

Inter-American Dialogue

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Featured Q&A With Our Board of Advisors

Q Nearshoring, the trend in outsourcing businesses to nations that are closer, both culturally and geographically, is continuously increasing. To what extent are we seeing this trend in Latin America? What are the top destinations in the region for nearshore investments? What steps could countries in the region take to boost their attractiveness for nearshore investment?

A **Board Comment: Rui da Costa:** "Nearshoring is not a new phenomenon, but its current popularity is clearly a reflection of the benefits US companies have found in extending their businesses into Latin America. As such, there is opportunity today for Latin America to join China and India as a competitor in the world market for high value goods. The increase in direct capital investments from abroad is the result of many factors. First, Latin American countries are taking vital steps to improving their economic competitiveness, making the region an attractive destination for direct foreign investment ... Another factor contributing to direct foreign investment are multilateral trade agreements, such as NAFTA and the recently signed CAFTA, which provide structural incentives for US companies to look south. These incentives include reduced trade barriers, improved labor conditions, and stronger legal systems that ensure the protection of intellectual property. Also key is the success of Latin

America's cluster model. Clusters of firms active in the same sector can significantly improve their competitive performance by learning from each other and working together to move up the value chain, upgrade production processes, and develop new or improved products. One of the strongest examples is the IT cluster in Costa Rica. Nearshoring isn't a new activity for Costa Rica. Since 1995, over 30 foreign electronics firms have located plants there, including HP, Intel, Microsoft, Lucent Technologies and Siemens. For over 30 years, Costa Rica has built a comprehensive educational system and emphasized the presence of IT in the curriculum. A tremendous effort has gone into ensuring that educational facilities produce appropriately skilled knowledge workers and professionals to contribute to the develop-

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PHOTO OF THE DAY



Brazilian President Luiz Inacio Lula da Silva, center, formally announced Saturday he would run for re-election in October. See story on page 2.

Photo: Agencia Brasil.

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NEWS BRIEFS

Chavez Announces Appointment of New Defense Minister

Venezuelan President Hugo Chavez said Saturday he would appoint Gen. Raul Isaias Baduel as defense minister, "effective in the coming days," the Associated Press reported. Baduel, who helped lead forces that helped return Chavez to power after he was briefly overthrown by dissident officers during an April 2002 coup, will replace Adm. Orlando Maniglia. Chavez did not say why he was making the change. Baduel said Venezuela needs to prepare for an "asymmetrical war," echoing a term often used by Chavez, who accuses the United States of planning to invade Venezuela.

Lawmakers in Panama to Debate Canal Expansion Proposal

Panamanian lawmakers are expected to start debating today President Martin Torrijos' \$5.25 billion proposal to expand the Panama Canal, Reuters reported. Approval of the plan is considered a foregone conclusion, since Panama's ruling party has a majority in the legislature. After it is approved, the proposal faces a constitutionally mandated popular referendum.

Bolivia to Sue Enron Execs, Former Officials for Fraud

The Bolivian government said Friday it would sue former executives of US energy company **Enron** as well as ex-government officials for fraud in relation to a natural gas pipeline to Brazil built in the 1990s, Reuters reported. Among those slated to be charged is ex-President Gonzalo Sanchez de Lozada. Energy Minister Andres Soliz said Enron paid bribes and made illegal profits, which the government will attempt to recover.

Political News

Venezuela Rejects Peru's Complaints About Chavez's Comments

In the latest diplomatic spat between Venezuela and Peru, Venezuela on Sunday rejected Peruvian complaints that President Hugo Chavez meddled in Peru's affairs last week when he called incoming President Alan Garcia a "lapdog" of the United States and said Garcia had won Peru's election fraudulently. In a statement, Venezuela's ministry of foreign relations said Chavez's comments, made late last week during an official visit to Panama, were in response to attacks by Garcia. "[Chavez] limited himself to responding to the insults hurled against him by Mr. Garcia, who far from giving signals of bringing about a detente in

cannot have relations with such an irresponsible government, with such an irresponsible president, no way," the Venezuelan president was quoted as saying by Reuters. The two governments withdrew their respective ambassadors earlier this year after Chavez exchanged insults with Garcia and Peru's outgoing president, Alejandro Toledo.

Lula Formally Declares Candidacy for Re-election

Brazilian President Luiz Inacio Lula da Silva on Saturday formally declared his intention to run for re-election in October. Lula, who the latest polls show would easily win a first-round victory on October 1, told a convention of his Workers' Party that he would step up his fight against poverty in Brazil and build on his government's economic achieve-

“While Alan Garcia is Peru's president and I am the president of Venezuela, quite honestly, we cannot have relations with such an irresponsible government, with such an irresponsible president ...”

