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Inter-American Dialogue

LATIN AMERICA ADVISOR

Featured Q&A *With Our Board of Advisors*

Q **Caught between foreign energy companies on one side and hard-line political opponents on the other, Bolivian President Carlos Mesa must decide soon on whether to sign into a law a controversial hydrocarbons bill that imposes a 32 percent direct tax on foreign oil and gas companies—and pleases no one. What would ensue in Bolivia if Mesa signs the bill? Would the foreign firms, who think the tax is too high, halt investments? Would political opponents, who think the tax is too low, once again threaten to paralyze the country? What would the international community, including the International Monetary Fund, do? Is Bolivia headed toward nationalization of its hydrocarbons sector?**

A **Guest Comment: Ivan Rebolledo:** "If the past is any indication, protests and chaos will soon begin—yet once again. President Mesa is more than likely to veto the new hydrocarbons law in coming days due to the fact that the law is unfriendly to investors and jeopardizes the state of the economy and the government's fiscal sustainability. On the other hand, an executive veto gravely threatens political stability and the president's tenure in office, as it will inevitably spark social and political conflicts. The future of President Mesa will depend on these protests and how quickly they expand to include diverse sectors of the population, especially if deaths result from the rather certain violence. Less radical elements of the left and center—attempting to heighten their national status—as well as members of conservative traditional parties hoping to protect their political future from a growing leftist populism could also join in protests. It is also important to keep in mind that Mesa's very healthy popularity (54 percent in urban settings) could keep him afloat through short-term negative social and political reactions were they limited to the most extreme elements of Bolivian politics and society. If Mesa were forced out of office as a result of Evo Morales and his protests, Morales could easily be seen as the catalyst, surely harming his future political aspira-

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PHOTO OF THE DAY

The government of Colombian President Alvaro Uribe is requesting $130 million in additional counternarcotis assistance from the US. See story, page 2.

Photo: Casa Narino.

Inside This Issue

NEWS BRIEFS

Brazil Sells $500 Million in Bonds

The Brazilian government sold $500 million in bonds maturing in 2019. As a result of the bond sale, which reopened a $1 billion issue placed in October, Brazil has about $1 billion left to raise on international capital markets under its $6 billion borrowing program for this year.

Source: Reuters.

Colombia to Privatize Ecogas

The Colombian government said Tuesday it plans to privatize **Ecogas**, country's largest natural gas pipeline company, through a 750 billion-peso share sale. The government will first offer 75 million shares worth 10,000 pesos each to current and former employees, as well as to pensioners, making five-year loans available to finance share purchases. Any leftover shares will be sold in a second offering to private and foreign investors. Ecogas, which operates 3,644 kilometers of pipeline, transports natural gas from northern and eastern Colombia to the central part of the country. The International Monetary Fund has urged Colombia to sell the company as part of its loan agreement with the Andean nation.

Source: SNE, Reuters.

Fixed Gross Investment in Mexico up 7.4 Percent in February

Fixed gross investment in Mexico rose 7.4 percent in February compared to the same month a year ago, the finance ministry said Tuesday. Investment in machinery and equipment jumped 13.8 percent in February, led by an 18.9 percent increase in spending on imported items. For the first two months of this year, gross fixed investment was up 8.8 percent compared to Jan-Feb 2004.

Source: finance ministry.

Political News

Mesa Rejects Hydrocarbons Bill, Returns it to Congress for Changes

Bolivian President Carlos Mesa announced Tuesday he would not sign into law a controversial hydrocarbons bill and would send it back to the country's Congress for changes, saying the bill as drawn up is too divisive, Reuters reported. "The unity of Bolivia is at serious risk ... This law is an instrument to divide Bolivia," Mesa was quoted as saying during a nationally televised address last night. Bolivia's Congress passed the bill, which would slap a 32 percent non-deductible direct tax on foreign oil companies, last week, despite opposition from the companies, which said the bill would put investment in the sector at risk, and from Bolivia's powerful Movement Toward Socialism party, which is demanding Congress approve a 50 percent royalty on oil companies. The bill also threatened to jeopardize Bolivia's loan agreement with the International Monetary Fund.

