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FEATURED Q&A

Have Decades of Dollarization Been Good for Ecuador?



After nearly 20 years of dollarization and despite significant drawbacks, it is "highly unlikely" that Ecuador will try to adopt a national currency, commentators say below. // File Photo: Max Pixel via CC license.

Q Nearly 20 years have passed since Ecuador's decision to dollarize its economy in January 2000. What have been the advantages and disadvantages of dollarization for the South American country? What consequences does having a dollarized economy have on Ecuador's economic situation today, and will it ever go back to floating its own currency? How likely is it that President Lenín Moreno's government will resort to the International Monetary Fund to help resolve its latest economic problems?

A Mauricio Pozo, former Minister of Finance of Ecuador and academic advisor at Universidad Internacional SEK: "Ecuador underwent dollarization 19 years ago. It has been clearly positive, allowing the country to adequately deal with political crises such as those that occurred at the beginning of the 2000s, with the overthrow of two then-presidents. Without dollarization, such incidents would have meant deep macroeconomic imbalances such as the accelerated depreciation of Ecuador's currency, rapid inflation growth and disproportionate hikes to interest rates, precisely as occurred in 1999 before dollarization. Likewise, under the sucre, the fiscal disorder as seen in the last few years, which translated into high fiscal deficits, would have led to the depreciation of our currency in order to cover fiscal imbalances. Or, simply, the budget deficit would have been covered by printing money without backing, thus producing serious macroeconomic imbalances similar to the problems that Venezuela currently faces. Dollarization requires a flexible and modern labor market, the free flow of capital

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TODAY'S NEWS

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Under Pressure, Maduro Courts Venezuela Military

President Nicolás Maduro on Sunday demanded loyalty from Venezuela's troops in response to a top military attaché in the United States publicly breaking ranks and backing Juan Guaidó as the legitimate head of state.

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POLITICAL

Mexican Policies Embrace Migrants

Mexico's new president, Andrés Manuel López Obrador, has moved decisively to encourage migrants fleeing poverty and violence in Central America to stay and work in Mexico, making it easier for them to get visas.

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BUSINESS

Search Goes On for Missing in Vale Dam Disaster

The chief executive of Brazilian mining giant Vale, Fabio Schvartsman, apologized without taking responsibility for a dam collapse Friday that could be the deadliest in the country's history.

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Schvartsman // File Photo: Vale.

POLITICAL NEWS

Facing Pressure, Venezuela's Maduro Courts Military

President Nicolás Maduro on Sunday demanded loyalty from Venezuela's troops in response to a top military attaché in the United States publicly breaking ranks and backing opposition leader Juan Guaidó as the legitimate head of state, *The Wall Street Journal* reported. Col. José Luis Silva became the first high-ranking officer to officially abandon the government since Guaidó, 35, the newly named head of the National Assembly, declared himself acting president at a massive street protest against Maduro last week. "The armed forces today have a fundamental role in the re-establishment of democracy in the country," said Silva in a video posted on social media. Maduro has called for "grand military drills" next month and visited several bases over the weekend to demonstrate that his legitimacy is backed by the army, Russia-based media outlet RT reported. "We are preparing for the most important military exercises in our history," Maduro told troops. At an emergency session of the U.N. Security Council on Saturday, U.S. officials traded rhetorical jabs with Venezuela's top diplomat and Russia's U.N. envoy, *The Washington Post* reported. Moscow's ambassador to the United Nations, Vasily Nebenzya, accused the United States of trying to "engineer a coup." Guaidó has promised amnesty for soldiers who support him. Silva's defection came as Venezuelan diplomats and consular employees in the United States prepared to head home after Maduro broke off relations between the two countries following President Donald Trump's recognition of Guaidó's legitimacy. Meanwhile, Maduro's government on Sunday backed down from demands that U.S. diplomats leave the country almost immediately and instead provided a 30-day window for talks, Reuters reported. The Trump administration warned of a "significant response" if American personnel were threatened or intimidated. "Any violence and intimidation against U.S. diplomatic personnel,

Venezuela's democratic leader, Juan Guaidó, or the National Assembly itself would represent a grave assault on the rule of law and will be met with a significant response," U.S. national security advisor John Bolton tweeted Sunday. European countries have called on Maduro to hold early elections within eight days, with France, Germany and Spain threatening to follow the United States and nearly every major country of the Western Hemisphere in recognizing Guaidó. Maduro has received backing from China, Russia, Syria and Turkey, as well as socialist allies Cuba and Bolivia. The White House on Friday appointed neoconservative Elliott Abrams as special envoy to Venezuela, *The Washington Post* reported. Abrams promoted the 2003 invasion of Iraq and, in the administration of Ronald Reagan, backed U.S. military engagement in Central American civil wars during the 1980s.

