LatAm INVESTOR

The UK's only Latin America-focused investment magazine Q2 2020

POTENTIAL ENERGY

Paraguay wants international investors for industrial, agribusiness and infrastructure projects

An exclusive interview with Paraguay's President, Mario Abdo Benitez

Latin America's Coronavirus Crisis:

A special feature on how Covid-19 is impacting the region's economy and capital markets

ALSO INSIDE:

Canning House predicts Latin American social trends in 2020

IHS Markit analyses the latest financial data from the region

We highlight some of the best luxury hideaways


ECL
NO SMOKING

A Mildly Eventful Quarter

Dear Readers,

What an eventful three months since our last edition. It is striking how quickly we've accepted the surreal conditions as a new, albeit hopefully temporary, normal. From a slightly selfish, professional view, it's been a fascinating time to be the editor of an investment magazine.

Over the last two months our team has been looking at how coronavirus will shape investment and business trends in Latin America and how different countries will fare. The advantage of being a quarterly publication is that it's forced us to avoid all of the quick – and understandably erroneous - 'hot takes' and work on stories that can give insight on how Covid-19 will impact the region over the next year.

The result is our Coronavirus Special Report, which begins on page 43. Over ten pages we look at the economic and financial impact of Covid-19 on Latin America. We have features from our correspondents in Mexico and Brazil on how the region's two largest economies are reacting to the virus. We have expert analysis from BancTrust on how coronavirus is moving Latin American capital markets. And we roundup the best and worst cases from around the region. In general, poor health systems, cash-strapped governments and a large informal sector make Latin America particularly vulnerable to the crisis. However, some countries seem to be handling it very well.

One surprise success story is Paraguay, which has already issued a $1billion 'coronavirus bond' to raise funds to fight the pandemic. It implemented a strict lockdown early, followed that up with a fiscal and monetary stimulus and, so far, has cases under tight control. As Paraguayan president, Mario Abdo Benitez, explains in our exclusive interview on page 30, the next challenge is to get the economy moving again. In our Paraguay Report, which starts on page 9, leading figures from the country's public and private sector outline the best investment opportunities the country has to offer.

Paraguay has a young population, an abundance of low-cost renewable energy and a rapidly diversifying export basket but it wants international capital and expertise to take its economy to the next level. Moreover, in the current situation it is keen to fast-track projects.

Elsewhere in the issue, you will see the usual features, including our new-look IHS Markit analysis on pages 4 and 5. And if you'd had enough of working from home in the UK, take a look at some of the spectacular Chilean properties on page 56.

Here's hoping that the next three months are less eventful than the last. Until next time,

James McKeigue

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Latin America: COVID-19 brings economic woe

Andrew Harker, Economics Director
Economic Indices, IHS Markit

Overview

The economic prospects of Latin American countries have suffered a severe blow due to the global coronavirus disease 2019 (COVID-19) pandemic, which at the time of writing shows no signs of abating and looks set to result in a global economic recession. The disease, and efforts to contain it, are already starting to take a heavy toll on the region's economies.

The latest IHS Markit PMI data highlight the impact the virus has already begun to have on the economic performance of Latin American countries, with manufacturing data for March showing new orders falling sharply amid declining demand at home and abroad, production being scaled back and business confidence slumping.

Forecasts made towards the end of last year, such as the International Monetary Fund's (IMF) World Economic Outlook, are set to be revised sharply lower when next updated, with GDP likely to fall widely and unemployment expected to rise. The region's central banks have acted swiftly to offer support to their respective economies, and in particular their ailing currencies, with widespread interest rate cuts enacted. However, much greater support is going to be needed during 2020 and beyond.

Argentina

The COVID-19 pandemic is set to bring further woe to the already-struggling Argentinian economy. Even before the outbreak, the IMF was predicting another year of falling GDP, but with the global economy set to enter recession the prospects now look even worse.

In contrast to some other Latin American countries, the Argentinian government prioritised the fight against COVID-19 early on and ordered strict measures to try to prevent the spread of the disease. This will inevitably lead to economic disruption initially but will hopefully mean an earlier victory over the virus. The Central Bank of Argentina continued to loosen monetary policy in March, cutting rates for the eighth time since mid-December. That said, they still stand at 38%.

Brazil

The prospects of the Brazilian economy seeing growth of GDP in 2020 appear to be waning as the COVID-19 outbreak hits global demand and is likely to harm business conditions in Brazil as well. The IHS Markit Brazil Manufacturing PMI signalled the first decline in the health of the sector for eight months in March. Central to the deterioration was a renewed contraction in new orders, with the pace of reduction the most marked since January 2017. Production also fell, while firms scaled back employment to the greatest extent in just over three years.

The Central Bank of Brazil has acted in the face of a sharply depreciating currency and fears of economic recession, cutting interest rates by 50 basis points to a new low of 3.75% and intervening in the foreign exchange market as diminishing risk appetite across global markets saw investors flock to the US dollar. Currency depreciation has caused inflationary pressures to build in the manufacturing sector. According to the IHS Markit PMI data, manufacturers saw the sharpest rise in their purchase costs for around a year-and-a-half and primarily linked this to exchange rate factors. Subsequently, firms raised their own selling prices at the fastest pace since September 2018. The combination of weakening demand (both at home and abroad), and building inflationary pressures reinforces the view that difficult times lie ahead.

Colombia

The COVID-19 outbreak looks set to throw the Colombian economy off course during 2020. Latest data from the Davivienda Colombia Manufacturing PMI, compiled by IHS Markit, showed that manufacturing production decreased for the first time in nine months during March amid the sharpest reduction in new orders for almost three years. Meanwhile, business confidence dropped to the lowest in the eight-year series history, with firms worried about the potential for an extended economic downturn.

A collapse in the price of oil since the COVID-19 outbreak occurred around the start of the year has hit the economy hard and contributed to a marked depreciation of the peso - the currency is down 24% against the US dollar since the start of the year.

The Central Bank of Colombia responded by cutting interest rates for the first time in two years to 3.75%, the lowest since May 2014. Measures to help boost liquidity have also been introduced. However, given the global nature of the pandemic and stringent measures introduced in Colombia to try to prevent the spread of the disease, the economy is now set to see GDP contract in 2020, rather than expand, as had been expected just a few months ago.

Mexico

After having decreased by 0.1% in 2019, Mexican GDP had been expected to return to growth in 2020, but the COVID-19 pandemic looks set to put paid to any hopes of expansion this year.

The economic impact has already started to show, according to the latest IHS Markit Mexico Manufacturing PMI, despite the government not having implemented stringent measures to prevent the spread of the virus at the time of data collection. New orders to manufacturers decreased markedly during March, and at the sharpest pace since the survey began in April 2011. Subsequently, output also moved into contraction territory and sentiment regarding the year ahead outlook for manufacturing production slumped to the lowest on record. The potential for a global recession weighed on confidence at firms.

The Mexican peso has also come under pressure, losing 31% of its value against the US dollar since the start of 2020. In response, the Bank of Mexico cut interest rates in an unscheduled meeting on March 20th, taking them down 50 basis points to 6.5% - the lowest for three years. It is likely that a greater fiscal and monetary policy response will also be required as the outbreak develops in Mexico and economic conditions worsen further.

Key Forecasts and Manufacturing PMI data

Brazil

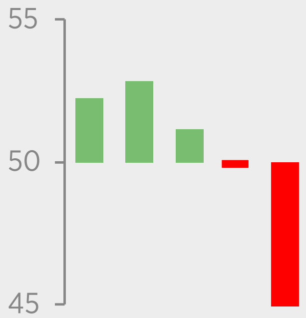
GDP: -5.3%

Inflation (year end): +3.6%

Unemployment Rate: 14.7%

PMI APR
36.0
MAR: 48.4

Source: IHS Markit



Colombia

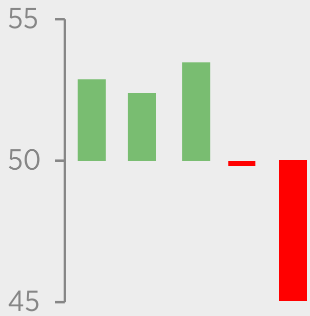
GDP: -2.4%

Inflation (year end): +3.4%

Unemployment Rate: 12.2%

PMI APR
27.6
MAR: 49.3

Sources: IHS Markit, Davivienda



Mexico

GDP: -6.6%

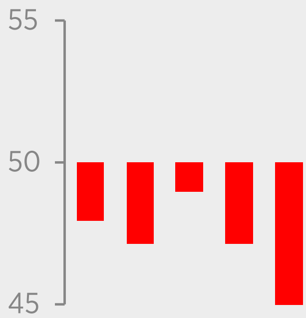
Inflation (year end): +2.7%

Unemployment Rate: 5.3%

PMI APR
35.0
MAR: 47.9

Sources for all forecasts: International Monetary Fund, World Economic Outlook October 2019

Source: IHS Markit



Coronavirus Changes Chile's Challenge

Covid-19 has stopped protests in the country, but the government's response raises new risks for business, writes Leandro Lima, Control Risks' political and security analyst for Chile...

The Covid-19 pandemic has reshaped Chile's risk landscape. On one hand coronavirus has drastically reduced protest activity across the country, yet the government's response to the crisis has exposed businesses to a new set of operational, regulatory and labour risks. Moreover, while the protests have stopped, coronavirus measures taken now could fuel worker grievances in the future.

This turnaround highlights the significant impact of the pandemic on the country. Since Chile's first case was reported on March 3rd, the number of Covid-19 infections has continued to steadily increase. Chile currently has the third-highest number of confirmed cases in Latin America despite being just the seventh-most populous nation in the region. Although that also reflects the country's extensive testing regime, which is the best in the region.

Social unrest on pause

The disruptive wave of protests and violent clashes between rioters and police that began to rock Chile in October of 2019 was originally triggered by a rise in public transport fares. But the unrest, which persisted until mid-March 2020, eventually evolved to demand the rewriting of the country's constitution. Yet, in light of escalating public health concerns and calls for social distancing, President Sebastián Piñera and Congress postponed a public referendum on a new constitution, originally scheduled for April 26th, by six months to October 25th. Most protest leaders have recognised the need for the delay and have conceded to the rescheduling. In the short-term this has brought peace to Chile. Because replacing the constitution is a highly polarising issue, the postponement has temporarily eased some of the tensions that have fuelled demonstrations both for and against the revision process.

Other risks on the rise

Although the public health crisis has led to a containment of social unrest in Chile, it has created other operational and regulatory risks for businesses operating in the country that echo those common to other nations across the world aiming to curb the pandemic. The mobility of workers is increasingly challenging. Although there has been no nationwide forced quarantine to date, the federal government of Chile has imposed lockdowns and established sanitary checkpoints in a number of municipalities, or comunas, throughout the country. For businesses and workers who conduct on-site work and cannot function remotely, the lockdowns have posed exceptional operational challenges. Although the transportation of goods is permitted in order to preserve supply chains, long queues at checkpoints are leading to severe delivery delays.

On the regulatory front, Piñera has pressured companies to change their business plans and introduce price controls in an attempt to prevent increases in the cost of living and to mitigate the socio-economic impacts of Covid-19 on the population. Most notably, the annual adjustments of tariffs on private healthcare providers have been postponed from July to November. Meanwhile, the energy sector is unlikely to be permitted to adjust tariffs for the foreseeable future; the tariff freeze established in November 2019 will likely remain despite upwards market pressures, such as the local currency devaluation, that would normally require energy generators to raise tariffs.

In terms of labour risks, on April 1 Piñera enacted the Employment Protection Act due to businesses' concerns about their capacity to keep their full workforce amid the pandemic. The initiative is controversial among unions and workers alike, however, as it allows companies to suspend work contracts temporarily. Although affected workers can receive cash transfers from the government to cover part of their wages, labour relations will likely deteriorate given the unions and workers' disapproval of the suspension and the uncertainty of when and whether contracts will be resumed. Any negotiations and dismissals going forward will likely be more contentious within the next six months. There are also increased uncertainties regarding the payment of workers' pension contributions, with legislation on the horizon that would require companies to pay 100% of the required contribution during a contract suspension.

Economic fallout

Chile, which relies heavily on commodity exports, is especially susceptible to the Covid-19-induced global recession and slowing of foreign trade. Chile's main export is copper, which accounts for 46% of total exports. With copper prices falling 20% between January and April 2020 due to weak global demand, the economy has been hit hard. Internal consumption in the country has also plummeted. Although Piñera launched an $11.7billion plan to support the economy with cash transfers to low-income families and tax benefits for small and medium-sized businesses, Control Risks' strategic partner Oxford Economics estimates that GDP will shrink by 3.3% for 2020.

Chile's Upcoming Political Calendar

ELECTORAL PROCESS | **CONSTITUTIONAL PROCESS**

NOVEMBER 2019 (Constitutional process)
Agreement in Congress to draft a new Constitution

OCTOBER 2020 (Constitutional process)
Constitutional referendum, and selection of the constituent assembly format

APRIL 2021 (Electoral process)
Election of governors and mayors

APRIL 2021 (Constitutional process)
Election of constituent assembly members

JULY 2021 (Electoral process)
Parties' primary elections for president

NOVEMBER 2021 (Electoral process)
Parties' primary elections for president

DECEMBER 2021 (Electoral process)
Second round run-off

UNTIL JUNE 2022 (Constitutional process)
Referendum to approve the final

Outlook

The risk of civil unrest risk is likely to remain low over the next three months, as demonstrations and public gatherings across the country will remain limited. However, protest activity is likely to gain momentum again as Chile's political calendar resumes in October with the constitutional referendum. Voters are expected to approve the creation of a new constitution, and the actual drafting process throughout 2021 will be contentious. Protests will occur whenever controversial issues are under consideration—particularly those related to the pension, healthcare, and education systems.

As social distancing measures are likely to be gradually lifted in the coming six months, Operational and labour risks will decrease accordingly. Regulatory risks will persist as the Piñera administration has been under popular pressure to enact regulatory changes and prevent the cost of living from increasing since unrest began in October, well before the COVID-19 crisis began. The constitution redrafting process will create regulatory uncertainties over the next two years. The economic environment will remain challenging in the foreseeable future as the global recession will continue to affect Chilean exports, and the long-term costs of the internal lockdown persist.

Chile entered the coronavirus crisis in a much stronger macroeconomic position than the rest of the region. It's been able to implement 'developed world' style economic protection for its citizens, while maintaining a sustainable fiscal deficit and debt-to-GDP ratio. It also has much stronger institutions, which has allowed it to carry out a sophisticated strategy that combines extensive testing and with a partial lockdown.

However, it is politically divided and the unprecedented measures being used to fight coronavirus require political consensus. With a vaccine not expected to be commercially available for 18 months Chile will find itself returning to divisive political problems while still battling Covid-19.

MARKET-MOVING EVENTS CALENDAR

MAY

Friday 1st
8:00 PM - Argentina - Tax Revenue APR
8:00 PM - Dominican Republic - Interest Rate Decision

Monday 4th
5:00 AM - Peru - Inflation Rate YoY
6:00 PM - Brazil - Balance of Trade

Wednesday 6th
12:00 AM - Colombia - Inflation Rate YoY
9:00 PM - Brazil - Interest Rate Decision
9:00 PM - Chile - Interest Rate Decision

Thursday 7th
11:00 AM - Mexico - Inflation Rate YoY
11:00 PM - Peru - Interest Rate Decision

Friday 8th
12:00 PM - Brazil - Inflation Rate YoY
2:00 PM - Ecuador - Inflation Rate YoY
2:15 PM - Salvador - Inflation Rate YoY

Tuesday 12th
11:00 AM - Mexico - Industrial Production YoY
8:00 PM - Paraguay - Balance of Trade

Thursday 14th
3:00 PM - Colombia - Industrial Production YoY
3:00 PM - Colombia - Retail Sales YoY
6:00 PM - Mexico - Interest Rate Decision

Friday 15th
6:10 AM - Peru - GDP Growth Rate YoY
4:00 PM - Colombia - GDP Growth Rate YoY Q1

Monday 18th
12:30 PM - Chile - GDP Growth Rate YoY Q1

Wednesday 20th
7:00 PM - Argentina - Economic Activity YoY

Thursday 21st
3:00 PM - Argentina - Consumer Confidence
8:00 PM - Paraguay - Interest Rate Decision

Tuesday 26th
11:00 AM - Mexico - GDP Growth Rate YoY Q1
11:00 AM - Mexico - Economic Activity YoY
12:30 PM - Brazil - Foreign Direct Investment
7:00 PM - Argentina - Retail Sales YoY

Wednesday 27th
2:30 PM - Peru - GDP Growth Rate YoY Q1
7:00 PM - Argentina - Balance of Trade

Friday 29th
12:00 pm - Brazil - GDP Growth Rate YoY Q1
1:00 pm Chile Copper Production YoY APR

JUNE

Monday 1st
2:00 AM - Peru - Inflation Rate YoY
12:00 PM - Brazil - Unemployment Rate

Thursday 4th
1:00 PM - Mexico - Foreign Exchange Reserves
3:00 PM - Colombia - Exports YoY

Friday 5th
12:00 PM - Chile - Inflation Rate YoY
2:00 PM - Ecuador - Inflation Rate YoY

Tuesday 9th
11:00 AM - Mexico - Inflation Rate YoY

Wednesday 10th
11:00 AM - Mexico - Industrial Production YoY
12:00 PM - Brazil - Inflation Rate YoY

Thursday 11th
3:00 PM - Dominican Republic - Inflation Rate YoY
11:00 PM - Peru - Interest Rate Decision

Friday 12th
3:00 PM - Colombia - Industrial Production YoY
3:00 PM - Colombia - Retail Sales YoY

Monday 15th
11:30 AM - Brazil - BCB Focus Market Readout
2:00 PM - Panama - GDP Growth Rate YoY Q1

Tuesday 16th
12:00 PM - Brazil - Retail Sales YoY
10:00 PM - Chile -Interest Rate Decision

Wednesday 17th
9:00 PM - Brazil - Interest Rate Decision
10:00 PM - Peru - GDP Growth Rate YoY

Tuesday 23th
7:00 PM - Argentina - GDP Growth Rate YoY Q1
7:00 PM - Argentina - Unemployment Rate Q1

Thursday 25th
11:00 AM - Mexico - Retail Sales YoY
6:00 PM - Mexico - Interest Rate Decision

Friday 26th
11:00 AM - Mexico - Economic Activity YoY
5:00 PM - Paraguay - GDP Growth Rate YoY Q1
8:00 PM - Colombia - Interest Rate Decision

Monday 29th
12:00 PM - Brazil - Unemployment Rate
7:00 PM - Argentina - Economic Activity YoY

Tuesday 30th
1:00 pm - Chile - Copper Production YoY

JULY

Wednesday 1st
5:00 AM - Peru - Inflation Rate YoY

Thursday 2nd
12:00 PM - Brazil - Industrial Production YoY

Friday 3rd
11:00 - Mexico - Consumer Confidence
3:00 PM - Colombia - Exports YoY
5:30 PM - Uruguay - Inflation Rate YoY

Saturday 4th
5:00 PM - Colombia - Inflation Rate YoY

Monday 6th
2:00 PM - Inflation Rate - YoY

Tuesday 7th
11:00 AM - Mexico - Auto Production YoY
7:00 PM - Argentina - Industrial Production YoY

Wednesday 8th
12:00 PM - Brazil - Retail Sales YoY
12:00 PM - Chile - Inflation Rate YoY

Thursday 9th
11:00 PM - Peru - Interest Rate Decision

Friday 10th
12:00 PM - Brazil - Inflation Rate YoY

Monday 13th
11 AM - Mexico - Industrial Production YoY
5:30 PM - Uruguay - Industrial Production YoY

Wednesday 15th
12:55 PM - Peru - GDP Growth Rate YoY
10:00 PM - Chile - Interest Rate Decision
10:45 PM - Panama - Inflation Rate YoY

Wednesday 22th
7:00 PM - Argentina - Economic Activity YoY

Thursday 23th
7:00 PM - Argentina - Retail Sales YoY
8:00 PM - Paraguay - Interest Rate Decision

Monday 27th
11:00 AM - Mexico - Economic Activity YoY

Thursday 30th
7:00 PM - Colombia - Cement Production YoY

Friday 31st
1:00 PM - Chile - Copper Production YoY
1:00 PM - Chile - Industrial Production YoY
8:00 PM - Colombia - Interest Rate Decision
8:00 PM - Dom Rep - Interest Rate Decision

Special Report

The Paraguay **Report**

HUNTING FOR PROFITS

Paraguay wants international investors to turn its natural wealth into a 21st-century economy

IN-DEPTH SECTOR ANALYSIS

Biofuels – Trade – Infrastructure – Finance

MACROECONOMIC SPOTLIGHT:

Central Bank President, José Cantero, on Paraguay's economic growth

PRESIDENTIAL PERSPECTIVE:

Paraguay's President, Mario Abdo Benitez, explains how his country is fighting Covid-19

FINANCE SPOTLIGHT:

Finance Minister, Benigno López, on why UK plc should come to Paraguay

Paraguay

CAPITAL
Asunción

CURRENCY
Guaraní

CONTINENT
South America

OFFICIAL LANGUAGE
Spanish

POPULATION
7 m

Politics

PRESIDENT
Mario Abdo Benitez

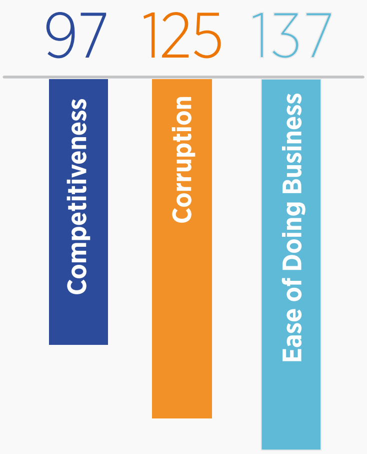
EXECUTIVE BRANCH
The current Head of Government is Mario Abdo Benítez

LEGISLATIVE BRANCH
The post dictatorship 1992 Constitution gave significant power to Congress, which is arguably the most powerful of the three branches of state. The bi-cameral Congreso is made up of a 45-person Senate and an 80-strong Chamber of deputies.

JUDICIARY BRANCH
The nine-member, Supreme Court of Justice (Corte Suprema de Justicia) is the highest court in Paraguay. And, thanks to recent appointments, its least corrupt. Below that are regional trial and appellate courts.

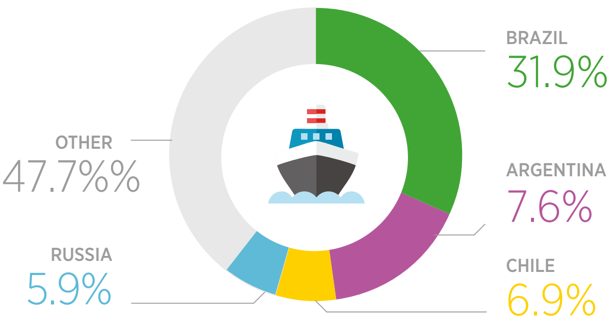
The last elections were held on April 2018 and the next are due in April 2023.