- Hugo Chavez

bilateral relations, appears to put his self-promotion first through an attempted confrontation with [Chavez]," the statement read. Late last Thursday, Chavez ruled out relations with Peru under Garcia and said the incoming leader's victory over nationalist Ollanta Humala, whom Chavez openly supported, in his country's June 4 run-off election may have been the result of fraud at voting stations during ballot counting. "I was left with many doubts. I think Ollanta won the election," Chavez was quoted as saying by the Associated Press. Peru's foreign ministry responded on Saturday, noting the election was deemed free and fair by election monitors from the European Union and the Organization of American States, according to the AP. Chavez also called Garcia a "lapdog" and "tool" of the US, and ruled out relations with Peru. "While Alan Garcia is Peru's president and I am the president of Venezuela, quite honestly, we

ments. "I am once again a candidate to build on what is going right, correct what went wrong, and do lots of things I didn't have time to do," he was quoted as saying by Reuters. The Brazilian leader also said he would continue the country's assertive foreign policy stance. "Brazil today is more respected internationally, and, if we stay on the right path, we can consistently boost our role in the world," he said. Lula's election in 2002 prompted fears he would reverse the country's pro-market economic course, but his government has mostly pursued a conservative economic policy, limiting spending and maintaining high interest rates to slow inflation. Lula's popularity suffered last year amid revelations of a congressional bribe-for-votes scandal and allegation of illegal campaign contributions involving the PT. However, his popularity has since rebounded amid Brazil's recent positive economic performance, and polls show him easily defeating

his closest rival in the October election, former Sao Paulo state Governor Geraldo Alckmin of the Brazilian Social Democratic Party. Lula said Friday he plans to keep Vice President Jose Alencar as his running mate.

Economic News

WTO Chief Warns of Talks' Collapse

World Trade Organization chief Pascal Lamy warned Friday that global trade talks risked collapse without a breakthrough soon, Reuters reported. In a television interview, Lamy said the United States must take action on agricultural subsidies, the European Union on agricultural tariffs, and major developing countries on industrial tariffs. "If a deal on this key triangle of issues is not there soon, there is a risk that this whole round will fail," Lamy was quoted as saying. The WTO director-general's comments came ahead of a meeting of trade ministers this week. On Thursday, ministers from about 50 countries will meet in Geneva to try to forge a draft deal covering agriculture and manufacturing. "We need big political decisions to be taken now," Lamy said. The US and EU each insist it is the other's turn to make concessions, while developing countries such as Brazil and India are demanding more concessions on agricultural trade. [Editor's note: look for related Q&A in tomorrow's issue of the *Latin America Advisor*.]

Company News

Judge Cancels Sale of Varig After Employee Group Misses Payment

A Brazilian bankruptcy court judge on Friday canceled the sale of **Varig** after an employee group failed to make a \$75 million downpayment for the struggling airline, the Associated Press reported. Judge Luiz Roberto Ayoub said he would not take steps to liquidate Varig, which appears to be near financial collapse, having canceled scores of flights. The flight cancellations reportedly left hundreds of Brazilians in Germany for the World Cup



Election Watch: Mexico



A Round-up of Recent News Ahead of Mexico's July 2 Election

- According to two newspaper polls published on Friday—the last two polls allowed before this Sunday's vote under election rules—**Andres Manuel Lopez Obrador is locked in a statistical tie with Felipe Calderon**, the Associated Press reported.

In their polls, both *Reforma* and *El Universal* found voter support for Lopez Obrador of the leftist Party of the Democratic Revolution (PRD) at 36 percent, versus 34 percent for Calderon, of the conservative governing National Action Party (PAN). *Reforma's* survey of 2,100 registered voters was conducted June 17-19 and had a margin of error of 2.5 percentage points, while *El Universal's* poll of 2,000 registered voters from June 16-19 has a margin of error of three percentage points.



Photo: Lopez Obrador campaign Web site

- According to a survey by **Credit Suisse** released late last week, **60.6 percent of investors think Lopez Obrador will win this Sunday's election**, versus 39.4 percent who think Calderon will win. Among foreign investors, 68.9 percent predict a Lopez Obrador victory against 31.1 percent for Calderon. Local investors are more divided, with 51.1 percent seeing Lopez Obrador winning versus 48.9 percent for Calderon.

- In what was billed as his campaign's grand finale, **Calderon on Sunday warned that a Lopez Obrador presidency would be an economic "horror movie" for Mexico**.



Photo: Calderon campaign Web site

"We've seen this movie before," Calderon told as many as 100,000 supporters at the Azteca soccer stadium in Mexico City. "It's a horror movie that cost Mexicans dearly." Calderon was referring to Mexico's past experience with economic crises, including steep peso devaluations and soaring inflation caused by populist spending programs.

