, Menkos also acknowledges that there has been investment in social infrastructure to reduce poverty.

The protests and violence by the police were sparked by a decree introducing a 5% increase in pension contributions charged to workers and employers, along with reduced benefits, part of a package of measures designed to reduce losses at social security body INSS (Instituto Nicaraguense de Seguridad Social). By some calculations, pensions would be cut by as much as 12%. What gave the issue a particular political sting was that there have been claims of misallocation of funds and dubious investment projects within INSS. Faced by the sheer size of the demonstrations, and a death toll that could be as high as 63, President Ortega rescinded the decree, but this does not seem to have been enough to diffuse the country's major internal confrontation.

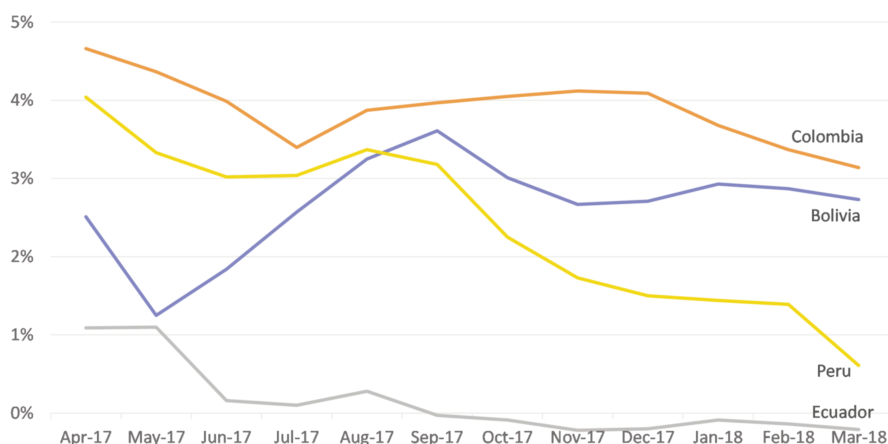
Juan Felipe Celia, a deputy director at the US-based Atlantic Council, says that the protests were initially over the government's plan to increase workers' social security contributions, but explains that they widened out from there to include other issues such as censorship and the lack of political freedoms in the country. Asked whether the IMF – which had recommended social security reforms – was indirectly to blame for the uprising, he said the real responsibility lay with the government for trying to impose drastic changes without even consulting congress or the business community. As a result Cosep (Consejo Superior de la Empresa Privada en Nicaragua – the top business community organisation and a traditional ally of the government, ended up opposing the measures. Celia says the economic crisis in Venezuela may also have been a factor – Venezuela's subsidised oil exports to Nicaragua have been sharply reduced

The Banco Central de Nicaragua says that GDP grew by an average of 5.2% in 2010-2017. Last year growth was 4.9%, led by livestock, agriculture, fishing and aquiculture, hotels and restaurants, the financial sector, and manufacturing. Inflation closed the year at 5.7% and public sector debt stood at 47% of GDP. The labour market is highly informal, with as much as 70% of those of working age paying no taxes and receiving no benefits.

ECONOMIC HIGHLIGHTS

ANDEAN COUNTRIES

Andean Countries: Inflation rate (%)
Percentage variation (year-on-year)