Global Rankings



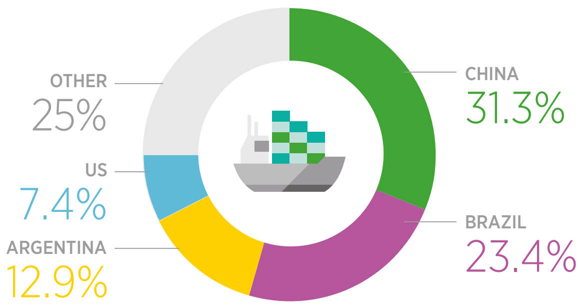
Main Trading Partners

Exports



Soybeans, livestock feed, cotton, meat, edible oils, wood, leather, gold

Imports



Road vehicles, consumer goods, tobacco, petroleum products, electrical machinery, tractors, chemicals, vehicle parts

INFLATION
2.5%

GDP (PPP)
$43 bn

GDP GROWTH
-1.0%
2020 est

GDP PER CAPITA (PPP)
$13,599

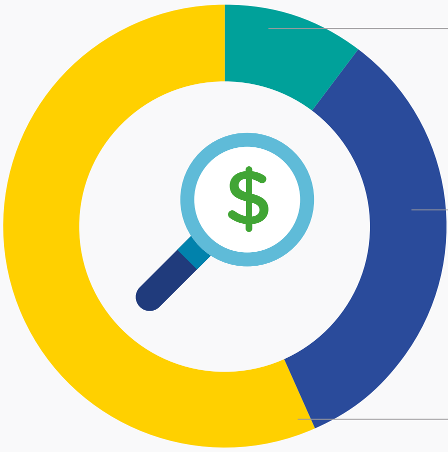
National Tax Rates

CORPORATE
10%

PERSONAL INCOME
10%

SALES
10%

GDP Composition

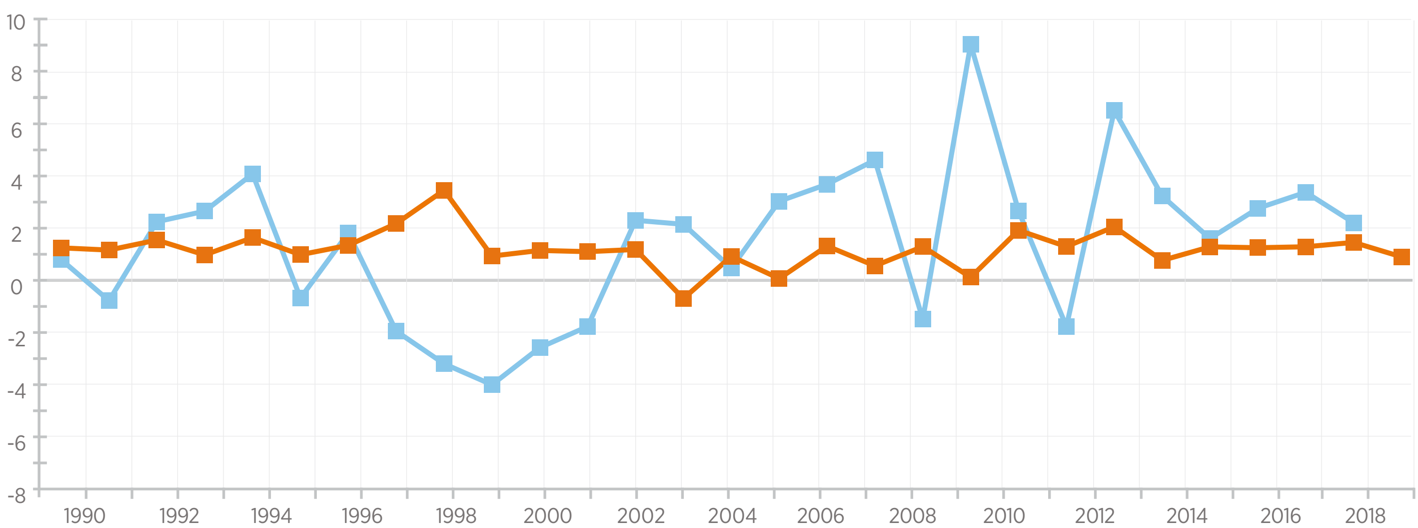


AGRICULTURE
10.2%

INDUSTRY
33%

SERVICES
56.8%

GDP per Capita Growth (Annual %) **Foreign Direct Investment, Net Flows (% of GDP)**



Sources: World Bank, World Economic Forum, Transparency International, CIA World Factbook

Paraguay's **Potential**

After 15 years of growth, the country was embarking on structural reforms when coronavirus hit; now they are more vital than ever...

For a country with a young population and bright future, it's striking how fixated Paraguay is with the past. The War of the Triple Alliance, an uneven battle that pitted Paraguay against Brazil, Argentina and Uruguay from 1864 to 1870, came up in plenty of interviews. The war was notable for its incredible ferocity – judged by deaths per Paraguay's population it was the most brutal in world history – and the courageous yet doomed defiance of the Paraguayans. But more importantly for investors, is the economic impact. It cut short Paraguay's belle epoque, when the country led Latin America in railways, telegraphs and steelmaking. And by distorting demographics and reducing the territory by half – it forced Paraguay into almost a century of economic isolation.

Santiago Pena, Director of Banco Basa, Paraguay's oldest local bank, and a former Finance Minister, believes the economic effects of the war can be felt until this day. "The biggest impact was that it shut us off from the wave of European immigration that was about to drive growth in Latin America. From the beginning of the 1900s we saw the biggest migration in the history of the world as hundreds of millions of Europeans fled war, hunger or privation at home to search for a better life in the Americas. This boost of population and ideas helped Argentina become the fifth-largest economy in the world by 1920 and kickstarted new industries, such as mining in Chile and cattle-raising in Uruguay. But they generally avoided Paraguay because we had been destroyed by war. So, we continued to suffer for decades. It also made us wary of making too much noise as we were surrounded by two much larger, aggressive nations. That kept us an isolated, backward nation and it's only in the last 30 years that we've begun to emerge from that shadow."

When a palace coup ended Alfredo Stroessner's 35-year dictatorship – the longest in Latin American history - in 1989, it kickstarted a liberalisation of the Paraguayan economy. In this report you will read how everyone from banks to rum-makers, suddenly found themselves free to trade with the world. It wasn't smooth sailing. The 1990s were a chaotic decade of political instability and economic suffering that culminated in financial crises in 1997 and 2001. But beneath the chaos, important progress was being made. Export quotas were abandoned, state monopolies disbanded and the exchange rate allowed to float. As the new century progressed, Paraguay was ready to reap the benefits.

Steady growth

Between 2005 and 2018 the economy grew at an average annual rate of 4%. Under the steady supervision of the Central Bank, the country's macroeconomic position improved with its ratings moving up from selective default, all the way up to just one notch below investment grade. Meat and grain were the pillars of the economy, with production of the latter growing exponentially. Today Paraguay is the fifth-largest soy exporter in the world. The tiny country of just seven million people produces enough food for 70 million.

But Paraguay wants to be more than just a bread basket. Its shared ownership of three hydroelectric dams on its borders give it more electricity per person than any other country in the world. At present Paraguay uses just 20% of its power, meaning it has scope to offer abundant supplies of low-cost green energy to industrial users. It has also created a number of fiscal regimes, such as the maquila, to offer attractive tax structures to manufacturers.

Finally, it has one of the youngest populations in Latin America, which ensures an expanding and competitively-priced workforce. These factors have already driven the development of a car-parts industry, that generates $600million in exports per year. Meanwhile an even more ambitious plan to turn Paraguay into a world-leader in renewable fuels is being spearheaded by the Brazilian ECB Group's plans for an $800million 2nd-generation biofuel plant. It's the first in the southern hemisphere and will be the first time for more than 150 years that Paraguay leads Latin American industry. As the Paraguayan economy becomes more sophisticated, with a great emphasis on services and industry, its needs will be more aligned with what UK plc can offer.

Structural flaws

But while the macroeconomic improvement was impressive, Paraguay still retained many structural flaws. Its education system is poor, even by regional standards, its public health system is chronically underfunded, and its creaky infrastructure, especially in transport, water and electricity, isn't fit for purpose. These basic flaws exacerbate inequality, as decent public education, health and infrastructure help to level the playing field. But they also limit economic growth. Without good health or education, Paraguay's demographic boon will turn into a curse, while the poor infrastructure is already constraining the economy.

The state's ability to fix these problems is impaired by the chronic disfunction of the state itself. Approximately 80% of income goes towards paying bureaucrats' salaries, many of whom have been on the books since Stroessner's time. This also damages the business environment. Anecdotally, and off-the-record, interviewees spoke of functionaries "that create problems to then sell you a solution". Those stories are backed up by the data, with the World Bank's Ease of Doing Business ranking currently placing Paraguay in lowly 125th position.

The problem isn't always outright corruption. Guillermo Krauch, President of the British Paraguayan Chamber of Commerce, notes that bureaucracy is also a challenge. He notes that the paperwork for setting up a new company can "take longer than expected", while foreigners should expect "difficulty and delay" when setting up a new bank account. Most frustrating of all is that "regulations change many times" forcing investors to constantly adjust their business plans.

Reform

Paraguay has all the building blocks for economic growth but is being held back by several structural flaws. So, it is little wonder that current President, Mario Abdo Benitez, won the 2018 election on a platform of reform. Thus far there have been some significant, if unspectacular, successes. A modest fiscal reform managed to simplify the tax code and add 1% of GDP to the country's tax take, without changing the headline figures of 10 plus 10 plus 10 (corporation, income and VAT) that international investors find so attractive. Then a raft of anti-money laundering legislation looks like it has done enough to ensure that Paraguay will be kept of the Financial Action Task Force Grey List. Now a pensions regulator is being created to improve oversight of the country's different retirement reforms. The government has also progressed with infrastructure, continuing with the public private partnership law enacted by its predecessor. Until the coronavirus outbreak it appeared to be a government pursuing steady, incremental technical reforms that wouldn't change the formula that had delivered economic growth.

But then coronavirus hit. The rapid spread of the pandemic left no time for steady, incremental actions and the government showed a new radical side. Paraguay was one of the first countries in Latin America to implement a lockdown and it unveiled the largest fiscal and monetary package in its history to mitigate the blow for its people. So far, the measures seem to be working. Paraguay has some of the lowest coronavirus numbers in the region. International investors have also given their support. Paraguay's $1billion bond to raise funds to fight the impact of Covid-19 was seven times oversubscribed. As President Benitez explains in his exclusive interview on page 30, the crisis demonstrates why the structural reforms are so important.

The country is now easing its lockdown and is aiming to restart economic growth. That will create opportunities for British businesses as key infrastructure, industrial and agricultural projects are fast-tracked. Of course, you have to be a brave investor to commit money to emerging markets in the midst of a pandemic. But with depressed asset prices and a pro-business government keen to attract international firms – this looks like a great time to invest in Paraguay.

CONTENTS

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THE UK VIEW:

HM Ambassador to Paraguay,

Matthew Hedges,

explains how Britain is resetting relations with the country...

LATAM INVESTOR: *In 2013 the UK reopened its embassy in Paraguay; how is the bilateral relationship now?*

AMBASSADOR HEDGES: It's in a solid place. If you look at international issues, such as multilateral cooperation, chemical weapons or Venezuela, then we share a lot of the same viewpoints. It's important to stress that the bilateral relationship continued, even when there was no British Embassy in Paraguay from 2006 to 2013. Of course, having a physical presence helps and once the embassy was reopened we saw several positive impacts. There was a big spike in Paraguayan exports to the UK, while it allowed us to work more closely with different organisations here. For example, in defence we have brought British military officers to train Paraguayan forces. This year we sent two Paraguayans to Sandhurst for the first time in more than a decade.

Another example is higher education. That's a business opportunity for UK universities but it's also an area where the embassy partners with the Paraguayan government to provide scholarships. Indeed, in recent years we have expanded the number of Paraguayan Chevening Scholars receiving grants to study in the UK. So, we leveraged that close relationship when we brought over a delegation of nine British universities to look at some of the opportunities in the Paraguayan education market.

LAI: *Paraguay scores poorly on corruption rankings; is it a challenge for UK firms here?*

AH: Plenty of British businesses are doing good, clean business here, which shows that corruption is not an insurmountable barrier. Like many other countries in the region it is facing challenges in the rule of law and corruption, but in the last five years we've seen successive Paraguayan government make steady improvements in these areas.

One of the big recent advances is anti-money laundering, AML, where there has been a culture change, with the Paraguayan business and political elite now keenly aware of the risks of not dealing with this issue seriously. A raft of new legislation was passed that will improve the legal AML framework and should help Paraguay in its Gafilat review due later this year.

LAI: *Where are the investment opportunities for British companies in Paraguay?*

AH: The context for international investors here is very positive. If you look at the macroeconomic foundations and political stability it stands out from its regional peers.

For example, Paraguay's currency, the guarani, has survived for more than 70 years without any major crisis. It has a competitive tax regime, where companies pay just 10% corporation tax. There are also various initiatives, such as the maquila regime and free zones, that offer extra incentives for particular industries.

It also has some interesting characteristics that should drive economic growth in the future. It has an incredibly young demographic, with around 60% of its population under 30 years old. If that is well managed then it should be a big positive for the economy as it will add to the workforce and boost consumer demand. Another exciting area is energy. Paraguay owns half of the Itaipu Dam, which is the world's largest producer of renewable energy. Together with other, smaller dams shared with Argentina, it means that Paraguay has an abundant supply of low-cost, green energy. But British firms should come now to take advantage of this unique situation. By 2030 it's estimated that Paraguay will use 50% of its electricity, up from less than 20% today, so the opportunity will not last for ever.

Paraguay doesn't just offer low-cost labour, competitive tax regimes and plentiful renewable power. Thanks to its membership of Mercosur it can also give UK companies tariff-free access to the much larger markets of Brazil and Argentina. We've already seen car parts manufacturers take advantage of these benefits, with a massive growth in that industry over the last ten years.

Finally, it's worth noting that agriculture is still the backbone of the Paraguayan economy, with soy and beef the country's two major exports. It is a very productive agriculture sector – a country of just 7 million people produces food for more than 70 million – but with the right technology it could be even more so. We've been trying to introduce British agritech to the Paraguayan market. We've used some government funding to set up a demonstration smart farm, that allows UK companies to tweak their products to Paraguayan needs and also showcases the benefits that British technology could bring.

LAI: ***Paraguay is little-known in the UK; how are you trying to increase awareness?***

AH: Most British perceptions of Paraguay are rather outdated. So, part of my job is to help people understand what the real Paraguay is about. That includes detailing the advantages I outlined above. Fortunately, this government and its predecessor have both been keen to sell their country abroad and you see lots of international trade missions, conferences and interviews.

I'm also realistic. I know that it can be hard to convince a UK business delegation to come to Paraguay, so we combine with regional visits. For example, the recent visit of British universities was part of a wider trip that included stops in Uruguay and Bolivia.

Once British businesspeople understand the incredible advantages that Paraguay has – especially in workforce and energy – they are normally keen to explore more for themselves. I think our strongest selling point is that we've seen a wave of investment from the larger economies, such as Brazil and Argentina into Paraguay. The fact that the rest of the region wants to do business here should be a clear sign to British investors.

LAI: ***How is this government different to its predecessor?***

AH: There is a clearer awareness and greater sense of action on facing some of the challenges that we talked about. In addition to the AML legislation we have seen some very influential political figures go through the justice system and in some cases even receive prison sentences or fines. That is unprecedented in Paraguayan history. Those judicial cases probably helped to release some political tension and help explain why Paraguay was untouched by the wave of protest that swept much of Latin America towards the end of 2019. This government understands well the change in the national mood, where people have grown tired of impunity for the elite. Indeed, a central theme in the election campaign of this government was improving the country's institutions. At present one of the most respected institutions in the country is the central bank, which has steadily steered Paraguay's macroeconomic fundamentals.

LAI: ***Post Brexit will we see a UK–Mercosur trade deal?***

AH: It's still very, very early but we welcomed the signing of the EU-Mercosur deal. Of course, it still needs to go through the scrubbing phases and be ratified by the national parliaments. But elsewhere in the region, and the world, we saw the UK sign 'continuity agreements' with countries that already had an association agreement with the EU. We can't really do a 'copy and paste' with a deal that we aren't part of, but it could well provide a useful foundation for our future negotiations with Mercosur. We will be watching it very closely.

Investing in Paraguay

Paraguay is shunned by international investors and scores poorly in global rankings yet the reality is much more positive...

Paraguay is relatively unknown among British businesses. The little that is known is often negative. The typical view from London paints Paraguay as a small, poor, isolated economy. Moreover, that negative view is backed up by the stats. The GDP per capita of $6,000 is the lowest in South America. It's also the only country in the region not to have a direct flight to the US, nor an embassy in China. Then you have its lowly position in influential indices. Paraguay's 125th place in the World Bank's influential Ease of Doing Business ranking, and even worse 137th in Transparency International's Perceptions of Corruption Index, suggests a bureaucratic and corrupt business jurisdiction. It's little surprise then that international investors steer well clear of the place. Foreign direct investment accounts for less than 1% of Paraguayan GDP – well below the Latin American average of almost 4%.

Santiago Peña, Director, Banco Basa

If our job was just to collect statistics, we could stop the article there. But having spent weeks interviewing the leading local and international investors in the country, our team discovered the truth to be more nuanced. We found a well-regulated, stable economy where the business environment is improving each year. Of course, more needs to be done. Legal security, in particular needs work. But with Paraguay just one notch away from investment grade, British businesses would do well to refresh their understanding of the country.

> *"I was amazed that when we went to speak with international investors in the US or Europe, many did not even know where our country is on a map*

Outdated

One man well-placed to judge Paraguay's progress is Santiago Peña. Spells at the IMF, Central Bank of Paraguay (BCP), Finance Ministry and now in the private sector as a Director of Banco Basa, the country's oldest local bank, mean he's seen the advances first-hand. "In 2013, when I was Director at the BCP, Paraguay issued its first ever bonds on the international market. I was amazed that when we went to speak with international investors in the US or Europe, many did not even know where our country is on a map. When they typed 'Paraguay' into their Bloomberg terminals it came back with 'not found', which shows you how little people knew about us.

"We knew that it was vital to first get the international financial investment because that means Paraguay starts appearing on key indices. It made us more visible as then you had ratings agency judging our macroeconomic strengths. Then that makes it easier to get foreign direct investment FDI into the real economy. Since issuing our first sovereign debt we had a series of upgrades. That wasn't just because we made progress in those years but because the ratings agencies eventually caught up with the reality of Paraguay's progress since the start of the 2000s. Investors were looking at our strong macroeconomic fundamentals and asking the ratings agencies why Paraguay wasn't investment grade. You often get institutional inertia. When I was Finance Minister one of the rating agencies once accompanied a Paraguay rating with a press release that was identical to the previous year's, which clearly didn't make sense. That's why some investors, even today, don't realise all that Paraguay has to offer."

Money laundering myth

One of the most negative perceptions of Paraguay is that it is an offshore finance centre for illegal money. It was placed on the Financial Action Task Force (FATF) Grey List in 2011, with a review due later this year. It's clear that Ciudad del Este, a bustling trade entrepot that lives off commerce with neighbouring Argentina and Brazil, also hosts widespread smuggling. This is an unintended consequence of a special tax clause in the Mercosur agreement that allowed Paraguay lower tax rates in recognition of its less-developed status. But this, say the Paraguayan business and political elite, doesn't make it an offshore haven that launders drug money or finances terrorism.

"In recent years we have seen a steady move to tighter money laundering controls in Paraguay", says Nestor Loizaga, Managing Partner of Ferrere in Paraguay, a regional corporate law firm with offices in Uruguay, Paraguay, Bolivia and Ecuador. "Three years ago, the previous government passed legislation to eliminate bearer shares. It was the local banks that pressed for the legislation because if it wasn't passed, they would be placed on the Financial Action Task Force Grey List and lose their correspondent accounts. Indeed, international banks present here, such as BBVA and Itaú would have had to close their Paraguayan operations. This year the government passed a new package of AML legislation that is now in the process of being implemented. The fact is, the majority of Paraguay's business and political class want the country to have world-class anti-money laundering processes because illicit financial practises are not a serious driver of the economy and the consequences of being financially blacklisted are simply too severe."

Well regulated

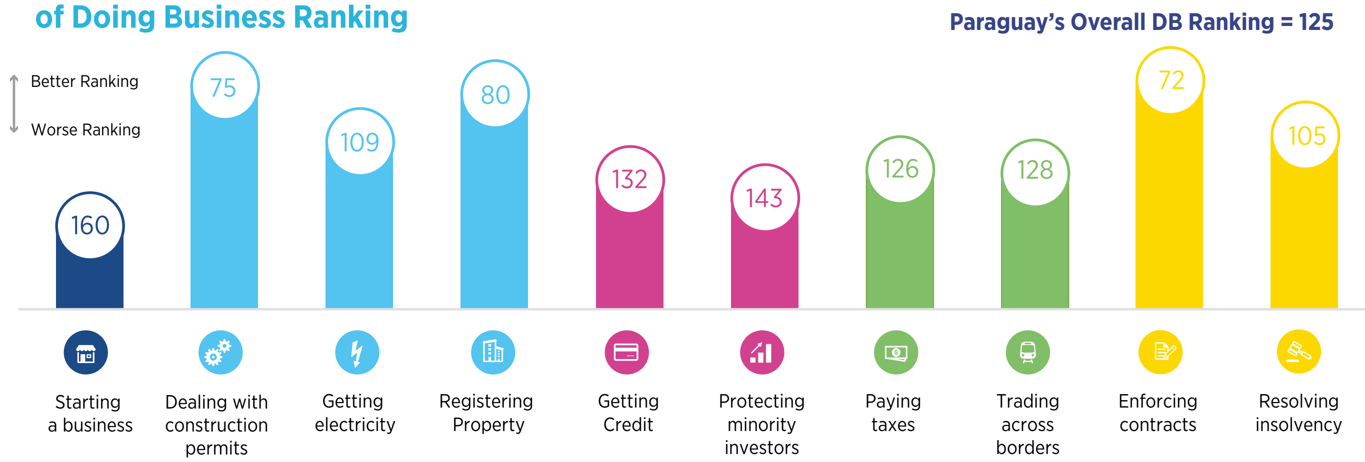
Countries that score poorly in World Bank rankings tend to have weak institutions. And that is certainly the case in Paraguay. However, two of the most important institutions for investors, the finance ministry and the central bank, are also considered the best in the country.

"In general, Paraguay is a well-regulated jurisdiction", says Rodolfo Vouga, Managing Partner of local corporate law firm, Vouga Abogados. "We have benefited from prudent macroeconomic management while the Central Bank of Paraguay (BCP) ensures a conservative banking sector. We had two banking crises, one in 1996 and one in 2002, where many local banks went bust. We've gone from having 60 banks to around 15 or so today. The BCP is very selective about banking licenses, for example some Argentine banks wanted to set up in Paraguay but their application was denied because authorities didn't want to import the instability from neighbouring countries."