Mexican Policies Embrace Migrants

Mexico's new president, Andrés Manuel López Obrador, has moved decisively to encourage migrants fleeing poverty and violence in Central America to stay and work in Mexico, making it easier for them to get visas and work permits, *The New York Times* reported Friday. One new policy would reduce the time it takes to get a humanitarian visa from months to just several days, according to the report. Meanwhile, Mexican officials on Friday promised to provide protection to asylum seekers who are sent back across the border from the United States under a new U.S. policy enacted last week, the *Los Angeles Times* reported. The new Department of Homeland Security policy could force the migrants to wait months or even years in Mexico while their cases are considered by U.S. courts, according to the report. "The Mexican government does not agree with the unilateral measure implemented by the United States government," Roberto Velasco, a spokesman for Mexico's foreign ministry, said in a statement. "However ... we reiterate our commitment to migrants and human rights." Velasco said the U.S. Embassy informed Mexican officials that 20 Central American

NEWS BRIEFS

Anti-Government Protesters, Police Clash in Honduras

Anti-government demonstrators in Honduras over the weekend clashed with riot police during protests marking the first anniversary of the inauguration of President Juan Orlando Hernández, Agence France-Presse reported. "There are people who have been gassed and beaten" by police, opposition leader and former President Manuel Zelaya told reporters. Thousands of people took to the streets in the capital, Tegucigalpa, and across the country, accusing Hernández of electoral fraud and demanding his resignation.

Chubb Ties Up With Banco de Chile for Expansion

Zurich-based insurer Chubb Limited announced today that it has entered into a 15-year distribution agreement with Banco de Chile, the largest bank based in Chile. Chubb will distribute its life and general insurance products on an exclusive basis in Chile through Banco de Chile's channels, including branches, automated teller machines, direct marketing and digital tools. Based in Santiago, Banco de Chile has nearly 400 branches and serves more than two million customers across the country. Chubb did not disclose financial details.

Flooding in Northern Argentina Costs Farmers \$230 Million: Report

Flooding across Argentina's northern Santa Fe province has cost farmers there \$230 million, the *Buenos Aires Times* reported today, citing data from the Rosario Board of Trade. Corn, soybean, sunflower, cotton and sorghum crops were all badly affected by the January rains. The flooded region, which extends into Paraguay, Uruguay and Brazil, has received about five times more rain than expected since the beginning of the year.

asylum-seekers would be returned to Mexico on Friday afternoon at the San Ysidro Port of Entry, the largest border crossing between San Diego and Tijuana.

BUSINESS NEWS

Search Continues for Missing in Vale Dam Disaster

Authorities in Brazil on Sunday called for the evacuation of about 24,000 people as new rains threatened to trigger a second mining dam collapse after Friday's devastating dam break that has left scores killed and at least 230 people still missing, Reuters reported. One of the Córrego do Feijão iron ore complex's tailing dams, owned by Brazilian mining giant Vale, burst Friday morning as employees gathered in the company's cafeteria near the town of Brumadinho in Minas Gerais, sending a wall of water and mud across the facility and nearby homes. "We have a situation of imminent risk, but there hasn't been a rupture of this dam until now and we are monitoring it," said Pedro Aihara, a spokesman for the state fire department, as he called off the search for victims in order to focus on the evacuation, Reuters reported. According to a list released by Vale, the confirmed death toll rose to 37 by Sunday morning. The state government of Minas Gerais has ordered the complex closed and on Sunday said it was requiring Vale to allocate 11 billion reais (\$2.91 billion) for victims of the catastrophe, Folha de S.Paulo reported. On Saturday, prosecutors ordered Vale to reserve five billion reais for environmental damages. Friday's dam burst released 13 million cubic meters of toxic tailings into the Paraopeba river, according to the report. Vale chief executive Fabio Schvartsman apologized without taking responsibility for the incident in a television interview on Saturday, Reuters reported. "Apologies to society, apologies to you, apologies to the whole world for what has happened," he said. "I don't know who is responsible, but you can be sure we'll do our part." President Jair Bolsonaro, who flew over the disaster area in a helicopter on Satur-

day, said he had accepted an offer by Israel to send search equipment that could find people buried in the mud, BBC News reported. Video from the scene shows a tall highway bridge apparently washed away by the initial burst of water, with hundreds of acres of land coated with red-brown mud. While the 2015 collapse of another Vale dam, the Samarco joint venture

with BHP, likely still stands as the country's biggest-ever environmental disaster, Friday's dam burst would be its deadliest. Federal prosecutor José Adércio Sampaio told Reuters said that, depending on Vale's culpability in the new disaster, it may change how his task force handles its 155 billion reais case against Samarco over the 2015 disaster.

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and sound public finances with savings in order to avoid adverse impacts of shocks, especially external shocks. These requirements, among others, have not been met. This has weakened the exchange regime of dollarization. However, dollarization has the confidence and the support of a large majority of Ecuadoreans, which makes the return to a national currency almost impossible. Exports, investment, remittances and external financing are the sources that drive dollarization, and it is where the government must focus its efforts."