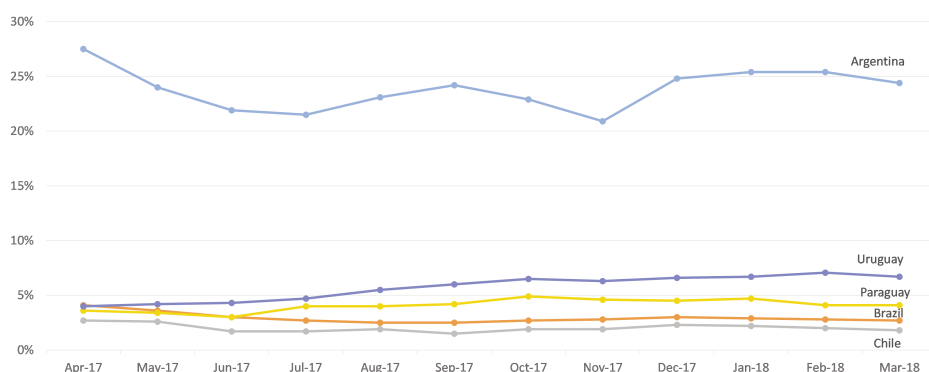


Source: *Local central banks. No reliable data available for Venezuela.*

Andean Countries: GDP growth								
Quarterly figures are year-on-year growth								
GDP	**end 2017***	**2018 forecast****	**Q3 2016**	**Q4 2016**	**Q1 2017**	**Q2 2017**	**Q3 2017**	**Q4 2017**
Bolivia	3.9	4	4.7	4.2	3.8	3.9	-	-
Colombia	1.8	2.6	1.2	1.6	1.2	1.3	2	1.6
Ecuador	1	1.3	-1.6	1.5	2.2	3.3	3.8	3.0
Peru	2.5	3.5	4.5	3	2.1	2.4	2.5	2.2
Venezuela	-9.5	-5.5	-	-	-	-	-	-
**Figures from the United Nations Economic Commission for Latin America & Caribbean December 2017*								
***Figures from the United Nations Economic Commission for Latin America & Caribbean April 2018*								
Quarterly growth based on figures from the local central banks. Bolivia has ceased providing quarterly y-o-y GDP data.								

BRAZIL & SOUTHERN CONE

Brazil & Southern Cone: Inflation rate (%)
Percentage variation (year-on-year)



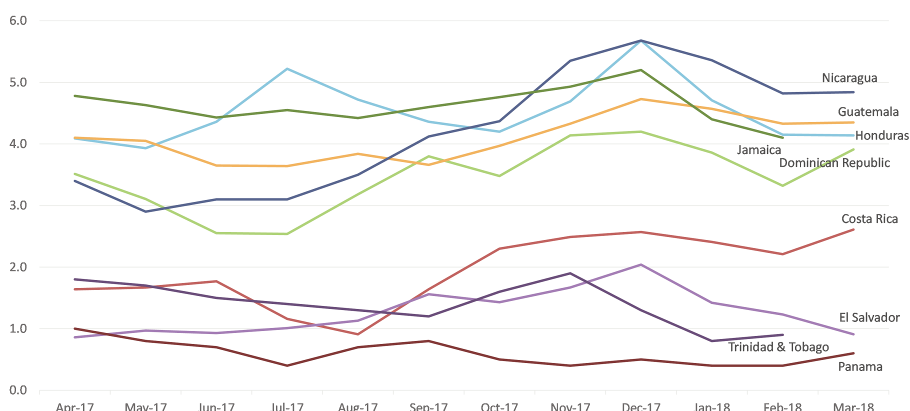
GDP growth (%)							
	End 2016 (from CEPAL August 2017)	**2017 (from CEPAL October 2017)**	**Q4 2016**	**Q1 2017**	**Q2 2017**	**Q3 2017**	**Q4 2017**
Argentina	-2.20%	2.40%	-1.90%	0.40%	2.90%	4.20%	4.0%
Brazil	-3.60%	0.70%	-2.50%	-0.40%	0.30%	0.10%	2.1%
Chile	1.60%	1.50%	0.50%	0.10%	0.90%	1.50%	2.2%
Paraguay	4.10%	4.00%	-0.30%	3.40%	-2.40%	3.00%	-
Uruguay	1.50%	3.00%	N/A	4.40%	2.80%	2.20%	2.0%
Annualised quarterly growth based on figures from local central banks.							

ECONOMIC HIGHLIGHTS

CENTRAL AMERICA & CARIBBEAN

Central America & Caribbean: Inflation Rate

Percentage variation (year-on-year, selected countries, latest available data)