Paraguay's economy is very stable by regional standards and that's reflected in its currency, the guarani, which is the oldest in Latin America and has survived more than 70 years without any major devaluations. What's fascinating is that the currency survived several bouts of political turbulence. "I always try to explain to international clients that there are two Paraguays", says Loizago. "One is political, while the other is business and historically there is a clear distinction between them. If you look at our neighbours, you see these radical swings in policy with each new government completely changing the rules of the game for the private sector. In Brazil, Argentina, Bolivia and Ecuador you have clear examples of very strong policy swings from one government to another. That doesn't happen in Paraguay. Even when we had a socialist president, Fernando Lugo in 2008, his impact on legislation was moderate and the business environment didn't


The rapidly-changing skyline of Paraguay's capital Asunción, reflects the country's rapid economic growth

Breaking Down Paraguay's World Bank Ease of Doing Business Ranking



really change. In essence there is a deep-rooted consensus here, where most Paraguayans are relatively conservative and don't want to upend the system – just improve it slightly."

If you were to make any criticism of the BCP you could perhaps say that it is too conservative. Like the famous aphorism of generals fighting the last war, the BCP is focused on avoiding a repeat of the Paraguayan financial crisis. Yet William Kent, the CFO of Credicentro, Paraguay's largest fintech, disagrees. "In Paraguay there are still three million people that don't have access to the financial system. I don't blame regulators for that. Return on equity for banks in Paraguay is much higher than in the rest of Latin America and they make a lot of money here every year, so it's a great place for banks to do business."

"The BCP is open to modernising and new ideas and it recently made financial inclusion one of its strategic aims. That makes us a natural ally. To the BCP's credit it is not looking to limit the price of money, access to banking or innovative models, like fintech. It is just concerned about the source of funding, fighting AML and maintaining the stability of the financial system."

Legal security

Of course, Paraguay is not a paradise. The biggest challenge in the business environment, highlighted by nearly all of the interviewees, is legal security. "The legal system here has recently seen some important improvements", says Loizaga. "The Supreme Court has been cleaned up by some impartial appointments. However, in the lower courts you can still have problems. There are some occasions where you have a corrupt opponent and a corruptible judge, where you can predict the outcome of a case before its heard. The good thing is that you can appeal and eventually take it as far as the Supreme Court, which is clean. Unfortunately, that can take between six to eight years – a wait that would paralyse many projects."

Legal security is a massive theme for investors and few British companies will fancy waiting eight years to get a just decision. However, arbitration clauses in contracts can provide a handy solution, says Vouga. "We are betting on arbitration because we have seen other successful Latin American economies, like Peru, use it as a way to circumvent an unreliable domestic legal system. Of course, the best option of all is to pick good local partners and providers to avoid legal disputes."

The judiciary is not the only weak institution in Paraguay. Many other parts of Paraguay's bloated bureaucracy also damage the business environment. "One of the underlying problems is that we have an inefficient state", says Carlos Jorge Biederman, owner of the KFC and Pizza Hut franchises in Paraguay, and President of the Paraguay Chamber of Advertisers. "There are lots of public functionaries who have been in the same position for decades. Indeed, many that entered during the government of Alfredo Stroessner. That matters because it means there is an entrenched bureaucracy, which subconsciously acts against innovation and efficiency." That's confirmed by Gustavo Volpe, President of the UIP, Paraguay's most important industrial association. "Most of the local authorities are not very efficient, so they can bog business down with unnecessary paperwork."

But despite the challenges, Volpe remains positive. "Most of the international companies to Paraguay know all of this. They weigh up the challenges and they still come because the rewards outweigh the risks."

In recent years reforms improved Paraguay's business environment. It was just starting to gain international attention when the coronavirus crisis hit. As you can see in our interviews with various government ministers, Covid-19 is accelerating the structural reforms. It is increasing pressure on the state to become more transparent and efficient. Meanwhile the fall in asset prices and credit will create opportunities for cash-rich investors looking to pick up quality businesses and projects at a low cost.

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ECONOMIC SPOTLIGHT:

President of the Central Bank of Paraguay,

José Cantero,

on why his country will cope with the coronavirus crisis...

LATAM INVESTOR: *How will coronavirus impact the Paraguayan economy?*

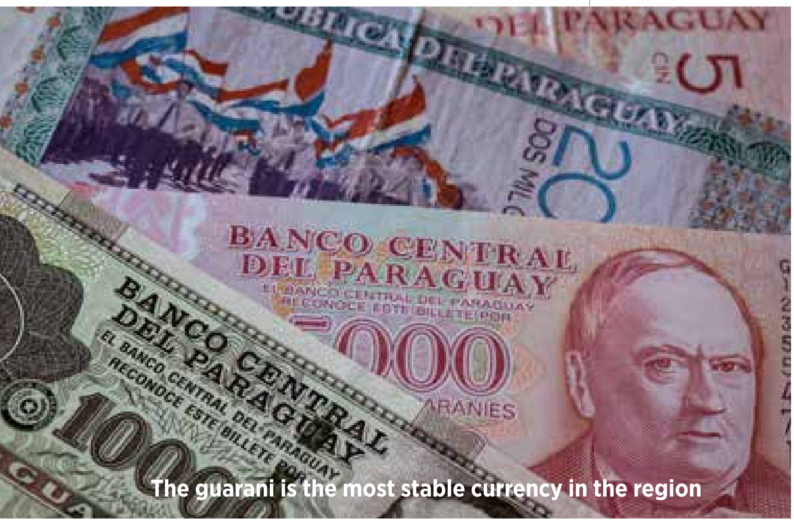
JOSÉ CANTERO: Clearly this is a fast-moving situation. At the moment we don't know if this will be something seasonal or if it will cover a longer period. I think the quick response of the Paraguayan state is a positive sign that it can cope with the crisis. Paraguay was the first government in the region to close schools. It was a joint decision led by the Ministry of Health and the Ministry of Finance, while the BCP was consulted. Ultimately, we felt that taking quick, decisive action equated to making an upfront payment that would avoid worse economic damage later on. Moreover, it sent a signal to the Paraguayan people that this was something to take seriously. It is a form of nudge theory, whereby our decision about schools encouraged families to take further actions, such as cancelling meetings or improving sanitary habits.

We realised that this would have an economic impact, so we announced a package of fiscal, social, financial and monetary measures to help the population. All the time, we ensured that the measures taken wouldn't have a negative effect on Paraguay's macroeconomic stability. We want to protect the health of the people but not with knee-jerk reactions that cause more damage later on. We have further counter-cyclical stimulus that we can deploy later on if necessary.

LAI: *What are Paraguay's macroeconomic strengths?*

JC: Paraguay has a very long track record of prudent macroeconomic management. We are an island of stability in a region that has always been volatile. Our currency the Guarani has been around for more than 70 years. That macroeconomic solidity has been the foundation of the uninterrupted economic growth of the past 15 years. Moreover, we strengthened that prudent macroeconomic management in 2011 by adding inflation targeting to the BCP's mandate. We now have a target of 4%. Then, in 2013, we passed a fiscal responsibility law that limits governments to running an annual fiscal deficit of 1.5%. In extreme cases, such as last year when growth was hit by a drought, it can be expanded to 3%. In many ways the countercyclical response to the slowdown in the first semester of 2019 demonstrates the strengths of Paraguay's economic management. There was a co-ordinated fiscal and monetary response.

Our banking system is a catalyst for growth. Primarily in terms of solvency because of its abundant levels of Tier 1 and Tier 2 capital, liquidity and capacity of management. It means that local companies have access to competitive sources of finance. Another strength, is the growing diversification of Paraguay's economy. You have growing manufacturing, including in completely new areas such as car assembly, which have been kickstarted by foreign direct investment. Manufacturing has thrived because of our low tax burden and competitive labour force. Indeed, industrial exports are now worth $1billion, which is almost as much as our meat industry. Even if you look at agribusiness you can see diversification taking place. Since 2015, manufactured agri-exports, such as oils or processed meats, have been worth more than sales of primary materials, such as grain or livestock. This process of diversification will continue because the growth prospects for these industries are very strong.



The guarani is the most stable currency in the region

LAI: ***Last year's drought hit Paraguay hard; is it as dependent on water as Chile is on copper?***

JC: 2019 was the first time that we had such a dramatic climatic impact. Normally a drought doesn't hit both hydroelectric production and agriculture production at the same time. The important point to note is that the water that powers our hydroelectric dams comes from a different drainage basin to the water that sustains soy production. So, in 2019 we were unfortunate that two different droughts, one in Paraguay and one in southern Brazil, hit at the same time. So yes, it's true that a lot of our GDP is related to rainfall, but normally you don't get two simultaneous droughts.

Indeed, Paraguay is a lot less dependent on agriculture than people realise. It only directly accounts for 9% of GDP, whereas services are more than 50%. However, I would agree that Paraguay needs to see accelerated diversification. Fortunately, all the conditions for this economic transformation are in place in Paraguay. With the new trade agreements that the country signed last year, the macroeconomic stability and the relative ease of doing business – it is ready to attract the international investors needed to start new sectors.

LAI: ***What is the biggest threat to Paraguay's economy?***

JC: There are various structural reforms needed to take Paraguay to the next level. Most of them will take a lot of time, but the cheapest in terms of economic, social and political cost is to improve the business climate. It will give you the most significant benefit in the shortest time. That doesn't mean that you should abandon other long-term aims such as improving education – ultimately Paraguay has to run both the 100-metre sprint and the marathon. Improving the business environment will allow us to capitalise on the strong macroeconomic fundamentals that we already have. Since 2003 Paraguay has maintained an impressive level of economic stability and improving the business environment will enhance our attractiveness further to international investors. Indeed, we've seen this government make progress on institutional themes. It has passed a raft of legislation, such as the anti-money laundering laws, that improve the legal framework or investors.

Even if you look at the response to the coronavirus crisis you can see the alignment of the three branches of the state, which shows a level of political maturity and consensus.

LAI: ***The BCP is one of Paraguay's most respected institutions but some say it's too conservative…***

JC: There is an interesting difference between central banks on South America's Atlantic coast and those on the Pacific. In Chile, Peru and Colombia, the central banks have a more restricted remit. But along the Atlantic, in Uruguay, Argentina, Brazil and Paraguay, the central banks have much broader mandates. In our case, we regulate the finance sector, the insurance sector, we manage the $550million deposit guarantee fund (which restored trust after the 1997 banking crisis) we also produce most of the country's economic statistics and guarantee real estate deposits. All of that is in addition to conventional central bank duties of monetary policy and, more recently, inflation targeting.

A new pensions regulator is being formed and that role will probably be given to us. So, I would say that we have quite enough on our hands without taking more risk. I think the conservative attitude of the BCP helps explain Paraguay's macroeconomic strength. We manage risk and ensure steady monetary policy and inflation, so that the private sector has the right conditions for growth.

Finally, the conservative nature of the BCP is in harmony with the mood of the people. There is a consensus in Paraguay. We've had dramatic episodes in our history and now appreciate the benefits of stability. That's why our currency, the guarani, has survived for 70 years, while others in the region have succumbed to hyperinflation.

A Green Future

An $800million, second-generation biofuel project shows how international capital and expertise can help Paraguay add value to its natural resources...

Paraguay is blessed with raw materials. Its rich soil, abundant water and generous sunlight allow a country of just 7 million people to produce food for more than 70 million, while massive hydroelectric dams give it more electricity per person than any other country on earth. The Paraguay-Parana waterway is also a vital trade route that's allowed the country to develop the world's third-largest river fleet. Finally, it has one of the youngest populations in Latin America, with 70% of all Paraguayans below 35 years old.

But despite these natural advantages Paraguay remains a poor country, with a GDP per capita of $6,000. The reason is that it is failing to add value to these strategic assets. Most of the soy it produces is sent to Argentina for processing. And it only uses 20% of the electricity it generates, with the rest sold cheap to neighbouring Argentina or Brazil. As for the river fleet, it transports Brazilian and Bolivian cargo through Paraguay without adding anything to the local economy. Finally, a failed education system means that the country isn't making the most of its demographic window.

The contrast between Paraguay's natural wealth and economic poverty is no secret. Indeed, adding economic value has become a national goal. And in recent years there have been positive signs of success. Industry has grown steadily, helping to diversify the economy and add growth. But now an emblematic new project looks set to kickstart a brand-new sector in Paraguay and position the country as a global leader in renewable energy. The $800million plan of Brazil's ECB Group to build Latin America's only second-generation biofuel plant is a gamechanger. It will harness Paraguay's key strengths – agriculture, electricity and workforce – on a grand scale, creating exciting opportunities for British businesses.

Omega Green

ECB Group, the firm behind the Omega Green project, already has two biofuel plants in Brazil. But what makes the Paraguayan project stand out is that it will be using second-generation biofuel technology to produce HVO, a renewable diesel, and a renewable aviation fuel known as SPK. These will be made from the biproducts of Paraguay's thriving farming industry, such as animal fat and all types of vegetable oil, including soy, sunflower and palm.

"The crucial difference between the first and second-generation biofuels is the technology", explains Erasmo Carlos Battistella, CEO of ECB Group.

"They are 'drop-in' fuels. That is to say you can use anything from 1% to 100% of this fuel in conventional vehicles. First generation biofuels have to be used as part of a mixture with conventional fossil fuels, however these second-generation fuels can be put straight into a car or plane without any problems. That's a crucial difference because it makes the potential size of the market much bigger than a biodiesel that can only work in combination with a fossil fuel.

"It also means that second-generation biofuels can have a greater positive impact on the environment: advanced biofuels are today one of the main tools for reducing CO2 emissions. The other important characteristic is that they can work at much lower temperatures. "First-generation biofuels can only work at -5 Celsius, whereas Omega Green will produce fuel that can work at -45 Celsius, optimal for use by airlines, an industry that needs effective solutions to reduce CO2 emissions. Again, that makes it a much more versatile fuel."

A winning partnership

As Paraguay's Minister of Industry and Commerce, Liz Cramer, makes clear in her exclusive interview with LatAm INVESTOR, Omega Green is "exactly the type of investment that we need to attract". It isn't so much about the money – although the $800million project is the largest private-sector investment in Paraguay's history and will help boost the country's notoriously low foreign direct investment. But more because it leverages the country's competitive advantages.

It may sound cliché to talk of win-win partnerships. But Omega Green will benefit from the country's low-cost energy, workforce and feedstock, while Paraguay will find a way to make more money from its natural riches.

Paraguay's main competitive advantage is agriculture. It's the world's fifth-largest soy producer, despite being a fraction of the size of the other major producers - the US, China, Brazil and Argentina. Its beef exports are also booming, reaching $1.2billion in 2018, up from around $200million at the start of the century. That makes it a ready source of the vegetable and animal oils that Omega Green needs to produce biofuel. "The most important thing is that we have the feedstock", says Battistella. "Paraguay is already a major producer of animal and vegetable oils. Crucially, it also has the potential to increase output. That matters to us because we envisage strong growth in the coming decades. Moreover, the excellent soil and climatic conditions means that we can develop diversified sources of feedstock here. For example, we are talking with a group of investors that want to grow pongamia to supply us with vegetable oil."

Paraguay is also keen to develop a new market for its agricultural produce. Its diplomatic relations with Taiwan, a legacy from the Stroessner era, has stymied exports to China, which doesn't recognise Paraguayan biological certificates. That's created a real challenge in soy, explains Hector Cristaldo, President of the UGP Paraguay's largest agricultural trade association. "China is the elephant in the room. It is the largest importer of soy, with 67% of global imports, yet we can't sell to it directly as it doesn't recognise our phytosanitary certificates. That means we are left with just 33% of the world market. Moreover, it increases our dependency on Argentina as we have to process our soy there so that it can then be sold to China." One solution is to turn some of that soy into a valuable fuel that can be sold to industrial consumers around the world.

Then you have Paraguay's competitive electricity supply. "We have an abundant supply of low-cost green power, which is particularly well-suited to energy-intensive industries", says MIC Vice-Minister Luis Llamosas. At present Paraguay sells 80% of its electricity cheaply to Brazil or Argentina but Omega Green gives it a more lucrative use for that power. Meanwhile, Paraguay's electricity brings many advantages for ECB, explains Battistella. "After feedstock our main input is energy. Thanks to the Itaipu and Yacyreta dams, Paraguay has some of the lowest energy costs in the region. Moreover, it has abundant supply, which means we don't need to worry about energy security as we grow.

"Finally, and this is very important, it is renewable electricity. Our whole business proposition is to be green and help the planet reduce emissions, so it wouldn't make much sense if our industrial process was powered by gas or coal-fired power plants. Paraguay's secure, abundant and low-cost renewable electricity matrix is a perfect fit for Omega Green."

Then, you have the Paraguayan people themselves. Omega Green will create 20,000 jobs directly and through its supply chains. Harnessing the country's young and expanding workforce. As Llamosas explains, "it's great to have a demographic bonus, but it's also a big challenge for us, the Paraguayan government, to create good jobs for our young people." Indeed, the government is working with ECB to help train a local workforce, says Battistella.

"Therefore, we have developed a training program, by which a team of expatriates will help create the next generation of Paraguayan biofuel professionals."

FUEL OF THE FUTURE?

In recent years biofuels have come under pressure from alternative solutions, such as electric vehicles. The most emblematic EV manufacturer, Tesla, saw its share price quadruple since May 2019 and with a market cap of £135billion is now the world's second-most valuable carmaker. More significantly, all the major conventional carmakers have committed to massive EV programmes in coming years. So will biofuels demand continue to grow?

Battistella doesn't see electric vehicles as a threat. "We are selling something that is complimentary and we are both trying to fix the same problem – emissions. What people need to realise is that biofuels are liquid solar energy. What I mean by this is that our fuel derives its energy from plant or animal fats and oils. Given that the animal obtains its energy from eating grass or feeds, then the source of all of our energy are plants. The plants, as we all know, get their energy from the sun via photosynthesis. So that means that the energy source for all of our fuels is the sun – that's why biofuels are liquid solar energy.

"I support electric vehicles as long as they are reducing emissions. But if the electricity that powers the battery is coming from gas or coal fired power plants, as is the case in most of Europe, Asia and the US today, then we have a problem. Another issue is the electric cars themselves. They use much more copper, lithium and rare earth metals than a conventional car, so making an electric vehicle produces extra emissions. Finally, we need to look at what happens to the battery once it has been used. If it is not processed responsibly it will cause further environmental damage. There haven't been many studies into the lifecycle of electric vehicles and batteries, which is a marked contrast to the biofuel industry where we are forced to adhere to rigorous standards."

Crucially for Paraguay, the second-generation biofuel that Omega Green will be producing is even more resilient against electric vehicles. "It is a much more practical option for most consumers", says Battistella, "because it can simply be poured into existing engines. That is especially true in the aviation industry – biofuel can power a commercial flight from London to Sao Paulo, which isn't possible with a battery."

Erasmo Carlos Battistella, CEO ECB Group

Food security myth

Detractors of biofuels claim that they undermine food security by using up precious crops. But with second-generation biofuels that isn't the case, explains Battistella, as they can be made from agricultural waste products. "With soy we don't use the soy bean but the oil that is produced as a bi-product. People do not eat soy oil – indeed the market currently has a surplus of 40 million tonnes per year. It's the soy flour that is used to make animal feed that helps to produce the cows, chicken and pigs that the world needs. In fact, the support that the biofuel industry gives soy by purchasing surplus soy oil encourages farmers to plant more soy, thereby increasing overall food supply." The food criticism makes even less sense in Paraguay, a country with a large surplus that already exports grains and meats to the rest of the world.

Future

Omega Green's scale and cutting-edge technology mean it's an ambitious project for Paraguay. Over the next decade it will add $8billion to Paraguay's economy – a huge contribution to a GDP that currently stands at $45billion. Yet Minister Cramer hopes this is just the first step on Paraguay's journey to becoming "a world leader in green energy". Battistella agrees and predicts that the plant will be the catalyst for Paraguay to create a bio-industrial cluster. "In the same way that a refinery often helps to kickstart a petrochemical industry, the fuel we produce can form the basis for bio-plastics… By 2030 I expect to see a huge industrial park around Omega Green. with several world-leading green companies making renewable products that can help change the world."

If this happens it won't just kickstart a new industry, it will transform the country. Gustavo Volpe, President of the UIP, Paraguay's most important industrial association, is adamant that these types of projects will help create a new Paraguay. "I really believe that the best way to develop a society is through industry. I'm not just talking about economic growth but about social development. In 2011, industry accounted for just 10% of Paraguayan GDP. Now it's 32%, so we have seen a massive growth in a short period of time." Llamosas is confident that it will happen. "I expect that our GDP per capita will grow exponentially over the next decade. Today it is $6,000 per capita but we want to double or even triple it."

It is to this government's credit that it is working hard to attract world-class industrial projects like Omega Green. Moreover, the fact that companies like ECB are willing to commit hundreds of billions of dollars in a long-term investment is a reflection of Paraguay's hard-won macroeconomic strengths. "Paraguay is a financially and economically stable country, which stands out in the region", says Llamosas. Indeed, its currency, the guarani is the oldest in Latin America. Of course, the spread of coronavirus makes it more difficult to offer stability to long-term investments. Yet Battistella, believes that pandemic-related turmoil could presage a shift to biofuels. "The dramatic crisis is demanding important changes in the way companies work.

"One of those changes is undoubtedly the energetic matrix that we will have once economic activity returns around the world. This global downturn shows what we can achieve in reducing emissions. Today it is the economic recession that is bringing down the level of emissions, but the question we must ask ourselves is: will we increase emissions again once the economy recovers? I believe that we have an opportunity for a structural change in global energy and to achieve an economy that coexists better with the environment. Advanced biofuels are at the forefront of that change and we are proud to be part of that change."

It's been a long-time – 150 years to be precise – since Paraguay last led Latin America's industrial development. Halfway through the 19th century it had the region's first iron foundry and a railway before the likes of Brazil, Argentina, Colombia or Mexico. Back then British companies played a role, sending engineers and machinery to help Paraguay's industrial development. The UK is still involved today, with British bank Barclays helping to raise finance for Omega Green. As Paraguay's biofuel cluster grows there will be plenty more opportunities for UK plc.

TRADE SPOTLIGHT:

Paraguay's Minister of Industry and Commerce,

Liz Cramer,

explains why British businesses should come to her country...

LATAM INVESTOR: ***What's behind the recent FTA successes?***

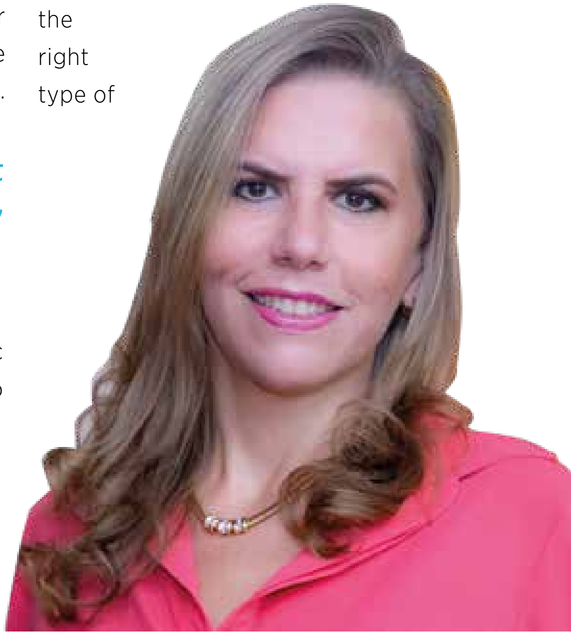
MC: We are fully aware that we need to diversify the Paraguayan economy and strengthen exports – either through access to new markets or diversification of our exports. So, while 2019 was a tough year for the Paraguayan economy it was very productive in terms of international agreements. The main one was clearly the provisional free trade agreement with the EU. It's important to note that we don't need to wait for other countries in Mercosur to ratify this. There are several parts of the agreement that can be implemented on the basis of the agreement between Paraguay and the EU.

