

The Pacific Pumas

An Emerging Model for Emerging Markets

by Samuel George



BertelsmannFoundation



Introduction

As the global economy sails against stiff headwinds, it is easier to highlight what countries are doing wrong, not what they are doing right. Focusing on sluggish growth or dwindling reserves may yield a compelling indictment of the global economic system, but it offers little guidance for improvement.

We understand that there are problems. It is time we focused on the solutions.

Following the financial crisis of 2008, emerging markets seemed capable of reinvigorating global growth. More recently, developing countries have faced trying macroeconomic conditions as the United States tightens monetary policy.

But the all-too easy grouping “emerging markets” by no means constitutes a cohesive bloc. Countries across the globe may experience turbulence, but some have taken steps that will help them weather the storm, and to subsequently emerge as responsible, contributing members of the world economy.

Herein lies the importance of the Pacific Pumas. We believe Mexico, Colombia, Peru and Chile are forging a path for Western Hemisphere emerging markets that are committed to sound macroeconomic policy, global integration and stronger democratic institutions.

Their work may be incomplete, but success breeds influence, and their model has proven attractive for a number of other countries in the region.

For over 30 years, the Bertelsmann Foundation and the Bertelsmann Stiftung have developed an expertise in European and trans-Atlantic issues. In the 21st century, Latin America could play a pivotal role in expanded trans-Atlantic relations, unifying developed and developing economies. We began our coverage of Latin America by looking to the past with the 2013 study *Surviving a Debt Crisis: Five Lessons for Europe from Latin America*. Now we turn to the region’s future with the Pacific Pumas—the budding stars of Latin America.

Bertelsmann Stiftung founder Reinhard Mohn once wrote that the foundation’s projects “could examine ways that would make democracy more efficient and capitalism more human”. We believe this is exactly the trend we are discovering in Mexico, Colombia, Peru and Chile.

To highlight these positives instead of belaboring the pitfalls, we present the *The Pacific Pumas: An Emerging Model for Emerging Markets*.

Annette Heuser
Executive Director
Bertelsmann Foundation

Andreas Esche
Director
Bertelsmann Stiftung

The Puma:

A powerful, fast, agile, lean and stealthy animal. Efficient and resourceful, this New World cat can thrive in mountainous highlands and humid rainforests.

It is a fitting mascot for the emergence of Mexico, Colombia, Peru and Chile.



Executive Summary

The Puma: A powerful, fast, agile, lean and stealthy animal. Efficient and resourceful, this New World cat can thrive in mountainous highlands and humid rainforests.

It is a fitting mascot for the emergence of Mexico, Colombia, Peru and Chile.

These four countries along Latin America's west coast have taken great strides in recent years, and they are poised to emerge as regional leaders. Like the animal, these Pacific Pumas are comfortable operating quietly, away from the spotlight. But their positive momentum is difficult to ignore.

United in the Pacific Alliance, the Pumas represent more than 200 million people with a US\$2.22 trillion GDP; their combined global trade accounts for half of the Latin American total, while the depth and breadth of their free-trade agreements have positioned them to increase commerce with Europe, the US and Asia.

This is the story of the advancement of Mexico, Colombia, Peru and Chile—the Pacific Pumas—and of the opportunities they have moving forward.

The text is divided into two sections:

- The first section considers the emergence of the Pumas individually. It begins with an overview of the four large Latin American countries that have matured economically and politically precisely as their region, the Pacific, has become a cauldron of global growth. The second chapter highlights the macroeconomic stability of the four, while the third considers their democratic maturation. The section concludes with a chapter on the Pumas' embrace of globalization, suggesting their preparedness for a 21st century economy.
- The second section analyzes the Pumas' global opportunities. Through the Pacific Alliance, Mexico, Colombia, Peru and Chile can leverage their individual success through a pact large enough to attract international attention. Chapter 5 debates the importance of the Alliance, while Chapter 6 considers its ramifications throughout Latin America. Chapter 7 examines the importance of the Pumas in greater trans-Atlantic relations, and Chapter 8 reviews the opportunities and challenges the Pumas face in dealing with China.

Together, the two sections outline a golden opportunity for the Pacific Pumas to achieve internal prosperity and stability, while emerging as regional leaders and strategic partners of the US, Europe, and East Asia.

Significant challenges remain: Violence, corruption and inequality still plague parts of these countries, while the four countries' macroeconomic foundations will be tested in the coming years. Yet the text is optimistic, arguing that hard work and propitious timing have put the Pumas in a position to finally achieve their potential.

The Pacific Pumas have much ground to gain, but if they can continue along their current path, they may well be forging an emerging model for emerging markets.





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I. The Pacific Pumas

1. The Pacific Pumas
2. Pumanomics
3. Improved Governance
4. Puma Integration

As the world grapples to stimulate employment, development and innovation, a new club of countries has emerged as an engine of regional growth. Through sound macroeconomics, improved governance, and increased global integration, Mexico, Colombia, Peru and Chile have rallied in recent years. Rather than following the lead of their increasingly protectionist and interventionist neighbors, these Pacific economies have taken their cues from the Asian Tigers of the 1980s.¹

While global attention has been trained on Brazil, the “Pacific Pumas” on Latin America’s figurative and literal periphery have quietly become economic overachievers. This anonymity will be short lived. The four countries have already spearheaded a regional free trade and cooperation pact, the Pacific Alliance, which has captured global attention. Given the rise of China and the US pivot to the East, the Pumas are poised to play a significant role in an emerging Pacific century.

Puma economic growth has been strong and consistent, averaging 4.69 percent annual growth since 2005.² Setting aside 2009, a year of global economic tailspin for which Latin America bore little responsibility, average annual Puma growth nudges above 5.5 percent. These figures compare favorably to the Association of Southeast Asian Nations (ASEAN) over the same span (4.42 percent growth, or 4.80 percent excluding 2009).³

This economic performance has coincided with rising incomes. The Colombian, Chilean and Peruvian middle classes each expanded by more than 10 percent between 2000 and 2010, while some estimate that the Mexican middle

class already accounts for more than half the population.⁴

Inflation, a scourge of Latin American development, has been held in check across the Puma economies. Strong foreign reserves have allowed members to assume countercyclical macroeconomic positions—a rarity in Latin America. Puma sovereigns are investment grade, and their issuances are hot. In January 2013, Mexico issued US\$1.5 billion in bonds at a yield of 4.2 percent, 110 basis points higher than comparable US Treasuries. Later in the month, Colombia issued US\$1 billion in bonds at only 88 basis points above US notes. Both issuances were oversubscribed.⁵

On paper, the Pumas roar. But what is driving these figures, and are they sustainable?

THE ANATOMY OF A PUMA

The Puma’s success stems from political and macroeconomic stability, an embrace of global integration and expanding private consumption.

• Improved Governance

Latin America is notorious for weak democratic institutions, short time horizons and malleable “rules of the game”. Yet, in recent years, the Pumas have generally adhered to established democratic systems with reasonably legitimate elections. The “rules of the game” have been observed by major political parties, and (Mexico’s Andrés Manuel López Obrador aside) transitions from right-leaning to left-leaning executives, and vice versa, have been smooth.⁶

Not only have Puma countries executed transitions admirably, but their new leaders have accepted existing economic

and political structures. Countries that have bent to the left have done so without adopting the statist model popularized by Venezuela’s former president Hugo Chávez and his *Alianza Bolivariana para los Pueblos de Nuestra América* (ALBA) coalition. Countries that have tacked to the right have done so without eliminating social programs or leaning on the barracks. Crucially, Puma central banks have maintained the independence required to pursue macroeconomic stability.

• Global Integration

Mexico, Colombia, Peru and Chile have aggressively pursued liberalized trade, adopting a strategy that proved successful in East Asia in order to more fully integrate with East Asia. Taking a page from ASEAN’s playbook, the Pumas have spearheaded more deep-seated regional integration. The Pacific Alliance has already removed duties on 92 percent of inter-Puma trade—a figure scheduled to increase to 100 percent within 15 years. This is an impressive accomplishment for a region where integration has long been elusive.

While the US has concluded free trade agreements (FTAs) with Mexico (1994), Chile (2004), Peru (2009) and Colombia (2012), the Pumas have expanded well beyond the Western Hemisphere, participating in numerous inter-continental trade pacts. Mexico, Peru and Chile are members of the Asia-Pacific Economic Cooperation and are active negotiators in Trans Pacific Partnership (TPP) dialogues. All four Pumas have successfully negotiated FTAs with the European Union. The *Mercado Común del Sur* (MERCOSUR), an economic bloc of mostly Atlantic South American countries,⁷ has not.

The strategy has paid off. Resource-rich Peru and Chile have tapped into East Asian growth, providing the raw materials that help build that region's megacities. Mexico and Colombia have exploited closer commercial ties to the US. All told, Puma exports increased by an annual average of 4.66 percent (unweighted) since 2000 and are forecast to grow six percent annually through 2017.⁸

• Private Consumption and Investment

Funneling raw materials to global superpowers is old hat for the Pacific Pumas. However, increases in private consumption hint that their recent success is rooted in more than simply capitalizing on strong commodity prices. As poverty decreases and the middle class broadens, Puma countries are forecast to see private consumption expand at an average annual rate of five percent over the next six years.⁹

Mexico, a country of roughly 120 million people, has ten cities with more than one million inhabitants, and 18 with more than 700,000. Colombia (population 46

million) has four, and nearly five, cities with more than one million inhabitants.¹⁰ Multiple, large urban centers portend expanded consumption that will be buttressed by gross fixed investment, forecast to average 8.39 percent annual growth across the Puma economies over the next six years.¹¹ The emergence of true middle classes in these four countries will help them expand their economies beyond digging things out of the earth and shipping them overseas.

THE PUMAS IN A GLOBALIZED WORLD

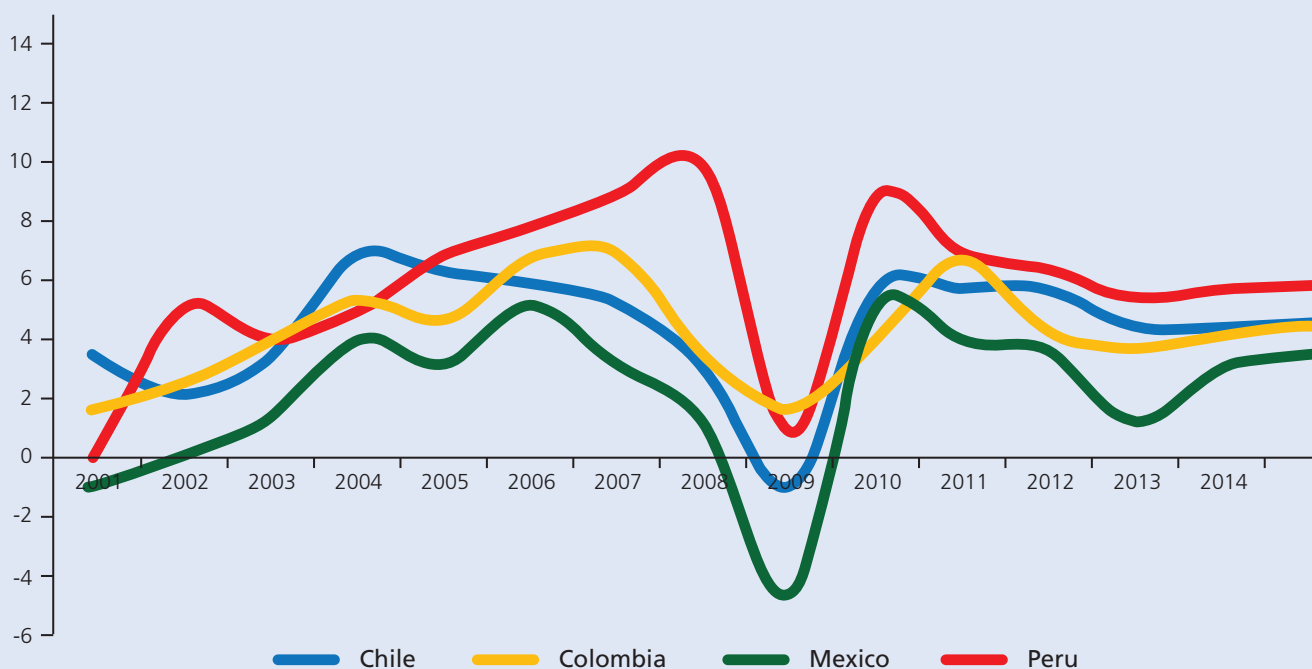
Puma momentum is real, and the timing could not be more propitious. In the near term, emerging markets may face trying macroeconomic conditions, but the Pumas' relative fiscal and monetary balance have them positioned to withstand the turbulence. In the medium and long term, as the US and Europe pivot to the east, and as emerging Asia shifts up the development tables, the Pacific Pumas occupy prime real estate in a reconfigured global economic ecosystem.

If Latin America's west coast was a global backyard during the American century, it could well be center stage in a Pacific century.

The Pumas are already making economic and geopolitical waves. United in the Pacific Alliance pact, the Pumas together are more populous than Brazil. They account for roughly 37 percent of Latin American GDP and 50 percent of the region's trade. The *Mercado Integrado Latinoamericano* (MILA), the Pumas' shared stock exchange, will be the largest in Latin America should Mexico join, as expected, in 2014. Smaller Latin American countries have taken note. Costa Rica has already joined the Pacific Alliance, and Guatemala, Panama and Uruguay are keen to follow, suggesting that the Pumas could emerge as leaders in Latin America.

But the Pumas' strategic influence extends beyond the region. For the United States, the Pacific Alliance represents a key ally in an effort to influence 21st century trade. For Europe, where growth remains anemic, the Pacific Pumas offer

Puma Growth in the 21st Century (Percent Change)



Source: International Monetary Fund Data (Forecasts after 2013)

economic opportunities. For Asia, the Pumas offer resource security and access to market expansion.

THE OPPORTUNITY OF A CENTURY

The Pumas are far from perfect. From the urban shanties looming over Ciudad Juarez to isolated rural communities along the Strait of Magellan, bare feet and callused hands do not always square with the strong growth figures. The optimism in Mexico City is not always felt in Chiapas.

The notion that Mexico is emerging from its drug war would be news to citizens of Guerrero, where the murder rate rivals that of Cote d'Ivoire.¹² Chaos in neighboring Venezuela fuels the perception of a safer Colombia, but viewed independently, it can still be a dangerous place.¹³ Peruvian growth is in part predicated on fickle commodity prices, and its democracy upon a fickle electorate. Chile remains saddled with a flawed constitution, one of many legacies of a painful military dictatorship.

Significant challenges remain, to be sure.

But the Pacific Pumas have a golden opportunity, forged by hard work and good timing. Neighboring countries have demonstrated that economic bonanzas can be easily squandered on subsidized gasoline and metro passes. Are the Pacific Pumas prepared to run with the Tigers of the East? Or will they be ensnared in the traps of the past?

The Pumas: Getting to Know You

Country	Indicators					Forecasts 2013- 2018		Rankings		
	Population 2014 (Millions)	Population Aged 0-14 (Percent)	Average GDP Growth 2004 - 2013 (Removing 2009)	Average Annual Export Growth 2004 - 2013	2013 Inflation (Percent)	Private Consumption Average Annual Growth (Percent)	Gross Fixed Investment Average Annual Growth (Percent)	Ease of Doing Business Rank (Latin America)	Competitiveness Rank (Latin America)	Macroeconomic Environment Rank (Latin America)
Chile	17.40	21	5.42	3.61	1.73	5.00	6.88	1	1	1
Colombia	46.05	28	5.05	6.59	2.22	4.47	6.43	3	6	4
Mexico	119.41	29	3.39	5.72	3.60	3.58	6.75	4	3	6
Peru	31.42	29	7.28	4.83	2.81	5.43	7.38	2	5	2

Chart Sources: Indicators - IMF Data, World Bank Development Indicators; Forecasts - Economist Intelligence Unit Reports, January 2014. Ease of Doing Business Rank - The World Bank; Latin American Competitiveness Rank and Macroeconomic Environment Rank from Global Economic Forum's 2013 - 2014 Global Competitiveness Report.

2 Pumanomics

The argument in favor of Puma economies is about more than growth statistics: Latin America has grown before. But previous economic expansion has often been built upon shaky fundamentals, with those in privileged positions accumulating as much wealth as possible before the entire system collapsed.

Cycles of Latin American booms and busts¹ entrenched long-standing and flagrant inequality while governments' short time horizons undermined any coherent development strategy. In the last half century, millions of indigent *campesinos* streamed into Latin American cities whose formal job market could not adequately absorb them. They made their livings in makeshift economies just as they made their homes in makeshift *favelas* that tumble down hillsides in cities such as Bogotá, Caracas, or Rio de Janeiro.

GDP growth alone cannot fix this. Latin America must match expansion with long-term macroeconomic *stability* to make that growth inclusive and consistent over the long term.

Mexico, Colombia, Peru and Chile have not accomplished this yet. But recent trends suggest that they are on their way to doing so. The Pacific Puma economies have demonstrated consistency, stability and resilience despite persistent global economic turbulence. Uniquely for the region, the Pumas have paired consistent growth with low inflation and fiscal prudence. They have stoked investment and private consumption while also making inroads against poverty.

These developments have rested upon three pillars of macroeconomic stability: 1) central bank maturity, 2) floating exchange rates, and

3) fiscal responsibility. Each is considered individually.