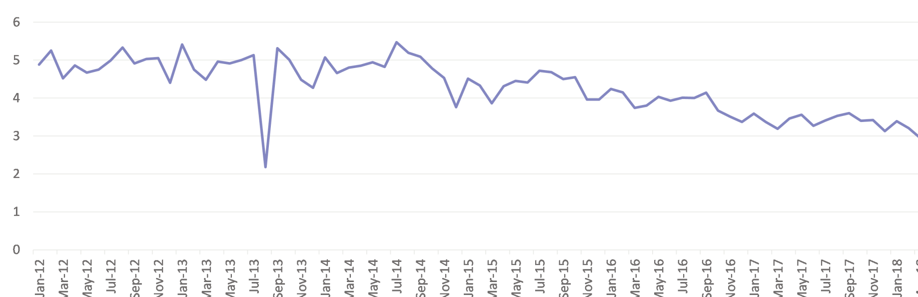


Central America & Caribbean, selected countries: GDP growth							
Quarterly figures are year-on-year growth							
GDP	**end 2017***	**2018 forecast***	**Q4 2016**	**Q1 2017**	**Q2 2017**	**Q3 2017**	**Q4 2017**
Costa Rica	3.9	4.1	4.1	2.9	2.7	2.8	3.2
Dominican Republic	4.9	5.1	5.9	5.3	3	3	6.5
El Salvador	2.4	2.5	2.6	2.3	2.3	2.4	2.4
Guatemala	3.2	3.5	3	3	2.3	2.7	2.9
Honduras	3.9	3.9	4.4	5.9	4.5	6.5	3.6
Nicaragua	4.9	5	3.8	6.6	4.3	3.2	4.3-
Panama	5.3	5.5	4.5	6.2	5.4	5.4	4.9
Jamaica	1.2	1.3	1.4	0.1	-0.1	range of 0.5%-1.5%	-
Trinidad & Tobago	-2.3	0.5	-6.9	-6.9	-3.2	3.1	-
**Figures from the United Nations Economic Commission for Latin America & Caribbean Dec 2017*							
Quarterly growth based on figures from the local central banks							

MEXICO & NAFTA

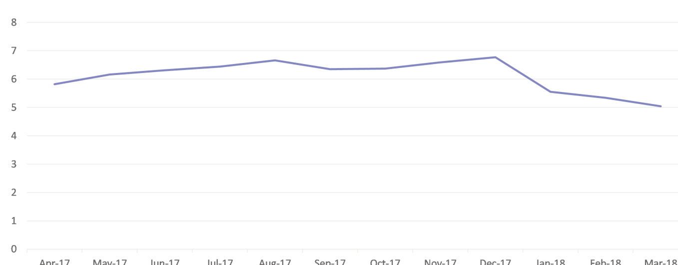
Mexico's unemployment rate

Economically active population



Mexico's inflation rate

Percentage variation (year-on-year)



Mexico's GPD

Percentage variation (year-on-year)

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

MEXICO

Mercurial AMLO

With the elections less than two months away, the economic policies of Andrés Manuel López Obrador (AMLO), the left wing nationalist leader of the Juntos Haremos Historia coalition, continue under scrutiny. While mistrusted by many in the business community, AMLO has continued to moderate his economic policy positions.

One thing is clear: AMLO has conserved his lead in the opinion polls, and is the candidate to beat – some would go as far as saying, barring any unforeseen and exceptional developments, that his victory is a *fait accompli*. One of the latest polls conducted in early May by BGC showed his support rising by two points on the previous month to 42%, nine points ahead of Ricardo Anaya (on 33%) at the head of the right-left coalition formed by the Partido de Accion Nacional (PAN) and the Partido de la Revolución Democrática (PRD). Former finance minister José Antonio Meade trailed in third place with 19% support.

An interesting reading of the electoral climate in Mexico came from a former opponent, Spanish political consultant Antonio Solá, a man many believe was behind a political 'dirty tricks' campaign against AMLO in the 2006 elections, which were won by Solá's then employer, Felipe Calderón (2006-2012). This time Solá says he expects AMLO to deliver a "historic" win with over 45% of the votes. In his opinion the politician has managed to continue presenting himself as the "anti-system" candidate, while at the same time reaching out beyond his core voters. In Solá's opinion he is being helped by the fact that his opponents are not strong candidates: Anaya has not yet fully developed his message and Meade struggles with the current government's poor record and "has nothing interesting to say to Mexicans". Solá said the PAN campaign slogan of 2006 – that AMLO was 'a danger to Mexico' – no longer applied. The candidate was however successfully channelling the "contained anger" felt by the Mexican electorate over the last "complicated" six years of the incumbent government.

The Mexican business community is not convinced. Many have been mistrustful of AMLO for many years. Old resentments surfaced again in early May when, during a campaign speech, AMLO named members of the business elite who he accused of conspiring against him in previous elections. He singled out Alberto Bailleres (of conglomerate Grupo Bal), Germán Larrea (of mining giant Grupo México), and Alejandro Ramírez (of cinema chain Cinépolis), and said "they are influence traffickers, not businessmen, who benefit from the current economic policy, from corruption". While these are among the richest men in Mexico there was no mention of the most powerful of all, Carlos Slim, of telecommunications giant América Móvil. The attack came against a backdrop of business concern over the candidate's commitment to reviewing the liberalisation of energy policies under the existing government and potentially to cancelling the US$13bn new Mexico City airport project. In April Slim had described the threat to cancel the airport project as being anti-business.

AMLO's statements drew return fire from the Consejo Coordinador Empresarial (CCE), one of the private sector's top lobby bodies, which published full-page advertisements in the national press under the headline "Así no" ("Not this way"). Bailleres, who is also a senior CCE official, said the candidate was "undermining confidence with these accusations and with this very aggressive discourse against the private sector". The paid advertisements insisted that Mexican entrepreneurs were "part of the solution, not part of the problem".

