INTER-AMERICAN DIALOGUE'S
LATIN AMERICA ADVISOR

FEATURED Q&A

How Can 'Mexico Cluster' Countries Foster Economic Growth?

Q A recent study by the Inter-American Development Bank concluded that, as a region, Latin America is recovering from the financial crisis in two distinct clusters. Countries that are net exporters with relatively strong ties to emerging markets and low dependence on remittances, as exemplified by Brazil, are 'very well positioned' in the new global environment. Conversely, economies with much stronger ties to industrialized countries, as illustrated by Mexico, are experiencing slower growth. How can countries belonging to the 'Mexico cluster' catch up to their 'Brazil cluster' counterparts? What trade and economic policies should those governments implement to encourage faster growth?

A Sergio Bitar, visiting senior fellow at the Inter-American Dialogue and former Chilean minister of mining, education and public works: "This new report from the Inter-American Development Bank proposes the existence of two 'clusters' in Latin America, the Mexican, which is expected to grow slowly, and the Brazilian, quickly. But, will be there two speeds in Latin America? Its data is solid and the conclusions are provocative. It challenges the reader, who knows that there is not such determinism, to seriously think about the policies and reforms that can lead each country down a positive economic path. Today, the future looks promising for Latin American countries: expansion of exports, high demand for natural resources at attractive prices, driven by Asia, substantial capital inflows and low interest rates. Also, most Latin American countries feel confident because they have comparatively good macroeconomic, social and political management. Nonetheless, nothing is guaranteed, neither rapid growth for South Americans nor slower growth for Mexico and Central America. Brazil and other South American nations should manage the risks of overheating, inflation and fur-

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Fujimori Gaining on Humala in Latest Peru Presidential Poll

Lawmaker Keiko Fujimori, pictured at a campaign event last month, is virtually tied with her rival, former army officer Ollanta Humala in a poll released Wednesday, a month before Peru's runoff election. See story on page 2.

File Photo: Fujimori Campaign.

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NEWS BRIEFS

Haiti Cholera Outbreak May Surge With Spring Rains

There has been a rise in new reports of cholera in rural Haiti, sparking worries that the spring rains may bring a surge of new cases, said Kathryn Mahoney, a spokeswoman for the aid group Partners in Health the Associated Press reported Wednesday. She added that the number of new patients in Mirebalais has tripled. Doctors Without Borders, however, has seen small spikes but does not expect to see a second peak of the disease, which has killed nearly 5,000 and sickened 250,000.

Protests in Argentine Province Continue Crimping Oil Output

Argentina's government on Wednesday acted to defuse strikes that threaten the country's fuel supplies, but demonstrations continued to hamper oil production in Santa Cruz province, Reuters reported. The Labor Ministry extended a round of talks between energy companies and refinery workers for five days and ordered conciliation for truckers who temporarily stopped fuel distribution in Buenos Aires province due to demands over pay. The refinery workers are demanding a 36 percent pay increase.

Brazilian Regulator Approves BTG Acquisition of Panamericano

Brazil's antitrust regulator, CADE, on Wednesday approved investment bank **BTG Pactual**'s acquisition of troubled local bank **Banco Panamericano** with no restrictions, Dow Jones reported. BTG agreed to buy billionaire Silvio Santos' 51 percent stake in Panamericano for 450 million Brazilian reais ($281 million). Brazil's state-run Caixa Econômica Federal owns the other 49 percent of Panamericano.

Political News

Fujimori, Humala in Virtual Tie a Month Before Peru Runoff

Keiko Fujimori, a right-leaning lawmaker, has caught up to leftist Ollanta Humala a month before they face off in the second-round of Peru's presidential election a month from today, according to a poll released Wednesday, Reuters reported. The Ipsos Apoyo poll shows Fujimori, the daughter of jailed former President Alberto Fujimori, with 38 percent support. Humala, a former army officer is just one percentage point ahead in the poll, which has a margin of error of 2.2 percentage points. The survey was conducted between April 23 and 30. In the pollster's previous survey, published 10 days ago, Humala led Fujimori 42 percent to 36 percent. The survey released Wednesday led stock prices to surge in Peru. The IGRA stock index soared 6.12 percent, its largest one-day gain since November 2008. "The market is pricing in that Keiko could be the next president," José Menor, an analyst at Lima's **Juan Magot** brokerage, told Reuters. Since losing the 2006 presidential election, Humala has moderated his tone, but he still causes concern among investors who believe he may roll back the free-market reforms of Alberto Fujimori. Humala has said the country must do more to lift poor Peruvians out of poverty and has also tried to soothe investors by promising to curb inflation, keep the budget balanced and respect the country's free-trade agreements. Fujimori, whom investors have favored, has a graduate degree in business from New York's Columbia University, but many also dislike her because of her father's convictions for human rights abuses and corruption. The Ipsos Apoyo poll was the second in the past week that has shown Fujimori gaining on Humala. On Friday, a Datum poll showed that Humala had 41.5 percent support among voters, while Fujimori had 40.3 percent.