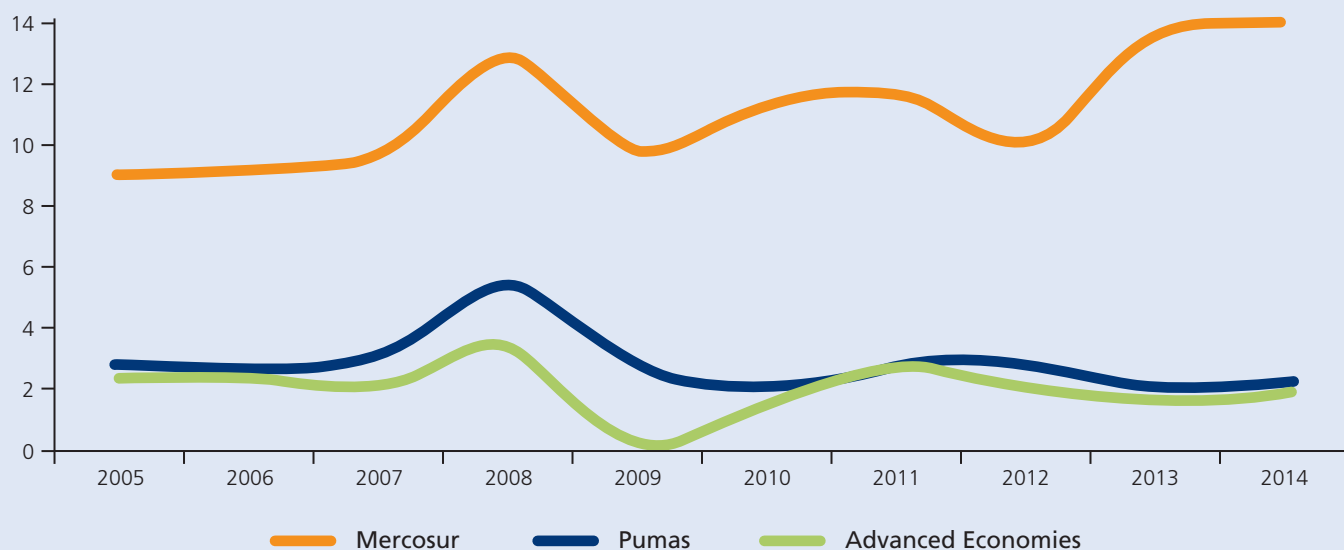
THREE PILLARS OF MACROECONOMIC STABILITY

• Central Bank Maturity

Improved central bank performance and independence has solidified Puma macroeconomic stability. Gone are the days of switching on the printing press to cover fiscal deficits. Inflation has been held within central bank bands across the Puma economies.² Not since Mexico in 2009 has annual inflation in a Puma country topped five percent, and the Andean Pumas have averaged 2.62 percent since 2010 (besting a global average of well over three percent through that span).³

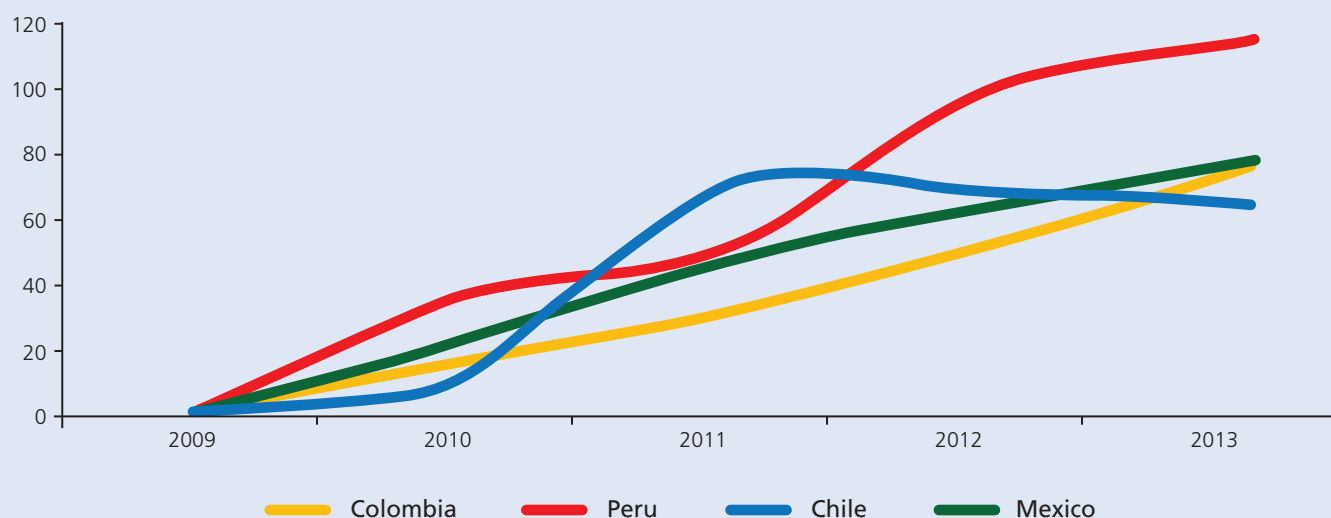
Low inflation combined with burgeoning reserves (on average, Mexican, Colombian, Peruvian and Chilean reserve

Inflation (Annual Percentage)



Source: IMF Data, Inflation, Average Consumer Prices (Unweighted)
Note: Argentine inflation—and thus Mercosur inflation—is likely higher than reported.

Puma Reserve Accumulation (Percent Change since 2009)



Source: IMF International Financial Statistics
2009 = 0, Reserves Reported in SDRs

▲ Strong reserves have positioned the Pumas to outlast turbulence in currency markets.

positions have increased by 80 percent just since 2009⁴) have permitted the Pumas to assume countercyclical fiscal and monetary positions—a rarity in Latin America. Chile tapped its sovereign wealth fund in 2008 to finance a fiscal stimulus, while all four aggressively cut base rates during the global financial crisis, offering more dovish monetary policies that would be risky under inflationary pressure. With the exception of the Bank of Mexico, they have slowly retightened rates as growth rebounded.

A subtle, more targeted intervention approach has helped. The Central Reserve Bank of Peru, for example, has increased reserve rates on Peruvian banks to curb annual credit growth that had exceeded 20 percent—a more precise intervention than blunt base-rate hikes.

Thanks in large part to central bank independence, the Pacific Pumas have established the credibility required to float their currencies on the open market—an important accomplishment for mid-sized economies that are dedicated to maintaining sovereign monetary policy and free flows of capital.

• Floating Exchange Rates

Emerging markets have struggled to establish successful exchange rate regimes since the end of the Bretton Woods monetary system in the 1970s. Many initially turned to some form of a peg—crawling or fixed—in order to anchor exchange rates and stymie hyperinflation. These pegs proved difficult to defend and they often unraveled into currency crises both in Latin America and in Asia.

The Pacific Pumas have been early adopters of managed currency floats,⁵ meaning that domestic currency conversion rates are allowed to fluctuate based on market impulses. Central banks help guide or stabilize movements via forex interventions, such as calls or puts on US dollars, or swaps that offer hedges without committing reserves.

The flexible rates have allowed the Pumas to absorb shocks to their real economies, perhaps best evidenced during the global financial crisis that began in 2008. By January 2009, Chilean, Colombian and Peruvian currencies had all fallen sharply against the dollar as investors rushed to perceived safety. Such pressure has

previously proven disastrous in emerging markets where rigid currencies and brittle monetary systems ultimately cracked under stress. However, with the flexibility of the float, Puma central banks were not forced to exhaust reserves defending pegs, nor were they forced to gamble against speculators betting on devaluations. The Pumas absorbed the rapid depreciation and rebounded swiftly.⁶

The Pacific Pumas' mettle will be tested as the US begins to unwind easy monetary policies forged during the global recession. The mere rumor of US Federal Reserve "tapering" in August 2013 led to Mexican and Colombian depreciations and general disquiet in emerging market currencies. Yet, due to strong fundamentals and hard fought international credibility, Puma currencies have not faced as intense pressure as currencies in other major emerging markets such as South Africa, Turkey and Argentina. Moreover, given their ambitions to boost exports, the Pumas could well benefit from weaker currencies, and their dedication to the float is unlikely to waver.⁷

• Fiscal Responsibility

Fiscal responsibility is a tall order for growing emerging-market countries. Hugo Chávez's final reelection push in Venezuela in 2012 highlighted the electoral bounty to be reaped from a well-timed stimulus.⁸ Meanwhile, as Chilean President Michelle Bachelet found in the years that she nurtured Chile's sovereign wealth fund (2006 – 2008), fiscal discipline during a boom can cause discontent, even within one's own constituency.⁹

However, the Pacific Pumas have demonstrated fiscal restraint through their years of growth. Chile has knocked public debt below 10 percent of GDP and its structural deficit to roughly one percent. Meanwhile, it has replenished its sovereign wealth funds: Now endowed with over US\$15 billion,¹⁰ the funds are more valuable than prior to the 2008-09 stimulus.

Peru has flipped a structural deficit into a surplus, which it has maintained for all but two years since 2006. Colombian external debt has dropped from 40 percent of GDP in 2003 to 22 percent today with hard currency reserves nearly double their 2009 value.¹¹ Bogotá has even codified fiscal discipline with legislation that requires a deficit below one percent of GDP by 2020, even while transfers to conflict victims and at-risk groups are expected to increase.¹²

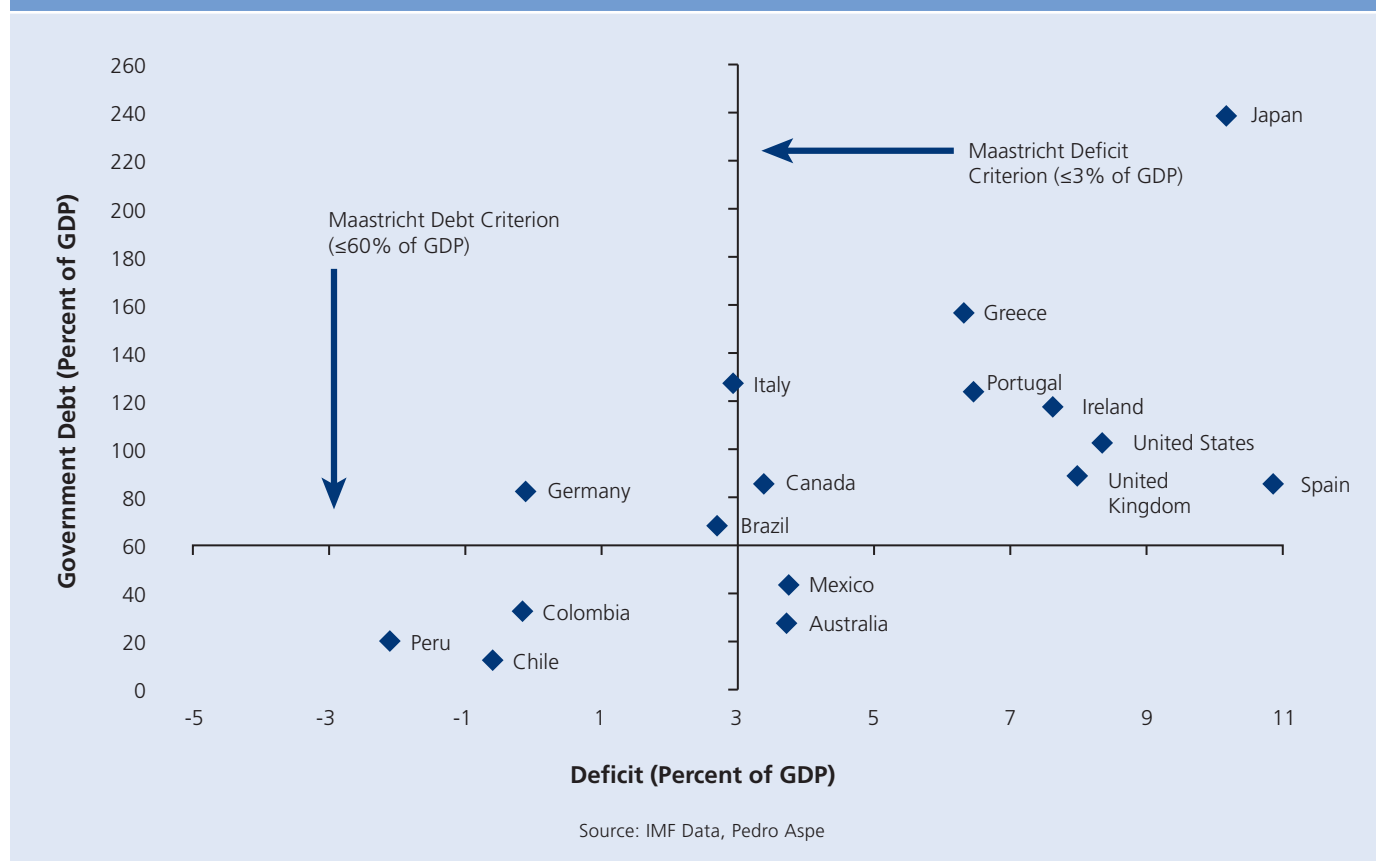
Mexico remains the fiscal wild card. The country's Finance Ministry reports tax intake worth only 9.8 percent of GDP in 2012, far less than the Organization for Economic Co-operation and Development (OECD) average of 33 percent.¹³ Mexico has leaned on the coffers of the state-owned oil company *Petróleos Mexicanos* (PEMEX) to bridge the funding gap, but this revenue strategy, near-sighted to begin with, may become

more implausible following the country's energy reforms.

The *Pacto por México*, a reform coalition spearheaded by President Enrique Peña Nieto, did pass a fiscal reform in October of 2013 that should increase tax intake, but conservatives believe that the reform extends the *depth* of duties paid by the existing tax base without increasing the *breadth* of the base—a nettlesome issue in a country where many jobs remain off the books. The reform also raises taxes on Mexico's manufacturing *maquiladora* sector—a move competitiveness specialists question given its sluggish growth in 2013.¹⁴

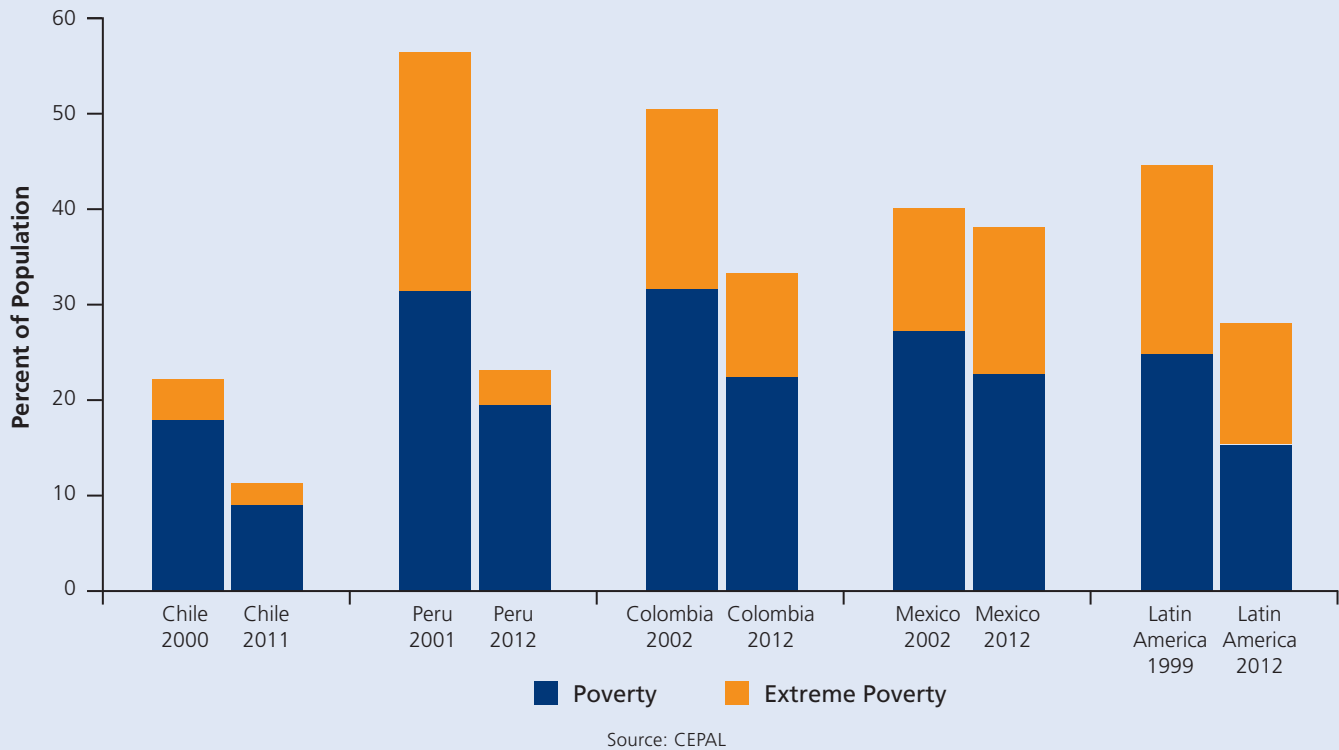
All four Pumas will face fiscal tests in coming years as citizens' expectations of services to be provided by the state grow. Puma governments must find ways to improve tax efficiency without negatively affecting growth momentum.

Debt and Fiscal Deficit in 2012



▲ In an era of debt and stimulus programs, the Pumas have demonstrated impressive fiscal restraint.

Poverty Reduction in Latin America



▲ The Pacific Pumas have made inroads against poverty while maintaining a business friendly environment.

THE (LATIN) AMERICAN DREAM: PUMA EMPLOYMENT, CONSUMPTION, AND INVESTMENT

With this improved macroeconomic foundation, the Pacific Pumas have fostered a positive environment for consumption, investment and business. Poverty remains a fact of life for millions of citizens in these four countries, as it is for billions of people in emerging markets around the world. Yet the Pumas have made rapid progress in this regard as well. The Colombian poverty rate has dipped from 45 percent in 2005 to 34.1 percent in 2011.¹⁵ Peruvian poverty fell 17 percent between 2006 and 2010,¹⁶ and Chilean poverty has been cut in half since the 1980s.

Poverty is down throughout the Americas, including in the more statist countries of the ALBA alliance, such as Venezuela, Ecuador and Bolivia. But the Pumas have matched ALBA improvements without the economic distortions.

As the middle class expands, the *Economist Intelligence Unit* forecasts that the Pumas will enjoy five percent annual private consumption expansion over the next six years, representing a newfound domestic growth motor encompassing 214 million people.¹⁷ Gross fixed investment, forecasted to grow 8.39 percent annually across the Puma economies over the next six years, will buttress consumption increases.¹⁸ An Alliance-wide commitment to infrastructure

could pave the way for foreign direct investment, which has steadily increased for the Pumas.¹⁹

Businesses and investors are taking notice: The World Bank's Doing Business report ranked Chile, Peru, Colombia and Mexico (in that order), as the most business-friendly countries in Latin America.²⁰

While much work remains,²¹ Puma economies are humming, poised to capitalize on opportunities presented by an emerging Pacific Asia while creating a roadmap for the rest of Latin America.

3

Democratic Maturation

The *Pacific Pumas* is the story of macroeconomic maturation: an emerging region's model for integrating into a globalized world. Of crucial importance to the narrative, however, are the improved democratic governance and institutions of Mexico, Colombia, Peru and Chile. A country's governance and economic health are mutually dependent, and institutional distortions, just like economic distortions, can ultimately cause a financial system to collapse.¹

Puma democracies are imperfect, but improved stability, moderation, and a commitment to reform differentiates them not only from other growing Latin American countries, but from many emerging markets around the globe as well.

Mexico's 20th-century bureaucratic authoritarian government had little time

for the niceties of democracy, but it was not particularly ideological. The PRI may be responsible for perpetuating Mexico's deeply ingrained culture of corruption, but it is not guilty of polarizing the electorate.

In Colombia, "full electoral competition has been unbroken since 1974."² Perhaps owing to the threat of left-wing violence, or perhaps as a remnant of the 1957 *Frente Nacional* power-sharing agreement, Colombian governance has not suffered the ideological vicissitudes of its neighbors. Chile, for its part, has a long history of compromise-oriented democracy dating back to the 19th century (with the glaring exception of the military dictatorship of 1973 – 1990).

Peru, with a history of populism, military interventions and wild-card presidents,³ has the most tenuous claim to

pragmatism of the four. Many feared that the ascension of supposedly left-leaning President Ollanta Humala in 2011 would put Peru on a populist course: The Peruvian stock market sank 12.5 percent following the election.⁴ By the end of 2012, however, the markets had recovered and Humala polled favorably among 75 percent of Peru's major business leaders, even while his national approval rating fell below 50 percent.⁵

The Pumas' moderation not only fosters democracies strong enough to withstand populist impulses, but it enables the private sector to expect that the rules of the game will remain relatively consistent.

Individually, Mexico, Colombia, Peru and Chile all face different governance challenges. A closer look at each case highlights both the progress made and

Political Overview

	Current Executive (*end of current term)	Previous Executive	3+ Democratic Elections Since 2000	Key Issues in 2014
Chile	Michelle Bachelet Nueva Mayoría (Center Left) 2014-2018*	Sebastián Piñera Coalición (Center Right) 2010-2014	✓	<ul style="list-style-type: none"> • Potential constitutional reforms • Resolving student protests • Will Bachelet be dedicated to the Pacific Alliance?
Colombia	Juan Manuel Santos Partido de la U (Centrist) 2010-2014*	Álvaro Uribe Primero Colombia (Center Right) 2002-2010	✓	<ul style="list-style-type: none"> • Legislative elections (March) • Presidential elections (May) • Ongoing peace negotiations
Mexico	Enrique Peña Nieto PRI (Centrist) 2012-2018*	Felipe Calderón PAN (Center Right) 2006-2012	✓	<ul style="list-style-type: none"> • Implementation of Energy Reform • Can <i>Pacto por México</i> succeed without PRD? • Can the Mexican left find its voice?
Peru	Ollanta Humala Gana Perú (Center Left) 2011-2016*	Alan García APRA (Center / Center Left) 2006-2011	✓	<ul style="list-style-type: none"> • Will Humala lose the left? • Protests of FDI in Mining Sector • Sustaining growth despite weakening terms of trade

remaining tests that must still be met in order to unlock the growth potential of the Pacific Pumas.