- Lopez Obrador said Sunday that his rivals—nervous about his possible election—**were tempted to commit fraud** to keep him out of office, according to *El Universal*. "They go with the temptation to commit fraud," said Lopez Obrador. Meanwhile, the PAN yesterday called the Federal Electoral Institute, or IFE, an "inefficient authority." PAN's representative before the IFE, German Martinez Cazares, said IFE had failed to enforce a resolution ordering the PRD to pull television spots accusing Calderon of supporting a controversial multibillion dollar bank bailout in the mid 1990s.

soccer tournament stranded. Ayoub confirmed that **VarigLog**, the airline's former cargo unit, had offered \$500 million to buy Varig, but said no decision would be made until consultations with the airline's creditors take place, probably this week. In a June 8 auction, the employee group, **NV**

Participaco, had offered to buy Varig for \$449 million, but failed to make an upfront payment of \$75 million by Friday. Varig, which declared bankruptcy a year ago, has been struggling to stave off collapse under the weight of some \$3.5 billion in debt.

Featured Q&A*Continued from page 1*

ment of Costa Rica. Despite the growth of nearshoring in the region, countries must take significant steps to attract FDI that focuses on high value industries, which pay higher wages and drive prosperity ... In addition to implementing stabilizing economic policies, countries must also invest heavily in education programs and information and communications infrastructure, and strengthen legal systems across the region to ensure the protection of intellectual property."

A **Guest Comment: Peter Ryan:** "Nearshoring is a trend that is driving US investment into Latin America. The key benefits of nearshoring are easy access in terms of travel, enhanced cultural/commercial familiarity with the onshore customer, and linguistic skills. US firms realize the ever-growing population and purchasing power of the domestic Latino market and are making bilingual labor (English and Spanish) a priority ... The top destination for nearshore investment is Mexico, where there are increasing numbers of US firms that have established contact center operations, in addition to a sizable home-grown outsourcing sector dedicated to serving the US market. In addition, the ongoing liberalization and political reform that has characterized Mexico, as well as most nations in Latin America, has not gone unseen by US investors. While other countries in Central America have also pushed their efforts to attract nearshoring investment from the US, Mexico is the only one that offers scalability and multiple urban locations ... Countries in Latin America have tremendous scope for developing their nearshore presence. Key steps to take in order to increase their viability include: lowering telco charges as much as possible and deregulating telephone service; working with the private sector to ensure a steady stream of qualified agents matriculate from educational institutes; reforming antiquated labor laws that may exist, which discourage investment; and ensuring that inflation and agent benefit growth is kept at a bare mini-

mum. Should a location be able to provide such stability, it has the potential to develop a significant level of investment over the long term."

A **Guest Comment: Philip Peters:** "The strongest external driver is the decision by US companies to increasingly include the nearshore into their global sourcing priority, given the competitive cost savings and productivity gains the nearshore offers when compared with offshore destinations. Over the last three years, the average rate of nearshore growth in the Caribbean has been 105 percent, followed by 38 percent and 35 percent in South and Central America, respectively. As a region, compounded nearshore growth has been 56 percent. Only 5 percent of South America's 750,000 agents serve US companies, while 80 percent of Central America and the Caribbean's 65,000 agents serve US companies. Leading companies driving nearshore employment and service include Avaya, Nortel, SER Solutions, Genenys, Aspect, Sykes, Teleperformance, Sitel, Convergys, and Dell. To sustain this growth, economic development agencies have to accelerate spending on IT and bilingual education, and build out greater physical office-ready capacity. Countries such as Argentina, Panama, the Dominican Republic, and Jamaica, which have liberalized their telecommunication sectors, are bigger winners. While attracting large US firms should continue, greater focus needs to be paid to strengthening and deepening the operational performance of local entrepreneurial firms in the business process outsourcing and call center vertical to ensure sustainability."

Rui da Costa is a member of the Advisor board and Managing Director for Latin America & the Caribbean at Hewlett-Packard Co.

Peter Ryan is an Analyst for Contact Center Outsourcing and Offshoring at Datamonitor.

Philip Peters is CEO of Zagada Markets and Lead Analyst of the company's research arm, Zagada Institute.

Latin America Advisor

is published every business day by the Inter-American Dialogue, Copyright © 2006

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Subscription Inquiries are welcomed at
freetrial@thedialogue.org

Latin America Advisor is published every business day by the Inter-American Dialogue
1211 Connecticut Avenue, Suite 510
Washington, DC 20036
Phone: 202-822-9002 Fax: 202-822-9553

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