The Mercosur-EU trade agreement isn't just significant for Paraguay – it's the largest trade deal in the world. It will lead to tariff-free access for up to 93% of Mercosur production, as duties are gradually cut over the years. Our imports will also become cheaper as 90% of EU production will eventually be able to enter Mercosur without paying tariffs. We believe that Paraguay in particular can benefit as a point of distribution or assembly for European firms that want to enter Mercosur. We are also negotiating with South Korea, Canada and Singapore. The talks with the EU may have taken a long time but they will help with other negotiations as it gives us a template for dealing with other trading partners.

LAI: ***Where are the best opportunities in Paraguay for British firms?***

MC: Britain, in its new economic reality outside of the EU, will no doubt be looking for different markets. Mercosur is a huge market of more than 260 million people and Paraguay is the perfect way to access it. We can offer a competitive base to manufacture for Mercosur because we have low energy costs, an affordable, productive and competitive workforce and an attractive tax regime. We've already seen the rapid growth of an auto-parts industry as international firms have taken advantage of these factors. Indeed, it's worth noting that while the agricultural sector struggled in 2019 – and impacted the whole economy – services continued to grow. We are keen to expand in new areas, such as fintech and telecoms, and they are sectors where the UK has plenty of expertise. As Paraguay starts to grow in more sophisticated industries there is increasing demand for the type of investment and know-how that Britain can bring to the table.

We recently relaunched our export promotion and investment attraction agency – Rediex. We want it to attract the right type of



international investment that can kickstart new export industries and clusters in Paraguay. A good example of this is the $800 million Omega Green project led by ECB Group, a Brazilian firm. This advanced biofuel plant has the potential to consume 20% of our soy output and turn it into a more sophisticated value-added product which has several markets eager to implement greener and sustainable fuel practices. It's not just biofuels, eventually it will become a cluster for green industry, with products such as renewable plastic among others.

This is exactly the type of investment that we need to attract. It will create an industry that puts Paraguay at the forefront of where the world is going in the 21st century. It also has a large positive impact on our country because its local supply chains will support 20,000 Paraguayan families. Crucially your readers need to understand that we don't just want to sell our young workforce and cheap, green energy to anyone. We have abundant supplies of both but they are finite. Therefore, we want to offer them to industries that will really have a positive multiplying impact in Paraguay. Omega Green will position Paraguay as one of the world leaders in green energy.

LAI: ***How will Paraguay's economy be impacted by coronavirus?***

MC: We foresee that Paraguay, like many other economies in the world, will suffer from short- and medium-term effects of the necessary quarantine to fight against Covid-19, but Paraguay's unique blend of sectors also makes it a resilient country that produces what the world demands right now and after: commodities, food products, pharmaceuticals and light manufacturing related to medical and chemical industries. We hope that our short-term sacrifices in implementing a strict and early quarantine, since March 11th, have ensured that our population is safe, healthy and productive in the long-term.

LAI: ***What about challenges, such as labour skills and electricity distribution?***

MC: We only consume 20% of the energy that we generate, with the rest sold to our neighbours, so there is no problem with supply. However, a historical lack of investment in distribution has led to some areas suffering from temporary power cuts. This government is accelerating an initiative, begun by its predecessor, to invest heavily in our electrical distribution network. We are rolling out 500kv high-tension lines to reduce congestion in certain parts of the grid. And we are laying the smaller 200kv lines and micro distribution needed to connect the end users with the substations. The state-owned electricity company, Ande's, investment budget for 2019 was $520million. We are also very responsive to the private sector. If a company highlights a problem to the government, then Ande can send a team to reinforce the substation in that area. So, we are troubleshooting in the short-term while investing in the longer-term.

But let's be frank with your readers. Paraguay is an emerging market that is in construction. Not everything is perfect now, which is why early movers – investors who come now – will have an advantage and pay lower prices than those who come in five years when everything is fixed. I will share with you another insight: Paraguay is one notch below investment grade, and we remain so even in these turbulent times, so assets now are still relatively attractive and affordable than they will be in five years.

As for the local workforce, it is actually one of our strengths. We have a demographic bonus, with a young and growing workforce that means there is availability of labour and demand for jobs. That helps to keep wage costs competitive. Moreover, many of the international companies here say that Paraguayans are among the most productive workers of their global operations. Historically, education was a problem which is why Paraguay launched an ambitious scholarship programme. Currently there are 1,500 Paraguayans studying abroad in the world's best universities. The government pays for them to study MBAs or PhDs in any global top-ranked university on the understanding that they will return to the country once they graduate. The first scholars are beginning to return so we will start to benefit from the programme. It is true that there can be a lack of middle management in very niche industries. That's obviously the case for the emerging sectors that we are trying to promote in the country.

LAI: ***Paraguay is a small nation surrounded by giants; does that make Mercosur inherently unworkable?***

MC: Mercosur is an imperfect customs union. If we so wished, we could complain about it every day but that will not help us develop Paraguay's trade or industry. Brazil has more than 200 million inhabitants while Argentina has almost 50 million compared to our almost 7 million. Clearly there are lots of industries where we can't compete with them. However, we do not want to compete with Brazil. We want to integrate ourselves into its supply chains. In fact, Paraguay can help make Brazilian products more competitive by offering low-cost, specialized and complementary parts. Fortunately, the Brazilian government sees and understands this, which is why we concluded the auto parts, a subsector not covered by Mercosur, bilateral trade deal last year. We also reached last year an auto parts trade deal with Argentina.

Your readers probably understand that the world now competes as regional blocks. In North America you have new Nafta agreement, while in China the ASEAN countries have integrated themselves in Chinese supply chains. Soon Mercosur auto manufacturers will have to compete on a tariff-free basis with European cars so it's vital that we work together to become as competitive as possible.

Historic Opportunity

Infrastructure was already the biggest investment theme in Paraguay; now coronavirus will accelerate the building boom...

Paraguay's history can be read through its infrastructure. Its belle epoque halfway through the 19th century coincided with the construction of railways, telegraph lines and government buildings. Little was added in almost a century of economic wilderness and political instability following the crushing defeat in the War of the Triple Alliance.

The 35-year rule of dictator Alfredo Stroessner heralded another building boom. During the Strosnato around 3,500 km of asphalted highways were laid, two new large bridges improved connections with Argentina and Brazil, while the construction of the Itaipu dam gave Paraguay more electric power per person than any other country on earth. Stroessner was deposed in 1989 and the newly-liberalised economy encouraged sporadic private-sector infrastructure investment, such as fluvial ports that handle the new river cargo trade, and piecemeal public-sector roadbuilding.


UIP President, Gustavo Volpe

But there were no grand, iconic works to mark out the last 30 years as a powerful period in Paraguayan history. That's probably because the economic growth was accompanied by political chaos. And without strong leadership it's impossible to realise big projects. Infrastructure needs economic and political stability. Moreover, because projects take time to plan and build, a country needs to sustain those conditions for several years.

It's no coincidence that the first signs of an infrastructure revival came with Paraguay's first economically and politically strong post-dictatorship president, Horacio Cartes (2013 to 2018). He passed a public-private-partnership (PPP) law to encourage private-sector infrastructure investment and also initiated a plan to improve Paraguay's failing power distribution grid. The progress has accelerated with the current government, which invested $1billion in infrastructure in 2019. It didn't just spend money, it managed to do something with it. Approximately 1,000 km of road were built last year, taking Paraguay's total to 8,000 km. Increasing your country's total stock of roads by 15% in one year is no mean achievement but it's only the start. The government has unveiled plans to invest a further $1billion per year on infrastructure for the next decade. This is in addition to billion-dollarinvestment programmes in electricity distribution and water treatment. The sums being invested, in addition to the new PPP model, make this an exciting investment theme for UK companies.

> "Within five years we should have a reliable electricity supply. In total, $1.5billion will be invested in our electricity grid between 2019 and 2024

Commercially viable

Regular readers will have read about infrastructure deficits in most other countries in the region and Paraguay's deficit of $25billion isn't the largest that we have written about. But what makes it interesting is that so many of these projects are commercially viable. One reason is because of the strong macroeconomic position of Paraguay, which will improve with the renegotiation of electricity export prices with Brazil in 2023.

"Over the next decade Paraguay will be building hospitals, transmission lines, roads and schools", says Rodolfo Vouga, Managing Partner of local corporate law firm, Vouga Abogados. "Moreover, thanks to the extra funds that will likely come from the Itaipu renegotiation in 2023, we will have money to make them

Paraguay is at the beginning of a decade-long building boom

happen."

The other reason these projects are commercially viable is that the country's infrastructure simply hasn't kept paced with its strong economic growth. "The Chaco is another massive opportunity", says Vouga. It was ignored for much of our history, as a barren desert. But now technological advances, such as drought-resistant crops, have opened up its potential." Guillermo Mas, CEO of Construpar, the largest roadbuilder in Paraguay, and President of Cavialpa, a local construction chamber, agrees about the potential of the Chaco. "It makes up more than 60% of the country and is becoming very prosperous. You have strong dairy, meat and rice industries there. Opening up the Chaco and improving its links to export markets will create a direct economic return."

Nestor Loizago, Managing Partner of the Paraguay office of Ferrere, a regional corporate law firm, is another who believes that the country's infrastructure has lagged its economic growth. "A huge wave of Brazilian investment, that began in the 1970s, sparked a boom in agricultural production. We only have one bridge with Argentina and one with Brazil, which means an incredible amount of our imports and exports go through these strategic points. This government is adding more bridges but probably the most exciting infrastructure project is the bi-oceanic corridor. This is a new road that will eventually connect Paraguay to Chile's Pacific ports. It's strategic and, most important of all, it's actually happening."

Financing

Until the arrival of Cartes there was only one way to build infrastructure in Paraguay – a conventional public tender. His government introduced two more mechanisms for the state to procure infrastructure. The turnkey model, which involves the state committing to buy sections of a road as they are completed by the construction company. Then you have PPPs, where the state creates a fund that uses future revenues, say from road tolls, to repay the private-sector investor. At present, the conventional model still dominates, with just three large turnkey works, including Paraguay's stretch of the bi-oceanic corridor and one PPP project – expanding part of the highway from Asunción to Ciudad del Este – currently approved.

Of the new models, turnkey has proved the most successful so far. Perhaps because it is something of a compromise, the private sector has to finance each tranche of work but is able to recoup its investment at regular and pre-agreed intervals from the state. "Turnkey projects in Paraguay operate under law 5074", says Loizaga. "We saw a few projects successfully use this model under the previous government.

Incredibly the financing for these turnkey projects were getting better rates that the Peruvian Government's sovereign paper. That's notable because Paraguay is not investment grade like Peru, yet investors liked the macro story and the prospects for infrastructure inside a well-run economy. I think that this is a good option for investors. Especially if they come with a pre-packaged project that is already designed and present it to the government, it will be easier to get it off the ground. Paraguay does not have a financing problem – indeed it has credit lines worth $1.5billion with the IBD and CAF in approved loans for infrastructure that have not been dispersed."

But while turnkey projects have gotten off to a quick start there are some

... Continues on page 32

President of Paraguay,

Mario Abdo Benitez,

on his country's battle with coronavirus and why it's still the perfect partner for UK plc...

LATAM INVESTOR: *How will coronavirus impact Paraguay's economic growth in 2020?*

PRESIDENT BENITEZ: The initial projection was for 4% economic growth in 2020, driven by the rebound of our agricultural and livestock sectors as the farming sector recovered from the drought in 2019. But now, the outbreak of the Covid-19 pandemic, which has hit the world economy, has impacted Paraguay's growth figures for 2020. The hit to production related to the health emergency and the consequent lockdown measures will be far more serious than the losses we saw after the global financial crisis of 2008 to 2009.

The IMF's latest global economic outlook predicts a global recession with a 3% contraction. For Latin America and the Caribbean, the situation is even worse with an estimated fall of 5.2%. In the case of Paraguay, the IMF is more positive and believes the economy will only shrink by 1%. That reflects Paraguay's fundamental macroeconomic strengths and the positive impact of our coronavirus package of fiscal and monetary economic measures worth 9% of our GDP.

The fiscal component amounts to 4.6% of GDP. It's comprised of a health spending boost worth 1.2% of GDP, direct transfers to formal and informal workers impacted by lockdown of 1.8% of GDP and extra capital to the guarantee and credit fund for SMEs. It also includes additional funding for social security and public services, worth 1.6% of GDP, as citizen payment has been deferred.

In monetary terms the Paraguayan Central Bank has significantly reduced interest rates. Moreover, it has added liquidity amounting to 4.5% of GDP, through financial measures, such as the reduction of required reserves. It's the largest monetary package in Paraguay's history and we are confident that these measures will mitigate the negative economic impact of the lockdown and lay the foundations for a solid economic recovery in the second half of 2020 and in 2021.

LAI: *Paraguay is 125th in the World Bank Ease of Doing Business Rankings; how will your government improve the business environment?*

PB: The government has been working on a package of structural reforms that aim to improve the business environment, our economic competitiveness and strengthen institutions. It's not enough to increase public investment, we need to improve the efficiency and quality of the spending. We are conscious that reforms of health, education and social security are urgent to empower the human capital and ensure sustainable growth over the medium term. Improving the business environment is one of our key aims.

Despite the fact that 2019 was a bad year for the economy, we managed to advance in our reform agenda. We have passed an important package of anti-money laundering legislation, while we also updated our tax system. The changes to the tax system will make the system fairer and also improve the business environment because it reduces the effective tax rate on profits and simplifies the tax code, which should encourage micro businesses to enter the formal economy.

To the same end, we created a new legal structure – Company of Simple Shares – which is a great tool for investors in Paraguay. We are now refining that regulation and working on a unified platform for opening and closing companies that should make it easier to start a new business in Paraguay. We have more legislation sitting in Congress that will also work to reduce bureaucracy for business and make it easier for SMEs to access credit. We have a particular focus on SMEs because they employ 76% of the Paraguayan workforce.

LAI: *What are Paraguay's competitive advantages to attract investment?*

PB: In recent years Paraguay has improved the environment for international investors, maintaining a healthy rhythm of economic growth, with low and stable inflation and sustainable fiscal accounts.

One of the main advantages is our low tax take for businesses. Then you have the special tax regimes for attracting investment, for example we have favourable taxes for free zones and public-private-partnerships. Finally, you have our people, which offer both a young workforce and a growing middle class.

LAI: *Paraguay has positive demographics; how is your government taking advantage of the opportunity?*

PB: Equipping the human talent of our young population and preparing them for the challenges of the future of work is one of the objectives of our government. It's estimated that our demographic window will continue until 2054, which gives us time to enact real change.

Paraguay's strategy is to build quality health and education systems, with the main emphasis focused on the initial stages of life. At present we are working on a reform of both systems. In the short-term they have both been impacted by the Covid-19 pandemic and we are creating a fund to help them survive the crisis. Moreover, education and training will be key for us to be competitive in the global economy, allowing us to boost productivity and create a higher standard of living. In the coming years we will see significant increases in demand for health and education, which is why we are working now to ensure new professionals have the skills and preparation necessary to be the teachers, doctors and nurses of the future.

We realise that this demographic window will only be positive if our abundance of young people is translated into an increase in productivity that results in greater earnings and higher savings that can be used for investments.

LAI: *There is limited trade and investment between Paraguay and the UK; how do you plan to improve the business relationship?*

PB: Since the reopening of UK Embassy in Paraguay in 2013, bilateral relations have been strengthened. We know that the UK sees us as a commercial ally, with a stable economy and key sectors like agribusiness, energy, trade and services. On our side, we have identified more than 60 items that Paraguay could export successfully to the UK. They are mainly from the agribusiness sector, such as soy, maize, meat, leather, vegetable oils, organic sugar, stevia and rice. On the other side of the trade, we buy heavy machinery, alcoholic drinks, vehicles, fuels and chemicals from the UK, which shows that our economies are complimentary.

In 2019 trade between the two countries was worth $157 million and we are convinced that we can strengthen this. We also want to continue our good work in education cooperation, through programmes like Chevening and Becal, so that Paraguayan citizens can study post-graduate degrees in the UK. Paraguay and the UK maintain strong historic links in diplomatic, economic, commercial and investment areas. We are sure that our country can find more opportunities in the UK, especially given that we are strategic partners.

LAI: *Your period as president ends in 2023; what will your legacy be?*

PB: I hope that when the presidential period finishes, we will have strengthened the Republic's institutions, having built upon the macroeconomic bases that we will have preserved. We will leave the important legacy of a health system and public education that offers a quality service to all Paraguayans without exception and we will have a state that is more efficient and a tax system that is fairer.

... Continued from page 29

limiting factors. As Minister of Public Works and Communications, Arnoldo Wiens, explains in his exclusive interview with LatAm INVESTOR, "Turnkey projects are seen as problematic for the country's cashflow". In simple terms the Ministry of Finance doesn't appreciate committing to make a series of relatively short-term payments. A preferred option are PPPs, which provide longer-term financing, but are also more complex.

PPPs

Over the past decade, we've seen a host of Latin American countries attempt to use PPPs to procure infrastructure with varying degrees of success. It took Colombia around seven years of legal wrangling, failed projects and corruption claims before it really got to grips with the model. Yet Colombia is one of the success stories because it has, at least, managed to build important project under the model. In Peru the infrastructure programme was stalled for years and is only now restarting.

So, it is perhaps little surprise that it has taken Paraguay five years to finally execute its first PPP project. "Paraguay's new PPP law is well drafted", says Loizaga. "In an ideal world all of the $10billion infrastructure programme would be built under this mechanism, but the state doesn't have the capability to manage many PPP projects. Here in Paraguay there are lots of important infrastructure works that need to be built and our fast-growing economy would make them economically viable.

However, our fiscal responsibility law prevents the government from running an annual fiscal deficit above 1.5% - although in exceptional years, such as 2019 it can run to 3%. Here the Ministry of Finance has decided that the PPP projects still count as a liability on the nation's fiscal account, which means that they will be limited by the fiscal deficit restraint."

It's widely agreed that, for now, the government can only process a few of these complex projects. "The PPP law works OK for building roads", says Alejandro Pierra, Partner at GHP, an Asunción-based legal boutique. "That's because roads are relatively simple projects that don't involve lots of interaction between multiple government agencies. However, we tried to build the new airport with a PPP and it failed because it's a complex project that involves many different entities and regulations. The law gives the prerogative to the MOPC, which is fine for building a highway but doesn't make sense when you have something like an airport where lots of other authorities have a critical role to play." Ironically Pierra thinks the lack of institutional capability to procure infrastructure stems from the Stroessner era. "Back then, if the president wanted to build a road, he just found the money and told the ministry to make it happen. So, we don't have a culture of interaction between ministries to build infrastructure."

It's not just the public sector that is struggling to cope with PPPs. Jose Luis Heisecke, the CEO of Constructora Heisecke, a large local infrastructure builder, and CEO of construction chamber Capaco, admits his firm has found the new model difficult. "We are used to dealing with the government, where the Ministry of Public Works and Communication is the ultimate boss, even if the money is coming from other sources, such as the IDB or CAF. The PPPs are very new for us and local companies, including my own, are not accustomed to going out and raising the finance to build a road."

For many British investors, PPPs would

COMMUNITIES

In other Latin American countries one of the biggest hurdles to executing infrastructure projects has been opposition from local communities and environmental groups. Yet in Paraguay, these issues have been less pronounced.

One man well placed to judge the potential challenge is Walter Biederman, a former Paraguayan Ambassador to Colombia, who founded a local environmental NGO and co-authored the seminal book on Paraguay's indigenous peoples - Los Indígenas del Paraguay. "I worked as a consultant to a British oil company in the Chaco and we never had any problems here. Normally, international investors that come here adhere to the best practices.

Moreover, local regulation has improved considerably and it's well enforced so there isn't much room for error. In general Paraguayans are not conflictive people. So as long as they don't feel that you are taking advantage of them there won't be a problem. However, if you are coming to Paraguay because you think you can get away with a practice no longer allowed in your home country then you are in for a shock."

That view is shared by Mas, whose company has built projects across the length and breadth of Paraguay. Though he makes an interesting distinction.

"In the Chaco you don't get community problems because you are mostly dealing with large landholders. These are people who want your project to succeed because you are improving their access to market. In the east of the country, it's a different situation as it is more densely populated with lots of small landholdings. I feel that sometimes the situation in the east is manipulated by politicians or social movements."

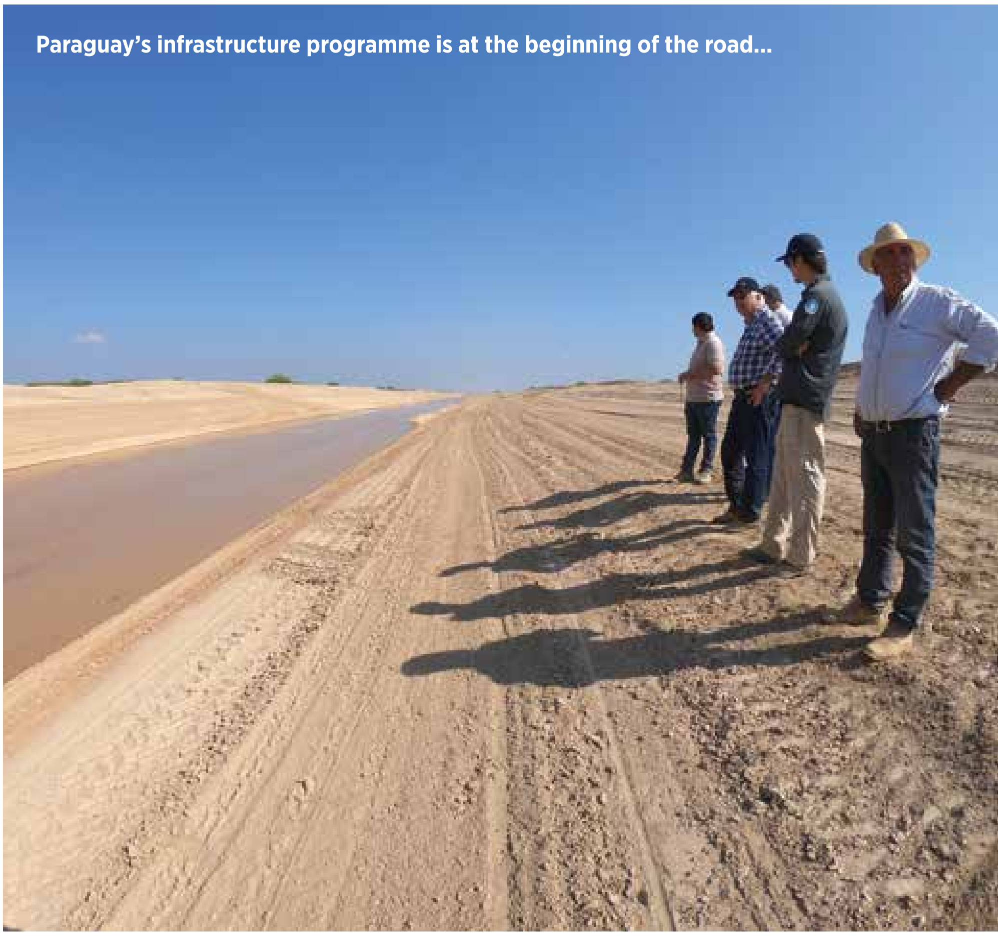
be the preferred way to play the Paraguayan infrastructure story. And Minister Wiens expects the model to become increasingly common. "I think APPs will account for around 30% of the infrastructure built over the next decade. The model has financial advantages and over time we will become more adept at using it."