THE MEXICAN REFORMS: A CRITICAL STEP FORWARD

Mexico cannot unleash its true economic potential until the country addresses the bottlenecks that protect vested interests but preclude market sophistication. Trade policy reforms in the early 1990s⁶ positioned Mexico to become a global manufacturing hub, but they proved incomplete. In particular, sections of the service sector—largely unaffected by opened borders—survived the reforms with inefficiencies intact. With an underperforming energy sector, inefficient taxation and stifling private-sector monopolies, Mexico needs a reform package with punch.

In his first year at the helm, President Enrique Peña Nieto of the centrist PRI party has attempted to make up for decades of action deferred. His current push for reform is an intensely political process, with the future of the Mexican economy hanging in the balance. The process has been turbulent, but it appears to be yielding results.

Through his *Pacto por México* agreement of December 2012, President Peña Nieto brought the country's three major political parties, PRI, PAN and PRD,⁷ to outline a broad and ambitious agenda for fiscal, banking, education, telecom and political reforms. While these are all important, it is energy reform that could prove the crucial springboard for Mexican growth.

Between offshore oil and shale gas, Mexico has the resources for an energy revolution, but PEMEX, the state-owned energy giant, lacks the capacity to fully exploit either. Despite massive shale gas reserves (the world's sixth largest, according to Duncan Wood of the Wilson Center⁸), PEMEX has been unable to meet spiking domestic gas demand. With pipelines from the US operating at capacity, Mexican gas prices have

increased just as those across the border have dropped precipitously.

For industry, Mexican oil-based electricity runs at roughly twice the price of US gas-based electricity. Bloated energy costs eat away at the price advantages Mexico hopes will entice US firms to relocate south, threatening Mexico's hard-fought foothold in global manufacturing. A successful energy reform⁹ could attract the investment needed to unleash the energy revolution in the country's industrial sector.

On December 12, 2013, the Mexican Congress approved an energy bill that will open the country's oil and gas sector to international investors. The legislation, which proved more investor-friendly than initially expected, represented a major breakthrough in President Peña Nieto's quest for reform.

The process has not always been smooth. Conservative PAN factions and business leaders remain bitter about fiscal reform, spearheaded by the leftist PRD. Meanwhile, the PRD withdrew from the *Pacto por México* in November 2013, objecting to PAN leadership of energy reform.

The Pacto's initiatives are, therefore, no *faits accomplis*. They are multi-step legal and political processes that could be ambushed by protests that bring Mexico City to a grinding halt or vested interests willing to fight tooth and nail to protect privileged positions.

Nevertheless, the process underscores impressive political sophistication. President Peña Nieto may be the reform movement's figurehead, but the policy proposals are not populist in nature. Rather, they are a concerted effort to create the institutional foundation required to support the weighty potential of the Mexican economy. The press might refer to the lengthy dialogues between parties as "horse trading", but for Mexico—a one-horse country for much of the last century—it is evidence of a burgeoning democracy.

THE COLOMBIAN PEACE PROCESS: FARC, FISH HEADS AND TOADS

Colombia's emergence has not been hindered by unsophisticated or spendthrift economic management,¹⁰ but rather by the persistent social instability that has plagued the country for decades and that has displaced roughly ten percent of the population.¹¹ From *guerrillas* to paramilitaries to drug cartels (and the interconnections between the three) the problem has always been the violence and the deterring effect this has had on private investment, especially on long-term infrastructure projects. This same violence has also prevented Colombia from becoming a truly inclusive democracy.¹²

A lasting peace that extends beyond major metropolitan areas is fundamental to unlocking Colombia's growth potential. The last two Colombian presidents have expended significant political capital addressing the lingering conflict, though they have chosen sharply divergent tactics. President Álvaro Uribe (2002 – 2010) confronted the guerrilla head-on. His violent military offensive punished the largest rebel force, *Fuerzas Armadas Revolucionarias de Colombia* (FARC), halving the faction's troops and killing a number of its influential leaders.

President Juan Manuel Santos, who took office in 2010, seeks to capitalize on the rebel's reduced capacity and influence by negotiating a definitive peace accord. At first glance, the talks between the Colombian government and FARC leaders (which have occurred in Havana since November 2012) would seem unlikely to yield lasting results. After all, the FARC's ideological leaders are not believed to have significant control over a disjointed *guerrilla* movement that may be more interested in drug profits than in the movement's original Marxist principles.

However, the Havana dialogues are not meant to end the violence, at least not immediately. Rather, they are geared towards establishing peace with the

Paseo de la Reforma: Mexican Reforms Under President Peña Nieto

Reform	Approval	Support	Opposition	Reforms	Goal
Telecom & Competition	June 2013	PAN, PRD, PRI	PAN and PRD resist PRI efforts to protect Televisa	<ul style="list-style-type: none"> Create autonomous regulators (IFT & CFCE) Increase competition by auctioning off four TV chains Create two free-to-air channels, along with a government channel 	Economic growth, employment, and competition
Education	September 2013	PAN, PRD, PRI	CNTE (dissident teachers' union) won some concessions to protect its members	<ul style="list-style-type: none"> Evaluation system based on merit Curb the power of teachers' unions End the practice of retirees selling or passing down their positions 	Society of rights
Fiscal	October 2013	PRD, PRI	PAN walked out on debate, feigning its concerns, among them increasing VAT in northern states, were ignored.	<ul style="list-style-type: none"> Establish universal pension system and unemployment insurance Increase tax rates for the wealthy and corporations Reduce maquiladora reimbursements 	Democratic governance
Banking	November 2013	PAN, PRD, PRI	PRD sought changes, but they were struck down by PAN and PRI	<ul style="list-style-type: none"> Facilitate collection of loan guarantees by creating specialized courts Allow banks to register losses in order to increase the amount and number of loans to SMEs Give government more regulatory power over financial firms 	Economic growth, employment, and competition
Political	December 2013	PAN, PRD	PRI, but PRI had to offer reform to entice PAN and PRD to join <i>Pacto por Mexico</i>	<ul style="list-style-type: none"> End ban on reelection for legislators and mayors Allow independent candidates to run for public office Replace state elections-monitoring institutions with a federal one (INE) 	Democratic governance
Energy	December 2013	PAN, PRI (PRI allowed foreign-contracting rather than just profit-sharing to win PAN back after fiscal reform debacle)	PRD opposed profit-sharing and private or foreign contracting and pulled out of the <i>Pacto por Mexico</i> in protest	<ul style="list-style-type: none"> Open oil and gas industry to private and foreign investment through cash, profit-sharing, and production licensing Strips STPRM (Pemex union) of its five board member positions 	Economic growth, employment, and competition

Source: Bertelsmann Foundation, *The Economist*, *EL Universal*, *Reuters*, *Forbes*, *LA Times*

political wing of FARC, thus isolating the faction of the movement that is fighting for illicit gains. As of now, the two factions are co-dependent. The political FARC provides ideological legitimacy,¹³ while the operational FARC offers financing, be it through drugs, kidnapping or other destructive activity.

In the 1990s, the Colombian military (and paramilitary) attempted to battle the FARC by *quitando el agua del pez*—draining the water from the fish. In practice, this meant locating the *guerillas* and “removing” anything (or anyone) that might hide or protect them. This led to a spiraling tit-for-tat between different armed forces, ultimately rendering

Colombia one of the most dangerous countries on the planet in the 1990s.

The current peace process represents a different strategy. Instead of draining the water from the fish, the government hopes to remove the fish's head. If the government can make peace with FARC's political wing (its “brain”), this would

undermine the group's justification for continued conflict. The remaining "gangster" element of FARC, now lacking ideological support, would be isolated, exposed, and doggedly pursued.

An eventual peace deal might well guarantee political participation for the former rebel combatants based on a quota system (the country already reserves two senate seats for representatives from the country's indigenous communities, and two lower house seats for Afro-Colombians).

The plan is contingent upon the Colombian right accepting the left into the democratic sphere, by no means a given. In February 2014, *Semana*, a Colombian weekly, offered evidence that the Colombian military—independent of the government—was spying on the peace talks.¹⁴ That same month two prominent left-leaning politicians

received death threats from shadowy paramilitary organizations.¹⁵

The Colombian phrase *tragar un zapo* (swallow a toad) might translate into English as "a tough pill to swallow". By offering institutional legitimacy and political inclusion to FARC leaders in Havana, Colombian officials are swallowing toads by the handful. But once Colombia can achieve what has been an elusive peace, it can then begin to flex its economic muscles.

CHILEAN DEMOCRACY: UNFINISHED BUSINESS

On March 11, 2014, Michelle Bachelet donned Chile's presidential sash for a second time after having handily won a December 15 run-off election (Bachelet previously served as president from 2006 – 2010). According to her 2013 electoral platform, she will focus on education, tax reform and adjustments to—if not

an outright overhaul of—the Chilean constitution. The three objectives are intertwined, and they reflect Chile's 25-year effort to responsibly reform a severely flawed document.

Forged under General Augusto Pinochet's military dictatorship (1973–1990), Chile's 1980 constitution carved out a series of authoritarian enclaves, designed to allow General Pinochet to cloak his heavy-handed rule in the guise of democracy.¹⁶ With an influential, unchecked military presence, weak legislature, concentrated presidential powers, and a binomial electoral system that ensured disproportionate conservative representation, Pinochet's constitution hardly provided a bedrock for Latin America's most advanced democracy.

Much to Chile's credit, however, subsequent governments did not attempt to delegitimize this constitution

Timeline – The Colombian Peace Process

1948 - 57	1960s - 1990s	1998	2000	2001	2002
<ul style="list-style-type: none"> 250,000-300,000 killed in "La Violencia", a 10-year civil war between conservatives and liberals. In 1958, both sides agree to form the National Front and ban all other parties. 	<ul style="list-style-type: none"> Many of Colombia's left- and right-wing extremist groups form. Political violence and assassinations are prevalent. Efforts to integrate FARC into politics are ineffective. 	<ul style="list-style-type: none"> Conservative President Andres Pastrana Arango grants FARC a safe haven the size of Switzerland in the south-east as part of peace talks. The zone is off-limits to the army. 	<ul style="list-style-type: none"> Pastrana's "Plan Colombia" wins billions in mainly military aid from the US to fight drug-trafficking and rebels who profit and protect the trade. Peace talks deteriorate. 	<ul style="list-style-type: none"> Government, FARC sign San Francisco agreement, committing both to negotiate ceasefire. 	<ul style="list-style-type: none"> Independent Alvaro Uribe assumes presidency, promising to crack down on rebel groups. As Uribe is sworn in, explosions rock Bogota.
Uribe's first term: 2002 - 2006		Uribe's second term: 2006 - 2010		Santos' first term: 2010 - present	
<ul style="list-style-type: none"> Uribe carries out aggressive military campaign against FARC, pushing guerrillas out of towns and back into rural areas. New law offers reduced punishment for paramilitaries who turn in their arms. Rights groups say the legislation is too lenient. 		<ul style="list-style-type: none"> Uribistas win overwhelming electoral victories. Uribe continues heavy-handed campaign, including a cross-border strike in Ecuador that sparks diplomatic crises with Ecuador and Venezuela. Colombia extradites 14 paramilitary warlords to the United States. 		<ul style="list-style-type: none"> Juan Manuel Santos, Uribe's former Defense Minister, elected president. FARC unilaterally releases several hostages. Santos opens exploratory talks with FARC guerrillas. Uribe accuses Santos of "giving impunity to terrorists". 	
November 2012 - May 2013		May 2013 - November 2013		November 28 - Present	
<ul style="list-style-type: none"> Havana discussions begin. Early topics include land access, rural development, infrastructure, poverty reduction, and agrarian stimulus. Agreement on these topics reached in May 2013. 		<ul style="list-style-type: none"> Parties open discussions on political participation. Topics include improved access to media, regional "Councils for Reconciliation and Coexistence", changes to ease the formation of political parties. Parties reach agreements on these topics in November 2013. 		<ul style="list-style-type: none"> Seventeenth round begins. Both parties agree to postpone the contentious topics (ending the conflict/demobilization and transnational justice) and move to addressing international drugs. 	

Source: BBC America, ColombiaPeace.org

outright—an approach that would have likely interrupted the country's steady economic growth. Rather, iterations of the center-left *Concertación* government (1990–2010) methodically reformed the document, often in close consultation with the private sector and the political opposition. All told, the original constitution has undergone 131 amendments, affecting 79 of its 120 articles.¹⁷

The current Bachelet government appears poised to address the remaining deficiencies instilled by the Pinochet government as well as the growing pains of a country transitioning to the developed world while still facing persistent inequality. If these changes can promote upward mobility and a more inclusive democracy, they will bolster the country's economic rise.

But Chile must come to terms with student protesters, whose strikes have intermittently shut down schools and immobilized streets since 2006. The students balk at Pinochet-era education laws that favor affluent pupils¹⁸ and university fees that reach US\$1000 monthly. Bachelet's platform proposes full subsidization of public universities within six years (though this would not

address the flawed high school model). She would pay for this by increasing corporate tax rates from 20 to 25 percent, still far below the weighted OECD average of just roughly 35 percent.¹⁹

Bachelet's efforts to improve democratic inclusiveness are equally important. Following the Pinochet years, Chile's vulnerable and nascent democracy took a cautious, centrist approach. Twenty-five years later, this method threatens to ossify the political process. The country's curious binomial election system stipulates that each congressional district must split its two seats between the first and second-place parties, unless one of the two can garner two-thirds of the vote—a relative rarity.

This system disincentivizes participation because split districts are the most likely outcome—one reason more and more Chileans are not bothering to go to the polls. If it's a foregone conclusion that one liberal and one conservative will win, why vote? In fact, only 50 percent of eligible Chileans voted in last November's general election.²⁰ Bachelet will seek to reform the binomial system, though this will require politicking because her coalition lacks the congressional 3/5 quorum required to change it.²¹

Finally, Bachelet's incorporation of former student leaders and more leftist factions into her *Nueva Mayoría* coalition is an important step forward for Chile. While some²² view this as a concerning leftward veer, it is far better to incorporate these elements into the formal political dialogue than to exclude them from it. A century of repression has not eliminated the Chilean left. Far better to have leftists participate in Chile's *democracia de los acuerdos* (democracy based on agreement), rather than to have them battling against it.

PERU: THE MATURATION OF A PUMA CUB

Peru earns its stripes based on economic performance and an openness to trade that has positioned it to capitalize on Asia's rise. In terms of democracy, however, this Pacific Puma still has some growing up to do.²³

The country has taken important strides. Peru has held three successful presidential elections since the ousting of the semi-authoritarian Alberto Fujimori (1990 - 2000), and the winners of those elections have generally followed the rules of the game. Peru has executed party transitions: Three different political coalitions have led 21st century Peru.

The Road to Redemption: Chilean Constitutional Reforms Since 1989

Year	Reformer (Party)	Reforms
1989	Military government & <i>Concertación de Partidos por la Democracia</i>	<ul style="list-style-type: none"> • Limited penalization of groups previously viewed as subversive • Increased number of elected senators and added civilian member to National Security Council • Modified constitutional amendment mechanism • Removed president's ability to dissolve lower house
2005	President Ricardo Lagos (<i>Concertación</i>); Supported by Conservative Senators	<ul style="list-style-type: none"> • Cut presidential term from six years to four years • Eliminated ten unelected senate seats reserved for military-affiliated personnel • Eliminated several prerogatives of the armed forces and police chief • Increased power of congress
2014 (potential)	President Michelle Bachelet (<i>Nueva Mayoría</i>)	<ul style="list-style-type: none"> • Revise binomial electoral system • Address high-majority requirement for educational reforms • Inclusion of rights for women and indigenous groups • Extend presidential term limit from four years or allow consecutive terms

The first two presidents respected a constitutional ban on immediate reelection, and current President Ollanta Humala, who took office in 2011, has promised to do the same.²⁴ Two successive presidents have run on left-leaning platforms without subsequently dismantling Peru's free-market economy, suggesting an important modicum of stability in Lima.

Nevertheless, the country's political system remains rudimentary. In contrast to Mexico, Colombia and Chile, political volatility has been a norm in Peru. The country suffered eight coups in the 20th century, while presidents averaged less than three and a half years in office. A more recent consequence of this instability has been the diminished importance of political parties. Beginning with Fujimori's "anti-political" campaign in 1990, Peruvian presidents have built political parties as short-term vehicles they could ride to power.²⁵ These rickety coalitions that lack philosophical underpinnings are subsequently held together by the meting out of sinecures and favors.

Operating without a strong party foundation, Peruvian presidents have struggled to pursue a coherent direction. For example, President Humala governs to the right of how he campaigned. Business may breathe a sigh of relief, but voters who backed the president based on his left-leaning platform feel duped.²⁶ Without any defined governing philosophy, Peruvian presidents' personal exploits (and foibles) attract more attention than reform packages. These factors have inhibited the country's ability to fully translate growth into tangible improvements—one reason why the approval ratings of the last four presidents have deteriorated through the course of their presidencies.

Peru's economy has benefited from buoyant Asian commodity demand. To manage this windfall—and, ultimately, to manage *after* the windfall—the country's democracy must improve. Successful elections and transitions represent an important step forward. But until there

is more institutional stability, Peruvian politics remain something of a crapshoot, threatening to turn the current economic winning streak into a bust.

MOVING FORWARD

Puma democratic gains are not irreversible. The December 9, 2013 sacking of Bogota's left-leaning Mayor Gustavo Petro by a right-leaning inspector general on rather flimsy grounds underscores the tenuousness of Puma institutional stability. We have yet to see if an elected, left-leaning Colombian or Mexican executive would adhere to existing frameworks. But all democratic systems in the world suffer from significant flaws. Deficiencies notwithstanding, the democratic conditions in Mexico, Colombia, Peru and Chile have become increasingly stable, and the rules of the game increasingly clear and reliable.

These improvements have helped position the Pumas to become regional leaders. Most of Latin America may be growing, but it is the Pumas, along with *Pumitas* such as Uruguay and Costa Rica, that are simultaneously maturing politically. Mexico may have similar 2013 growth figures to those of Venezuela, but if the Mexican reforms are successful, it will be well positioned for consistent future growth, while Venezuela will be but one day closer to its reckoning.

Brazil's market size swamps that of Colombia or Peru, but investors may tire of the *Custo Brasil*, the implicit operational cost of trying to do business in that country, and they will be enticed by the Pumas' business-friendly governance. Argentina maintains its perennial growth potential, but unpredictable rules of the game hinder firms' and families' ability to plan for the future—something that can be done with relative confidence across the Andes in Chile.

Puma democratic maturity can compare favorably to governance in emerging Asian countries as well, where the heavy hand of the state in countries such as China or Vietnam could face increased social backlash in coming years.

Improved Puma governance may not appear in any given year's growth charts, but over time it will create conditions that could allow strong performance to be sustained in the future.

4

Puma Integration:

Running with the Tigers

If geography is destiny, Pacific Latin America is not a bad place to be in the early 21st century. East Asia has emerged as a cauldron of global growth and trade, while the US and Canada remain economic powerhouses and hubs of innovation. Colombia, Peru, Chile and Mexico have the good fortune of both having direct access to the Pacific's intricate web of supply chains *and* of possessing the raw inputs—the copper, iron ore, and hydrocarbons—that are so valuable to emerging East Asia.

Much of Latin America has benefited from strong commodity prices over the last ten years. What differentiates the Pumas is their effort to create deeper linkages, with both traditional trans-Atlantic partners and emerging Asian

partners. The statistics suggest the effort has been successful: The Pumas have averaged 4.7 percent annual growth in exports since 2001, and the IMF forecasts Puma exports to grow six percent annually through 2017.¹

But trade liberalization, itself, is no panacea, and export-led growth raises a host of challenges. The Andean Pumas, with resource-heavy export portfolios, must avoid the looming pitfalls of commodity reliance. Mexico, on the other hand, must encourage the rise of its manufacturing sector while addressing the gap between winners and losers of trade.