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> *— José Menor*

Company News

Internal Bribery Probe at Avon Widens to Latin America Operations

An internal investigation by cosmetics seller **Avon Products** into potential bribery of foreign officials has found millions of dollars in questionable payments made to officials in countries including Mexico, Brazil and Argentina, *The Wall Street Journal* reported Wednesday, citing an unnamed person familiar with the matter. The amounts of money involved are "not insignificant," the person said. The probe originally focused on possible bribery of officials in China, but has expanded to look at similar activities in other countries. The company has also found questionable activity in India and Japan. The activity happened from as early as 2004 until last year. The Foreign Corrupt Practices Act, which became law in 1977, makes it illegal to bribe officials of foreign countries. One employee connected to operations in those countries has been suspended and additional suspensions are possible, the person told *The Wall Street Journal*. Separately, the New York-based beauty products seller said Tuesday in a filing with the Securities and Exchange Commission that it fired its former head of global internal audit and security and three top executives in China due to bribes that were paid for improper entertainment and travel expenses for Chinese officials. Avon had suspended the executives last year. "Pending the outcome of the internal investigation and compliance reviews, additional personnel actions may be taken in the future," Avon said Tuesday in the SEC filing. "The allegation that triggered our investigation was in China. Conducting compliance reviews in additional markets is the appropriate thing to do in investigations of this type," the company said Wednesday, adding that it "has made regular, timely and material disclosures since the internal investigation began in 2008, including our most recent Form 10-Q filing on May 3." The probe began after an employee wrote to Avon's chief executive officer, Andrea Jung, alleging that company executives were involved in improper spending with Chinese officials. Avon is holding its annual meeting today, where shareholders are likely to express concerns.

Jung

File Photo: Avon Products.

Brazil Helps Boost Mapfre to 14 Percent Rise in Profit

Spanish insurer **Mapfre**, the country's largest insurance company by market value, on Wednesday reported a 14 percent increase in net profit for the first quarter, fueled in part by the company's activities in Brazil, EFE Dow Jones reported. Mapfre's profit from its international direct insurance operations grew to 134.7 million euros ($199.7 million) in this year's first quarter as compared to 53 million a year earlier. A capital gain related to Mapfre's joint venture with Brazilian lender **Nossa Caixa** boosted the first quarter earnings. Profit from direct insurance in Spain contributed 204.7 million euros in the first quarter, a decline from 230.6 million a year ago. Mapfre's international business will soon see a boost from a agreement with **Banco do Brasil**, through which the Spanish company will distribute insurance products in the South American country, said Esteban Tejera, Mapfre's general director. Operations outside of Spain contributed 40 percent of the company's earnings last year, he added. Mapfre suffered a 64.1 million euro loss related to this year's earthquakes in Japan and New Zealand. In last year's first quarter, Mapfre took an 80.8 million loss due to the earthquake in Chile. The company's total revenue increased 4 percent in the quarter to 6.13 billion.

Featured Q&A

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ther appreciation of their currencies to avoid a slowdown. Then, they must increase their rates of investment, promote specialization and innovation. Mexico and the small countries of Central America can implement reforms to elevate agricultural and oil production, which are in high demand in international markets. All countries should improve education, science, technology, infrastructure and the qualities of public and private services and acquire a strong command of information technologies. Higher productivity is the critical issue. We also know that good economic management is not enough. Mexico and Central America need to contain the threats of organized crime and strengthen democratic institutions. And all societies must expand citizens' participation, and enhance social inclusion. As the future is not predetermined, we should intensify the debate on how to define a sound program, to articulate internal consensus and leadership to make this a really great decade for Latin America. If governments are complacent or negligent, they will lose a good opportunity. If they are ambitious and persistent they can progress substantially."