AMLO is clearly alternating a tough line with a more conciliatory position – a technique he seems to be using across various issues. In later statements on the airport, for example, he clarified that his main concern was that, as the project is currently structured, it will absorb too much public money – around half of all federal public sector investment. "Why don't we do a concession? I wouldn't have a problem," he said in a subsequent speech (the idea of a concession had earlier been floated by Slim). AMLO later said he wanted "peace and love" with business, and had issues only with a small group that had benefited from close ties with the government.

Where there does seem to have been some peace and love was in Mexico City on 7 May during a meeting between López Obrador and Larry Fink, chief executive of BlackRock, one of the world's largest asset managers. AMLO's team has been meeting international fund managers for some months now. Carlos Urzua, AMLO's adviser and potential finance minister, said the two men had an "affable" meeting during which they had "clicked". The candidate told Fink that under his leadership a future Mexican government would uphold the rule of law, fight corruption, and not expropriate private property. Fink was also due to meet the other main candidates.

Not all foreign observers are optimistic. Citibanamex, the local unit of US-based financial giant Citigroup, issued a report in May projecting that a "probable" AMLO victory in the elections would bring lower growth, higher inflation, and a weaker peso. The report said that by 2022 there would have been 0.7 percentage points less GDP growth, the peso would be 19% weaker against the US dollar, and inflation would be 23% higher (the numbers are calculated over the three years 2019-2022). Chief Economist Sergio Luna, the report's author, said the main problem would be the combination of electoral promises (such as holding back energy and basic food prices) and the threat to reverse pro-market structural reforms. These would eventually generate "macroeconomic inconsistencies". Luna emphasises that the other two candidates support the continuation of the structural reforms initiated by the present government. Goldman Sachs in contrast has been more optimistic, valuing AMLO's move closer to the economic mainstream on various issues. London-based Capital Economics is also seeing Mexico in a broadly positive light, commenting in April that "despite the growing prospect of an AMLO presidency financial markets appear relatively unfazed". It noted that in a letter to *El Financiero*, the candidate had promised to respect the independence of the central bank, the existing fiscal rule, and that he would review, rather than repeal, enabling legislation for big energy and construction contracts. Capital Economics does however think that the candidate's fiscal proposals are "unambiguously expansive", boosting growth in the short term but possibly storing up sustainability problems for the medium and long term.

Nafta renegotiation prospects slightly improved.

Although it remains difficult to assess the real state of the Canada-Mexico-US renegotiation of the North American Free Trade Agreement (Nafta) the signs in April and early May were broadly positive, if increasingly overshadowed by the Mexican election campaign. The difficulty is that both Donald Trump and AMLO have used populist and anti-trade rhetoric to appeal to domestic political constituencies. If AMLO is in fact elected as the next president of Mexico, there are many unanswered questions about how the negotiating dynamic between them will work.

What is known is that there has been movement on the automobile local content regulations, but no breakthrough. Canadian foreign minister Chrystia Freeland has spoken of "progress" at the talks. The US side is reported to want a deal done before the end of May. At the beginning of this month AMLO said (through economic adviser Graciela Márquez) that he might be ready to abide by any Nafta agreement if reached before 1 July, election day. Earlier suggestions by Trump via *Twitter* that a new Nafta deal might be conditional on immigration agreements to "stop people going through Mexico and into the US" were rebuffed by Mexican foreign minister Luis Videgaray.

ARGENTINA

Warning lights flashing

As this issue went to press Argentina was putting together emergency financial support from the International Monetary Fund (IMF) after a run on the peso forced the Banco Central de la República Argentina (BCRA) to tighten interest rates, at the risk of derailing the government's economic recovery programme.

As recently as last March we were pointing out that in terms of its ongoing fiscal and current account deficits Argentina remained one of the region's countries most exposed to external shocks. What seems to have happened in early May was only partly an external shock, but certainly a bout of negative market sentiment about the country's economic numbers.

The peso has been weakening against the US dollar for five months – losing around 18% of its value in the year-to-date. President Macri said on 8 May that in response to the run on the currency his government was seeking a flexible support line from the IMF. *Bloomberg* news agency said the credit line might be as much as US$30bn. In the preceding 10 days the BCRA raised its benchmark interest rate three times from 27.5% to reach 40%. The Buenos Aires stock exchange fell by 5.3% at its worst point on 8 May before recovering some of its losses. The peso stabilised on the same day at 22.48 to the US dollar. Treasury minister Nicolás Dujovne said "We're looking for preventive financing for Argentina to bring stability to the market. We've begun talks with the IMF to have a preventive line of credit, bearing in mind that the IMF have given support to our gradual programme."