This chapter begins with an overview of Puma integration, featuring Mexican

and Chilean case studies. The chapter concludes by considering the challenges the Pumas face in their pursuit of integration.

PUMA TRADE IN A GLOBALIZED WORLD

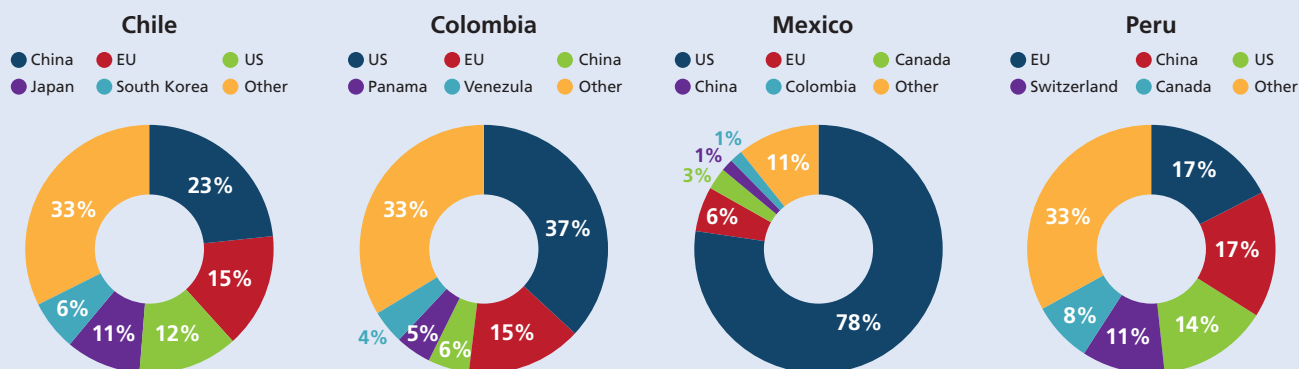
The Pumas' embrace of trade began mostly in the 1980s and 1990s, when many Latin American countries lifted tariff and regulatory barriers that had been designed to protect domestic industries.² Unilateral reforms eventually led to a "surge" in trade, especially with non-traditional partners in East Asia.³ More recently, the Pumas have been active participants in bilateral and multilateral free trade agreements. They have aligned with those countries seeking to accomplish bilaterally and regionally

Puma Free Trade Agreements with Major Economies

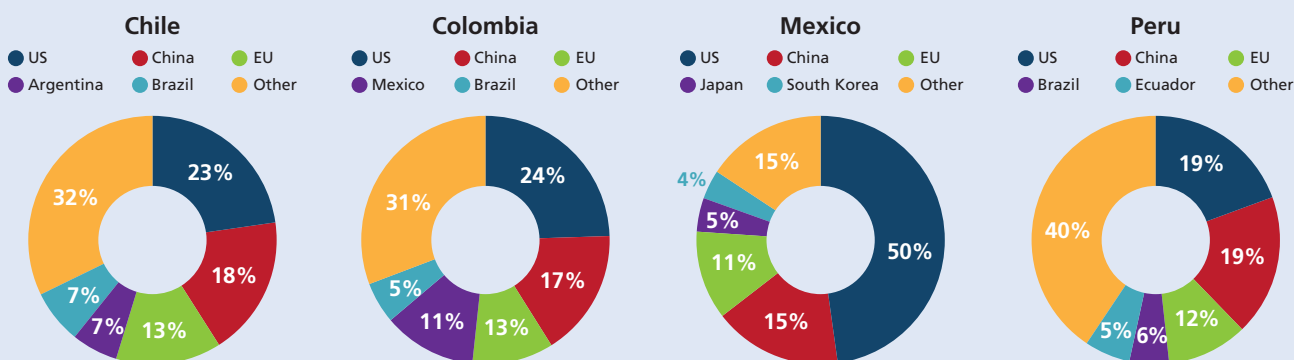
	Chile	Colombia	Mexico	Peru
Australia	FTA (2009)	FTA (proposed)	FTA (under negotiation through TPP)	FTA (under negotiation through TPP)
Canada	FTA (1997)	FTA (2011)	FTA (1994 - NAFTA)	FTA (2009)
China	FTA (2006)			FTA (2010)
EU	FTA (2003)	FTA (2013)	FTA (2000)	FTA (2013)
India	PTA (2007)	PTA (proposed)		
Japan	EPA (2007)	FTA (proposed)	EPA (2005)	FTA (2012)
South Korea	FTA (2004)	FTA (signed in 2013, not in force)	SECA (under negotiation)	FTA (2011)
Thailand	FTA (signed in 2013, but not in force)			FTA (2011)
US	FTA (2004)	FTA (2012)	FTA (1994 - NAFTA)	FTA (2009)
Vietnam	FTA (signed 2011, but not in force)		FTA (under negotiation through TPP)	FTA (under negotiation through TPP)

Assisting Sources: Inter-American Development Bank, Barbara Kotschwar

Puma Exports by Destination, 2012 (Percent of Total Value)



Puma Imports by Origin, 2012 (Percent of Total Value)



Source: World Trade Organization

what the World Trade Organization has been unable to accomplish globally: free trade.

Some fear that these types of agreements could lead to trade regionalism, but the Pumas have used them to forge linkages all over the world. All four have signed FTAs with the US, Canada, and the EU, while simultaneously integrating into East Asia's "noodle bowl" of pacts. China, Japan, South Korea, Singapore and India have all concluded agreements with at least two of the Pumas.

Many of the deals go well beyond simply liberalizing trade in goods. They also include "comprehensive provisions on services...intellectual property rights... investment, government procurement, trade facilitation and competition".⁴ The Korea-Peru and Australia-Chile

agreements are considered "the gold standard of FTAs".⁵

Efforts to integrate into global trade have paid off. Spurred by strong copper prices, Chilean trade with China increased from US\$1.34 billion in 2000 to US\$17.94 billion in 2012 (the two signed a free trade agreement in 2006).⁶ Peruvian exports to China increased 42 percent between 2010 and 2012, due at least in part to the Peru-China Free Trade Agreement that came into effect in 2010.⁷ Mexican trade with the US increased more than 500 percent in the first 20 years of NAFTA,⁸ while Colombian exports are up nearly 50 percent just since 2010.⁹

This integration, in both the Atlantic and Pacific, has primed the Pumas for the world's future trade ecosystem. With the WTO's Doha Round stalled,

the globe's foremost trade initiatives are the Trans-Pacific Partnership (TPP), which focuses mostly on reducing tariffs and harmonizing regulations in Pacific Rim countries, and the Trans-Atlantic Trade and Investment Pact (TTIP), which intends to harmonize EU-US trade regulations. These deals represent 38 and 40 percent, respectively, of global GDP, and they could well set the standard for 21st century trade.

Mexico, Peru and Chile are already participants in TPP dialogues. Colombia, withheld from TPP on a technicality,¹⁰ can ensure that its voice is heard, and that its regulatory and tariff standards are up to snuff, through Pacific Alliance dialogues. The Pumas, and Mexico in particular, are concerned that they cannot participate in TTIP dialogues, which have been limited to US and EU participants (see Chapter

CASE STUDY A

The Mexican Model: Becoming a hub

Notwithstanding Chile's rash brush with neoliberalism in the 1970s, Latin America's true shift from protectionism began in 1985 with Mexico's ascension to the General Agreement on Tariffs and Trade (GATT). It continued in 1994 with the North American Free Trade Association (NAFTA). Today Mexico has free trade agreements with 44 countries; that is more than twice as many as China and four times more than Brazil.¹¹

These agreements coincided with sharp increases in Mexican trade: In 1985, the volume of Mexican exports totaled just 27.6 percent of its 1995 value. By 2000, Mexico exported double the 1995 volume.¹² Mexico subsequently doubled the value of its exports again between 2000 and 2010. Along the way, the country established itself as Latin America's manufacturing capital, exporting more of such goods than the rest of the region combined¹³—a point of interest to other Pumas hoping to expand in this sector.

Mexico's embrace of free trade helped fuel the sector's emergence for two reasons: First, it precipitated swift increases in foreign direct investment. Attracted by newfound ease in moving products across the border into the US, international firms outsourced tasks along the value chain to Mexico before importing finished (or nearly finished) products north. From 1980 through the advent of NAFTA on January 1, 1994, Mexico averaged just US\$2.6 billion in net FDI inflows. From 1994 through 2012, that average jumped to nearly US\$19 billion.¹⁴

This investment has radically influenced Mexico's export portfolio. In the 1980s, hydrocarbons accounted for 61 percent of Mexican exports. By 2012, manufactured goods represented a full 81 percent of Mexican exports.¹⁵ The FDI has also induced knowledge spillover, and Mexico has advanced in high-tech goods: It is the world's preeminent exporter of flat-screen TVs, and a major producer of domestic and medical appliances.

Secondly, liberalized trade forced efficiency improvements. International competition pushed previously coddled producers towards reforms that would otherwise be difficult and time consuming to legislate. Forced to compete with China, domestic firms had to sink or swim as China cut into Mexico's manufacturing exports to the US after joining the WTO in 2001. Twelve years later, Mexico has taken significant strides towards closing the productivity gap with the Asian giant (an effort assisted by increased Chinese wages and trans-Pacific transportation costs), and has nearly recovered its share of manufacturing exports.

While Peru and Colombia may look to the Mexican blueprint to establish their own industrial sectors, the Mexican model has also encountered some of the pitfalls of global integration, particularly an emerging gap between winners and losers of trade. Within firms, wages remain stubbornly low—a boon for owners of capital, but a burden for labor. Between firms, larger multinationals have been able to capitalize on FTAs and foreign investment; smaller (often informal) firms have not. Nationally, Mexico's manufacturing sector is concentrated in the north, a region whose growth has far outpaced the more rural south.¹⁶

Moving forward, Mexico must ensure that more firms are exposed to the benefits of liberalized trade. If it does not, and if existing inequality persists, there will almost certainly be a backlash to Mexico's model for integration.

7). Nevertheless, the Pumas' pre-existing pacts and ongoing discussions with the EU and the US can help ensure that their regulations match those enumerated in any future TTIP deal.

Alternatively, countries not party to either pact (the four BRICs—Brazil, China, India, and Russia—stand out in this regard) could find themselves either isolated or pressured to subsequently join a pact they did not help design.

PUMA TRAPS: BEATING RESOURCE RELIANCE

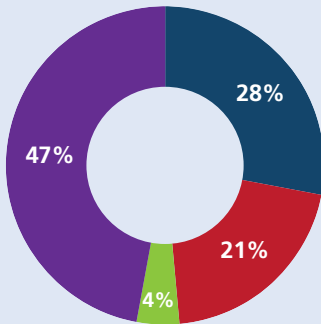
Puma trade may be rapidly increasing, but the infamous commodity trap looms. The Pumas—Chile, Peru and Colombia in particular—have greatly benefited from the highest crude oil and metal prices observed since World War II.¹⁷ There is no shortage of pundits arguing that their recent growth is predicated solely on strong commodity prices. Should these falter, the argument continues, so too would Puma progress. Even if prices remain strong, overreliance on commodity exports threatens to prevent the linkages the Pumas need to expand beyond resource reliance.

Basic theory of supply and demand suggests that commodity prices may soon come back down to earth. On the one hand, demand may be in decline. As Chinese growth tapers, and as OECD demand for Chinese goods remains sluggish, the country no longer stockpiles copper and ore reserves, instead pursuing a “hand-to-mouth” buying pattern.¹⁸ On the other hand, commodity supply has increased. New investments inspired by boom-era prices are only now coming online, portending expanded supply. Credit Suisse forecasts that global copper production will increase four percent annually between 2012 and 2015, leading the investment bank to conclude that “copper scarcity is a thing of the past.”¹⁹

The writing is already on the wall. Between 2011 and mid-2013, global copper prices fell 35 percent, iron ore 40 percent, and gold 36 percent. Mineral shipments leaving Peru's Callao port

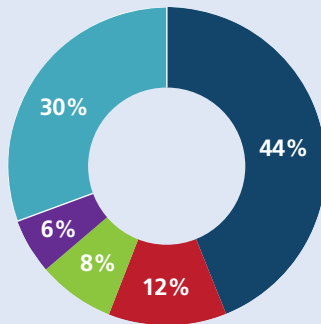
Chile Exports by Value, 2012

- Refined copper and copper alloys, unwrought
- Copper ores and concentrates
- Unrefined copper, copper anodes for electrolytic refining
- Other



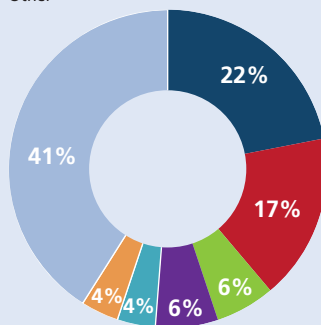
Colombia Exports by Value, 2012

- Petroleum oils, crude
- Coal / Coal Products
- Petroleum oils, other than crude
- Gold
- Other



Peru Exports by Value, 2012

- Gold (including gold plated with platinum)
- Copper ores and concentrates
- Refined copper and copper alloys, unwrought
- Petroleum oils, other than crude
- Flours, meals and pellets, of meat or meat offal
- Lead ores and concentrates
- Other



Source: United Nations Data

were down 12 percent through the first six months of 2013.²⁰

Yet the unwinding of the boom need not be cataclysmic. For one thing, commodity exports will not disappear overnight. Chinese growth may decline, but seven percent annual growth over the next five years (as forecast by the IMF) is not exactly a depression. Moreover, demand from other resource-starved Asian countries will likely increase. Between 2000 and 2010, mineral imports to India, Indonesia, Malaysia and Thailand all averaged more than 20 percent annual

growth.²¹ Even the bearish forecasts have copper prices *above* the average price between 2003 and 2008, which were years of strong growth for Chile and Peru.²²

In terms of linkages, conventional wisdom holds that commodity exports generate few forward and backward employment opportunities. Where raw resources are simply withdrawn from the earth and shipped abroad, few “downstream” jobs are created, little technology is needed and a country does not cultivate spillover knowledge.²³

CASE STUDY B

The Chilean Model: Export Diversification

Chile is another Latin American veteran of liberalized trade, having experimented with reduced tariffs since 1974. In the early 1970s, Chile remained fortified behind import substitution industrialization (ISI) policies. Luxury goods faced tariffs as high as 750 percent and all imports required administrative approval.²⁴ The country rapidly embraced global markets following the 1973 coup d'état, but the rigid neoliberalism implemented by the military junta led to falling real wages, soaring unemployment and a soft underbelly of corporate debt—vulnerabilities exposed in 1982 when 800 firms filed for bankruptcy and GDP contracted by 14 percent.²⁷

Beginning in the mid-1980s, however, Santiago adopted a more measured tack towards real integration. Marked by a steady decrease in tariffs (from 15 percent in 1988 to near 3 percent in 2010),²⁸ a propensity for bilateral trade agreements, and a concerted effort to develop non-traditional exports, these policies led to two decades of sustained growth, including during the years that *predated* the booming commodity prices of the 2000s.

Crucially, Chile's opening led to a blossoming of non-traditional exports. At the farm level, Chileans have long held comparative advantages in production. However, not until the country pursued more liberal trade did producers of wine, fruit and fish have access to external markets and equipment inputs, as well as the competitive exchange rate needed to trade internationally.²⁹

The emergence of Chilean wine is a testament to the model's success. Wine, which began the 1990s accounting for roughly one percent of Chile's non-copper exports, finished the decade at nearly six percent. Presently, Chile is the world's seventh largest wine producer, after nearly doubling exports in 2012.

As Chilean viticulture improved, foreign capital poured into the sector. Simply between 1995 and 2000, wine-related FDI equaled 14 times the 1990-1994 value. In some cases, European firms opened joint ventures with Chilean producers—one reason that the award-winning Concha y Toro's wine is now sold in at least 135 countries.³⁰

▲ Commodities still represent a major component of the Andean Pumas' exports

But perhaps this is an oversimplification.²⁴ As with industrial goods, commodities pass through a series of production phases as they are refined, for example, from iron ore to steel or from oil to gasoline. This process requires advanced technology. The problem is that the technology has historically been housed elsewhere. For example, Chile, the world's largest producer of copper, builds only one percent of the world's fabricated copper products.²⁵ Mexico exports crude oil to the US and imports refined fuel.

As the Pumas develop internal investment muscle, and as they continue to earn the faith of international developers, more downstream linkages could occur domestically. Chile has already set the stage, moving from an imitator to an innovator in exporting wood pulp and wine (as opposed to logs and grapes). If the other Pumas can follow suit, perhaps natural resources can be a foundation for an expanding economic ecosystem, as opposed to the first and last words in Latin American development.

PREPARING POST-BOOM ECONOMIES

The Pumas understand that booming commodity prices may not last forever,

and even if they did, simple raw resource exports are unlikely to generate holistic development. Thus, Mexico, Colombia, Peru and Chile are attempting to achieve deep integration both regionally and with the global economic hubs in the Atlantic and Pacific with the goal of establishing niches in trade networks and supply chains beyond commodities.

Executing the strategy, however, requires far more than signing as many free trade deals as possible. The Pumas must make sure that the benefits of export-led growth are more evenly spread. Improved infrastructure is a good place to start. All four countries face unforgiving topography, and as a result, in-country transportation from remote regions to exit points implies great expense. Colombia, for example, does not have the domestic transport system required to conduct major trade with East Asia: It is three times more expensive to ship a container from Bogotá to the Caribbean port of Barranquilla than it is to ship the same container from Barranquilla to Hong Kong.³¹

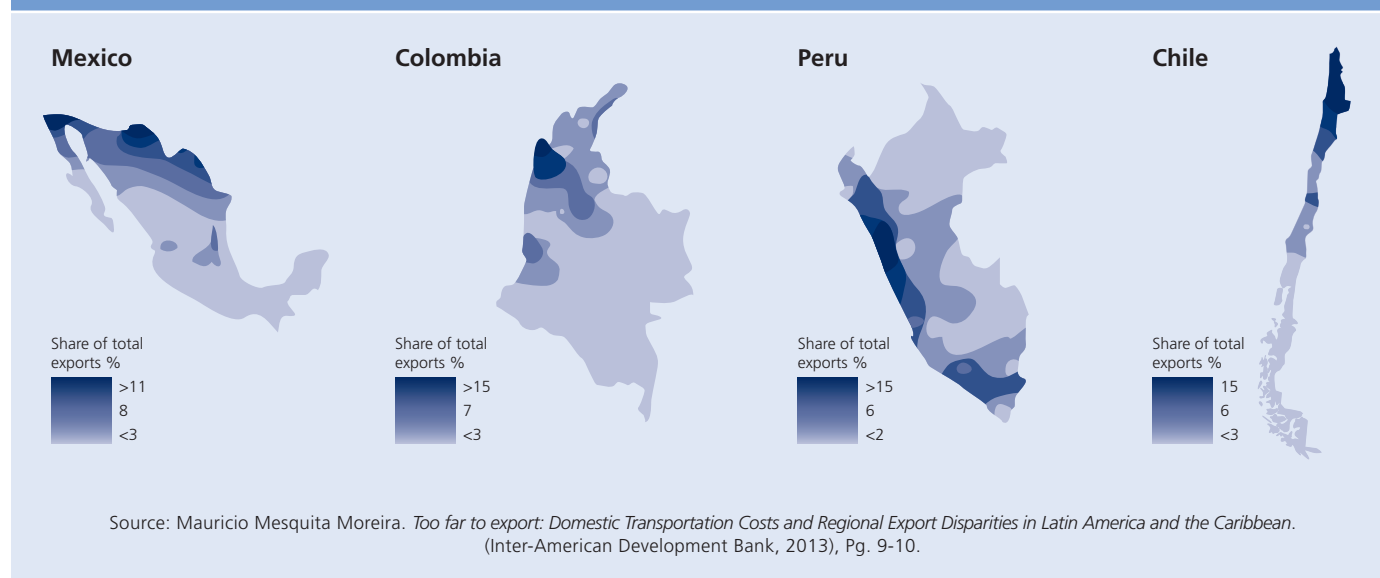
An Inter-American Development Bank study³² coordinated by Mauricio Mesquita Moreira estimates notable export increases for all four countries

with even just a one percent decrease in in-country transportation costs. The study forecasts 7.8 percent expansion of manufacturing exports in Colombia. In Mexico, the study found that the one percent reduction in transportation costs in the south could lead to a five percent increase in total exports. In Peru and Chile, where pockets of the population in remote areas struggle to integrate into trade networks, the study found that agricultural, mining and manufacturing exports would all expand roughly four percent with a one percent decrease in internal transportation costs.