Power demand

Paraguay has less roads per person than every other country in Latin America bar Haiti, so you can understand why this government is so keen to build them. But there are plenty of other vital works that will take place in coming years. One of the most important is electricity distribution, says Gustavo Volpe, President of the UIP, Paraguay's largest industrial association.

"Despite generating lots of electricity, the power supply is unreliable and you can suffer blackouts. Fortunately, this problem is in the process of being fixed. The government is investing hundreds of millions of dollars in upgrading the transformers and distribution lines and within five years we should have a reliable electricity supply. In total, $1.5billion will be invested in our electricity grid between 2019 and 2024."

Guillermo Krauch, President of the Paraguayan British Chamber of Commerce, is a former director at the state-owned electricity utility who understands the challenge well. "Paraguay's power sector is managed by the National Electricity Administration (Ande by its Spanish acronym). It is a vertically-integrated state company in charge of generation, transmission and distribution. Ande owns three hydropower plants that provide the country's electricity supply: 210 megawatt (MW) Acaray, 14,000 MW Itaipú, which is co-owned with Brazil's Eletrobras who shares half the power, and 3,100 MW Yacyretá which splits production evenly with fellow owner, Argentina.



Paraguay's infrastructure programme is at the beginning of the road...

"Paraguay's maximum demand is 3,500 MW, which means the excess is sold to our neighbours. However, electricity consumption in Paraguay is growing at a rate of around 7% to 8% per annum in MW, meaning Paraguay must double the capacity roughly every ten years. The challenge for Ande is not generation, but improving the grid to handle the increased demand. "This is a great opportunity for British investors as Ande will be holding tenders worth more than a billion dollars in the coming years as it upgrades the grid. The main aims are to connect the two mega hydroelectric dams, which will give the grid more flexibility, and to add transforming capacity to improve the quality and reliability of the power provided to customers." The Chamber is keen to support UK firms looking to work with Ande.

It's clear that Paraguay needs more infrastructure. Moreover, it has the money to build it. Whether through direct government funding, development bank finance or future earnings from commercially viable projects. Finally, the government has shown its determination to build it. That resolve is likely to be strengthened by the coronavirus crisis.

Large infrastructure projects are one of the most direct ways for Paraguay to kickstart economic growth and create employment. The fact that work on more than 250 infrastructure projects continued throughout Paraguay's coronavirus lockdown, demonstrates its strategic importance.

If this administration delivers its plans it will build more roads in five years than Stroessner did in 35. History will judge if this is another golden age of Paraguayan infrastructure.

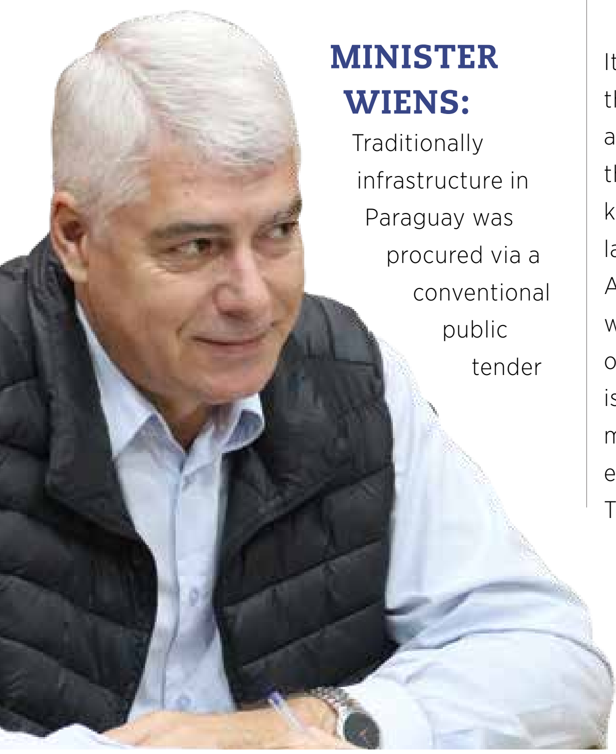
INFRASTRUCTURE SPOTLIGHT:

Minister of Public Works and Communication,

Arnoldo Wiens,

explains how infrastructure will drive Paraguayan growth...

LATAM INVESTOR: *Please tell us about the new 'turnkey' model of building infrastructure in Paraguay.*



MINISTER WIENS: Traditionally infrastructure in Paraguay was procured via a conventional public tender model. However, the last government approved law 5074 for turnkey projects. Under this mechanism companies or consortiums come with their own funding. There were many attempts with different projects that failed due to design flaws or were too complex for the turnkey model, which made it prohibitively expensive for the state. But eventually we developed a successful turnkey project – it was 47 km of highway from Naranjal to San Cristobal. It worked very well, with the road broken into five tranches. As each tranche was completed it was delivered to the state, which paid it in full.

It is now a functioning highway and the turnkey mechanism is being used again for the Paraguayan stretch of the bi-oceanic corridor. This is a 570 km highway, which is currently the largest paved road being built in Latin America. It is 25% completed so far and we expect it to reach 50% by the end of the year. The third turnkey project is Costanera Sur in Asuncion. This is a more complex project as it has larger environmental and social impacts. There are two elements to the plan.

The first involves strengthening the embankment of the River Paraguay as it runs along our capital city. That will be built under the turnkey model. Then the second is the construction of 2,500 houses, which will be financed under the conventional tender model with a $100million loan from the InterAmerican Development Bank (IBD). These will replace the informal residences that currently suffer from seasonal flooding.

LAI: *Paraguay recently passed a PPP law; how successful is this model?*

MW: The public private partnership law was also passed by the previous government. The APPs, as they are called here, involved many failed initial attempts. It was unsuccessfully used for the new airport but when we came to power, we cancelled that project – the airport will now be built under the conventional model – because there were too many irregularities and we didn't want APPs to be tainted in Paraguay. But eventually we found the right project for Paraguay's first APP – the widening of Ruta 2, the highway that connects Asuncion with Ciudad del Este. It is the country's most important road and trade will benefit from having two-lanes in both directions. The project was stalled when we took over but we have managed to get it moving again.

When we look at other countries that adopt PPPs we can see that it often takes five years for the model to be successful. It needs time for the public sector to accrue expertise and understanding of the model, while the local bank and construction companies also have to adjust. Now we have this first APP under construction it will allow us to build up understanding. The Ministry of Finance is very keen for us to use the model and working with the IBD we created a shortlist of seven potential APP projects, which we have now narrowed down to two likely targets. That is the duplication of Ruta

1, which heads south from Asuncion, and a 50 km section of Ruta 6.

LAI: ***Which model will be more common over the next ten years?***

MW: Our government target is to invest $10billion over the next decade on infrastructure – excluding water works. I think that around 60% of the new infrastructure will be built under the conventional model, with loans from the likes of the IDB, CAF etc. Turnkey projects will probably make up 10% because they are seen as problematic for the country's cashflow. I am hopeful that perception will change. Because all though it's true that they require quick payment, they also build infrastructure quickly, which means that the state begins to benefit economically at an earlier stage. Perhaps when we have built more infrastructure under the turnkey model, we can study the economic benefits of their quick completion and counter the current criticism against it. I think APPs will account for around 30% of the infrastructure built over the next decade. The model has financial advantages and over time we will become more adept at using it.

LAI: ***Many Latin American countries have struggled to execute ambitious infrastructure programmes; why will Paraguay succeed?***

MW: I think that the Ministry has shown good management of APP projects. We were right to cancel the airport APP when we did. We also cancelled a large, controversial bus turnkey project. They weren't popular decisions but we could see that these projects that we had inherited from our predecessor were badly designed. If you have a poorly-planned project then it doesn't matter what model you use, you will have problems. Moreover, we are not aloof. We are happy to received project proposals from the private sector, because we realise that they have in-depth knowledge in specific areas that we can't match.

Work is well underway on Paraguay's section of the bi-oceanic corridor - the first road to cross South America

Our ideal consortium is made of large local companies and international firms with a specific expertise. I think that any foreign player bidding for a project needs a local partner, because if not they will struggle to understand the unique characteristics of the Paraguayan market. However, I want our firms to work with international leaders, so that we can learn from their technology and expertise. That is especially relevant for some of the more complex projects, for example, the country's first suspension bridge. By the end of this government I am confident that Paraguay's stretch of the bi-oceanic corridor will be built. As will the second bridge to Brazil at Presidente Franco. Meanwhile Ruta 2 will have four-lanes along its entirety, while the new bridge to the Chaco, which will also improve links to Argentina, will be complete.

LAI: ***How has coronavirus impacted Paraguay's infrastructure drive?***

MW: The world has changed dramatically with the coronavirus pandemic. Indeed, it makes investment in public works even more important as it will be the engine of economic recovery in our country. The great thing about infrastructure is that it will give impetus to both the public and private sectors. Moreover, the MOPC has shown that it won't be derailed by the coronavirus crisis.

In March, as the crisis developed and the lockdown was activated, the Ministry achieved the best budget execution in its history with an investment of $680billion guaranies – around $105million – keeping 258 works around the country in progress and more than 80,000 Paraguayans in work.

Time to Trade

Paraguay is emerging from its historic isolation to establish itself on the global trade map...

Paraguay's economic history is one of isolation. 'An island surrounded by land' it's been physically and politically cut off from world trade for most of its life as an independent nation. But over the last 30 years that slowly began to change. Liberalisation of the economy allowed Paraguayan grains to enter global commodity markets, while entry to regional trade bloc Mercosur in 1991 was Paraguay's first ever trade agreement. In recent times, as Paraguay's exports have become increasingly sophisticated and competitive, the country's integration into global trade networks has accelerated. This government has already signed two new trade deals, while better quality and branding is helping Paraguayan products reach new markets. There is still much to do – incredibly Paraguay doesn't have a direct flight to the US – but the pace of change is quickening and the Paraguayan trade boom will create opportunities for both British importers and exporters.

Historic isolation

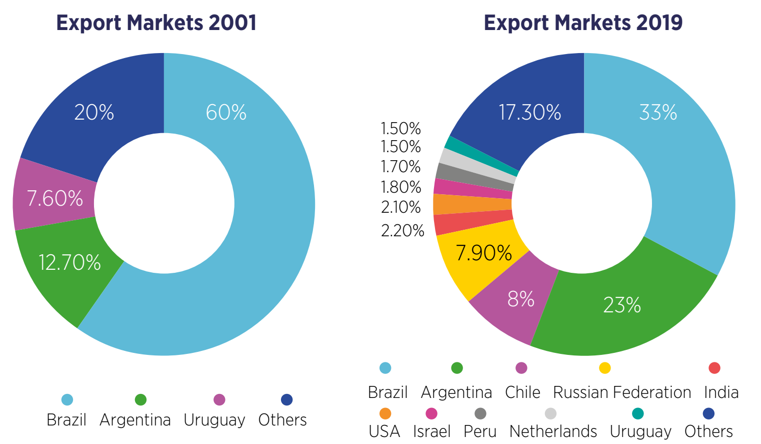
A quick look at a world atlas provides the most obvious reason for Paraguay's historic isolation. Its only access to the sea is through more than a thousand kilometres of the Paraguay-Parana waterway. The tough location meant that despite being one of the earlier Spanish colonies, it was soon usurped by Buenos Aires. But politics also played a part. Paraguay's first post-colonial ruler, José Rodríguez de Francia, cut the country off from the world for 30 years at the beginning of the 19th century, while dictator Alfredo Stroessner did something similar at the end of the 20th. Of course, the isolation wasn't always of Paraguay's choosing. The War of the Triple Alliance, left the country sandwiched between two hostile, giant neighbours, while the resulting economic devastation meant it missed out on the wave of European immigration that kickstarted growth in Latin America's newly-independent economies.

But Paraguay needs trade. It's no coincidence that the country's 'golden era', during the presidency of Carlos Antonio López, was a rare period of Paraguayan interaction with the world. López sent emissaries, including his son, to bring back the latest in European technology, human talent and ideas. Moreover, the world needs Paraguay. It's rich in fresh water, renewable energy and food and this country of just 7 million people currently produces food for more than 70 million. So, it was a historically significant moment when Paraguay ended more than a century of trade isolation by signing the Mercosur agreement in 1991.

Mercosur

"Paraguay is an export platform to the rest of Mercosur, which is a market of 260 million people", says Luis Llamosas, Vice-Minister of Industry and Commerce. "Today most of our industrial exports go to Brazil, where they can enter tariff-free." It's not just about selling goods to Brazil, explains Llamosas, it's a way for Paraguay to enter regional supply chains. Paraguay is already doing that through the manufacture of car components, which is one of the fastest-growing industries in the country. In the last ten years, annual auto-part exports have grown exponentially, reaching $600million in 2019 up from around $10million in 2000. "We want to help the Brazilian auto producers make their cars more competitive", says Llamosas. "We believe that if we focus on niche products and integrate ourselves into Brazilian supply chains, we can help them sell more cars globally. For example, we produce electric cables for car wiring at a far lower cost than they can in Brazil, so by adding our cables they become more competitive. But

Over the Past 20 Years Paraguay's Exports Have Found New Markets



this is complementary because clearly there are many other things, such as the assembly of mass-produced vehicles that we can't do because we don't have the scale." Surprisingly car component trade was not covered in the original Mercosur agreement, so this government finally secured the future of the industry by signing a specific agreement with Brazil and Argentina in 2019.

Singing an auto-parts FTA with its largest neighbours, demonstrates the government's commitment to establish Paraguay on the world trade map. But the fact that it needed to be done and took almost three decades to get over the line, shows the limits of the original Mercosur treaty. Incredibly another area that is not covered is meat, explains Federico Robinson, CEO of Ganadera Vista Alegre, one of the largest cattle producers in Paraguay. "The abattoirs here have an oligopoly, which allows them to control prices. Sometimes they reduce the numbers of animals being slaughtered, which creates a huge oversupply of cattle that pushes down the liveweight market. In an ideal world we should be able to take our livestock to Brazil or Argentina to be slaughtered."

In Paraguay you tend to hear more criticisms of Mercosur than you do in Brazil or Argentina. Rubén Ramirez, a former Paraguayan Foreign Minister, says there are two reasons for this. "Paraguay is relatively isolated, as we don't have a deep-water seaport of our own. That means we have to rely on our neighbours for access to world markets. The other challenge is that Mercosur is institutionally weak. The larger members, Brazil and Argentina, often choose which regulations they want to adhere to. Paraguay is the only member that follows all of the rules, even when it's to our disadvantage. There is no supra-national authority in Mercosur, unlike in the EU, so it makes it hard for a small member like us to get a level playing field."

> ***"Paraguay is an export platform to the rest of Mercosur, which is a market of 260 million people***

Luis Llamosas, Vice-Minister of Industry and Commerce

They are valid criticisms of Mercosur but even Ramirez sees the deal as positive overall, noting that it extends Paraguay's 'economic sphere of influence'. "Our location and neighbours add to the attractiveness of Paraguay for UK businesses. If you draw a 300 km radius around any of our main cities – Encarnación in the south, Ciudad del Este in the east and our capital, Asunción – you end up with a market of 50 million Paraguayan, Argentine, Bolivian and Brazilian consumers with a GDP per capita that ranges between $15,000 to $23,000 per year. Within that sphere of influence Paraguayan goods can be very competitive, so it's an important market."

EU megadeal

If Mercosur helped make Paraguay a relevant trade force in the region – the deal with the EU gives it global reach. In June 2019, after two decades of tortuous negotiations, Mercosur and the EU reached an agreement in principal for what would be the world's largest ever trade deal. In Europe there is considerable scepticism about the agreement becoming reality but the Paraguayan government is far more optimistic.

Didier Olmedo, Vice Minister of Economic Relations and Integration at the Ministry of Foreign Relations, fully expects the agreement to come into effect – and soon. "I am very confident this deal will happen. The wording still needs to be refined. And then it must be translated to the 18 languages of the EU. But we are optimistic that in the second half of the year it will be signed. The economic aspects of the treaty do not need to be ratified by the 26 national European parliaments. They will be passed by votes in the European Commission and the European Parliament, which is in favour of the deal. Even for those parts that need to be ratified by the national parliaments there is a bilateral mechanism. So as soon as a member, say, Germany, ratifies the deal it will come into effect. Needless to say, at our end there won't be any delay in ratification. This deal will allow us to play in the big leagues."

One reason for the European scepticism is the disparity of environmental standards between farmers in the EU and Mercosur. Events, such as the 2019 Amazon fires, which were partly caused by ranchers clearing land, undermine the deal in European public opinion. Olmedo dismisses these arguments. "It's ridiculous, given that we see forest fires in EU members like Spain or Portugal too. Moreover, if you look at the whole package you see that Paraguay, with its hydroelectric energy and waterway transport, is very environmentally friendly. This agreement also forces the parties to adhere to international standards so it's clearly going to be positive for the planet."

A cynic would suggest that the real reason for the opposition is that farmers in certain EU countries, say France and Ireland, do not want competition from South American ranchers. But this, says Olmedo, is based on a misunderstanding. "Under the terms of the deal, Mercosur's agricultural exports to the EU are restricted. Around 60% of our export offer will not be able to go to the EU because there is a strict system of maximum quotas. For example, we can only export 100 million tonnes of meat, well actually it's 66 million, once you strip out the bones." British firms should hope the deal goes ahead as officials in Asunción and London have indicated that the Mercosur-EU deal would be a time-saving template for a future deal with the UK.

Product and price

Signing big trade deals is a good start but Paraguay still needs to make quality products that can compete in international markets. The country already does that with commodities, for example it is the world's 5th-largest exporter of soy, but it needs to diversify. Increasing the range of goods and their markets will make the Paraguayan economy more resilient. It will also grow richer, as more value is added in the country, and generates employment for its burgeoning population.

One traditional industry that became more sophisticated in order to enter new markets is beef. During the middle of the 20th century most of Paraguay's cattle ended up being turned into corned beef by British firm Liebigs. But when the world grew out of love with corned beef, exports plummeted. Nowadays Paraguay's cows have a far fancier destiny, ending up as posh cuts in premium European and middle eastern markets, while secondary beef goes to Russia and Chile. Getting the world's wealthier consumers to choose your meat, isn't easy explains Antonio Espinoza, President of one of Paraguay's largest cattle ranchers, Emprendimientos Rurales. "There are two angles to this. The first is to meet all of the standards – quality, sanitary,

> *"In theory yearly GDP per capita is around $6,000 but from the volumes I see moving in the local market I'd say that the real figure is higher*

Pablo Pappalardo, Director, Grupo Pappalardo

health etc – that specific markets require. For example, our industry is pushing hard to be certified to sell to the US.

"The second is to add more value by giving your meat certain characteristics. There are categories such as grass-fed, organic, naturally-reared, that help your meat obtain a better price in the supermarkets. It's something that we have to work on as a country, from the cattle ranchers, through to the abattoirs – as they are the ones who do the selling - and even the government. One of the characteristics of Paraguayan cattle is that it is grass-fed, that could help us earn a nice premium in the US market. Argentine beef earned a great name and consumers around the world know it's something special. Paraguay hasn't got the volume to do that globally but we can improve our recognition in key markets. We are already seen as a premium meat in Switzerland because our cattle-raising conditions meet their strict criteria, while we also have an excellent taste."

The lesson is that not only does Paraguay need to make high-quality products, it also has to become more sophisticated in branding them. A good example of this is local rum maker, Ron Fortín. The reason that Paraguayan rum is relatively unknown, explains Javier Díaz de Vivar, President, Ron Fortín, "is that until 1989, when the Stroessner dictatorship ended, all the country's rum was made by a state monopoly. We would make a basic white rum, that we call caña, and then sell that to the state, which took care of the ageing, bottling and distribution."

"At the moment just 10% of our sales come from exports, with 90% being domestic, and I want to reverse that ratio over the next decade", says Díaz de Vivar. So, just like Espinoza and the meat industry, Fortín is improving its brand to suit international tastes. "Our rum fits well with a lot of the new trends shaping the consumer market in the developed economies: we have a great story, the product is high quality, we are environmentally-friendly and socially sustainable. People love the fact that we recycle all of the gasses produced in the fermentation stage and even sell some of it as cooking gas. Unlike other sugar plantations we have made a decision to keep cutting the cane by hand as that creates local employment. And we are organic, which is a big driver in many European markets."

Countries across Latin America have seen their exports to Britain grow strongly over the last decade. Except Paraguay. Aside from some soy derived products, there are very few Paraguayan goods in the UK. With the country diversifying its export basket now is the perfect time for UK importers to see what it's got to offer.

TWO-WAY TRADE

Paraguay's small local population and strong commodity industries encourage businesses to focus on its export opportunities. Yet strong local growth means it's also has potential to import more British goods. One man who has already proved this is Pablo Pappalardo, director and member of Grupo Pappalardo, a family conglomerate with logistics, industrial, energy and consumer goods divisions. Last year the group bought the Jaguar Land Rover dealership, in the largest Paraguayan purchase of a British brand for more than twenty years.

"We did it because we believe in British brands and know that they could do better in Paraguay. One characteristic of Paraguayans is that they value high-quality brands and will spend accordingly. We see that with some of the other brands that we distribute here, such as Ford, New Holland, Ferrero, Nutella, and Häagen-Dazs. In fact, I think that there is lots of potential for more UK brands in Paraguay. I would be keen to work with British biscuits, cheeses or marmalades.

JLR is a good example of the power of the British reputation here. Everyone in Paraguay knows that Jaguars and Land Rovers are excellent cars. Our job would simply be to make them more accessible to consumers here."

Moreover, Papparlardo believes the local market has more to offer than British companies realise. "In the last 15 years Paraguay's economic growth has averaged 4% per year. And growing local demand is exactly what you need when you are trying to introduce a new product into a market. Another important factor is that the growth is sustainable. Unlike many other countries in the region, where economies swing from boom to bust depending on the price of a commodity, Paraguay's success is based on a broad consensus in society. The government realises it needs the private sector and has established competitive tax rates. New governments can come or go but the same, pro-business attitude remains.

"In theory yearly GDP per capita is around $6,000 but from the volumes I see moving in the local market I'd say that the real figure is higher. There is still a substantial contribution from the grey economy. However, even the official number will rise in the coming years as this new administration has made inclusive economic growth one of its main objectives. I see the growing middle class every month when I look at our sales of our various brands."