> "The unity of Bolivia is at serious risk ... This law is an instrument to divide Bolivia."
>
> *– Bolivian President Carlos Mesa*

Colombia Asking US for $130 Million More to Fight Drug War

The Colombian government has requested an additional $130 million in counternarcotics assistance from the United States in the face of a renewed outbreak of coca cultivation, local daily *El Tiempo* reported Tuesday. The money was officially requested a few weeks ago to intensify fumigation and eradication efforts in the regions of the country where coca cultivation is most widespread. According to US congressional sources cited by *El Tiempo*, the government would use the funds to purchase at least 12 aircraft to establish a mobile fumigation unit to root out the resowing of coca and poppy crops. Despite the fumigation of a record number of illegal crops in 2004, the US Central Intelligence Agency said the amount of planted coca remained the same, demonstrating that coca farmers and drug traffickers have been successful in relocating their operations. Colombian National Police have told President Alvaro Uribe that more resources are necessary to combat the replanting. If approved, the supplementary aid would be in addition to the more than $600 million the US will likely send in continued support of Plan Colombia—the country's five year-old counternarcotics strategy—as part of the 2006 budget now being debated in Congress. The House International Relations Committee has scheduled a hearing for this afternoon to evaluate the progress of US involvement in Colombia. Witnesses scheduled to testify at the hearing include Office of National Drug Control Policy Director John Walters and US Assistant Secretary of State for Western Hemisphere Affairs Roger Noriega. Speaker of the House Dennis Hastert will also testify on Plan Colombia. In next year's budget, the Bush administration has requested an additional $463 million in funding and $90 million in foreign military financing for Colombia, according to the committee.

Economic News

World Bank to Provide up to $780 Million to Guatemala

The World Bank announced Tuesday it plans to provide up to $780 million to Guatemala over the next three years to reduce poverty in the Central American nation. In a statement, the Bank said it would support a new assistance program of between $460 million and $780 million for Guatemala from 2005 until 2008. The program aims to slash extreme poverty in Guatemala, where more than half the population is poor, by 50 percent between

1990 and 2015 by increasing public spending on human development and infrastructure, and by contributing to real economic growth of 5 percent per year. "The current policy environment in Guatemala is a window of opportunity to move forward on a more inclusive, accelerated growth and poverty reduction path," Jane Armitage, the World Bank's country director for Central America said. Guatemalan President Oscar Berger assumed office early last year with broad popular support, but that support has waned amid poor public security, economic performance below expectations, and political infighting [Editor's note: see a related Q&A in the February 18, 2005 issue of the *Latin America Advisor*]. The country's economy grew just 2.6 percent last year. The World Bank said the level of its assistance to Guatemala will depend on the government's ability to meet certain criteria, such as a stronger fiscal performance, increased governance and transparency, a reduction in inequality, and improved competitiveness.

Company News

Telecom Argentina Posts 279 Million-Peso First-Quarter Profit

Telecom Argentina reported a first-quarter net profit of 279 million pesos ($US 96.4 million), up from 124 million pesos for the same three months of 2004, Reuters reported. The company, which is controlled by **Telecom Italia** and local investment group **Grupo W**, attributed the year-on-year profit growth to an 84 percent increase in financial gains to 175 million pesos, as a strengthening peso currency lowered debt servicing costs in euros. The peso rose from 4.06 per euro at the end of 2004 to 3.78 per euro in March. Telecom Argentina's net revenues increased 22 percent year-on-year to 1.237 billion pesos during the first quarter due to an expansion of the company's mobile business, which accounts for about 40 percent of consolidated revenue. Telecom Argentine had 4.223 million mobile customers at the end of the first quarter, up 48 percent from the end of the fourth quarter of last year.

The Dialogue Continues

A continuation of the May 10, 2005 Q&A

Q Argentine officials, including President Kirchner, reportedly complained last week that Brazil's ambitious foreign policy agenda is coming at the expense of Argentina and other partners in the Mercosur trade bloc. What's behind the Argentine complaints? Are Brazil's Mercosur partners right to resent Brazil's foreign policy ambitions, or is Argentina, as one Brazilian newspaper put it, simply "whining"? Are Brazil and its Mercosur partners better off going their separate ways?

A Guest Comment: Arturo Porzecanski: "The belligerent attitudes displayed by the Kirchner administration toward Brazil are just another facet of the pattern of abuse heaped at multinational corporations, foreign bondholders and the IMF—abuse that is consistent with the neonationalist, neopopulist ideology of Peronism and which, by projecting an image of presidential *machismo*, helps an inherently weak Kirchner to stay in power. The fact is that Argentina's trade deficit with Brazil has been widening—it more than doubled versus last year during January-April—but there is no objective reason why this should lead to trade and other frictions with Brazil. After all, Brazil is the natural supplier of many processed and manufactured goods to Argentina; if Kirchner really wants Argentina to be more competitive, he should get off his white horse and start improving the country's poor investment climate."