The region's flawed efforts to liberalize in the 1990s remain a bitter memory. "Washington Consensus" is a pejorative term for many in Latin America. But globalization will not disappear, and the Pacific Pumas are preparing to capitalize from it. For the model to take hold, all four Pumas must focus not only on enlarging the proverbial pie, but also ensuring that more people get forks as well.

If Mexico, Colombia, Peru and Chile can do this, their macroeconomic and political stability will be matched by consistent growth in the foreseeable future.

Distribution of Exports: Mexico, Colombia, Peru, and Chile



▲ Currently, Puma export production is concentrated regionally. The Pumas must work to ensure that the entire country can benefit from an export-oriented trade strategy



II. Global Opportunities

- 5. The Pacific Alliance
- 6. Latin America Divided?
- 7. A trans-Atlantic Triangle
- 8. Harnessing the Dragon

5

The Pacific Alliance:

A Gathering of the Pumas

To this point, this paper has focused on the advancements of Mexico, Colombia, Peru and Chile individually. However, these countries' shared democratic improvements, macroeconomic stability and openness to trade make them natural partners, thus leveraging their power in a globalized world. Via the Pacific Alliance, the Pumas have added gravitas to their individual momentum and established their model as an attractive approach for many smaller and mid-sized Latin American countries.

Much like their European relatives, Latin American leaders have a sweet tooth for the summit, the annual meeting and the commission. Lofty goals and promises of solidarity are sealed with vigorous handshakes, bear hugs and kisses on the cheek. But beyond the

ubiquitous photos of smiling presidents, few concrete achievements emerge from these gatherings.

In theory, inchoate integration projects abound, from the regional MERCOSUR to the continental Union of South American Nations (UNASUR). In fact, the dream of a more unified Latin America has progressed little since Simon Bolívar crisscrossed the Andes in the early 19th century.

This could be changing.

The Pacific Alliance, a trade and integration bloc conceived in April 2011 and launched in June 2012, originally consisted of the four Pacific Pumas. The Alliance is a natural collaboration between like-minded countries that have

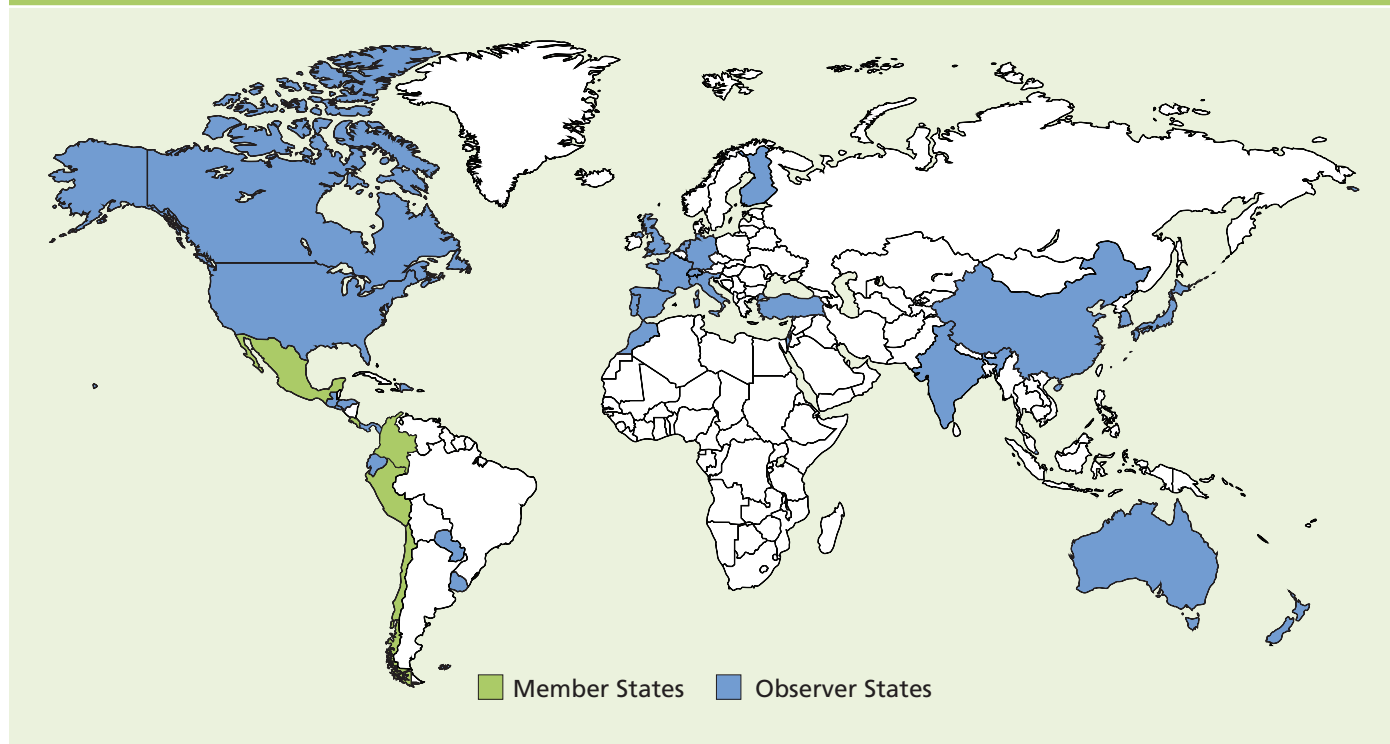
independently developed similar reforms and strategies, with an eye towards the East as both a trading partner and a model for development.

Through the Alliance, the Pacific Pumas do not *seek* reform. Rather, they hope to *amplify existing* reform and to synergize integration efforts in both the regional and global economy. For those in the Western Hemisphere (north and south) anxious to establish an alternative to the Atlantic-Latin American development model, the Pacific Alliance is the most exciting thing happening in the region.¹

THE PACIFIC ALLIANCE

Viewed as a unit, the Pacific Alliance converts a series of small to mid-sized economies into a global force. With 221 million people (counting Costa Rica),²

The Pacific Alliance



the bloc would supplant Brazil as the world's fifth most populous country, while a collective GDP of US\$2.219 trillion—roughly 37 percent of the regional total³—would place ninth globally. The Alliance's combined global trade, US\$1.045 trillion, accounts for 50 percent of Latin America's total.⁴

The Pacific Alliance is a residual of the larger Arc of the Pacific pact launched in 2007 that featured 11 Latin American countries along the continent's west coast.⁵ The Arc, itself, features a number of holdovers from the habitually underperforming Andean Community of Nations (CAN), founded in 1969.⁶

With each successive pact, the inner core whittled away countries that did not share an open-market strategy.⁷ As a result, Alliance members have a shared vision of economic development that eased a path for tangible results where regional, hemispheric and global multilateral trade dialogues have stalled.

As of June 2013, an agreement following the seventh Pacific Alliance Presidential Meetings in Cali removed all tariffs on 91.8 percent of inter-bloc merchandise trade, with the additional 8.2 percent to be liberalized incrementally over the next 15 years.⁸ This agreement made international headlines, but leaders from the participating countries were just as apt to stress the non-trade elements of the Alliance, such as shared embassies around the world, waived visa requirements and unified maritime and aerial services. In February 2014, presidents of the four countries announced that the Alliance will share a fund to finance infrastructure investments.⁹ In fact, the largest initial economic gains from the Pacific Alliance are likely to result from the liberalization of capital, not from trade.

For Mexico, the Alliance represents reintegration into Latin America following two decades of close association with the United States and Canada via NAFTA. For Colombia, slowly emerging from a long period of violence,

the Alliance offers an opportunity to engage as a regional player—something that the country's population, GDP and sound macroeconomic management suggests it could be. Peru, meanwhile, earns a measure of legitimacy from its participation in the Alliance. For a world that associates Peru with poverty, hyperinflation and exotic vacations, the Alliance offers a rebranding opportunity. For Chile, a sophisticated but small country, the Alliance allows for a projection of influence and an opportunity to emerge as a leader in Latin America.

A PUBLICITY STUNT?

To the seasoned Latin Americanist, perhaps numbed by the steady diet of short-circuited regional pacts, the excitement over the Pacific Alliance can seem disproportionate. After all, the members already shared bilateral free-trade agreements with each other prior to the Alliance, and they already had bilateral agreements with the US and the EU. Numerous Puma agreements with East Asia are already tangled into the latter's rich network of trade pacts. Moreover, they are not even major trading partners with each other: As of 2012, neither Mexico, Chile nor Peru counted a Puma country as a top five trading partner.¹⁰

For one, the Pumas do not exactly have compatible export portfolios. Chile will not get far trying to export copper to Peru—itsself a major copper producer. Secondly, poor coastal infrastructure and sheer distance do not portend smooth, cost effective supply chains. Given these issues, some consider the bloc little more than a publicity stunt. Brazilian Foreign Minister Antonio Patriota recently referred to the pact as a “marketing success”.¹¹

The response to these allegations is three-fold. First of all, a marketing success is by no means a bad thing for the Pacific Pumas. Mexico, Colombia, Peru and Chile have all enjoyed the successes outlined in the previous chapters, but independently they are often overlooked,

when they are not overshadowed by grisly headlines from the drug wars. If the Pacific Alliance can capture global attention on Puma improvements and amplify their voice in global trade negotiations—while perhaps attracting some international investment along the way—then the marketing success is just that: a success.

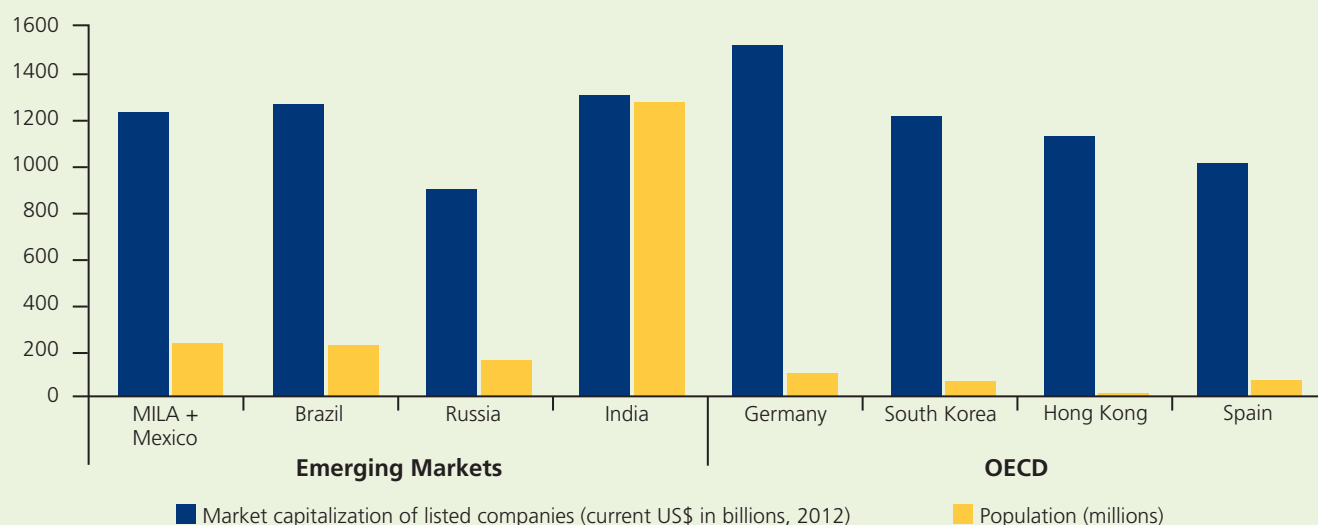
Second, all four countries have emphasized improved infrastructure and export diversification. Perhaps the Pacific Alliance can be the catalyst to instigate needed upgrades. For example, Colombia could assume the lower-level manufacturing elements of a supply chain before shipping unfinished products north to Mexico where more experienced manufacturers can complete the good.

Third, the true impact of the Pacific Alliance may not manifest itself in the real sector. Rather, financial sector integration could have the greatest impact. The Mercado Integrado Latinoamericano (MILA), a multilateral effort to integrate the Colombian, Peruvian and Chilean stock markets, evidences the Pumas' ability to negotiate barrier-breaking financial agreements. Founded in 2010, MILA indicates the potential of Puma cooperation to deliver ambitious and hard-fought results. Moreover, it buttresses the overarching Pacific Alliance strategy of pursuing regional cooperation in order to better integrate into global trade and capital flows.

WHY MILA MATTERS

The Pacific Pumas may be growing, but prior to MILA, their bourses remained largely overlooked. Outside of São Paulo and Mexico City, Latin American equity markets lack depth and breadth, with few companies listing publicly and transactions infrequent. The World Economic Forum's 2012 Financial Development Index of 62 major markets found Colombia, Peru and Chile to be in the bottom quintile in terms of stock market turnover rate. Meanwhile, Mexico, Peru and Colombia ranked in the bottom quarter of stock market value to GDP.¹²

MILA: A Bourse of Global Proportions



Source: World Bank Data

MILA Early-Harvest Agreements

MILA attests to the efficacy of the Pacific Pumas' "early-harvest" negotiations. Rather than quixotically pursuing an immediate integration of the three bourses, the parties sought a step-by-step model that allowed negotiators to methodically overcome knee-jerk opposition. By moving slowly and building linkages, proponents convinced regulators and brokerages of the three markets that, while they would lose complete autonomy, the end results would be a larger piece of a larger pie.

Phase I of MILA (completed in August 2011) built a foundation for the project. This phase implemented a communications system between Chilean, Peruvian, and Colombian brokerages that encouraged cross-border access to the three bourses. MILA created the technical infrastructure for, say, a Peruvian broker to partner with a Chilean broker who could intermediate the Peruvian's transactions on the Santiago stock exchange.²⁰

The first phase of MILA also ensured soliciting rights across the three stock markets, allowing a given country to advertise domestic listings in participating foreign countries. Securing Phase I reforms was not easy—Peruvian reluctance to accept a flat capital gains tax of 5 percent delayed implementation for months²¹—but by keeping expectations reasonable, Colombia, Peru and Chile established momentum for the project.

Phase II negotiations, currently under way, will attempt to eliminate inefficiencies baked into Phase I reforms. For example, Peruvian brokerages currently pay the intermediary Chilean firms for their services. The resultant markup eats into already thin margins. Direct access to the Chilean bourse would be preferable. Furthermore, settlement costs remain expensive. Sticking with the Peruvian/Chilean example, brokers execute the exchange by selling Peruvian *soles* to New York financial institutions for Chilean pesos that are then moved to Santiago. The transfer fees can equal up to 20 percent of the transaction.²²

Successful MILA II negotiations should lead to substantial increases in trade volume while costs would decrease. Suddenly, the pie would be far bigger still. From this point, it is but a short jump to MILA III: full integration, in which brokers can follow screens in Lima and immediately place an order for a listing in Santiago.

Not only small and illiquid, these markets can appear one-dimensional: Chile in retail and services (32 percent of capitalization),¹³ Colombia in financials and energy (78 percent of capitalization)¹⁴ and Peru in mining (53 percent of capitalization¹⁵).¹⁶ Such specialization may attract boutique investment, but it flies under the radar of the global herd seeking the “next Brazil”.

MILA could change this. Even without Mexico, MILA’s US\$700 billion capitalization places the bourse second only to Brazil in terms of market size in South America. With 544 firms, MILA offers the largest portfolio in Latin America.¹⁷ The potential integration of the Mexican bourse in 2014 would render a market of global relevance.

The Mexican Stock Exchange (*Bolsa Mexicana de Valores* or BMV) has openly revealed its desire to join MILA, signing a letter of intent to join only months after MILA’s introduction in 2011. For Mexican brokers, MILA would provide preferential access to the Andean listings, even if the BMV already has the liquidity and size the other Pumas lack. In September of 2012, BMV concluded a technical feasibility study, and proposed an entry date of mid-2014. If the BMV does join, a Pacific Puma bourse would rival the size of Brazil’s major stock exchange, BOVESPA, with the key caveat that, while Brazil appears increasingly inclined towards protectionism, the Pumas have expressed a commitment to deconstruct barriers to capital flows.

With this scale come cheaper transactions, as well as diversified risk—two factors that encourage an active market. Increased access should improve resource allocation, hopefully funneling investment to worthy firms. Moreover, whereas Puma markets may have been individually one-dimensional, combined, they offer a complementary mix.¹⁸ Finally, MILA’s backers hope international investors will be tantalized by this new, large bourse which will stand out in a way that, say, Lima’s bourse, alone, could not.¹⁹

PUMA CUBS: PART OF A GROWING FAMILY

The Pacific Pumas and the Pacific Alliance are different entities, as the positive momentum and opportunity enjoyed by Mexico, Colombia, Peru and Chile extends beyond the potential of the inchoate bloc. Moreover, the Pacific Alliance has expanded beyond the original Pumas. Costa Rica is completing the procedural steps required to join as a member; Guatemala and Panama could be next. Twenty-nine other countries, from China to the US, from Uruguay to France, have signed on as observers.

The expanding success of the Pacific Alliance indicates the regional power accrued by the four Pumas. The bloc appears to be a magnet for Latin American countries looking for an alternative to the Brazilian or ALBA development models; nine have joined as members or observers.

Of course, Alliance expansion raises a host of concerns. Initial success can largely be ascribed to the small number of like-minded participants. Fault lines could emerge if and when other countries join the fray. Can the Pumas safely integrate with Panama—a haven for tax evasion? Can Guatemala and Honduras, embattled in the war on drugs, agree to waive visa requirements with Mexico and Colombia? One fears that expansion could lead to the stagnation that seems to have doomed the WTO’s Doha Round.

But one thing is clear: The Pacific Alliance has established the Pumas as an important regional voice. The Alliance has reintroduced Mexico into the mix of Latin America’s large leaders. It provides brawn to Chilean brains, and it consolidates the voices of Colombia and Peru, even as these countries continue to consolidate internally. Marketing success? To a degree. Silly name? To be sure. But the Pacific Alliance has the potential to push Latin America towards Asian Tiger-styled economies, and Asian Tiger growth.

The Pacific Pumas are emerging as leaders and trend setters in Latin America. United through the Pacific Alliance, they are large enough, and have enough gravitational pull, to attract smaller regional countries into the fold. Mexico, Colombia, Peru and Chile have established their model as an alternative to the more statist ALBA bloc or the more protectionist MERCOSUR economic pact.

The Pumas have stressed that their effort is meant to facilitate regional integration—not to reinforce continental divisions. But an emerging consensus holds that the Pacific Alliance is a conscious effort to escape from beneath the looming shadow of Brazil, to promote regional integration that is more trade friendly than MERCOSUR, and to counter any residual ALBA influence.

The Economist has heralded a “continental divide”, writing, “The region is falling behind two alternative blocs: the market-led Pacific Alliance and the more statist MERCOSUR.”¹ The venerable Latin Americanist Andres Oppenheimer similarly concluded that “the economic divide between Latin America’s Pacific and Atlantic blocs [has become] increasingly visible.”² Grumblings from the 2013 MERCOSUR Social Summit in Montevideo suggested that elements of the Atlantic bloc themselves had succumbed to this interpretation.