Alfredo Ramos of Goldman Sachs said the request for IMF help was a positive development since it increased BCRA leverage and its ability to anchor the currency. But although officials have stressed their continuing commitment to a gradualist economic adjustment programme, the crisis is clearly an important setback to their plans and credibility. The run on the peso came amid general wobbliness over global emerging markets, but was also strongly influenced by scepticism over the government's fiscal adjustment programme, and the introduction of a new financial transactions tax for foreign residents that caused many investors to take refuge in US dollar assets.

Since March the BCRA has sold around 10% of its total foreign currency reserves in an attempt to counter peso depreciation, but with little success. It then moved to a second line of defence – tightening interest rates (of course, if interest rates are kept high for any prolonged period of time they could force an unwanted slowdown in the level of economic activity). According to Miguel Kiguel of consultancy Econviews, "Going for an IMF credit line is the least costly option in terms of Argentina's economic growth. It will help reduce country risk, and it will also allow access to credit for public-private partnerships." While this is a positive assessment, critics note that Argentina's current account deficit (5% of GDP) and high domestic inflation rate (around 24% per annum) are proving stubborn problems to treat.

ECUADOR

Fiscal consolidation efforts underwhelm

President Lenin Moreno unveiled his government's multi-year economic plan in early April, which aims to increase productivity, cut the fiscal deficit, promote investment, and generate employment. In mid-April, the government began to table measures in line with these goals, including a consolidation of the bloated public sector. Although the government's intentions are laudable, it remains highly unclear whether it will manage to

reduce the fiscal deficit and arrest a recent sharp increase in public debt without more significant revenue-raising measures, including tax increases.

Laudable aims

The underlying premise of the 2018-2021 Economic Programme for Fiscal Stabilisation and Productive Reactivation is solid: that economic growth cannot continue to be driven by fiscal stimulus, which in recent years has bolstered consumption but has come at the cost of spiralling levels of public debt. Instead, the administration is seeking to lift productivity, in an attempt to lift exports and thus enable cuts in government consumption. Making the business environment more friendly would also help diversify the economy, as well as bring in much-needed investment.

The plan outlines government efforts in four separate areas:

- **Fiscal stability:** involving efforts to reduce the deficit from an expected 5.6% of GDP in 2018 to just under 2.5% of GDP in 2021.

- **Public-sector restructuring:** including measures to improve the quality of public expenditure and cut the size of the public sector.

- **External sector:** boosting exports in order to improve the balance of payments and thus increase the sustainability of dollarisation.

- **Investment:** increasing productivity through strengthening operating conditions in the private sector

The plan is accompanied by 14 concrete measures that the government hopes to push through. Reflecting the importance of cutting the fiscal deficit, many of these relate to cost-saving measures, including saving US$1bn as a result of public-sector consolidation, including eliminating and merging ministries and secretariats. The government also hopes to raise US$810m over the 2018-2021 period by reducing tax evasion. In terms of improving the business environment, proposed measures include new tax incentives for foreign investors and better access to local finance.

Ministries set for merger

In mid-April, the government followed up on this plan with the unveiling of more details of the intended public-sector consolidation. Labour Minister Raúl Ledesma, together with the head of the national planning and development secretariat (Senplandes) Edison Garzón, announced that 1,000 civil service posts would be cut in the coming three years. In addition, 50% of the consultants employed by the public sector (amounting to 365) would be cut.

This will be partly achieved through a reduction in the number of ministries – which swelled under Moreno's predecessor, Rafael Correa – from 27 to 22. Rather than eliminating ministries altogether, this will be achieved by a merger of currently independent ministries, including Education and Sport, and Hydrocarbons, Electricity and Mining. By contrast, five public-sector entities will be eliminated, including the state cement firm, and a further four will be merged. There will be pressure on other state firms to improve their performance, perhaps with future concession sales in mind.

Forecast cost savings appear unrealistic

While the underlying premise of all of these efforts is positive, economists have generally reacted with some degree of scepticism regarding the extent of fiscal savings that the government hopes to generate though its plan. Saving US$1bn through public-sector consolidation is a large sum, equating to around 2.5% of total fiscal expenditure last year, and given that most ministries will be merged rather than eliminated, it is difficult to envisage that such a large sum can be saved. Equally, cracking down on tax evasion will be difficult without a significant increase in resources (which, given the fiscal policy stance, is unlikely), so revenue-raising projections may well also be missed.