A Guest Comment: Marisa Ferreira: "Despite Kirchner's complaints, Brazil and Argentina are closer than ever. Both countries are partners on a number of fronts and most recently have embarked on a continental energy integration plan. While historically they were rivals for regional leadership, Brazil—due to its size, economic weight, and political stability—has enhanced its role as a key moderator among its Latin American neighbors. Lula's presidency has marked an even more proactive foreign policy, traditionally known for its 'potential for conciliation.' Brazil has played a prominent international role in pursuing successful actions at the WTO against EU sugar and US cotton subsidies; maneuvering to secure a seat on the UN Security Council and the directorship of the WTO; and developing strategic alliances with China, India, South Africa, and the Arab countries. Moreover, both countries are at present facing different economic challenges. Brazil is enjoying a trade surplus and continues to attract foreign investment, whereas Argentina is rebuilding its economy after the 2001 collapse. Argentina has expressed its discontent about the asymmetry in their partnership and the politically charged commercial deficit it is experiencing with Brazil, just before Brazil's hosting of a summit with leaders from more than 30 Arab and South American countries. Adjustments within the neighborhood must be attained in the near future, if both countries are willing to make Mercosur a winner project."

Arturo Porzecanski *is an Adjunct Professor of Economics at New York University and former Chief Economist for Emerging Markets at ABN AMRO.*

Marisa Ferreira *is a Foreign Associate at Schmeltzer, Aptaker & Shepard.*

Featured Q&A
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tions. The new law has been criticized as diametrically opposed to the investment and the economic interests of Bolivia. The bill includes the forced migration of all contracts to the new terms in six months; the nationalization of hydrocarbons at the wellhead; the immediate application of a new tax regime that raises royalties to 18 percent and total taxes to 32 percent, without the possibility of deductions of other corporate taxes; the recapitalization of YPFB; the obligatory consultation of indigenous communities residing in areas where hydrocarbons projects would be undertaken, and a pricing regime that is not reflective of market prices. Promulgation of this law severely risks ongoing relationships with the IMF and other IFIs and bilateral donors, that are paramount to the government's fiscal well-being and who have already conditioned their future relationship with Bolivia on its continued respect for policies that support fiscal stability, international investment and contract law, and good governance."

A **Guest Comment: Phillip McLean:** "President Carlos Mesa now must solve a puzzle of his own making. Before he entered politics in 2002, Mesa was a popular television pundit who dispensed clever advice nightly to the country's leaders. Since becoming Bolivia's president in October 2003, following bloody confrontations between the military and protesters that resulted in 80 deaths, his highest priority has seemed to be the avoidance of a repetition of those tragic events. The referendum he put before the country last July was supposed to sooth tensions and give the public a stake in the choices the government would make on energy policy, one of the explosive issues animating the 2003 demonstrations. The referendum, however, was so broadly worded that, while it was approved, it resolved nothing. Now the Congress has tried to put voters' wishes into law, but the result is, like the referendum, ambiguous and pleases few. It is clear that Bolivia is about to retreat from the investor-friendly energy policy of recent years—that *inter alia* led to a huge increase in the country's gas reserves—but what energy companies, the country's creditors, and its friends abroad are above all looking for is a credible legal structure for energy development, virtually Bolivia's only export prospect. No one is better placed to do that than President Mesa."

A **Guest Comment: Manuel Rocha:** "Compromise or walking the middle ground usually pacifies opposing sides. One can argue that this is what the current bill tries to do, and that would be what President Mesa would argue he is doing were he to sign it into law. However, in the case of Bolivia the current hydrocarbons bill pleases no one, which means that the civil strife that has been going on for some time is bound to continue and could get worse. In the meantime, the foreign energy companies must reconsider whether it is at all worth it to continue to invest and do business in Bolivia. This will only continue to hurt the Bolivian people, who—blessed with generous energy reserves—cannot use these resources to address their most important and basic needs. The lack of a national consensus on how best to manage their tremendous oil/gas wealth is prolonging the suffering of the vast majority of Bolivians."

Ivan Rebolledo *is President of the Bolivian-American Chamber of Commerce.*

Phillip McLean *is a Senior Associate at the Center for Strategic and International Studies.*

Manuel Rocha *is Managing Director of The Globis Group LLC and a former US Ambassador to Bolivia.*

Editor's note: In a nationally televised speech last night, President Mesa announced that he would not sign the hydrocarbons bill into law and that he would send the bill back to Congress for changes. See related story on page 2.

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