Paraguay's Ambassador to the UK,

Genaro Pappalardo,

on why Brexit and coronavirus will strengthen ties between the two countries...

LATAM INVESTOR: *How do you hope to improve relations between Paraguay and the UK?*

AMBASSADOR PAPPALARDO:
I have been in the UK for three years, having arrived in March 2017. That was a very important moment, as Britain was still defining its role after Brexit. It was an excellent time to arrive because the diplomatic reset created opportunities to redefine the relationship between the UK and Paraguay. Brexit helped to change the mindset of British companies and encourage them to look beyond the EU to new markets. I have been working with some of these firms to help them take advantage of opportunities in the UK. Now, of course, we have coronavirus, which will also disrupt traditional trade patterns. It's still very early to see how things will settle after the current economic and financial chaos but I am optimistic that a stronger UK – Paraguay relationship, especially on the business side, can emerge from its aftermath.

LAI: *How has coronavirus impacted Paraguay?*

AP: I'm pleased to say that our government responded quickly and aggressively to combat the crisis. We implemented a lockdown on the 11th of March and cancelled flights to Europe by the 12th. Moreover, the Paraguayan people have responded very well and have adhered to the stringent terms of the lockdown. We have a very good and technically prepared Minister of Health and we have the lowest numbers of Covid-19 deaths and infections in the region. While the primary goal was to protect the health of our people, we know that we also need to keep our economy going. The Ministry of Finance and the Central Bank of Paraguay have already taken measures to stimulate growth and the government will be launching several investment projects to kick-start the economy in the second half of the year.

LAI: *Will coronavirus force the government to make radical changes?*

AP: Speaking in my personal capacity as a Paraguayan citizen, rather than as a career diplomat, I believe that certain structural reforms have been pending for several years. Since assuming power, this government has made clear its plans to improve the efficiency of the state through development-orientated, technical, incremental improvements. I believe the great challenge that coronavirus poses will accelerate the implementation of these reforms, since the need for an effective state is obvious. People want that - and this government has assumed such commitment.

However, I don't think it's right time to make aggressive changes. The economy has been weakened by the lockdown, while health spending needs to increase considerably. So, the priority of this government must be to sustain the economy and take care of the social aspects of less favored segments of the population. It wouldn't make sense to enforce radical changes, to the tax regime for example, because such changes would most probably create uncertainty when the companies are trying to survive, recover and protect jobs.

The situation in Paraguay is similar to the UK. A total lockdown with everything shut, which creates difficult situations for medium and small companies and their employees. As a result, it's not the time to create an extra disruption for the private sector.

LAI: ***Paraguay scores poorly in international business rankings; is it a tough place to do business?***

AP: According to the recent World Bank's Doing Business index 2020 we're classified as medium, together with Brazil and one above Argentina, we're far from the below average group. Nevertheless, I don't take too much notice of some of those rankings that usually do not capture the complete picture, the advantages and opportunities that Paraguay has to offer. If any of your readers are interested in learning more about Paraguay, they should contact the embassy and we will help arrange a trip for them. Paraguay is the type of place you need to get to know for yourself instead of trusting some of these global surveys. The reality on the ground is much different.

LAI: ***Paraguay has poor air connections with the US and UK; does that hinder trade?***

AP: I was the Ambassador of Paraguay to India, spending eight years in Delhi. We didn't have a direct flight and the distance and low volume of traffic made it impossible to even consider one. However, I arranged four trade delegations in that time and we saw how trade between the two countries increased substantially. It shows that while a direct flight is nice, it is not essential for business to happen.

Since I arrived to the UK, I have been trying to convince British Airways to fly to Paraguay. Maybe not a brand-new direct flight but a stop on its existing flight to Buenos Aires. We're still working to accomplish that, but fortunately we have a great flight from London to Asunción, via Madrid with Air Europa. The opportunities that Paraguay has to offer are definitely worth a one-hour stopover.

LAI: ***What are the best investment opportunities in Paraguay?***

AP: There are plenty of opportunities and one that is particularly suited for British investors is our robust infrastructure program. Due to the infrastructure deficit in Paraguay, the government plans to make significant public investments in the area, promoting at the same time the participation of PPPs and private parties in such projects.

One of the main projects that is being currently constructed is the Paraguayan portion of the bi-oceanic road corridor, which will stretch from Brazil's Atlantic coast to Chile's Pacific ports. I would love to see British trains running again in Paraguay. Your readers may not know this but we had one of the first railways in Latin America, which was built by British engineers.

Another big investment scenario is the northern Chaco region. This is a huge expansion of our land that was historically overlooked. Only 2% of the Paraguayan population lives there, despite the fact it makes up more than half of our total territory. Now, technological advances make it possible to turn this barren land into productive farmland and we already have large dairy industries there. There is scope for much more – for example we are helping one British firm to develop a forestry project. That growth is also leading to a new wave of projects in supporting areas, such as real estate.

We also have an investment attraction system called maquila, which offers favourable tax conditions to international companies that produce goods and services for export. Materials can be imported tax-free for assembly, then sold locally or exported globally with only one tax at a rate of just 1% on the value added. To date there are over 190 companies from the US, Japan, Brazil, Mexico, China and France working with the programme.

LAI: ***Paraguay avoided the wave of Latin American protests in 2019; why?***

AP: Although I'm not a sociologist, it's clear that Paraguay is a very stable country, economically speaking, and that's good news for investors. Our central bank is one of the most reputable institutions and has helped to keep our economy steady, at the macro-economic level, even when there has been dramatic political change.

Look at our currency, the guarani, for example. The guarani has been stable since the 1960s. I believe we are inherently a cautious nation, when it comes to the economy. And that's a big plus for international investors.

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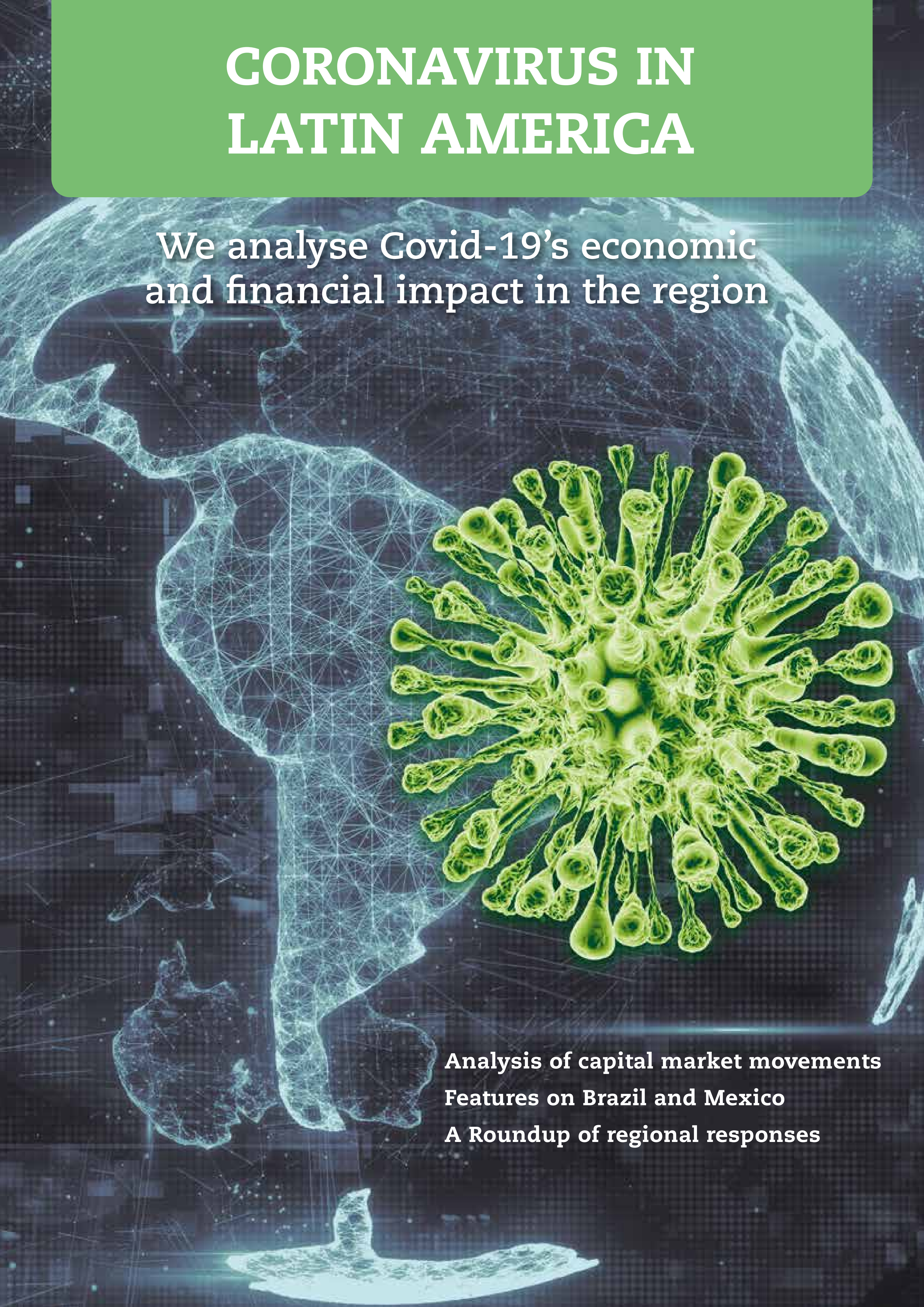
CORONAVIRUS IN LATIN AMERICA
We analyse Covid-19's economic and financial impact in the region
Analysis of capital market movements
Features on Brazil and Mexico
A Roundup of regional responses

Coronavirus and Latin American Markets

Covid-19 is upending markets across the region. It's inflicting plenty of losses but also creating opportunities...

As coronavirus spread west from Asia, fears grew for Latin America. If the virus was capable of overloading the health systems of rich countries like Spain and Italy, surely it would devastate a region characterised by underfunded hospitals, cash-strapped governments and informal economies.

A harbinger from Ecuador

In late March, Guayaquil, the 'Pearl of the Pacific', gave an early warning. The once-bustling port city was overwhelmed by the pandemic. Bodies were left rotting on the streets, police formed roadblocks outside to protect crowded medical centres and black-market prices of key drugs soared. Analysis from the Financial Times suggests that measured by 'excess deaths', the city's province, Guayas, suffered the world's most fatal coronavirus outbreak. The province saw a 485% increase in excess deaths in the fortnight spanning March and April compared to the historical average.

The economic cost in Ecuador also looks severe. The IMF expects the Andean economy to contract by 6.3% this year - an epic recession. Yet the reality could be even worse. Coronavirus has caught Ecuador at the worst possible moment. It was already struggling to meet the conditions of an IMF bailout, with its political and business elite unwilling to make the tough decisions needed to reform the economy. A bloated state is exacerbated by a private sector whose international competitiveness is hampered by Ecuador's use of the dollar. Meanwhile prices for its main export, oil, have plummeted.

Ecuador has around $42billion of debt owing to China, the IMF and bondholders. It is has agreed a temporary payment deferral – but ratings agencies have already labelled that a 'restrictive default'. Some sort of default is inevitable, but probably wouldn't ruffle too many feathers in a country that has only fully repaid two bonds since independence from the Spanish Empire. A far scarier prospect would be if Ecuador is forced to abandon the dollar. It would cause a financial crisis much like the one in 1999 that forced Ecuador to adopt the greenback in the first place. If de-dollarization happens then the recession would be worse than the 6.3% that the IMF is currently predicting.

The rest of Latin America

Ecuador's coronavirus deaths are tragic but not the cause of its economic woes. The lockdown, which Ecuador deserves praise for implementing early and adhering to rigorously, and falling global demand for its exports, exacerbated its already fragile macroeconomic position. Investors are now wondering how the rest of the region will fare. As you'd expect capital fled from emerging markets as the crisis progressed. According to the Institute of International Finance investors withdrew $95billion dollars from EM debt funds between January and April – far more than following the 2008 crisis. These outflows will create short-term financial pressure on Latin American governments and companies. The Economist ranked the financial strength of 66 emerging economies to see how they will cope with coronavirus. The index, which evaluates public debt, foreign debt, borrowing costs and reserve cover, placed Ecuador near the bottom on 55th place. Argentina, which was also struggling to fulfil the terms of an IMF bailout before the pandemic, is even lower at 57. And Venezuela, foots the table in 66th position. To give those numbers some context, Iraq is at 45.

But it's not all bad news. At the other end of the table, Peru is Latin America's highest performer in third position, while Paraguay and Guatemala surprise with top 20 finishes. Nearly all of Latin America's major economies are in the top half of the table, suggesting that they should be able to ride out the short-term financial impact of the virus. Indeed, Panama and Paraguay have issued coronavirus bonds. Both enjoyed successful issuances, with higher demand and lower rates than expected.

Diversified region

Once we move on from the initial financial shock, investors want to know

Each LatAm Economy will be Impacted by Coronavirus in Different Ways

Key transmission channels for external shocks by country

	Argentina	Brazil	Chile	Colombia	Costa Rica	Dominican Republic.	El Salvador	Guatemala	Honduras	Jamaica	Mexico	Nicaragua	Paraguay	Peru	Uruguay
G7 GDP growth	> 1.0	0.5 to 1.0	0.5 to 1.0	0.5 to 1.0	0.5 to 1.0	> 1.0	0.5 to 1.0	0.0 to 0.5	> 1.0	> 1.0	> 1.0	> 1.0	0.0 to 0.5	Not significant	Not significant
China GDP growth	> 1.0	0.5 to 1.0	0.5 to 1.0	0.0 to 0.5	0.0 to 0.5	Not significant	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.5 to 1.0	Not significant	0.0 to 0.5	0.5 to 1.0	0.5 to 1.0	0.5 to 1.0
US 10-year interest rate	Not significant	Not significant	0.0 to 0.5	-0.5 to 0.0	Not significant	Not significant	Not significant	Not significant	< -0.5	Not significant	Not significant	-0.5 to 0.0	< -0.5	Not significant	< -0.5
Energy prices	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	Not significant	Not significant	0.0 to 0.5	Not significant	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	Not significant	0.0 to 0.5	Not significant	Not significant
Non-energy commodity prices	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	Not significant	Not significant	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5	0.0 to 0.5
Air travel	> 1.0	Not significant	0.5 to 1.0	0.5 to 1.0	Not significant	> 1.0	Not significant	Not significant	> 1.0	> 1.0	> 1.0	Not significant	Not significant	Not significant	Not significant

> 1.0 | 0.5 to 1.0 | 0.0 to 0.5 | -0.5 to 0.0 | < -0.5 | Not significant

Note: The figures are partial elasiticites of real GDP growth to the corresponding variable.

Scource: World Bank, Semiannual Report for Latin America and the Caribbean

how each economy will recover. Most Latin American countries are used to dramatic economic crisis.

Some well-managed economies, like Chile or Colombia, have become very adept at reacting to sudden falls in commodity prices with counter-cyclical measures. But the fact that Covid-19 will impact demand for almost every good or service, as opposed to just a set of commodities, makes it harder for investors to predict the results.

As the World Bank points out in its excellent April report on the region: "Demand from China and G7 countries will fall dramatically, but potentially to different extents, with diverse implications for commodity exporters in South America and for exporters of manufactured goods and services in Central America and the Caribbean. The decline of oil prices will have deleterious consequences for countries whose exports earnings and budget resources critically depend on oil, but it will bring relief to net oil importers. Air traffic has fallen to a trickle as flights have been massively cancelled to prevent the spread of the virus. The resulting collapse in tourism will severely impact countries in the Caribbean basin, but others less so."

Another way the economic impact of this pandemic is different to the region's traditional recessions is because in addition to the typical external demand shock, caused by falling exports, it also brings a supply shock as local producers struggle to operate during lockdown. Evaluating each country's ability to manage the supply-side shock is complex because it involves a number of different factors.

Take Chile for example. Its strong institutions and relative wealth allow it to pursue a sophisticated policy of 'intelligent lockdown', accompanied by the most extensive testing in the region, that keeps more businesses open than in, say, Ecuador. However, as Control Risks explores in our feature on the country, Chile also has political weaknesses that may hamper production in the future. Coronavirus came in the midst of a political upheaval in Chile and labour relations are likely to become more problematic in the long term.

In this report we look at the economic impact of coronavirus in Latin America. We focus on the biggest economies, with individual articles on Mexico and Brazil, from our correspondents in each country. We look analyse the impact on capital markets, with a special feature written by BancTrust, a boutique investment bank focused on Latin America. And we round up the fiscal and monetary measures taken across the region, looking for clues from successful outliers such as Peru, Panama and Chile to see how economies may recover.

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Regional **Responses**

Coronavirus is impacting each country in the region differently; we analyse how it is playing out so far...

One striking element of the pandemic is that Latin American capital markets began to feel the crisis before its hospitals. Markets are forward-looking and capital began flowing out of Latin America in late January, long before Brazil had the region's first confirmed case on the 25th of February. Now, in the wake of the outflow, with asset prices depressed and more data available on how each country is responding to coronavirus, investors will already be looking ahead to see which countries will recover first.

Financial weakness

As the case of Ecuador – covered in the previous article – demonstrates, a country's ability to ride out coronavirus will depend on its financial and institutional strength entering the crisis and the policy decisions it takes during. That's why Argentina finds itself in a limbo. Its government reacted very quickly and aggressively to coronavirus, with a total lockdown. That helped to reduce infections and contain the disease. However, it already had a weak macroeconomic position before Covid-19 hit. Public debt was at 88% of GDP at the end of 2019 and with the economy set for a major recession this year, will probably reach 100% by the end of 2020. The IMF estimates Argentina's economy will contract by 5.7% in 2020. The tough financial position means that Argentina has only been able to increase health spending by 1% of GDP, while its combined fiscal and monetary coronavirus stimulus package is worth less than 2% of GDP. Meanwhile, interest repayments to bondholders stand at 3.3% and rising. Political pressure is building – understandably – for Argentina to prioritise health spending above paying foreign bondholders. But, regardless of the outcome of the restructuring deal with debt holders, Argentina has limited scope to provide further support to its economy. So the health and economic crisis is likely to worsen there.

In Venezuela the situation is even worse. That's because the country combines a poor macroeconomic position, with weak institutions and poor policy making. The Economist ranked the financial strength of 66 emerging economies to see how they will cope with coronavirus. Needless to say, Venezuela is bottom of the index, which evaluates public debt, foreign debt, borrowing costs and reserve cover. The country has no fiscal space for any stimulus package, while its hospitals were already devastated before the pandemic. Perhaps the only positive is that the crisis may presage a change in government.

Outliers

International rankings are a useful way to get a snapshot of a region but they don't tell the whole story. Panama and Costa Rica find themselves in the bottom half of the Economist's financial strength ranking. Yet so far Panama is handling the crisis very well. It was the first Latin American country to issue a coronavirus bond, obtaining 4.5% on a 54-year paper. It has also kept a lid on infections and launched a fiscal stimulus package worth more than 3% of GDP. Costa Rica's public debt has been building steadily for years but much of that money was invested in its excellent public health system, which is one of the best in the region. That's helped it have Latin America's lowest coronavirus death count. Paraguay is another interesting case. It had 0% growth in 2019, low international currency reserves and a dengue epidemic at the beginning of 2020. The Pan-American Health Organisation, highlighted Paraguay as one of the Latin American countries most at risk from coronavirus. Yet the country has confounded the doubters. A quick lockdown has kept the virus at bay while a fiscal package worth 2.5% of GDP is mitigating economic damage. It too, was able to issue a coronavirus bond at low rates, while the IMF predicts it will have Latin America's smallest recession in 2020.

Success stories

Among the region's large economies, the best placed appear to be the 'Andean 3' of Chile, Peru and Colombia. Peru responded with a combined fiscal and monetary package – the region's largest stimulus. That's good policymaking but also only possible because of the country's strong macroeconomic position entering the crisis. Its 2019 fiscal and current account deficits were just 1.6% and 1.5% respectively, while its total debt-to-GDP ratio was just 26%. Its reserves comfortably cover external financing requirements, while it bolstered its position by securing an $18billion precautionary credit line with the IMF. That financial strength is reflected in local currency, the Peruvian sol, which has held steady against the dollar, while most regional currencies have plummeted.

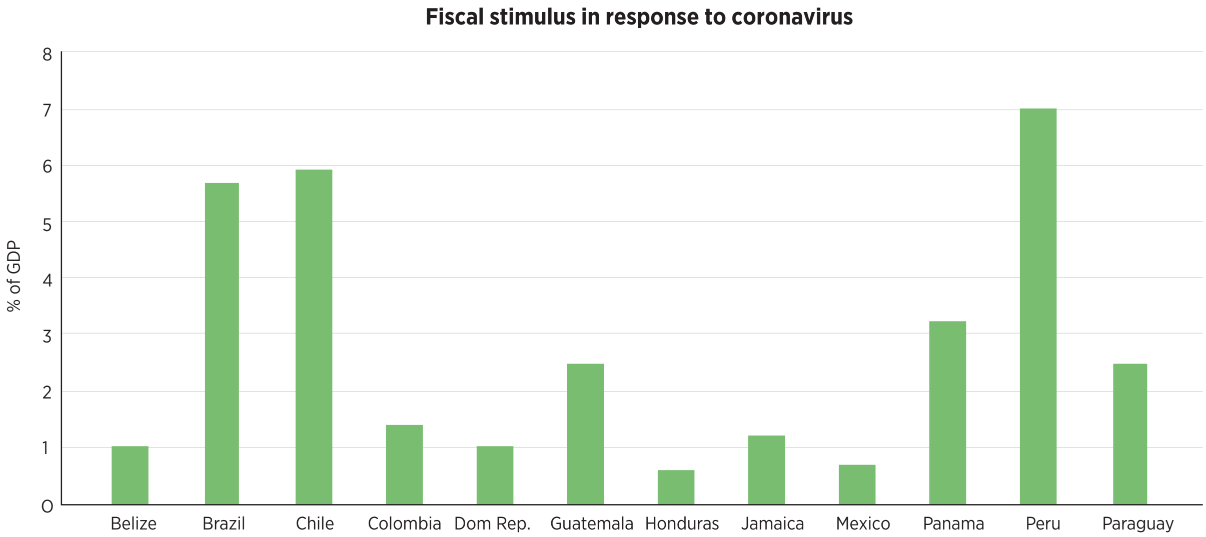
Chile also looks in a strong position. Its fiscal response was worth 6% of GDP, while its Central Bank launched the country's first ever quantitative easing (QE), with a $4billion programme of bank bond purchases. Following political protests last year, Chile was already beefing up welfare payments and social services and the pandemic will merely accelerate that trend. With a 2019 public debt-to-GDP ratio of just 28%, the country can afford to spend its way out of the crisis. Moreover, thanks to its strong institutions it is spending wisely. It has conducted more coronavirus tests than any other nation in the region, allowing it to implement a sophisticated, partial lockdown strategy that should restrict the 2020 recession to -3%. In the medium-term its copper exports should benefit from the global recovery.