A **Diana Villiers Negroponte, nonresident senior fellow at the Brookings Institution:** "The massive reallocation of production, trade and capital to the 'Brazilian cluster' has considerable bonuses for economic growth, but it poses additional macroeconomic challenges to the region, including pressure on the exchange rate. Since 2006, Brazil and the other BRIC nations have seen record inflows of both foreign direct investment and payments for commodities. Such inflows create rapid expanded growth and the need to channel these new monies into long-term productive capital projects. Chile has wisely created a Norwegian-type trust fund to ensure that present strong inflows can still be enjoyed over the longer term. The attraction of the 'Brazil cluster' is not necessarily a lasting phenomenon, but can evaporate relatively quickly with the discovery of new commodities and preferred suppliers. Historically, this occurred with 19th century British colonial investments in the nitrates of Peru. The 'Mexican cluster' suffers from its close commercial ties in goods and services with industrial countries and its reliance on remittances. The severe downturn in industrial production and construction impacted those countries directly and demand levels have declined relative to emerging economies. Recovery cannot depend alone upon the 2011 uptick in manufacturing capacity in the United States, although increased production of cars and light trucks to its 2008 level of 13 million units and heavy duty trucks to 265,000 will stimulate production of automotive parts. For both the 'Mexican cluster' and the 'Brazilian cluster,' future economic growth depends upon the development of a quality workforce. Education and innovation are critical to raising production levels, competing with lower-wage economies and raising standards of living for all workers."

A **Nora Lustig, professor of Latin American economics at Tulane University and nonresident fellow at the Center for Global Development and the Inter-American Dialogue:** "The two clusters mentioned in the IDB's report precede the global financial crisis. The 'Mexico cluster' grew slowly even when the U.S. economy was booming. The global crisis has exacerbated a trend that started—both symbolically and to a large extent in reality—around 2000, when China joined the World Trade Organization. In the 'Mexico cluster,' countries do not grow because capital accumulation is slow: public investment is limited and returns to private investment are low. Catching up will depend on higher returns to private investment and shifting output toward high-growth/high-productivity sectors. Keeping the currency from appreciating (and, going

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even further, keeping it depreciated), higher rates of public investment in infrastructure, targeted productive development policies, access to finance at reasonable interest rates and developing strategic ties with the countries on the rise could raise the return to private investment and spur growth. Limited fiscal space and wiggle room in monetary policy make implementing these policies challenging. Does the 'Mexico cluster' have a sector that can benefit from the expansion of emerging Asia? A natural candidate is tourism. China, for example, is not far from having millions of people joining the middle class. The 'Mexico cluster' should take advantage of it. Except for smaller countries, however, tourism may never reach a path-changing size. One interesting fact to note is, while there is one region and two speeds in economic growth, the decline in inequality experienced by Latin America during the past decade happened equally in the two clusters. There were no two speeds."

A Maria Velez de Berliner, president of Latin Intelligence Corporation: "The Mexico 'cluster' (including Central America) exemplifies how reliance on one major trading partner (the United States) skews trade and economic policy. While the 'Brazilian miracle' is an attractive growth model, policies aimed at catching up with it would be distorting, too. 'Clusters' do not have the industrial might and ample supply of natural resources Brazil has, nor is their participation in the global economy as deep and broad as Brazil's. Therefore, the internally generated growth potential of 'clusters' is limited and cannot compare with Brazil's. Trade and economic policies that create sustainable growth demand a dependable environment that guarantees personal security and investment confidence. Despite claims to the contrary by 'cluster' governments, including Mexico, the on-the-ground reality is that personal and investment security in those countries is tenuous. Despite high levels of criminality in Rio de Janeiro and São Paulo, Brazil is not besieged by the internal insecurity of Mexico and its 'cluster.'

> "Despite high levels of criminality in Rio de Janeiro and São Paulo, Brazil is not besieged by the internal insecurity of Mexico and its 'cluster.'"
>
> — *Maria Velez de Berliner*

It is hard to commit to a long-term investment strategy when local and foreign investors do not know whether a partner would be kidnapped, assaulted or, worse, assassinated, or when the investor's operations might lie in the line of fire. Witness the exodus of the business community from Monterrey. Nor does it create confidence when investors cannot predict which direction policy would take when public and private institutions are infiltrated, or threatened, by corrupt, colluding officials or criminal elements. These conditions generate levels of insecurity that increase uncertainty and raise operational costs. With the exception of speculators, human and financial capital favors safe, predictable environments with low levels of uncertainty. Therefore, policies that reduce criminality, corruption and uncertainty are what 'cluster' countries need to generate growth that remains sustainable over time, thus enhancing the value added of limited resources."

The Advisor *welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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