To an extent, they are accurate. Puma policymakers believe that Brazil’s large population offers an internal growth motor that is underdeveloped in Mexico and Colombia, and difficult to fathom in Peru or Chile.³ Thus, Brazil can afford (or at least believes it can afford) protectionist trade policy. Given Brazil’s weighty influence in MERCOSUR, not

to mention the influence of Argentina and Venezuela, the Pumas do not wish to align with an increasingly defensive bloc.⁴

But here is the catch: The Pacific Pumas would greatly benefit from a unified Latin America, and in many cases, basic economic theory suggests they would be perfect partners. In fact, the Pacific Pumas have tried to deepen trade relations between the two “sides”. However, they have directly experienced the unexpected and often unnecessary shocks associated with conducting business with Latin American countries that do not share their free market, low tariff, non-interventionist strategy. The following three examples demonstrate these risks.

• Chilean Energy Insecurity

Chile, a net importer of coal, oil and gas has long faced energy insecurity. In the US, a negative energy shock may lead to higher prices at the pump. But in Chile, when Argentine gas supplies dried up in September 2011, more than 50 percent of the nation experienced power outages that “paralyzed the country’s copper mines and brought Santiago grinding to a halt”.⁵

Chile cannot satisfy spiking natural gas demand with domestic supply.⁶ At best, Magallanes, a gas producing region in Chile’s deep south, can support 40 percent of Chile’s demand for liquid petroleum gas, mostly limited to the south of the country. Former President Sebastián Piñera’s support for building five hydroelectric plants in pristine Patagonia generated more hot air than gas: Public backlash held Piñera’s approval rating in the 30s and the project itself is now four years behind schedule.

Thus when a natural gas bonanza unfolded in neighboring Bolivia and Argentina,⁷ Chile appeared perfectly positioned to benefit: Bolivia could supply Chile’s copper-mining north, while Argentine pipelines would feed the populous Chilean heartland.

Unfortunately, it never worked out that way. Santiago has been dogged by the vicissitudes of Argentine energy policy, where populism has meant whimsical rules of the game, meddlesome macroeconomic policies and disputed contracts.⁸ These issues have undermined Chilean trust in the availability of its neighbor’s gas exports.⁹

Meanwhile Chile has been unable to reach a gas export deal with Bolivia, where resource protectionism and hostility towards Santiago have defined President Evo Morales’ rise, and he has proven reluctant to tinker with this strategy.¹⁰ Morales has stubbornly demanded coastal territory in exchange for a pipeline to Chile, and La Paz has exhausted diplomatic capital petitioning territorial redress in international courts.¹¹

Unable to rely on its neighbors, Chile has been forced to find expensive, intercontinental sources of energy. Santiago invested in expensive liquefied natural gas infrastructure and it imports supercooled gas from Trinidad and Tobago and Equatorial Guinea—a strategy expected to expand during a second Bachelet presidency.¹²

• Colombia & Venezuela: The Politics of Trade

For Colombia, anxious to enlarge a manufacturing export portfolio, proximity to Venezuela offers opportunity. With Venezuelan production geared

World Bank's 2014 Ease of Doing Business Rankings: Latin America (World)



▲ Pacific Latin America has emerged as more business friendly

overwhelmingly towards oil, the country must import just about everything else. Moreover, certain Colombian and Venezuelan comparative advantages appear complementary, a fact not lost on a Colombia that seeks deeper integration into regional supply chains. Hydrocarbon derivatives readily abundant in Venezuela such as polyethylene and ethylene, can be converted into plastic goods such as polystyrenes, tubes, hoses and resins in Colombia.¹³

Between 2000 and 2008, Colombian exports to Venezuela nearly quadrupled in terms of value. The bulk of these exports were of manufactured goods: In both 2007 and 2008, eight of the top ten Colombian exports to Venezuela were non-commodities, such as vehicles

and vehicle parts, textiles and clothing accessories, plastics, machinery and electrical equipment.¹⁴ For the optimist, this relationship offered proof of Colombia's potential beyond commodity exports, and Bogotá hoped to use it as a foundation to hone manufacturing efficiencies for global markets.¹⁵

Unfortunately, the inherent risk in partnering with a boisterously populist neighbor proved far greater than the sheer economics would suggest. Colombian-Venezuelan ties began to strain in the mid-2000s when Bogotá's trade negotiations with the US precipitated Venezuela's exit from the Andean Community of Nations (CAN). The diplomatic relationship rapidly deteriorated, lost amid macho posturing

between Colombian President Álvaro Uribe and Venezuelan President Hugo Chávez, and it was severed in July of 2009 when the extent of US military presence in Colombia became public. On a whim, Chávez moved to replace Colombian trade with imports from Argentina and Brazil.

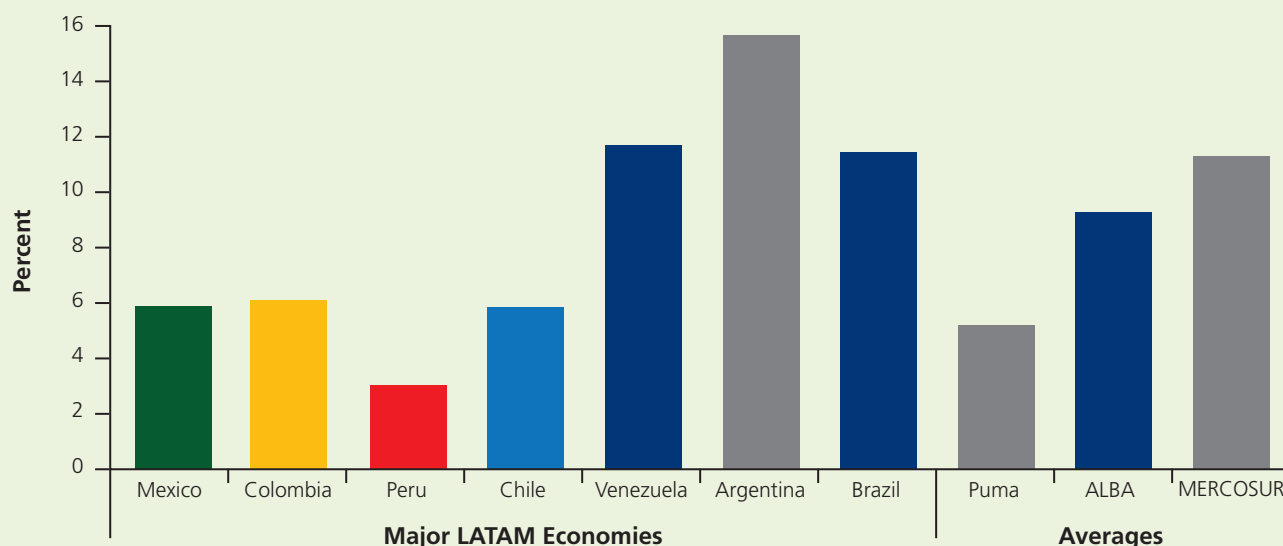
For a man oft-criticized for an inability to match rhetoric with results, Chávez made good on this threat. Between 2008 and 2010, bilateral trade fell from US\$7.29 billion to US\$1.68 billion,¹⁶ and Colombian exports to Venezuela plummeted from 18 percent to 3.6 percent of total exports.¹⁷ The losses hurt precisely the sectors Colombia hoped would thrive: Manufacturing exports tumbled, and Colombia's *total* exports of textiles dropped by more than half. According to one statistical analysis, the trade breakdown cost Colombia a full percent of real GDP growth in 2009.¹⁸

The clear message for Colombian technocrats and businessmen was that, when doing business with Atlantic-Latin America, all the work required to put an economy on a successful track can be derailed when a stubborn *paisa* bumps into a bombastic *llanero*. Colombia would be happy to rekindle trade with Venezuela, and by some accounts, their commerce has rebounded in the Santos – Maduro era.¹⁹ Nevertheless, Bogotá views the relationship with less enthusiasm, and the experience has influenced Colombia's desire to pursue intercontinental ties.²⁰

• Mexican Car Exports and MERCOSUR

Even Mexico, which in 2011 sent more than 83 percent of its exports north to the US and Canada,²¹ has been unable to avoid the pitfalls of South American protectionism. The *Complementación Económica No. 55* (ACE No. 55), signed between Mexico and MERCOSUR in 2002, supposedly ensured free trade in automobiles among the participants. For Mexico, the deal offered an opportunity to leverage existing economies of scale: Since the advent of NAFTA in 1994, Mexico had attracted international automobile

Average Applied Tariffs in 2012



Source: Inter-American Development Bank, German Institute of Global and Area Studies (Unweighted Averages)

firms,²² lured by an opportunity to export cheaply north across the Rio Grande.

ACE No. 55 opened South American markets to Mexican exports just as Brazil's expanding middle class portended a boom in automobile demand. Mexico initially specialized in exporting larger vehicles to Brazil, while Brazil exported smaller ones to Mexico.²³ However, as footloose capital and strong commodity prices led to appreciation of the Brazilian real, Mexican exporters established the upper hand: Their cars sold for a fraction of the price of similar, or in some cases, the same, models made in Brazil.²⁴ Just between 2009 and 2011, Mexican unit exports to Brazil increased by 152 percent, generating US\$2.1 billion revenue and a US\$696 million bilateral trade surplus.²⁵

For Mexico, these auto exports represented reintegration into South American trade. Mexico's bleak experience in 2008 and 2009, sucked into the Great Recession by the United States, laid bare the vulnerability of relying too heavily on one major trade partner.²⁶

Success with Brazil affirmed beliefs that Mexico could be a hub for manufactured goods sold south, just as it is a hub for goods exported north. For Mexico, the relationship represented the future the Pumas are building towards.

Until it didn't. In September 2011, Brazil responded to its increasingly uncompetitive auto industry by slapping a 30 percent import charge on motor vehicles and parts. ACE No. 55 should have protected Mexican vehicles from facing this tariff, but by February 2012, President Dilma Rousseff's administration moved to "restructure" the trade agreement. In order to save any semblance of the deal, Mexico accepted a quota system that would limit auto exports to Brazil to US\$1.45 billion in the first year, and US\$1.56 and US\$1.64 billion in the next two years. Furthermore, rules of regional content were slated to jump from 30 to 40 percent within five years.²⁷

Both measures stung. The quota resulted in a 26 percent revenue reduction, and Mexican light vehicle exports to Brazil

dropped 72 percent in February 2013. With Argentina imposing comparable restrictions, Mexican auto exports to Latin America declined 50 percent in early 2013.²⁸ The domestic content rule challenged what Mexico viewed as seamless integration into the international automobile parts supply chain—precisely the style of integration the Pumas have actively sought.

A PUMA MUST ROAM

The insinuation that Pacific and Atlantic Latin America have split into two hostile camps is not exactly accurate. Rather, the Pacific Pumas have directly experienced the unexpected and often unnecessary shocks associated with conducting business with Latin American countries that do not share their free market strategy. They have apparently learned their lesson, and they will avoid lurking puma traps.

It is much less painful to hang out with the Asian Tigers.

A Trans-Atlantic Triangle:

The US, Europe and the Pacific Pumas

The United States and Europe have forged a remarkably successful alliance over the last seventy years. The trans-Atlantic partners have helped power global growth and innovation while developing increasingly inclusive democracies. Together, the US and EU still account for over 48 percent of global GDP. They continue to buttress the international system, acting as major funders and stakeholders of the United Nations, the World Bank and the International Monetary Fund.¹

Alone, however, the US and EU will struggle to match the success of the last seven decades in the next seven decades. Following the Great Recession of 2008 and the Euro crisis of 2010, trans-Atlantic growth has sputtered, and emerging markets have assumed an increasingly important role in keeping the global economy afloat. A US and EU economic rebound is perhaps contingent upon linking into emerging-market growth. Thankfully, between the trans-Atlantic's advanced technology and sophisticated service sectors, they have the comparative advantages to do so.

Yet if global economic balances are shifting, the identity of new players remains unclear. The BRICs, for example, offer four distinct development paths, none of which are particularly conducive to trans-Atlantic political and economic preferences. In this light, Mexico, Colombia, Peru and Chile are valuable strategic partners.

The Pacific Pumas represent an emerging-market bloc committed to economic and democratic policies in-line with those of the US and the EU. If the Pacific Alliance can continue to expand in Latin America, then much of the Western Hemisphere will be aligned with the trans-Atlantic

model. For the US, the Pumas represent a potential partner in the Americas: the five countries account for more than half of the hemisphere's population, and upwards of 75 percent of its GDP.² For the EU, the Pumas represent access to high growth, investor-friendly (and Europe-friendly) markets, with a window to East Asia to boot.

Together, the US, EU and Pacific Pumas can set the foundation for an enlarged trans-Atlantic bloc prepared to negotiate the opportunities and challenges of a Pacific century.

THE FUTURE OF AMERICAN LEADERSHIP

On November 19, 2013, US Secretary of State John Kerry addressed a private audience at the Organization of American States' Hall of Flags and Heroes, where he underscored the end of the Monroe Doctrine and a future of Pan-American collaboration as equals. Though his words were warmly received, Secretary Kerry did not specify just who he expected to emerge as the US's key partner in the region.

The US has vacillated between cautious optimism, ambivalence and weariness regarding the rise of Brazil.³ Other large Latin American countries such as Venezuela or Argentina seem unlikely to actively cooperate with the US in the near term. Puma cubs such as Uruguay or Costa Rica are simply too small to act as equal partners with the US, fraternal rhetoric notwithstanding.

It is the Pacific Pumas, both independently and collectively as the Pacific Alliance, that stand to develop as the US's strategic partners in the region. Whether by design or happenstance, the Pumas are pursuing precisely the open market, private sector-

led, democratically governed development model Washington is anxious to entrench as the global standard. That the Pumas are adopting this model without heavy-handed prodding from the US is all the better, at least from Washington's perspective.

For US policymakers, the question becomes how to facilitate this momentum without poisoning the well. Former Brazilian President Lula da Silva has already criticized the Pacific Alliance as a rehashing of the Washington Consensus—still a politically toxic term in the region.⁴ If ALBA or MERCOSUR countries—not to mention opposition figures *within* the Pumas—can paint the Alliance's free-trade, pro-business policies as lackeyed deference to the US, any momentum could be derailed.

Cognizant of this, Washington has sought to subtly support the Pumas while maintaining a light footprint. In July 2013, the US joined the Pacific Alliance as an observer. Though the US may eventually become a member, for now the Obama Administration appears content with letting the Alliance mature under its own auspices. Outside of the spotlight, the US has assisted Puma integration, with the Treasury Department chipping in technical support on the combined stock market of MILA.

The US remains a fundamentally important trade partner for the Pumas. Since 2002 Mexico has sent an annual average of 82 percent of its exports to the US, while more than 50 percent of Mexican imports routinely arrive from its northern neighbor. Colombia shipped an annual average of 38.56 percent of its exports to the US between 2010 and 2012; no other country has received an average of more than five percent of Colombian exports.⁵ China surpassed the

US to become Chile's top trading partner in 2008, and Peru's top trading partner in 2011, but the US remains a close second for both countries.

Generally speaking, the US exports machinery, fuel, vehicles and agricultural goods in exchange for Puma commodities, both agricultural and mineral. Mexico stands as a key exception to this trend: Four of its five largest export categories to the US in 2012 were manufactured goods (electrical machinery, vehicles, machinery, and optic and medical instruments).⁶ This US demand is a major reason manufactured goods accounted for more than 70 percent of Mexican exports in 2012.

The Pacific Pumas and the US have used bilateral and multilateral agreements to facilitate their trade, a process that began with NAFTA in 1994 (discussed in Chapter 4 of this report). Eric Farnsworth, Vice-President of the Council of the Americas, argues that by linking these preexisting agreements with the Pacific Alliance agreements, the participants can reinvigorate the stalled Free Trade Area of the Americas,⁷ only this time limiting participation to what Peterson Institute economist Barbara Kotschwar calls "the coalition of the willing".⁸

Washington has also invited Puma representatives to help set standards for the future rounds of global trade dialogues. Three of the Pumas are active participants in the US-led TPP negotiations. Washington may maintain a low-profile in the Pacific Alliance—for example the US did not send a delegation to the group's 7th Summit in February of 2014—but this should not be interpreted as disinterest. The US is encouraged by the Alliance's progress, and does not want to emerge as a distraction. Rather, as a friendly bloc in the Western Hemisphere, the United States hopes to feature the Pacific Alliance as part of its vaunted pivot to the Pacific.

EUROPE AND THE PUMAS: OLD FRIENDS WITH NEW BENEFITS

The Pacific Pumas have also captured Europe's attention: Deutsche Bank described the four countries as "Latin America's new stars",⁹ while European Council President Herman van Rompuy referred to the Pacific Alliance as "a very promising initiative...that will allow us to team up at the multilateral level to promote our common vision on trade and economic cooperation".¹⁰ The German Business Association of Latin America dedicated its entire Latin America Day conference to the Alliance in 2013.

France, Germany, Italy, Portugal, Spain, Switzerland and the United Kingdom have all joined the Pacific Alliance as observers, and the Pumas already have bilateral FTAs with the EU (all while an EU-MERCOSUR trade agreement appears increasingly unlikely).

The allure of the Pumas is clear: For the eurozone to overcome its malaise, it must exploit the existing economic infrastructure connecting the old world to emerging markets. The EU is particularly suited to link into Latin American growth. Despite a turbulent history, the longstanding ties and cultural similarities between the two are currently assets to the relationship. European foreign direct investment, for example, can appear less jarring than Chinese or even US direct investment.

A closer look at trade and investment patterns reveals that new opportunities are on the horizon for Puma – EU relations.

• EU-Puma Trade:

While EU bilateral trade with Mexico, Colombia, Peru and Chile may be underwhelming, together, the Pumas are the EU's eighth largest trading partner. EU - Puma commerce outpaces trade between the EU and Brazil, as well as the EU and India.¹¹ Meanwhile, the EU is the Pumas' third largest trading partner (behind only the US and China), the second largest importer of Puma goods,

and the third largest exporter to the four Latin American countries.¹²

Puma trade with the EU typically follows a pattern of commodities-for-manufactured goods. In 2012, over three quarters of EU exports to the Pumas were of manufactured goods and machinery, while over three quarters of Peruvian and Colombian exports to the EU consisted of crude materials, minerals and animals.¹³ Chile and Mexico have had more success exporting manufactured goods to Europe, though copper typically accounts for 55 percent of Chilean exports to the region.¹⁴

Much like Puma trade with East Asia, the relationship with the EU is both advantageous, because the two regions have generally compatible spheres of comparative advantage, and threatening, as it further entrenches the Pumas in commodity production. Unlike with East Asia, however, European manufacturing exports tend to be higher-end, and thus often do not directly compete with Puma products.