Colombia's situation is the most precarious of the Andean 3, but still positive compared to the rest of the region. Its macroeconomic situation coming into the crisis was solid, albeit not perfect. Public debt-to-GDP stood at 51% in 2019, although that was mitigated by strong economic growth of 3.3% and a fiscal deficit of just 2%. Moreover, the collapse in the oil price hit the country's main export. These factors limited Colombia's fiscal stimulus to 1.5%. However, the Central Bank has been more aggressive with its monetary response. Two cuts of 50 basis points in March and April have brought the policy rate to a six-year low of 3.25%. With another cut expected in May, rates will be firmly in negative territory, below inflation that is hovering around 3.5%. In March, Colombia was also the first country in Latin America to implement QE with a $3billion programme that was more wide-ranging than Chile's and covered private and public debt. Another innovative measure was the presidential decree that forced Colombian banks to buy 'solidarity bonds' – ie government debt.

Coronavirus will have a particularly pronounced impact on Latin America. As Alejandro Werner, Head of the IMF's Western Hemisphere Department, told the FT, Latin America is particularly exposed to the impact of the coronavirus crisis because many of its economies were struggling even before they were hit with multiple shocks from weaker commodity values, the oil price crash and capital flight. "You never had severe recessions in all the countries together and therefore this will make for the worst growth year in Latin America in the last 50 years."

But as this Coronavirus Special makes clear, the extent of the impact and the speed of the recovery will vary dramatically between countries. Investors were quick to pull their capital from the region as the pandemic approached. Now the most forward-looking will surely be evaluating, which countries seem best-placed to recover.

Some Latin American Countries Have Implemented Large Stimulus Packages



Source: World Bank, Semiannual Report for Latin America and the Caribbean

A Brave **New World?**

LatAm economies, as well as emerging and frontier markets (EM & FM) have been severely hit by the global financial conditions on many fronts. The combination of record-high portfolio outflows, the plunge of commodity prices, the sudden stop of external financing and of economic activity has taken a toll on already weak macroeconomic conditions. Surviving the economic effects of this crisis will require significant efforts in terms of correcting macroeconomic imbalances that could translate into sharp FX depreciations, reductions on overall consumption and even debt restructurings. A sluggish global recovery in the aftermath of the pandemic could lead to a permanent and sizeable decline in capital inflows targeting LatAm and shrinking domestic capital markets.

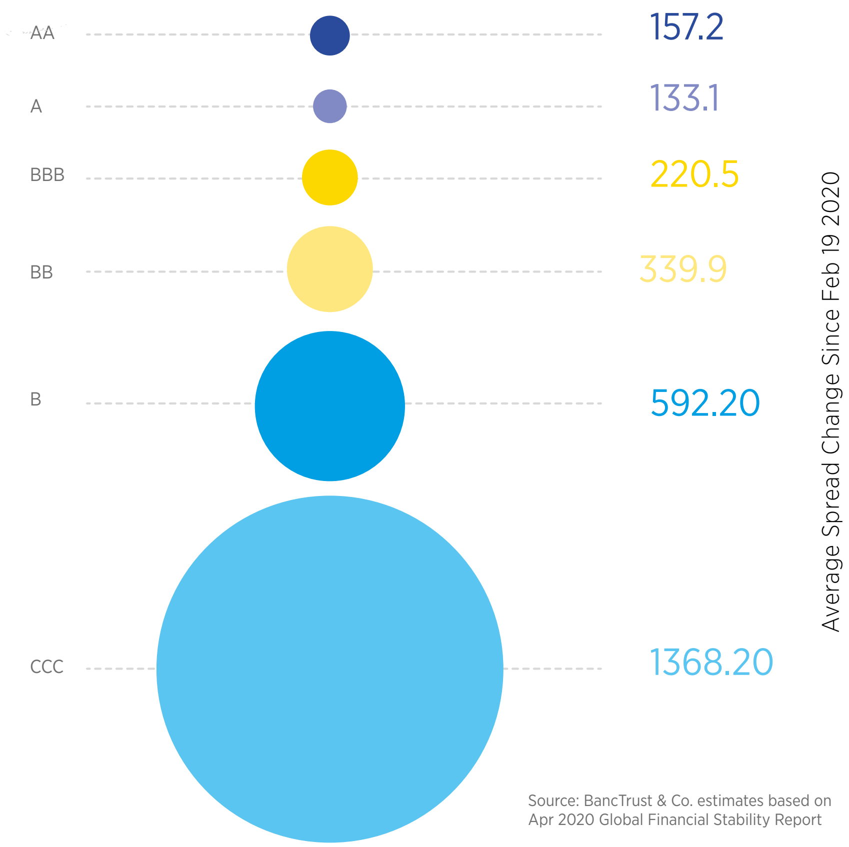
Limited policy space

The spread of the COVID-19 and the decline of oil and other commodity prices is an unprecedented combination of external shocks that has increased the prospects of global recession and led to a spike in global risk aversion almost overnight. In just a few months, the global expectations and assets prices have worsened severely, affecting in a greater extent EM & FM. In fact, from January to April this year, the IMF global growth expectations fell by 3 percentage points (pp) to -3%, but for LatAm countries the correction was of 6.8pp to -5.2%. The same pattern can be seen in the currencies and stock indices of most countries. The reasons behind the underperformance of these countries is clear: EM countries are less prepared to face the global crisis due to its higher dependence on external savings and on commodities exports and their lower policy response capacity. In turn, vulnerabilities translate into a sharp reversal of portfolio flows and currency depreciations that put upward pressure on inflation, while threatening financial stability. This has been the case in the last months, during which non-resident portfolio outflows from emerging markets reached a record of more than $100billion in the first quarter of 2020, the highest ever relative to their aggregate GDP.

The countries in greater need of financial assistance due to its limited fiscal space, high financing needs, or external financing vulnerabilities, have been the ones where the sudden stop of capital inflows has been more severe. While commodity-producing economies, such as Brazil, Colombia, Mexico, Russia, and South Africa, saw their currencies tumble by more than 20% in the first quarter of 2020, countries with lower external vulnerabilities or more prone to implement currency interventions or capital controls have been relatively less affected (see map). Similarly, the risk premiums on US dollar-denominated bonds have posted a steeper increase in those countries with a lower credit rating.

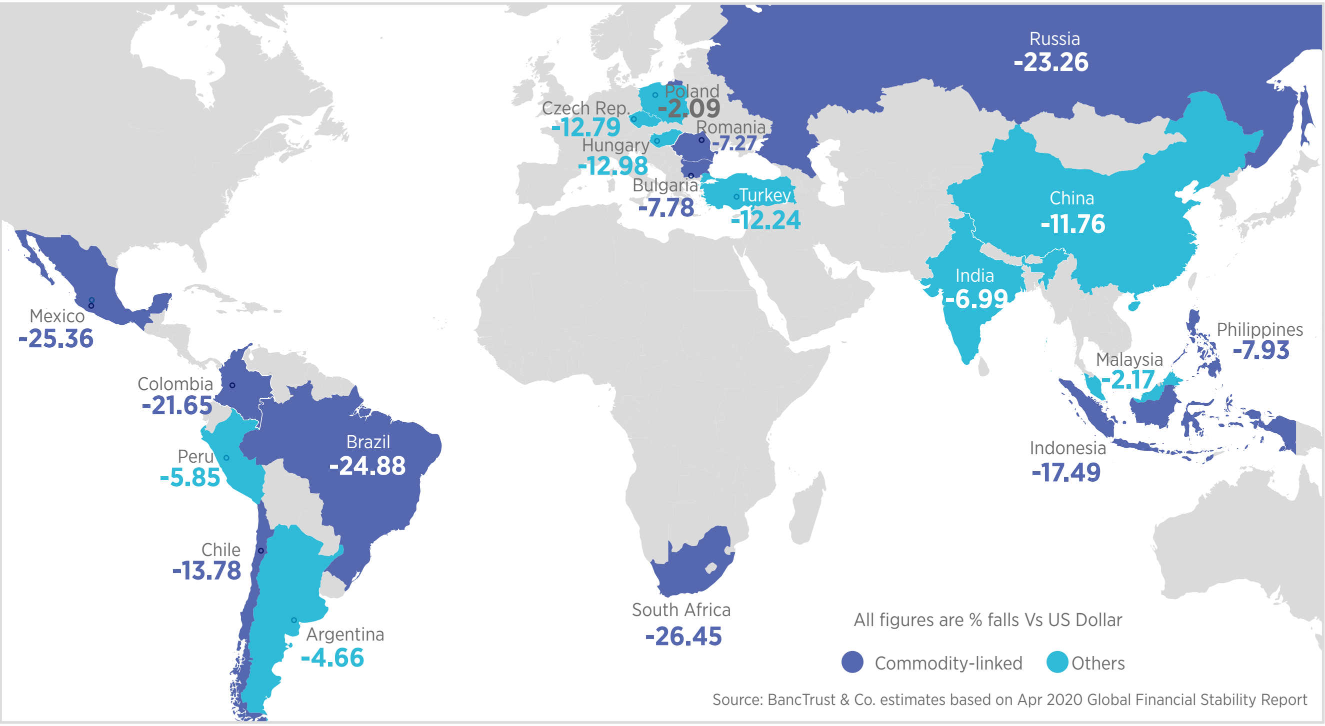
Spreads Rocketed for Lower Grades

Change in Emerging Market Bond Index Global (EMBIG) Spreads by Rating



Source: BancTrust & Co. estimates based on Apr 2020 Global Financial Stability Report

First Quarter Currency Performance Against the Dollar (%)

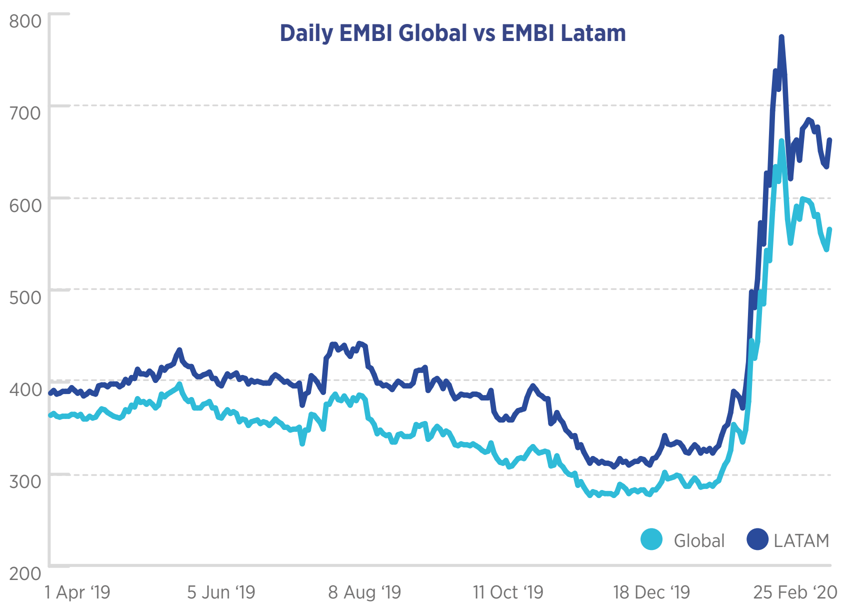


Source: BancTrust & Co. estimates based on Apr 2020 Global Financial Stability Report

What has been done so far?

To counter and mitigate the damage to their economies from the unprecedented stoppage of economic activity and capital flow reversals, local authorities have announced contingency measures, mainly in the form of increases in fiscal spending and easing of monetary conditions. Many countries with low fiscal space, have requested funding to international financial institutions, such as the IMF and World Bank, and opened credit lines with central banks of developed countries. These funds have a twofold function of supporting higher public spending and at the same time containing FX pressures. Central banks are relaxing their monetary policy and encouraging lending to SMEs, at risk of fueling FX volatility. To avoid the latter, some central banks have implemented currency interventions, like Brazil, Mexico and Russia, while others have opted for capital controls as they hold a more limited intervention firepower.

LatAm Bonds Hit More Than World EMs



Source: BancTrust & Co based on Bloomberg

What to expect ahead?

The strategy implemented by EM countries is broadly aligned with the recommendations given by international institutions such as the IMF and World Bank. Besides the humanitarian aspect, the main goal is to preserve the production capacity (i.e. potential output) and fending off massive bankruptcies to enable a faster rebound in the post-crisis.

However, the effectiveness of this approach will be conditioned by the duration of the crisis and to the speed of the recovery in the developed world, still subject to much debate all around the globe. A permanent impact on global growth will undoubtedly force adjustments on fiscal and external accounts. Solvency will be affected which will preclude a reduction in borrowing costs thus impacting negatively on financial intermediation.

Brazil Battles Cost of **Coronavirus Crisis**

The country treads a narrow path between reacting to Covid-19 and managing debt levels, writes Adam Patterson in Curitiba...

If a week is a long time in politics, a few months is a long time in global pandemics. This is especially the case for Brazil, which having gone through an economic and political rollercoaster over the last few years – corruption scandals, presidential impeachment and its greatest-ever recession – seemed to be finally turning the corner. When President Jair Bolsonaro´s administration entered power last year, the signs were good. Respected Finance Minister, Paulo Guedes, who promised pro-market policies and structural reforms, scored some early wins. GDP growth in 2019 was 1.1%, inflation and interest rates were at historic lows while the stockmarket hit record highs, growing 32%. Brazil was also the world's fourth-largest destination for foreign direct investment and M&A activity grew.

However, as 2019 turned into 2020, the Covid-19 hurricane hit. As Nassim Taleb put it: "fragility is the quality of things that are vulnerable to volatility". When the WHO officially called it a global pandemic on the 12th of March, Brazil had officially confirmed only 71 cases. But with lockdowns and social distancing measures announced by local and state governments, jitters transformed into concerns about the impact of the Covid-19 and the underlying strength of the Brazilian economy. By the end of March, with more than 5,700 cases confirmed and 201 fatalities, the real was at record lows to the dollar, and the country's main stockmarket index, the Ibovespa, had fallen 37% since the start of the year.

For Guedes, Covid-19 was a "fleeting crisis, with a wave of impact which will also [subside] strongly". He warned against suffocating the economy. Nonetheless, the federal government response escalated as the dual health and economic challenges became clearer. With the Senate passing the so-called 'War Budget', the government had more room for manoeuvre, allowing coronavirus-related spending to bypass constitutional spending limits.

Powerful economic response

Brazil's combined fiscal and monetary package to support the economy and reduce economic contagion was R$1.6trillion, which is around 20% of GDP and a big increase on the initial emergency measures of R$150billion. The package was not all new money, as some had been previously announced. On the fiscal side, it included: R$150billion of deferred tax collections and advanced social assistance payments, R$50billion in emergency aid to informal workers, another R$90billion in supplementing furloughed company payrolls plus R$88billion for state governments. The fiscal measures add up to 5.2% of 2019 GDP and, according to UK-based consultancy, Capital Economics, this would push Brazil's public debt ratio above 90% of GDP from the current level of 76%.

Separately, the Government has also announced the "Pro-Brazil" recovery plan led by the Presidential Chief of Staff, which aims to coordinate economic measures on job creation and infrastructure investment. The plan, initially criticised for a lack of details, projects R$280billion in PPPs, infrastructure concessions and fixed investment, and is expected to be rolled-out by October.

Monetary policy action also ramped up quickly to R$1.2trillion, which is 16.3% of GDP, in central bank liquidity injections, bank loans and reductions in compulsory reserves. The combined fiscal and monetary response is the largest in the region – yet Brazil may have to go further still.

Coronavirus crunch

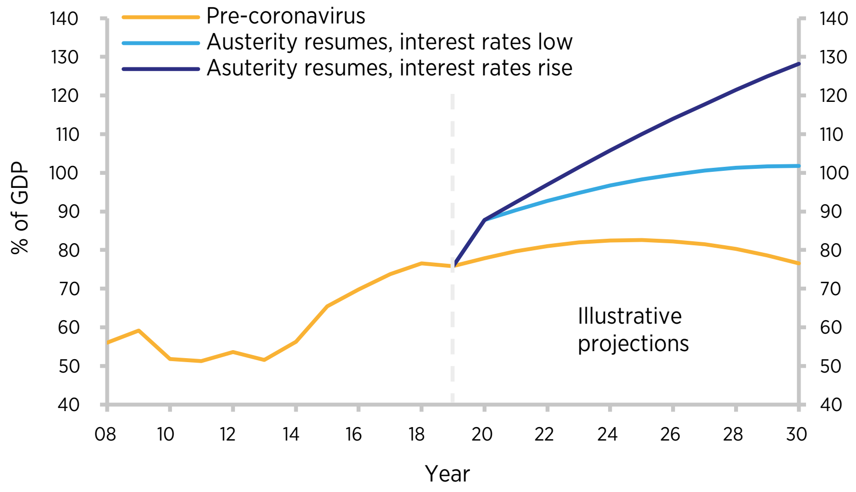
Government action will be necessary to support the economy as it is widely expected that Brazil's GDP will contract sharply this year. By how much is, in the words of Treasury Secretary Mansueto Almeida, "guesswork". At the time of writing, the country's coronavirus outbreak hasn't yet peaked, with 67,000 cases and 4,555 deaths, mostly concentrated in São Paulo, the country´s economic capital, Rio de Janeiro and the northern states of Amazonas, Ceará and Pernambuco. This adds to the uncertainty, so it's hard to tell just how bad the economic impact will be. The efficacy of government measures announced so far, post-lockdown activity and effect on major trading partners, especially the US, China and Argentina, all remain unclear.

Nonetheless, it's obvious that the 2% pojected GDP growth in 2020, that many analysts held as late February, is now impossible. Itaú, Brazil´s largest commercial bank, estimates the contraction in Brazil could range from 0.5% to 6.4% of GDP. Its base scenario is for a -2.5% drop in economic activity this year before rebounding from September – and that's assuming that isolation measures begin to wind down from the next month. The unemployment rate is projected to rise t0 16.2% in the second quarter, up from 11.65% - a potential loss of 5 million jobs.

And despite operating margins of public companies improving to 22% in 2019 from 12% in 2015, ratings agency Fitch estimates that a quarter of Brazilian companies are highly

How Covid-19 Hits Brazil's Public Debt

Government debt to GDP



Sources: Refinitiv, Capital Economics

sensitive to the financial impact of coronavirus, due to low liquidity, currency risk and credit supply issues. Around 90% of SMEs have already seen revenues fall and many companies will not survive to see the recovery. Only the most optimistic forecasts now see the stock market above 100,000 points by year-end. With economic activity under pressure, and despite currency turmoil, inflation is projected to dip below 3%. That will allow the central bank to cut interest rates from the current 3.75%.

Recovery

The recovery is not likely to be linear or even similar across sectors and regions. Many major cities and states have started to slowly ease lockdowns. One of greatest country risk factors this year may be political. Hugely popular Justice Minister, Sergio Moro, the well-known hero of the Lava Jato corruption probes, resigned on Friday the 24th, citing political interference in Federal Police investigations, shaking the Government and shocking the country. That followed the sacking of the Health Minister the week before. With political stress likely to remain elevated over the near-term, keeping the economy afloat – and Guedes onboard – will be key in helping to limit downside pressure to the country´s outlook.

The three Ds - depth, duration and deflation - of the Covid-19 recession will help define the shape of Brazil's recovery. Unlike previous recessions there is no major systemic cause of the downturn. Therefore, the uptick can be swift but certain parts of the economy could remain damaged and impaired well into the future. Some sectors, such as agribusiness, should remain robust. On a positive note, the market consensus expects an uptick in a basket of economic indicators from next year. Bradesco forecasts average annual GDP growth at 3% to 2023. It will be necessary however, to resume the path of reforms and stabilise the debt trajectory to ensure medium-term economic sustainability. Brazil's initial economic and financial response has been impressive – now it needs to plot a return to growth.

Coronavirus crisis plunges Mexico into its worst **recession in decades**

The government's slow public health response and weak economic measures have been criticised, but the crisis could create business opportunities, writes Louisa Reynolds in Mexico City...

Throughout March, as coronavirus spread through Mexico, President, Andrés Manuel López Obrador, could be seen hugging and kissing supporters. It was sharp contrast to neighbours Guatemala, that had already closed its borders and enforced a lockdown. On March 31, President Andrés Manuel López Obrador finally reacted, with a raft of strong health moves, including a lockdown that has been extended until May 30 and the suspension of non-essential activities. Now, with 16,752 confirmed COVID-19 cases and 1,569 deaths, Mexico has entered phase three of its emergency plan against the coronavirus pandemic.

This failure to react swiftly to the crisis could prove fatal yet Mexico is better prepared to cope than other countries in the Western hemisphere. With first-class medical schools, a team of well-trained epidemiologists and a basic healthcare system for those on a low income, Mexico has the tools it needs to respond to the pandemic.

According to official figures, Mexico has a total of 4,629 hospitals, specialised institutes and health clinics, a per capita coverage of 37.5 facilities per million residents, nearly twice as high as the 17.1 in the US. However, in impoverished and predominantly rural states such as Chiapas, Oaxaca and Guerrero, many hospitals are small and inadequately equipped to handle a COVID-19 outbreak.

Another factor in Mexico's favour is the fact that with only 7% of its population aged over 65, compared to almost 16% in the US and nearly 23% in Italy, Mexico has the fewest retirement-age citizens of all the countries in the OECD, club of 'rich' nations.

But Mexico also has the highest rate of obesity, which studies find exacerbates Covid-19, after the US. While 10.3% of the population and 10.3% of the population aged 20 or older – 8.6 million people – suffer from diabetes according to government data from 2018, conditions that can exacerbate the illness. Hypertension is even more prevalent, affecting 18.4% of the population aged 20 or older. The fact that 50% of those who have died from coronavirus in Mexico had diabetes and hypertension, illustrates the extent to which such conditions have left Mexico vulnerable in the face of the pandemic.

"Coronavirus isn't that lethal, except for people who have underlying health conditions that complicate it. Unfortunately, that's the case for many millions of Mexicans", Abelardo Ávila, a researcher at the Salvador Zubirán National Institute for Medical Sciences and Nutrition told El Universal newspaper on March 28.

Cost of coronavirus

Key sectors of the economy have already been hit hard by the coronavirus crisis. In an attempt to halt the spread of coronavirus, Ford, Honda, Audi and other automakers have limited or suspended production in Mexico, a heavy blow to an industry that generates 1.7 million jobs and 3.5% of the country's GDP. Mexico's tourism sector, which accounts for 8.5% of all goods and services produced in the country and 5.8% of its jobs, has also been hit hard by the crisis and in the destinations of Cancun, Playa del Carmen and Chetumal alone, more than 60,000 people have been laid off.

Market volatility has plunged the Mexican peso into record lows as the crisis has brought back demand for the US dollar. "Under current stress levels of global uncertainty and market volatility, the sharp depreciation in the Mexican peso has come on the back of a massive unwinding of carry trade flows into the peso", Olivia Alvarez Méndez, FX market analyst at Monex Europe, told Reuters. Furthermore, as a result of the low crude demand during the global lockdown, operators have been forced to get rid of the fuel through contracts in negative numbers, paying others to accept the oil. Mexican oil, just as American oil, has lost all of its value and in mid-April its price hit negative for the first time ever.