Meanwhile, efforts to bolster the business environment may flounder. Not only does President Moreno lack an absolute parliamentary majority, but there is no firm domestic consensus on the requisite measures needed to attract investment. The president's falling approval ratings, which stood at 46.6% in April, down from well over 75% in mid-2017, may also act as a restraining factor. With no new revenue-raising suggestions (including tax reform), it is therefore likely to prove difficult to meet the government's ambitious goals for deficit reduction.

COLOMBIA

Solid report card from the IMF

The IMF concluded its annual Article IV consultation visit to Colombia on 27 April and was overall very positive about prospects for 2018, echoing earlier prospects that it had made earlier in the month about the economy being at a "turning point". Yet notwithstanding the fact that GDP growth seems to be staging a firm recovery, the Banco de la República (Banrep, the Central Bank) still opted to cut interest rates in the monetary policy committee's 27 April meeting.

The Fund was sanguine about Colombia's economic performance last year, pointing to an only slight moderation in GDP growth (from 2% to 1.8%), while highlighting that at the same time the authorities made progress on efforts at fiscal consolidation (with the public sector deficit falling from 2.9% to 2.5% of GDP) and inflation fell sharply compared with 2016, with an end-2017 rate of 4.1% only narrowly missing the Central Bank's 2%-4% target range. Meanwhile, higher average global commodity prices helped boost export earnings and reduce the current-account deficit to 3.4% of GDP, which remained mostly financed by inward flows of foreign direct investment (FDI).

Improving fundamentals

The IMF was clear that it believed that the outlook for 2018 was even more encouraging, with GDP growth forecast to rebound to 2.7% on the back of investment and export growth. The Fund does not expect stronger economic growth to spur inflationary pressures; on the contrary, at 3.5% its end-2018 inflation forecast implies a further decline in price pressures. The fiscal deficit is also projected to continue to edge downwards (to 2.5% of GDP), as is the current-account deficit (to 2.6% of GDP).

In line with the nature of Article IV consultation reports, Colombia's report card was not entirely rosy, with the Fund highlighting several weak areas, as well as flagging downside risks to its central forecast. The main area in which the IMF urged the Colombian government to focus its efforts is on developing the country's infrastructure, which for decades has been a comparative weak point of the business environment, in part a consequence of the long civil conflict between the state and various insurgent groups. Even though the left-wing Ejército de Liberación Nacional (ELN) remains active, a peace agreement with the larger left-wing Fuerzas Armadas Revolucionarias de Colombia (Farc) is in place, which should help foster conditions for greater investment in physical infrastructure projects. Other areas highlighted by the IMF include tackling labour market informality, improving education standards and cutting trade barriers.

Central Bank opts for further interest rate cut...

Despite the firm outlook for GDP and low inflation projections, the Central Bank nevertheless opted to cut its benchmark interest rate on exactly the same day that the Fund completed its Article IV consultation visit. This continued an official policy of monetary easing, which saw the Central Bank cut rates sharply over the course of last year, from 7.75% to 4.5%. The latest interest rate cut takes the policy rate to 4.25%. Prior to the monetary policy committee's

meeting, Finance Minister Mauricio Cardenas stated that the central question was not whether to cut rates or not, but by how much, with the Bank considering both a 25 basis points reduction, as well as a bigger potential cut.

...but then may keep rates on hold

In the press release accompanying the Bank's final decision (a 25 basis points cut), officials justified their decision to continue easing monetary policy by stating that inflation was falling more rapidly than expected and also that economic activity had not been picking up as strongly as they hoped. In their view, this provided scope for cutting interest rates further in order to bolster domestic demand without jeopardising the official 2%-4% inflation target.

The main question is now whether the Bank will continue to cut interest rates. The next monetary policy committee meeting is scheduled for June. However, the subsequent publication of inflation data for April suggests that monetary policy makers may prefer to keep rates on hold for the time being. The Bank cited March's low monthly inflation figure as a key reason for the interest rate cut (0.24%), but April's result was much higher (0.46%). Although in year-on-year terms inflation was little changed in April (3.13%), if monthly inflation continues to rise in the coming months, the year-on-year figure will start to rise.

REGIONAL BUSINESS REVIEW

PERU

Mining picks up pace

Mining has always played a central role in the Peruvian economy, and after a period of slackness and political uncertainty, there are signs that the industry is once more getting in gear.