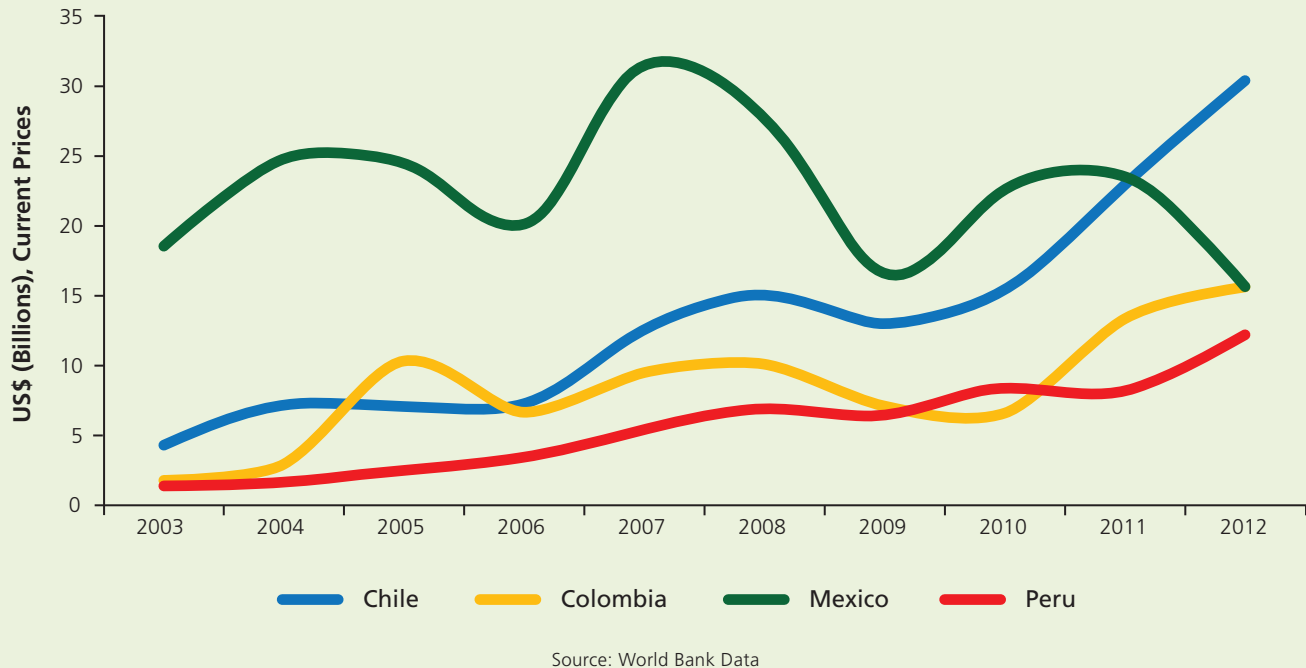
• EU- Puma Investment

The European Union is already the largest foreign direct investor in Latin America. While the bulk of this financing flows to the mining and hydrocarbon sectors, EU firms account for a large share of regional manufacturing and development investing as well.

Between German electronics, French chemicals, Spanish finance and Italian telecommunications, EU firms pursue a varied portfolio of ventures in Latin America that fit Pumas' goals of diversification.¹⁵

EU firms have also demonstrated a willingness to invest in "greenfield" manufacturing projects, as opposed to simply purchasing existing operations. Between 2003 and 2007, roughly 45 percent of new manufacturing FDI in Latin America came from the EU, up from 34 percent between 2003 through 2006. By comparison, Asia's share held at roughly 20 percent from 2003 to 2011.¹⁶

Foreign Direct Investment, Net Inflow



▲ The Pumas have become increasingly attractive recipients of Foreign Direct Investment. European investors may join this trend.

Moving forward, the Pacific Pumas will become increasingly attractive investment destinations for European firms. Mexico, Colombia, Peru and Chile can generate a rate of return difficult to realize in Europe, and they offer protection of investment not easily attained in many other emerging markets: EU members have already been stung by populist appropriations in non-Puma Latin America, most recently in Argentina and Bolivia.¹⁷

Finally, EU investors have demonstrated a clear preference for integrated Latin American countries (MERCOSUR and NAFTA countries received about 90 percent of regional EU FDI between 2006 and 2010¹⁸), as foreign firms seek to establish export-efficient bases within the region. The Lateinamerika Verein, a network of German businesses active in Latin America, has already observed increased German appetite for investment in Puma countries given the subsequent ease of exporting within the Alliance.¹⁹

A TRANS-ATLANTIC TRIANGLE

An enlarged trans-Atlantic relationship should benefit all sides. For the US, the Pumas could become reliable allies in hemispheric leadership. For the EU, the Pumas represent an economically growing, politically stable region with close ties to Europe. For the Pumas, ties to the EU and US offer access to influence and capital.

The EU and US can indicate their interest in incorporating the Pacific Pumas by addressing Puma apprehension over TTIP. The Pumas are not privy to TTIP negotiations, but the pact could affect the four Latin American countries, especially Mexico.

A Bertelsmann Stiftung and IFO Institute study forecasts that a comprehensive TTIP agreement could result in a decline of Latin American exports to both trans-Atlantic partners. Mexico, a country which relies on trade with the US, could see their exports to the US shrink by 16.04 percent. All told, the study concludes that TTIP could cost Mexico, Colombia, Peru and Chile 7.2, 2.6, 2.2 and

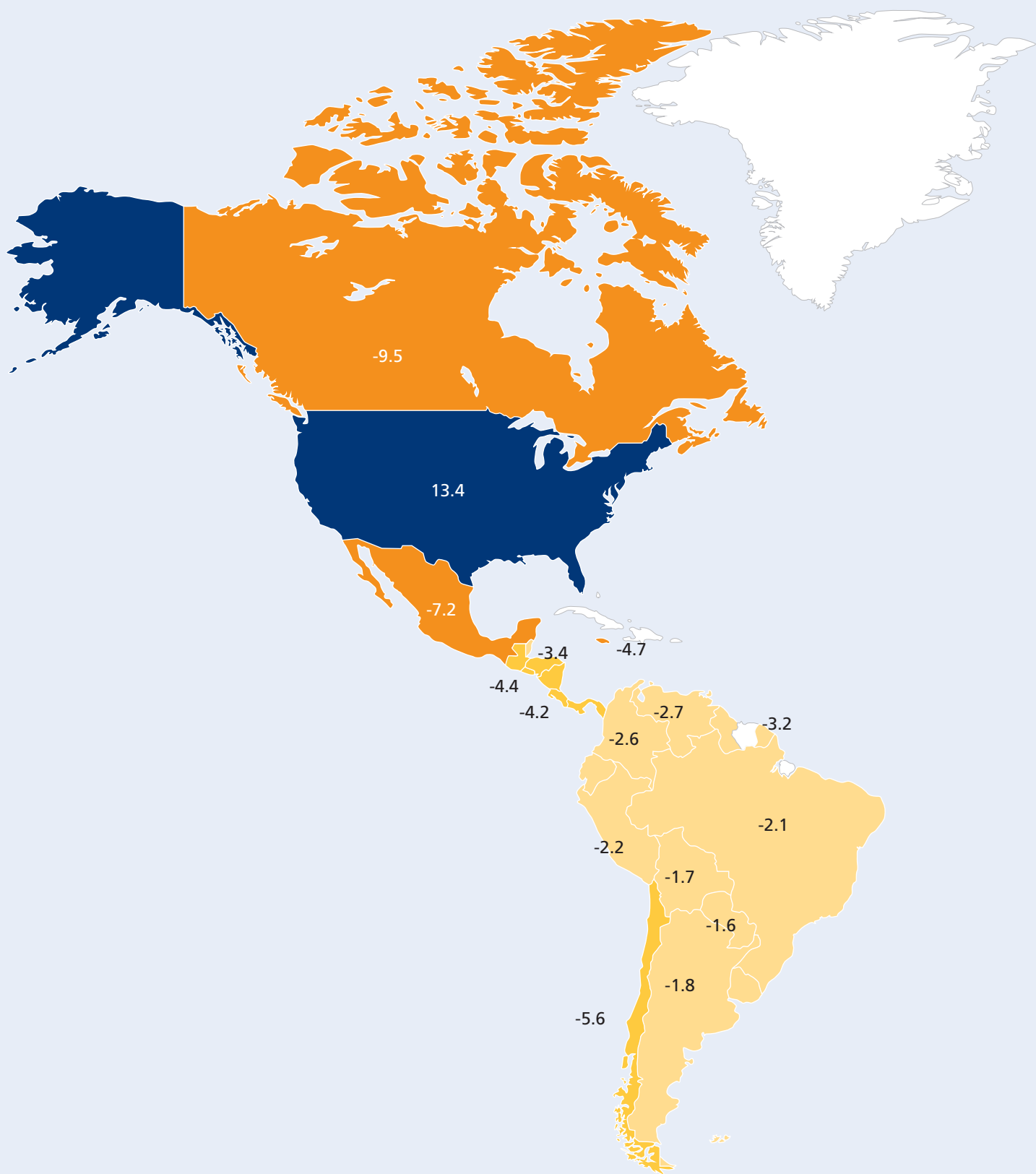
5.6 percent of per capita gross national income respectively.²⁰

The EU and US are reluctant to expand TTIP negotiations. Closing an FTA between 29 different countries is already rather complicated, and any expansion in the Western Hemisphere could imply expansion on the European side. Turkey, for example, shares Mexico's concern over not being at the table.

Nevertheless, the traditional trans-Atlantic partners can take steps to avoid alienating the Pacific Pumas. Given that tariffs are already low between the EU and US, the importance of TTIP lies in harmonizing regulations. The EU and US can seek bilateral modifications in their pacts with Mexico, Colombia, Peru and Chile to ensure that their agreements are up to date and in-line with TTIP standards. Meanwhile, if the Pumas can successfully align the standards of the Pacific Alliance with TTIP, this could help prepare Mexico, Colombia, Peru and Chile to act as partners and participants in 21st century trans-Atlantic leadership.



Long-term Forecast Change in Real Income per Capita Under Deep-Seated TTIP Agreement (Percent)



For the Pacific Pumas, China represents both an opportunity and a threat. Chinese commodity demand sparks growth and fills central bank coffers in South America, but it also threatens to stymie export diversification. Any Chinese slowdown could burst commodity prices, thus exposing a Puma vulnerability. Investment from the East offers opportunity at a time when OECD capital can seem scarce. But what strings come attached with Chinese FDI, and which sectors will be favored?

Meanwhile, Chinese manufactured goods offer consumption opportunities for the Pumas' newfound middle classes, but local producers may struggle to compete on their own home turf. That said, if the Pumas could leverage their own manufacturing, China represents a massive market embedded in the Pacific's intertwined trade routes. In short, the Pumas' ability to take advantage of their current opportunity may hinge upon their success in harnessing the power of the Dragon.

CHINA IN LATIN AMERICA

China has two prominent goals in Latin America: resource security and market expansion. The Pacific Pumas pique China's interest on both accounts. From oil to zinc to copper, the Pumas are richly endowed in the commodities China needs to build 21st century super-cities. This Chinese demand has bid up the price of commodities that pushed Puma growth, birthing a new middle class which could, in turn, afford to purchase manufactured goods from China.

Since the turn of the century, the relationship has unfolded in two major phases. The first, from 2000 to 2007, featured explosive trade growth. The second phase, beginning roughly in 2007,

centers on increased Chinese foreign direct investment (FDI) throughout the region. The dynamics of each phase are considered in turn:

• Trade

China's ascension to the WTO in 2001 sparked a trade renaissance. While much of the world feared an onslaught of cheap manufactured goods, for South America the emergence of the Dragon has had spectacular short-term benefits. China faces a resource dearth: outside of people and coal, it must import nearly all its resource inputs, inputs that exist in abundance in Latin America. Overall, in the first decade of 2000s, trade between the People's Republic of China and Latin America ballooned from US\$10 billion to US\$180.2 billion.¹ Chinese GDP growth averaged 11.42 percent from 2005 to 2009, and during those years, Chinese imports from Latin America increased by an annual average of 22.8 percent.²

This trade is at once both balanced and skewed. In South America, Chinese imports have closely tracked exports, with years of meager South American surpluses following a few years of minor Chinese surpluses (Mexico and Central America, on the other hand, trade at a notable deficit with China). Nevertheless, the trade portfolios are profoundly lopsided. In 2009, manufactured goods accounted for 99.2 percent of Latin American imports from China.³ That same year, agricultural and mining goods comprised 83 percent of Latin American exports to China.⁴

• Foreign Direct Investment

Foreign Direct Investment represents a second thrust of Chinese economic activity in Latin America. Chinese FDI has moved from around 2.3 percent of GDP in 2000 to around 5.5 percent of

GDP today—representing tens of billions of dollars in increases.⁵ Between 2000 and 2011, China directed just over 11 percent of these funds towards Latin America, making the region the second largest recipient of Chinese FDI behind Hong Kong.⁶

As with trade, Chinese FDI represents both an opportunity and a challenge for the Pacific Pumas. All four Pumas suffer an infrastructure deficit—Colombia and Peru acutely so. China has demonstrated a willingness to invest in infrastructure upgrades. However, 90 percent of Chinese FDI in Latin America is geared towards exploiting and exporting raw materials,⁷ threatening to further plant the Pumas in the resource-reliance rut that they are fighting their way out of.

THE PUMA AND THE DRAGON

While the Pacific Alliance bloc may help the Pumas interface with the East, the opportunities and challenges are distinct for Mexico, Colombia, Peru and Chile. As a result, each Puma's relationship with China is best reviewed individually.

CHILE AND CHINA: A MODEL FOR THE PUMAS?

Chile is the world's largest producer of copper. China is the world's leading copper importer and consumer. It stands to reason that sparks would fly between them.

In 2001, the year China joined the WTO, Chilean exports to the Dragon stood at US\$1.30 billion; a mere 32 percent of Chilean exports to the US. By 2006, Chilean exports to China had more than quadrupled. Five years later, in 2011, China had emerged as Chile's number one trading partner, importing US\$20.58 billion worth of goods—more than 16 times the 2001 figure.

Increased Chilean Trade with China, Increased Chilean Growth



Source: International Monetary Fund, Bertelsmann Stiftung

Commodities compose the bulk of these exports: In 2010, 67 percent of Chilean exports to China were of copper related materials alone. Chile's dual challenges in terms of harnessing the Dragon are, on the one hand, diversifying its export portfolio while, on the other, ensuring against the price vulnerability inherent in having one major consumer for one particular product.

Chile, the most developed Puma, appears to command a high level of respect from China. For example, in February 2013, the state-controlled China Minmetals Corporation acquiesced to Chilean requests to restructure a 15-year copper deal.⁸ That contract, based on 2006 copper spot prices of US\$1.50 a pound, clearly favored China as then-current prices hovered between US\$3 and US\$4 per pound. In contrast to the hard line Chinese firms have at times taken elsewhere, Minmetals agreed to restructure the contract to bring it closer in line with market values.⁹

Meanwhile, Chile has used trade negotiations with China to attract

attention beyond traditional exports. The 2005 FTA dialogues highlighted non-trade issues, such as labor cooperation, security and environmental standards. A subsequent 2008 service-sector supplement to the FTA represented the first of its kind between China and Latin America, with Chilean engineers, architects and lawyers participating in drafting the pact.¹⁰

Both in terms of commodity deals and portfolio expansion, China appears willing to work with Chile as a partner. In this sense, the relationship can be a model for the other Pumas.

PERU AND CHINA: HARNESSING FOREIGN DIRECT INVESTMENT

Peru, Latin America's leading producer of gold, lead, silver tellurium, tin, and zinc,¹¹ has emerged as a prominent destination for Chinese mining FDI, receiving US\$5 billion in investments between 2003 and 2011. The Andean country is now the second biggest Latin American recipient of Chinese mining FDI, and the fourth biggest globally.¹²

The relationship has been tumultuous, marked by high profit margins and production as well as frequent labor stoppages and allegations of safety and environmental negligence. It is also expected to expand. Peruvian Finance Minister Miguel Castilla forecasts that Chinese investment could grow exponentially in the next few years, hitting upwards of US\$20 billion by 2018.¹³

Lima can neither afford to discourage this investment nor to let Chinese mining firms run roughshod over domestic regulations. Harnessing Chinese investment will thus be crucial to Peruvian emergence.

The Hierro Peru iron mine, purchased by the state-owned Shougang Group in 1992, stands as China's seminal investment in the country.¹⁴ Having now celebrated its 21st anniversary, *Shougang Hierro Peru* has proven both profitable and controversial. Ranked the No. 1 business in Latin America in 2010 by the *Latin Business Chronicle*, the iron ore giant grew 123.9 percent in 2010, while

profits reached US\$700 million—a 456.1 percent increase over the 2009 value.¹⁵ However, the firm has been plagued by labor disputes and accusations of abuse related to pay and health conditions.¹⁶ Labor strikes occurred intermittently in the early 2000s, and annually since 2008, with clashes occasionally turning violent.¹⁷

So what is Peru to do? It must consolidate, clarify and strengthen its regulatory approach with Chinese state-owned enterprises. Lima can and must assume a more assertive role in negotiating terms and expectations with Chinese investors. Shougang's environmental violations may have as much to do with lax oversight as with Chinese malfeasance, and the company's use of lightly regulated, low-wage subcontractors to skirt minimum wage regulations reflects loopholes in Peruvian law as much as anything else.¹⁸

As Peru matures, the nature of Chinese investment may be improving. In 2008, Chinalco, the state-owned aluminum corporation of China, purchased the Peruvian Toromocho mine for US\$2.2 billion. Rather than importing Chinese labor, Chinalco has hired locally. It has also implemented community outreach programs, and worked with third-party advisors to establish an environmental management system. The Toromocho mine is subject to revised environmental standards, and Chinalco is investing upwards of US\$5 billion in project infrastructure up front.¹⁹

Nevertheless, controversy remains likely as Chinalco must “relocate” 5,000 people living on the site of the mine. This delicate process has already engendered blowback. How this relocation is handled may well indicate Peru's progress in harnessing Chinese investment.

MEXICO AND CHINA: A HEALTHY COMPETITION

Mexico's relationship with China is uniquely competitive among the Pumas. Since the creation of the *maquiladora* sector south of the Rio Grande in the

1960s, Mexico has geared its economy towards cheap, manufactured goods, exported predominantly to the United States. Therefore Mexico viewed China's 2001 ascension to the WTO with alarm.

The Chinese threat was twofold: On the one hand cheap Chinese manufactured goods could siphon US market share away from the *maquiladoras*. On the other hand, Chinese manufactures could swamp the Mexican domestic market.

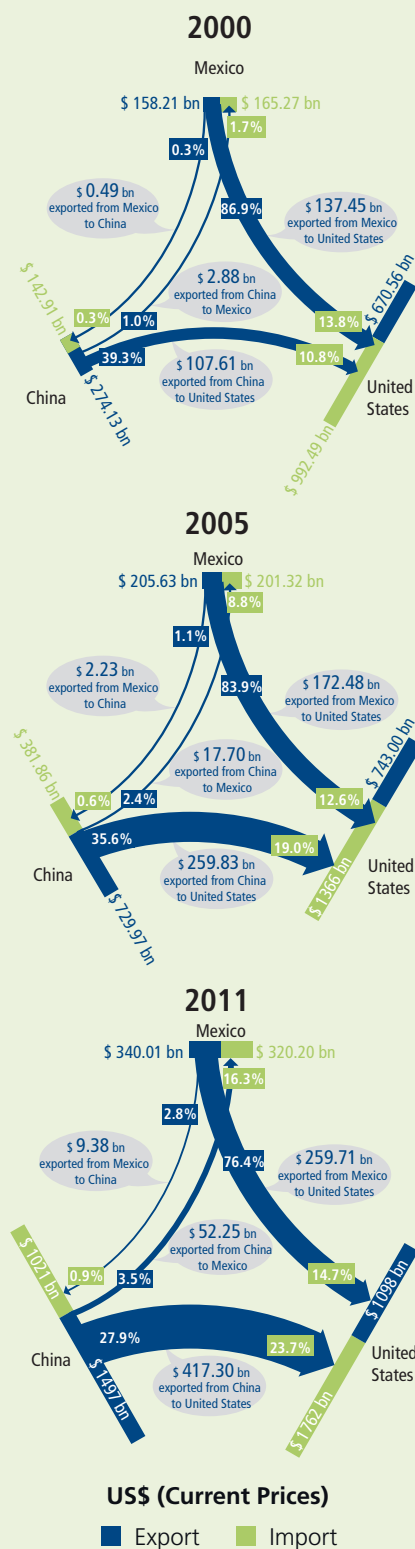
Statistics corroborated Mexico's concerns. China, which competes directly with Mexico on twelve of the latter's 20 main export-sectors to the US, surpassed Mexico in 2003 to become the number two exporter to the US behind Canada.²⁰ By 2007, Chinese exports to the US surpassed Mexico's by almost 60 percent. In terms of competition for the Mexican market, what was a US\$2.39 billion Mexican trade deficit to China in 2000 ballooned to US\$38.72 billion deficit by 2010.²¹

However, in a comeback that highlights the potential of the Pumas, Mexico has rapidly regained its competitiveness, especially in terms of exports to the US. In 2005, Mexican manufacturing exports had dipped to 11 percent of US imports. By 2012 that number had increased to 14.4 percent, surpassing previous highs.²²

Increased efficiency, a web of trade agreements and the elimination of many non-tariff trade barriers have factored in this reemergence. Increased Chinese wages, compared with generally stagnant Mexican wages, have also played a role.²³ While a *maquiladora* worker in Juarez may balk at the notion that her country is more competitive because her wage has flatlined, demographics suggest that Mexican labor will remain abundant and cheap, at least through the next two decades.