On April 15, Fitch Ratings cut Mexico's sovereign rating to BBB- from BBB, as Mexico faces its worst recession in decades as a result of the coronavirus pandemic, and two days later, ratings agency Moody's cut the debt of state oil firm Pemex to junk status, increasing financing costs for the firm and dealing a serious blow to the López Obrador administration.

Weak economic response

Faced with this dismal scenario, President López Obrador's response has been branded as "insufficient" by business groups, think tanks and opposition leaders. Six days after declaring the national coronavirus emergency, López Obrador announced a plan to "reactivate" the economy that included a tax cut for Pemex, continuing with existing social programmes, mainly consisting of subsidies for people with low incomes, and securing more government funds for housing and personal loans for employees with full-time jobs. His administration also plans to move forward with the projects planned before the epidemic broke out, such as the Dos Bocas refinery and other infrastructure projects.

López Obrador added that his administration will continue with its austerity measures, will not incur public debt and will not bail out companies or grant tax breaks to companies. As a result, he immediately came under fire from business groups that fear small and medium-sized companies, such as restaurants and retailers, which account for 52% of Mexico's GDP will be unable to survive the next few months.

As Mexico heads towards its expected peak of COVID-19 infections, forecast around May 10, poverty-fighting NGO, Oxfam México, has issued a report warning that three million businesses and 28 million workers could be at risk of losing their jobs or not making enough money to support themselves if the government doesn't support them through the coronavirus crisis. Oxfam predicts that 3 million businesses classified as non-essential, which generate an annual economic spillover of $49.5billion, will be affected in the short-term by the economic downturn caused by the coronavirus pandemic.

According to Oxfam, the government needs to provide financial support to businesses so that they can maintain their workforce and keep employees registered with the Mexican Social Security Institute (IMSS), while the 56% of Mexican workers employed in the informal economy who live day-to-day and don't have access to social security benefits should be paid a basic income during the crisis, thus allowing them to cover basic needs.

Mexico v China

In the short-term Covid-19 is bad news for North American Free Trade Argreement (Nafta) supply chains. US officials and firms are urging Mexico to re-classify some US-owned factories as essential, despite an increasing number of worker deaths in Ciudad Juárez, one of the country's main border cities and a major manufacturing industry hub. The US suggests Nafta supply chains could be permanently affected if Mexican factories do not resume production. On April 21, Christopher Landau, the US ambassador to Mexico, launched a Twitter campaign urging to protect supply chains and said the lockdown had affected the flow of essential parts and goods for businesses in the US and Canada. "If we do not coordinate our response, these chains can evaporate", Landau warned.

If it can survive the short-term disruption, however, Mexico is well positioned to benefit from the new global order that emerges after the coronavirus pandemic. During autumn 2019, the trade war between the US and China had already prompted US manufacturers to rethink their relationships with Chinese manufacturers, especially after the United States-Mexico-Canada Agreement (USMCA) came into effect on January 29 this year. With companies throughout the globe expected to alter their supply chains in the wake of the coronavirus crisis, in order to be less dependent on China and mitigate supply shocks from any future events of a similar scale, US companies are even more likely to manufacture products closer to home.

Mexico has clear logistical advantages over China. Mexican costs are also likely to fall in the wake of a recession, making it more competitive, While, another increasingly important advantage are the strong intellectual property laws that make it less likely for US goods to be copied in Mexico. In the short-term we can continue to expect plenty of bad news out of Mexico as coronavirus takes hold amongst the population and the economic cost begins to rise. However, longer-term this crisis may allow Mexico to gain share against its main competitor in the lucrative US market – China.

Social Trends in Latin America

Over the next decade, social issues will have a powerful impact on business opportunities in Latin America's 'big six' economies...

Canning House's inaugural LatAm Outlook 2020 examines how political, economic, social and security trends will shape Brazil, Mexico, Argentina, Colombia, Chile and Peru. In this article we focus on social issues, however, the whole report is available at www.canninghouse.org.

Over the last 12 months, Latin America has been characterised by new populist governments, strong social outbursts, a dissolved parliament and continued corruption scandals. The particularity of the unrest in Chile, which has occurred despite the country being considered an economic model for the region, have highlighted structural problems of inequality, corruption, and insecurity, not only in Chile, but further across the region.

Moreover, we have seen new trends emerging in these countries in recent years, including – interalia – an increasing lack of trust in authorities, disenchantment with democratic systems, a middle class with greater demands that feel unable to make additional social gains, increasing concern over migration, and polarisation between conservatives and progressives. When combined together, these factors collectively make the business environment more complex and challenging.

When it comes to Latin Americans' fears, there is a widespread perception that poverty and social inequality are among the main concerns in all countries across the region. In Mexico and Brazil, concern over inequality is overshadowed by increasing anxiety regarding crime and violence. In Argentina's stagflation-hit economy, inequality features, but is less of a concern than other pressing issues such as inflation and unemployment. However, in Chile poverty and social inequality are at the top of people's list of concerns by a comfortable margin, with the second highest concerns relating to financial and political corruption.

Increased expectations

The past twenty years have seen significant reductions in poverty, with all six countries halving the percentage of their populations below the poverty line. However, massive inequality will remain a major issue; Gini coefficients are in the 40-50 range, which is more in line with Africa than Europe - and this is not expected to significantly diminish over the decade.

The recent social protests and demonstrations across several countries have featured multiple sources of social discontent - poor public services, pensions, education, crime, political corruption. Protests are expected to continue for the foreseeable future - especially in the Andean countries, although the social-media-fed trend could spread to Mexico, Brazil or Argentina. The problems of inequality of power and influence will continue - with entrenched elites controlling the levers while others struggle to progress.

However, the middle classes that emerged from the last commodity upswing will not slide back into poverty quietly – especially now that they have revised expectations, ambitions for their offspring, and have social media and know how to use it. Indeed, penetration of social media platforms like WhatsApp is 90%.

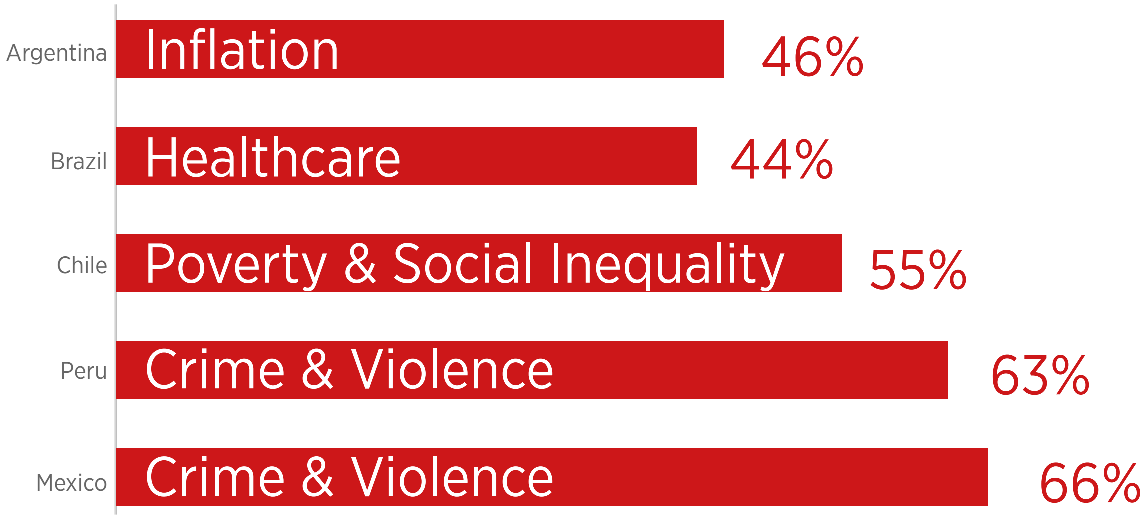
Unless popular expectations are met in full, or at least until popular discontent can once again be channelled through political parties, which, at the moment, is not a likely prospect, recurring social protests will be the norm and they will turn violent if anarchist, criminal or hooligan elements get involved.

Migration

The standard response of last resort to limited national opportunities has historically been migration. The two big sources of migration in recent years – Central America and Venezuela – will continue to dominate the picture. In its tolerance and willingness to absorb migrants, Latin America has recently offered an outstandingly humane example to an increasingly intolerant world. However, the scale of the problem - hundreds of thousands from Central America and 4.5 million to date from Venezuela - is expected to test the capacity of recipient countries, especially Colombia.

All of the ‘big six’ have made enormous progress in terms of democracy and development in recent decades but which still face serious challenges. Perhaps the main one is that of continuing to grow the size of the economic “pie” through continued open international trade and access to free markets, while improving its distribution in order to secure the consent of the governed. Given the highly unequal life chances of high proportions of their populations, that consent cannot be assumed. Our Outlook suggests that democratic government might become more populist, but it will survive; that economic progress will continue to be made, albeit slowly; and that continuing protests and disruptions will keep pressure on governments to share the benefits of progress more evenly. Governments – with the possible exception of Argentina - will also for the most part be fiscally responsible, but will be wary of erring too far on the side of austerity lest they provoke uncontainable social unrest. Our overriding conclusion is that most of the risks for international investors in the region are on the political and social side. Which makes it vital that British firms understand the region.

What are Latin Americans Most Worried About?
The single biggest fear in each country



Source: GLOBAL ADVISOR

Enjoy Chile's Natural Isolation

The Villarica View

This magnificent lakeshore property on Lake Villarrica is located in the middle of a beautiful park of approximately 1.6 hectares. The land leads directly to the lake and water rights come with the property deeds. Ideal for the extended family, there are 4 separate houses, with forests and trails that protect the privacy of each building.

The main house's 4 bedrooms and 5 bathrooms spread over 500 m2. The second is 180 m2, has 5 bedrooms and 4 bathrooms and is located in a private corner inside the park.

The other 2 houses are 140 m2 each, are located in a single, two-story building at the other end of the land.

The houses have large windows that, together with the native woods chosen for construction, allow you to feel inside the forest. As do the countless terraces, some in height above the vegetation, others among the treetops, which allow the most spectacular views of Lake Villarrica.

This exclusive property is being offered for sale through Engel & Völkers for $6.4million.

This spectacular house of former world number 1 tennis player, Marcelo Rios, is located in Chile's hidden valley - Valle Escondido. Designed by architect Gonzalo Mardones, it has a beautiful view of the golf course and mountain range. Characterised by its fine finishes and ample spaces, the house is built on three levels with access on the middle floor. There you have the living room with access to the terrace, the kitchen with a large dining room, a guest bathroom, the master bedroom suite with large walk-in closet, desk and gym. On the upper floor, there is a large study-living room and 5 bedrooms en suite. On the lower floor there is a games room, cinema, bathroom and bar with living room and exit to the terrace, barbecue, and garden. Ideal for the security conscious as it comes with its own bunker safe room.

This exclusive property is being offered for sale through Engel & Völkers for $3.3million.

For more information about these properties contact ENGEL & VÖLKERS Chile
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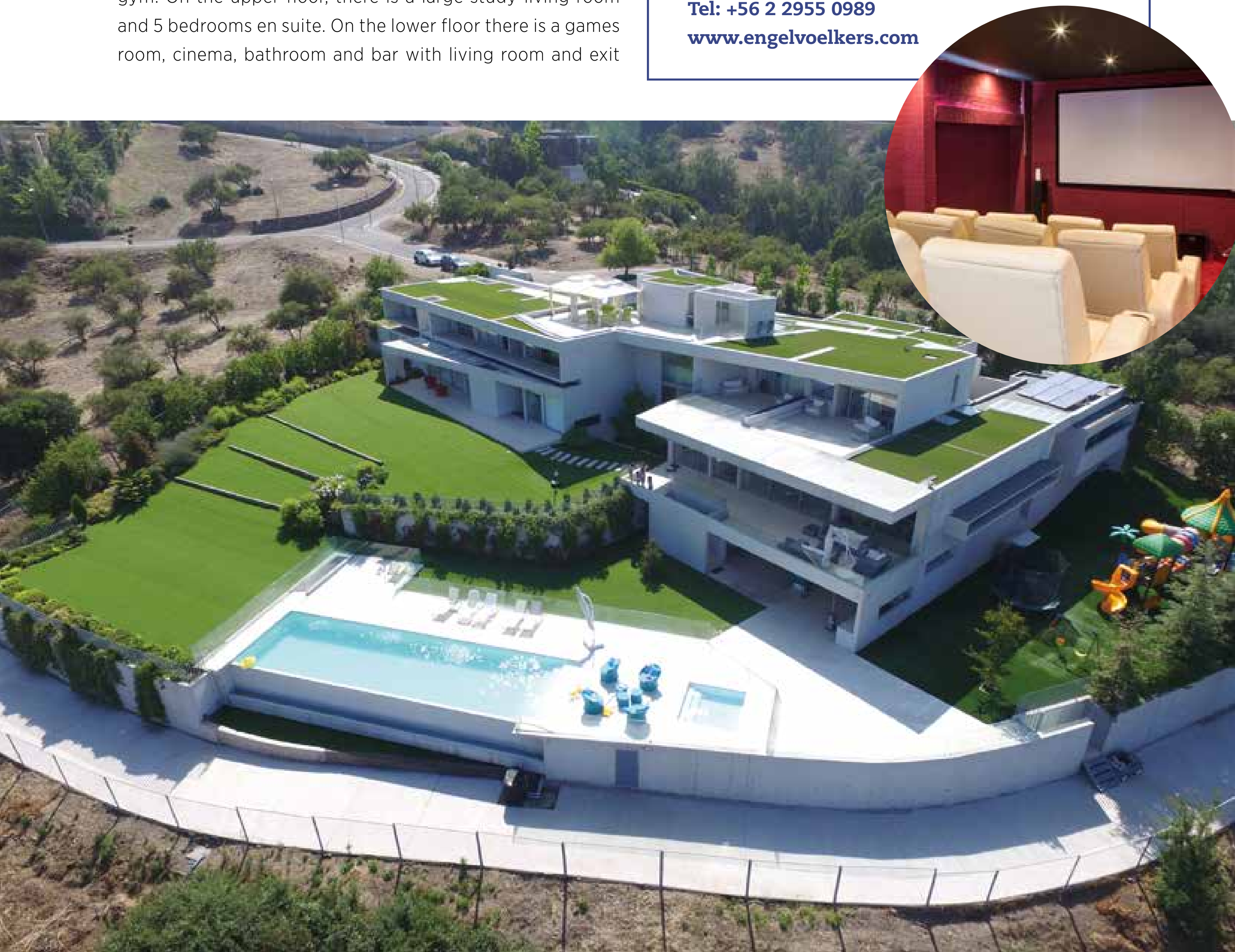
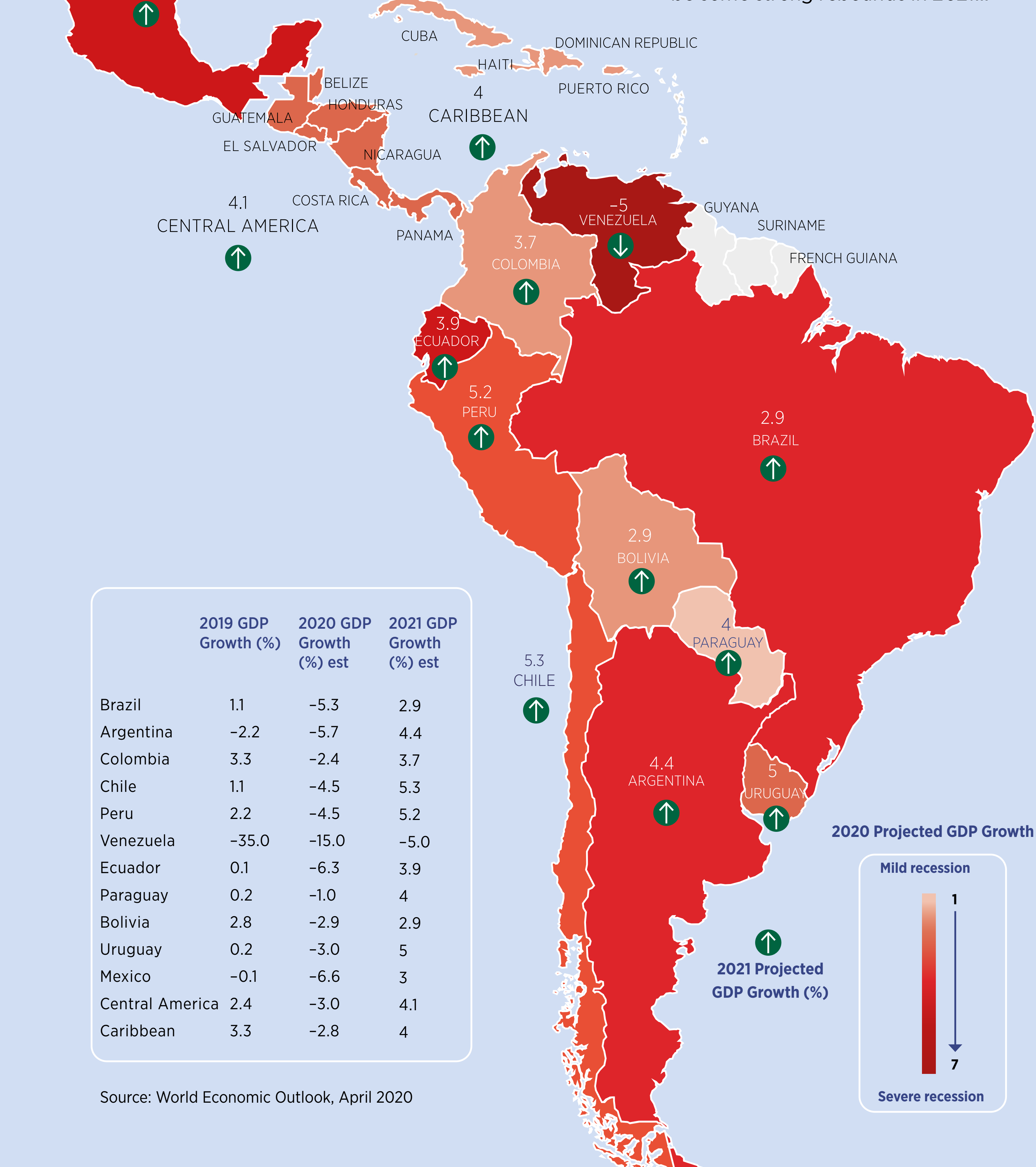


The Covid-19 Hit to Latin America's Economies

The IMF predicts that Latin America and the Caribbean will contract by 5.2% in 2020. A big change from the 1.8% growth it was expecting just a few months earlier. The outlook for 2020 looks grim yet there could be some strong rebounds in 2021...



	2019 GDP Growth (%)	2020 GDP Growth (%) est	2021 GDP Growth (%) est
Brazil	1.1	-5.3	2.9
Argentina	-2.2	-5.7	4.4
Colombia	3.3	-2.4	3.7
Chile	1.1	-4.5	5.3
Peru	2.2	-4.5	5.2
Venezuela	-35.0	-15.0	-5.0
Ecuador	0.1	-6.3	3.9
Paraguay	0.2	-1.0	4
Bolivia	2.8	-2.9	2.9
Uruguay	0.2	-3.0	5
Mexico	-0.1	-6.6	3
Central America	2.4	-3.0	4.1
Caribbean	3.3	-2.8	4

Source: World Economic Outlook, April 2020

PARQUE
LOGÍSTICO
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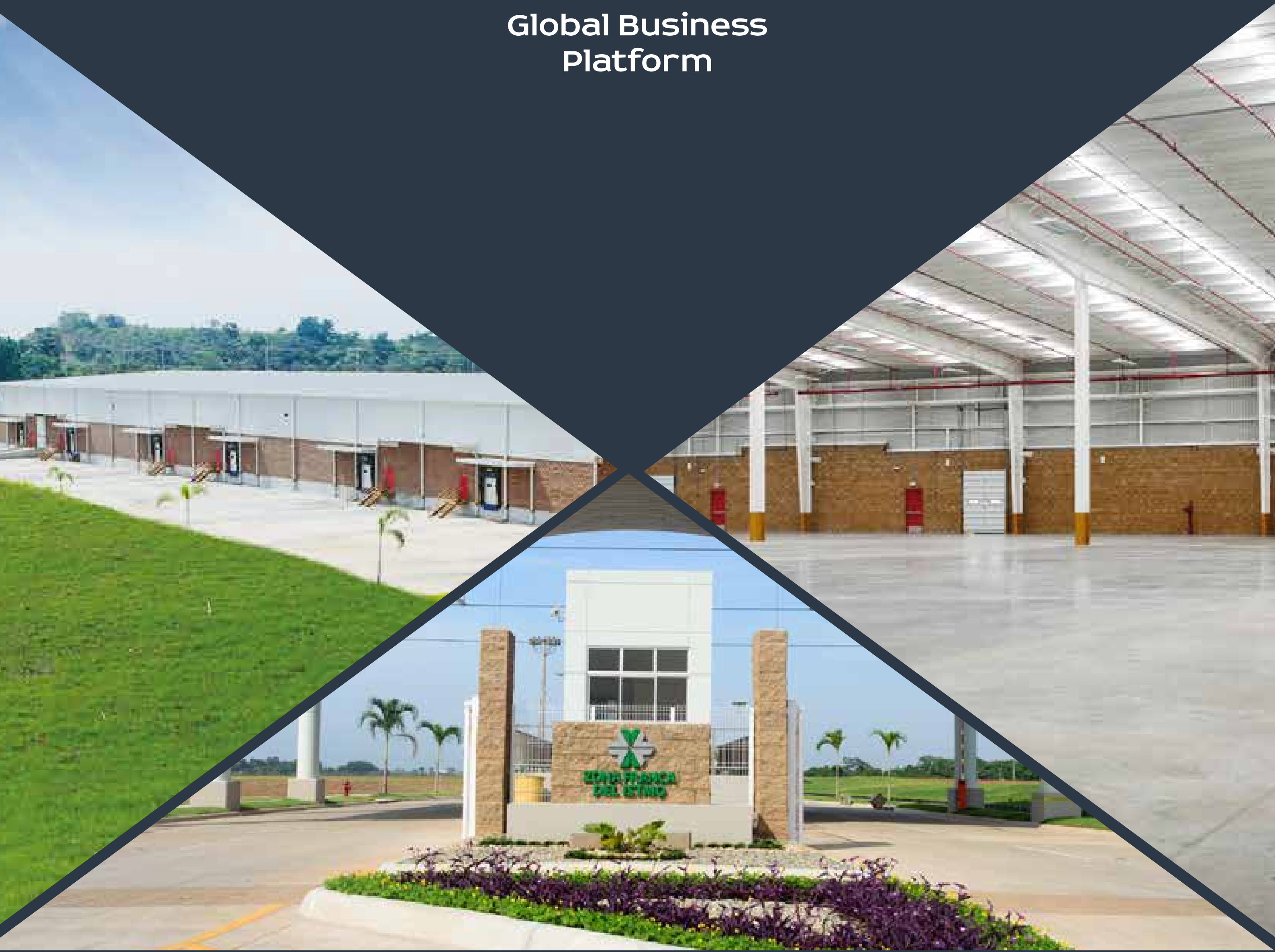
Global Business Platform



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* as at 31 March 2016