Recent data from the ministry of energy and mines (Ministerio de Energía y Minas – MEM) has been positive. In the first quarter of this year mining investment rose by 30.2% on year-ago levels to US$839m. Most of this money was spent on infrastructure and processing plants. Current production has also been strong. In Q118 copper production rose 0.6% to 564,025 tonnes (Peru remains the world's number two copper producer after Chile). Iron ore production rose 26.1% to 2.828m tonnes. There were also increases in zinc output (+4.0%), tin (+1.1%), and molybdenum (+17.3%). Gold production fell by 6.2% during the quarter to 33.43m grammes, and there were also falls in silver and lead. National statistics institute INEI said that its index of mining GDP rose by 5.45% in March, an increase attributed to new legislative incentives, a production start-up by Shouxin Peru, and favourable international prices.

The economy and finance ministry (Ministerio de Economía y Finanzas – MEF) has focused on what it calls the start of a "new mining investment cycle in the economy". In a document on Peru's macroeconomic outlook in 2018-2021 it stresses that the global outlook for mining is good, and that Peru stands to gain from that. It describes 2017 as a "solid" year for global mining companies, noting that the market capitalisation of the world's top 25 mining groups rose by 35% last year, the second continuous year of growth. Global mining investment rose by 15.1% last year and according to forecasts by S&P Global Market Intelligence, will rise by a further 15%-20% this year. The MEF document says "In an international context of an improved outlook for mining we are seeing the start of a new investment cycle, with construction beginning on new mines, some of which are already at an advanced stage."

There are currently 49 new mining projects under development, valued at US$58.5bn. MEF believes 10 of the projects, worth roughly US$10bn, will see the start-up of construction work this year. This includes Anglo American's

Quellaveco mine (US$4.8bn), Marcobre's Mina Justa mine (US$1.35bn), and Chinalco's Toromocho mine (US$1.3bn). The importance of mining investment is that it often drives the wider business cycle in the country. Although there is significant non-mining investment also going on, the ebbs and flows of the mining sector tend to predominate. As the MEF's bar chart shows, private sector investment (in red) and mining investment (in grey) both contracted in 2014, 2015, and 2016. A recovery started in 2017 and is expected to continue this year, with mining investment leading the way.

MEF points out that Peru remains a very competitive player in the international mining scene, with lower average copper production costs than Chile, the United States, and China.

While strong mining investment and growth will have a positive impact on the economy, it is also true that some projects can have serious negative environmental and social effects, use up scarce water resources, and antagonise local communities. The new Peruvian government is seeking to reduce some of the social conflict that has arisen around mining. It is seeking to rely on the concept of social licences and the introduction of a deputy minister for territorial governance in February last year. As part of negotiating a mining concession the government now requires mining companies to pay into 'social funds' which are used to help local communities. Under the terms of the concession for the Michiquillay copper project reached in February, mining company Southern Copper agreed to pay US$600m into a social fund for the local community, which will also receive 50% of the royalties received by the government. Mining companies have also made direct contributions to local funds. The government meanwhile has developed two further programmes, Fondo de Adelanto Social (FAS) and Programa de Endeudamiento Garantizado (PEG). FAS allows the government to carry out early public works to reduce 'social deficits' in areas of potential mining development (although its initial budget is very small at PEN50m, US$15.2m). PEG – still under development – will allow local governments to borrow for public works, with future income streams from mining royalties used as collateral.

It remains to be seen whether some of the major projects that have been frozen as a result of local resistance or other issues can be got back underway. There have been some hopeful signs relating to Southern Copper's giant Tía Maria project. In April the company said it has reached an agreement with a rival group which says it has an overlapping land claim which it had been pursuing in the Peruvian courts. The company said it hoped to get the remaining government approvals so as to start construction during the

course of this year. The development of Tía María was put on hold in 2011 and again in 2015, when local farmers protested over what they said would be the loss of water. Germán Larrea, chairman of the Southern Copper board, said "We think that the new administration of President Martín Vizcarra will work to give us equitable investment conditions, supporting stability, economic growth and social progress in Peru." However, Prime Minister César Villanueva made it clear that he would not "impose" mining projects on communities without them freely agreeing a social licence.

CHILE

Mining production set to rise

In line with other large commodity producers, Chile is feeling the benefit of rising global prices on its local economy. Copper prices remain well below the highs of 2012, but have risen by around 50% from 2016 lows. This is stimulating investment in local mining projects, which is likely to feed through to higher GDP and export growth. Meanwhile, the authorities are considering a revision to the mining code in the face of rising competition from other producers in the region.