A **Pablo Zambrano, executive president of the Industry and Production Chamber (CIP) in Ecuador:** "Although the U.S. dollar was already widely used for financial transactions in the late 1990s, in January 2000 the authorities took the dollar as legal tender and abandoned the Ecuadorean sucre as a last resort amid a serious economic and financial crisis. This decision was inevitable, given the risks of hyperinflation and further capital flight. The legacy of dollarization has been lower exchange-rate risk, the stabilization of salary purchasing power and increased private investment, undoubtedly driven by decreased price and policy uncertainty. Indeed, dollarization is a national asset, and it has more support than any politician or soccer team. The decreased policy uncertainty has a flip side, however. Dollarization means that domestic monetary policy, a tool in most small countries to counterbalance negative shocks, is impotent. Further, without a currency of its own, Ecuador remains at the mercy of U.S. economic developments and the resulting

effects of these on the relative value of the dollar. Adjustments to currency value misalignments are necessarily absorbed through domestic activity and employment, as without the option of currency depreciation, competitiveness can only be restored through productivity improvements and the resulting price falls. However, while dollarization has its costs, it remains a bedrock of economic and political stability in Ecuador. As an unyielding restriction on monetary manipulation, dollarization shields citizens from populist politicians and their abuse of the public purse to promote short-term political goals over long-run system sustainability.

“Dollarization shields citizens from populist politicians and their abuse of the public purse...”

— Pablo Zambrano

Currently, Ecuador is facing the consequences of Correa's fiscal policy mismanagement. The nation is now in the process of renewing the social pact necessary to sustain a robust dollarized economy. It is highly unlikely that President Moreno or any other politician will try to adopt a national currency. Moreover, de-dollarization is a move that would not only further weaken national institutions, but also make the current debt situation worse. The reality is that Ecuador needs dollars to finance its adjustment. Given international conditions, an agreement with the IMF is imperative. The expected arrangement with

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the IMF will boost investor confidence in the country, stimulating capital flows, and lay the foundations for progress toward stable economic growth.”

A **Marco Naranjo Chiriboga,** professor at Escuela Politécnica Nacional and Pontificia Universidad Católica del Ecuador:

“There has certainly been enough time to evaluate Ecuador’s dollarized monetary system. The advantages have definitely been clear, especially in relation to monetary stability. Ecuador, thanks to dollarization, has had single-digit annual inflation—less than 1 percent in the last two years, 0.2 percent in 2017 and 0.27 percent in 2018—and has eliminated exchange-rate risk. This contrasts with the previous 20 years. Between 1980 and 1999, cumulative inflation reached 44,000 percent, and cumulative devaluation of the sucre surpassed 73,000 percent. Monetary stability has allowed for economic recovery, which, except in 2016, has shown positive growth rates. Per capita income went from \$1,300 in 2000 to a little more than \$6,400 in 2018. Although Ecuador is currently undergoing an economic stalemate, the average economic growth rate for the 2015-19 period is 0.76 percent, and GDP rose from \$99.29 billion in 2015 to \$109.45 billion in 2018, according to the Central Bank. Per capita income in that period increased from \$6,099 to \$6,430. Dollarization has definitely contributed to the fact that the slowdown has not become a recession, and especially, to upkeeping monetary stability, which would have been impossible without the system—the government would have had to recur to inorganic emissions of money and devaluation to cover the fiscal deficit in the face of falling oil prices. Since 1972, the Ecuadorean economy depends on oil exports, which make up one-fourth of our fiscal income. When hydrocarbons prices increase, public spending tends to increase considerably. When prices fall, public spending is financed by increasing public debt and new taxes, which have a

recessive multiplier effect on the economy. However, the public debt acquired in recent years is expensive, with interest rates at almost 10 percent, which makes payments highly onerous (almost 10 percent of GDP, 50 percent of exports and more than one-third of the general budget). Ecuador needs a program that sets spending priorities and restructures public debt. For this, a deal with the IMF is imminent.”

A **Vicente Albornoz,** dean of business and economics at Universidad de Las Américas in

Quito: “On balance, Ecuador’s dollarization experience has been positive, not just because of what has been achieved, but also because of what has been prevented. Dollarization gave society confidence in the currency, and this had many positive consequences. The first was a fall in inflation, which dropped from 108 percent in September 2000 to less than 4 percent in January 2004. Such a sharp drop in inflation tends to require an economic contraction, but thanks to dollarization, this was not necessary, and the Ecuadorean economy’s growth was not interrupted. A consequence of the decrease in inflation was that savings and credit were able to grow. Credit’s increase occurred especially in the long term, which has allowed for increased investment in the country. With the exception of two quarters in 2009, Ecuador’s GDP grew every quarter since the second quarter of 2000 until the first quarter of 2015—an unusually long period of growth in Ecuadorean history. But the biggest advantage of dollarization has been preventing Ecuador from becoming Venezuela. The inexistence of a national currency impeded a populist government that was willing to maintain high public spending even at high fiscal costs—such as Rafael Correa’s government—from issuing inorganic money, thus unbalancing the economy completely. After so many years of stability, it is unthinkable for Ecuadoreans to return to a national currency, and an ‘organized de-dollarization’ is technically impossible.”

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