Chile's mining sector has had a disappointing few years, which has fed through to the broader economy through weaker GDP growth, a larger fiscal deficit, and lower export revenue. According to data from the mining index collated by the national statistics institute (Instituto Nacional de Estadísticas – INE) mining volumes fell by 1.7% in 2017, following a 2.8% contraction in 2016. This has fed through to weak underlying GDP growth, which came in at just 1.3% and 1.5% respectively in 2016 and 2017.

A turnaround?

Yet there are signs that the mining sector is recovering, with production rising firmly in year-on-year terms in recent months (5.8% in January, 17% in February, and 27% in March). Chile produces a range of mining products, including gold, silver, iron and coal, but mining is dominated by copper and an 18.9% increase in production during the first quarter of 2018, according to the copper commission Cochilco, is likely to have driven up overall mining volumes. Although this is partly flattered by a weak base for comparison, since copper output was suppressed in the first quarter of 2017 by a 43-day strike at the country's largest copper mine, Escondida, there are signs of rising production in other mines, indicating that the recovery in output is not entirely based on a return to normal production at Escondida. Cochilco is forecasting a 4.3% increase in copper production, to 5.76m tonnes, this year and a further increase to 5.94m tonnes in 2019, on the back of rising output at mines including Antofagasta's Antocuya, KGHM's Sierra Gorda, and Lumina Copper's Caserones.

Revisions to mining code are possible

Despite this forecast increase, the newly-inaugurated government led by President Sebastián Piñera is not resting on its laurels. Conscious that Peru is targeting rapid growth in its own copper production (*see the previous article in this issue*), the new government is mulling some revisions to the mining code in order to attract more investment, as well as ensure that investment leads to a consequent increase in exploration (large miners tend to hold onto concessions without active exploration). In order to address this problem, the new mining minister Baldo Prokurica has stated that the government is considering alterations to the mining code to compel companies that own concessions to actively exploit them. Other changes under consideration include providing greater assistance to the process of securing a mining license, as well as measures to encourage investment from small- and mid-sized mining companies.

Corporate Radar

Kroton expands again: Kroton, Brazil's largest private education company, said in April that it had acquired a controlling stake in Somos Educação, a group focused on the pre-school, primary, and secondary education segments. The takeover transaction totalled BRL6.2bn (US$1.79bn). Of this, the lion's share will go to Tarpon, an asset manager that held a controlling stake in the target company, with payment also likely to go to GIC, Singapore's sovereign wealth fund, which holds a minority stake. As a result of the transaction Kroton becomes the leading company in Brazilian education with net revenues of BRL7.5bn (US$2.17bn) and a market capitalisation of nearly BRL29bn (US$8.4bn). Analysts said Kroton was particularly interested in acquiring Somos Educação's Pitágoras learning system.

Chevron in trouble in Venezuela: US oil company Chevron was reported to have evacuated various executives from Venezuela after two employees were arrested in connection with a contractual dispute with state oil company PDVSA. The arrests were the first since a government crackdown on PDVSA employees and contractual partners last year, in which 80 people were arrested. According to sources cited by *Reuter's* news agency the two arrested executives could be charged with treason because they refused to sign an equipment supply contract. Chevron did not immediately comment although it acknowledged it was dealing with "personnel issues" in Venezuela; it said that as it sought to resolve them, oil production was continuing normally. According to opposition website *Caracas Chronicles*, the two executives had been arrested because they refused to sign a supply contract issued under an emergency decree which skips the competitive bidding process. Prosecutors say these decrees have been used as part of a bribery network. The implication, according to the *Chronicle*, was that the executives faced the prospect of years in jail "for refusing to go along with corruption". The incident, the *Chronicle* said, "has to stand as one of the most aberrant and self-destructive episodes of today's Venezuela".

JP Morgan on lithium options: Australian mining company Galaxy Resources said at the end of April that it had hired JP Morgan Australia to study strategic options for the development of its lithium and potassium project, known as Sal de Vida, in northern Argentina. Sal de Vida is considered one of the world's largest undeveloped lithium deposits. Galaxy had earlier put development work on hold amid reports in the Australian media that it was in talks to sell its stake in the project to Chinese or South Korean investors. According to current estimates Sal de Vida could generate around US$354m in annual revenues by producing 25,000 tonnes of lithium carbonate and 95,000 tonnes of potassium chloride. Galaxy said that it would reveal details of a feasibility study to develop the project in May.

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