Having successfully fended off (or at least survived) competition at the nadir of Chinese wages, Mexico may now view China as an opportunity for market

Trade Flows: Mexico, China and the US



Source: Bertelsmann Stiftung Global Economic Dynamics Visualizer, UN Comtrade

▲ Trade flows from 2000, 2005 and 2011 demonstrate that China has both captured an increasing percentage of the US market, while also opening a sizeable trade surplus with Mexico.

expansion, and not just as a threat. Whether Mexican automobiles can penetrate the Chinese market remains to be seen, but some firms are willing to pay to find out. Fiat is already shipping Mexican Fiat 500s to China, and Audi is considering a similar strategy.²⁴

Moreover, as Chinese consumption expands, demand increases for luxury goods—especially those perceived as popular in the West. For Mexico, exports that fit this bill include high-end tequila, mescal, pork and even wine. These operations are generally small to mid-sized enterprises owned by Mexicans, as opposed to the multinational manufacturers. With time and experience, Mexican exporters may begin to penetrate China, thus opening a new avenue for growth and diversifying away from the US.

COLOMBIA AND CHINA: WHAT MIGHT BE

Colombia is an Andean outlier with regards to China. With commodities making up more than 60 percent of the country's global exports, Colombia would seem destined to link into the same Chinese-Latin American trade flows that have sparked continental growth.

Yet it has not. Colombia remains far more tethered to the US than to China. As of 2011, roughly 40 percent of Colombian exports went to the US, while only three percent shipped west to China.²⁵ In terms of commodities, the numbers are even more skewed. In 2010 the US received 47.2 percent of Colombian commodities, while China imported 5.2 percent, only slightly more than what Colombia sent to Switzerland.

At the moment, Colombia does not have the infrastructure required to compete with its commodity-producing neighbors in order to export to China. Buenaventura, Colombia's largest Pacific Port, lacks the capacity to process heavy trade. Its draft is not deep enough for large vessels, the town itself is too small, and the linkages to Cali (the nearest big city) are underdeveloped. It is actually

more cost-efficient to take the longer Caribbean route and pay passage through the Panama Canal.

Chinese investment in Colombia has also run comparatively low: Of the US\$15 billion that China invested in Latin America in 2010, only US\$6.2 million landed in Colombia.²⁶ China plays an emerging role in Colombia's extractive industries, notably in hydrocarbons, but ambitious infrastructure projects, announced to great fanfare, have amounted to little. Chinese investors have been unable to build the 120 kilometer road connecting Buenaventura to Bugo, let alone the vaunted "land canal" that would cut through Colombia.

Nevertheless, Colombia's underwhelming economic ties with China may actually be a reason for optimism. Puma skeptics are quick to posit that 21st century growth stems from Chinese demand, and thus, is vulnerable to a Chinese slowdown. Colombia has increased exports and growth without Chinese demand. The country has averaged 4.67 percent growth over the last decade—one wonders what that figure might have been had it enjoyed deeper trade ties with China.²⁷ If anything, Colombia's march towards internal peace will allow for infrastructure upgrades that, in turn, will allow for increased trade with China, thus building on already strong growth figures.

AN OCEAN OF OPPORTUNITY

While each Puma faces different challenges regarding China, each has developed knowledge and experience useful to the others. Chile has quietly engaged China almost as a partner—a rarity for an emerging market. Mexico has proven that the Pumas can compete with the Dragon. Peru has forged a path towards both encouraging and regulating Chinese investment. Colombia, which hopes to increase trade with and investment from China, can learn much from the Chilean, Mexican and Peruvian experiences.

The Pumas should not discourage or fear China, and the Pacific Alliance's

overtures to Asia suggest that they have no intention of doing either. Rather, by harnessing the Dragon and leveraging China's need for resources, expect the Pumas to channel the relationship towards the opportunities, and away from the threats.

III. Prepared to Pounce?



Prepared to Pounce?

Mexico, Colombia, Peru and Chile have made noteworthy macroeconomic and democratic advancements in the 21st century. They have created a solid foundation for development precisely as the greater Pacific stands to emerge as a focal point of global growth. That the four countries have shared this “awakening” gives them the opportunity to join forces, exponentially increasing the group’s global impact and potential.

Yet persistent shortcomings could still derail this progress. Systemic corruption, violence, commodity reliance, and inequality are not exactly new phenomena for the four countries. Will the Pacific Pumas finally be able to exorcise these demons? Or are the trends outlined in this document simply symptomatic of a boom period, anticipating an eventual bust—a cycle so familiar in Latin America?

The answer remains to be seen, but one thing is clear: The Pacific Pumas have an opportunity.

They have an opportunity to entrench stable macroeconomic systems; to pursue levelheaded democratic governance; to eradicate extreme poverty; the opportunity to link into international trade networks and to prove that globalization can be a tool to address inequality.

United in the Pacific Alliance, the Pumas have the opportunity to emerge as regional leaders and flag bearers for Latin American integration; they have the opportunity to join a 21st century trans-Atlantic community that combines the experience and know-how of the US and EU with the growth potential of emerging markets. In a world that could see increased regionalism, the Pumas have the opportunity to be strategic partners to the United States, Europe and East Asia.

How the Pumas capitalize on this opportunity cannot necessarily be measured by any given year’s growth statistics. Similarly, protests in Chile, setbacks in the Colombian peace process, drug violence in Mexico or falling copper prices in Peru do not necessarily portend a dream deferred. In many cases, these are natural tensions inherent to maturing emerging markets.

Ultimately, the Pumas’ success should be measured in terms of creating and maintaining institutions worthy of the developed world while sustaining the growth potential and dynamism of emerging markets. Puma governments must tackle difficult reforms, even at the cost of some short-term growth, in order to remove long-term bottlenecks on their economies. In terms of regional leadership, the Pumas’ success should not be based on how many countries join the Pacific Alliance, but rather the depth and breadth of Alliance integration. In terms of global linkages, the Pumas must demonstrate an ability to turn free trade agreements on paper into more and better jobs in practice.

Mexico, Colombia, Peru and Chile do not need to be perfect, nor will they be. But if they can continue their positive momentum, they will blaze a trail for the Pumas of Latin America to run with the Tigers of the East.

Endnotes

Chapter 1

¹ Hong Kong SAR, South Korea, Singapore and Taiwan.

² International Monetary Fund Data, simple, unweighted averages.

³ International Monetary Fund Data, 2009-2012.

⁴ Michael Shifter and Cameron Combs. "Shifting Fortunes: Brazil and Mexico in a Transformed Region." *Current History*, February 2013, 52. Available online at <http://www.thedialogue.org/PublicationFiles/CurrentHistory-ShiftingFortunes-Feb.pdf>.

⁵ Robert Wood (ed.). "Country Report: Chile, February 2013." *Economist Intelligence Unit*, February 2013.

⁶ After 20 years of the center-left Concertación presidency, Chileans elected a right leaning government in 2010. After twelve years of the center-right PAN presidency, Mexico returned the centrist PRI to power in 2012. Colombia has moved from the more hardline presidency of Álvaro Uribe to the more pragmatic Juan Manuel Santos, while Peru has shifted from a technocratic executive to a (supposedly) populist president.

⁷ MERCOSUR includes Argentina, Brazil, Paraguay (currently suspended), Uruguay and Venezuela.

⁸ While this figure may pale in comparison to 1980's East Asian NIC annual export volume growth (12.29 percent), the Puma figures were observed during a global economic downturn in trade, and they compare reasonably with ASEAN – 5 average export volume growth (4.89 percent) over the same span. (Source: IMF Data).

⁹ Source: *Economist Intelligence Unit*.

¹⁰ Cartagena has a population of 900,000.

¹¹ Source: *Economist Intelligence Unit*.

¹² "Murderous Matches." *The Economist*, November 22, 2012. Available online at <http://www.economist.com/blogs/graphicdetail/2012/11/comparing-mexican-states-equivalent-countries>.

¹³ *Business Insider* reports Colombia's 2011 homicide rate as 16th highest in the world, between Congo and Lesotho. (See: <http://www.businessinsider.com/1homicidal-countries-2011-11?op=1>).

Chapter 2

¹ Through booms and busts of gold, silver, copper, tin, coffee, rubber, guano, iron, soy and an assortment of hydrocarbons, the region has a long track record of violent swings in production. Latin America's macroeconomic caprices have not spared the Pacific Pumas. Since 1950, Mexico has plowed through an economic miracle, a debt crisis, a peso crisis, and a recovery before slamming into the Global Recession of 2008. In the 1980s, Chile had years of 10.6 percent growth and 13.5 percent contraction; Peruvian annual inflation hit 2,775 percent in 1989, and 7,649 percent in 1990 (Source: International Monetary Fund Data).

² The Pumas have experienced macroeconomic unraveling in recent memory, and they appear to have learned their lesson. Mexican devaluations in the 1980s sparked the Latin American debt crisis. Chilean inflation averaged 23.76 percent between 1980 and 1985, while Peru battled through the decade (literally and physically) before inflation spiraled out of control in 1989 (See Francisco Gonzalez. *Creative Destruction? Economic Crises and Democracy in Latin America* (Baltimore: The Johns Hopkins University Press, 2012).

³ If anything, floating exchange regimes threatened to overly *strengthen* domestic currencies as investment poured in, thus undermining export competitiveness. This is particularly true in Colombia where the peso has rallied for much for the 21st century, dipping from just under 3,000 to the dollar in 2003 to around 1,800 to the dollar in 2013, despite a brief crisis-era slump. (Currency values according to XR Currency Charts available at www.xr.com). This pressure should ease as the US Federal Reserve tightens monetary policy.

⁴ Source: IMF International Financial Statistics

⁵ Roberto Frenkel and Martín Rapetti name Chile and Colombia as "pioneers" in implementing a managed float based on inflation targeting, having adopted this method in 1990 and 1991 respectively. Peru adopted such a float in 1994, and Mexico in 1999. (See Roberto Frenkel and Martín Rapetti. "A Concise History of Exchange Rate Regimes in Latin America." Center for Economic and Policy Research, April 2010, 23.

⁶ Liliana Rojas-Suarez. "The International Financial Crisis: Eight Lessons for and from Latin America." Center for Global Development Working Paper No. 202, January 2010. Available online at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1543451.

⁷ "Alliance of the Pacific calls for gradual withdrawal of stimulus." *FOREX News*, August 24, 2013. Available online at <http://convertcurrency.com/news/alliance-of-the-pacific-calls-us-gradual-withdrawal-of-stimulus>.

⁸ Erich Arispe and Bill Warlick. "Venezuelan Policy Continuity Likely After Chavez Victory." *Fitch Ratings*, October 8, 2012. Available online at <http://www.fitchratings.com/web/en/dynamic/articles/Venezuelan-Policy-Continuity-Likely-After-Chavez-Victory.jsp>.

⁹ Kirsten Sehnbruch. "The Bachelet Bounce." *Berkeley Review of Latin American Studies*, Fall 2009 – Winter 2010. Available online at <http://ias7.berkeley.edu/Publications/Review/Fall2009/pdf/BRLASFall2009-SehnbruchBachelet.pdf> and Larry Rohter. "Chile Copper Windfall Forces Hard Choices on Spending." *The New York Times*, January 7, 2007. Available online at <http://www.nytimes.com/2007/01/07/world/americas/07chile.html>.

¹⁰ James McKeigue. "A Lucrative Latin American Alliance." *Money Week*, August 23, 2012. Available online at <http://www.moneyweek.com/investment-advice/share-tips/a-lucrative-latin-american-alliance-60320>.

¹¹ Source: IMF International Financial Statistics.

¹² Federico Barriga, ed. "Country Report: Colombia, April 2013." *Economist Intelligence Unit*, Economist Intelligence Unit Limited, 2013.

¹³ Alejandro Schtulmann and Sergio Broholm. "Mexico's Tax Reform in the Works: Preview and Initial Considerations." *EconoMonitor*, February 18, 2013. Available online at <http://www.economonitor.com/blog/2013/02/mexicos-tax-reform-in-the-works-preview-and-initial-considerations/>.

¹⁴ Based on discussions with Instituto Mexicano para la Competitividad A.C. (IMCO) Director General Juan Pardinas and former General Director Roberto Newell. IMCO is a Mexican think tank that specializes in issues of competitiveness.

¹⁵ World Bank Database. Available online at <http://data.worldbank.org/country/colombia>

¹⁶ "Poverty Rate in Peru Falls 17% from 2006-2010." *People's Daily Online*, May 20, 2011. Available online at <http://english.people.com.cn/90001/90777/90852/7386733.html>.

¹⁷ Averages unweighted. Source: *Economist Intelligence Unit*.

¹⁸ Source: *Economist Intelligence Unit*.

¹⁹ Mexican foreign direct investment (FDI) has fluctuated, but it remains the top destination of the four. Source: World Development Indicators, World Bank Data.

²⁰ Source: The World Bank & International Finance Corporation. "Doing Business: Economy Rankings." Available online at <http://www.doingbusiness.org/rankings>.

²¹ The Pacific Pumas' Gini Coefficient (a common measurement of economic inequality), remains high, as it does throughout Latin America. Moving forward, the Pumas' ability to develop an internal consumptive motor hinges upon an ability to increase the buying power of the less well healed (and of the barefoot).

Chapter 3

¹ The relationship between institutional and economic failure is argued effectively and at length in Daron Acemoglu and James Robinson. *Why Nations Fail*. New York: Crown Business, 2012. It should be noted that these authors maintain a more pessimistic stance on Colombia's institutional development.

² John Peeler. *Building Democracy in Latin America, Third Edition*. (Boulder: Lynne Rienner, Inc., 2009), 148.

³ For a concise summary of APRA, Peru's populist movement, see Michael L. Conniff, ed. *Populism in Latin America*. (Tuscaloosa: University of Alabama Press, 2012). Military coups occurred intermittently between 1930-1979.

⁴ Teresa Cespedes and Caroline Stauffer. "Left-winger Humala wins Peru election, markets dive." *Reuters*, June 6, 2011. Available online at <http://www.reuters.com/article/2011/06/06/us-peru-election-idUSTRE75432720110606>.

⁵ Nick Rosen. "Poll: Peru's business leaders support Humala." *Peru This Week*, December 3, 2012. Available online at <http://www.peruthisweek.com/news-poll-perus-business-leaders-support-humala-13227>.

⁶ Reduced tariffs, deregulation and pursuit of a North American Free Trade Agreement (NAFTA)

⁷ *Partido Revolucionario Institucional* (PRI), *Partido Acción Nacional* (PAN), *Partido Revolucionario Democrático* (PRD)

⁸ According to a *Bloomberg View* Op-Ed, "The U.S. Energy Information Administration estimates that Mexico has the world's sixth-largest shale-gas reserves, with 555 trillion cubic feet of recoverable reserves (plus a further 13 billion barrels of recoverable shale-oil reserves)." See Duncan Wood. "Turn Up the Gas on Mexico's Energy Revolution." *Bloomberg View*, August 14, 2013. Available online at <http://www.bloomberg.com/news/2013-08-14/turn-up-the-gas-on-mexico-s-energy-revolution.html>.

⁹ The energy reform is not a done deal. The constitutional adjustments require ratification from at least 17 of Mexico's 31 state legislatures, though most analysts expect little obstruction from a sufficient number of PRI-friendly states. The legal implications may be more nettlesome. Advocates for more liberal reforms celebrate the bill's licenses, which function similarly to investor-desired concessions. Yet these concessions remain expressly prohibited, creating a gray area that could well end up in court.

- ¹⁰ Colombia has not suffered the severe macro fluctuations and economic collapses endemic to Latin America and much of the developing world in recent decades. It was the only major Latin American country not forced to restructure international obligations during the 1980s debt crisis that racked the region. Colombia emerged unscathed by the tequila crisis of the mid-90s and bounced back quickly from a one-year downturn during the East Asian crisis of the late-1990s. It has grown right through the great global recession. See: Jennifer Holmes, Sheila Amin Gutiérrez de Piñeres and Kevin Curtin. *Guns, Drugs & Development in Colombia* (Texas: University of Texas Press, 2009); and James Robinson. "A Normal Latin American Country? A Perspective on Colombian Development." November 21, 2005. Available online at http://scholar.harvard.edu/files/jrobinson/files/jr_normalcountry.pdf.
- ¹¹ "The Humanitarian Crisis in Colombia Caused by the Armed Conflict." International Organizations Position Paper: Colombia, 2011. Available online at [http://www.internal-displacement.org/8025708F004CE90B/\(httpDocuments\)/7C6B5E44F9918459C125797600398E72/\\$file/colombia-humanitarian-crisis-17nov2011-eng.pdf](http://www.internal-displacement.org/8025708F004CE90B/(httpDocuments)/7C6B5E44F9918459C125797600398E72/$file/colombia-humanitarian-crisis-17nov2011-eng.pdf).
- ¹² Acemoglu and Robinson, 277 – 283.
- ¹³ Inequality remains high in Colombia, and even people who have suffered directly from FARC violence can be sympathetic to the original ideology.
- ¹⁴ ¿Alguien espía a los negociadores de La Habana? *Semana*, February 3 2014. Available online at <http://www.semana.com/nacion/articulo/alguien-espia-los-negociadores-de-la-habana/376076-3>
- ¹⁵ Petro y Cepeda son amenazados por las Águilas Negras. *Semana*, February 4, 2014. Available online at <http://www.semana.com/nacion/articulo/cepeda-petro-son-amenazados-por-aguilas-negras/376125-3>.
- ¹⁶ Peter Siavelis. "Chile: The End of the Unfinished Transition." In Jorge Domínguez and Michael Shifter (eds.) *Constructing Democratic Governance in Latin America*, 3rd Edition (Baltimore: The Johns Hopkins University Press, 2008), 191 – 196.
- ¹⁷ Reforms in 1989 chipped away at unelected influences over Chilean democracy. More far-reaching reforms in 2005 reigned in executive powers while simultaneously restoring civilian oversight of the military. Source: Claudia Heiss. "Bachelet Appoints Group to Study New Constitution for Chile." *Int'l J. Const. L. Blog*, May 1, 2013. Available online at <http://www.iconnectblog.com/2013/05/bachelet-appoints-group-to-study-new-constitution-for-chile>.
- ¹⁸ According to Siavelis, the education law "transferred the authority for public education from the central government to the municipalities, creating huge gaps between rich and poor areas (Siavelis, 202)."
- ¹⁹ For OECD corporate tax income averages, see "OECD Corporate Income Tax Rates, 1981-2012." *Tax Foundation*, June 29, 2012. Available online at <http://taxfoundation.org/article/oecd-corporate-income-tax-rates-1981-2012>.
- ²⁰ Francisco Peregril. "Michelle Bachelet, presidenta electa de Chile tras una amplia victoria." *El País*, December 16, 2013. Available online at http://internacional.elpais.com/internacional/2013/12/15/actualidad/1387145955_299083.html.
- ²¹ Kristen Sehnbruch and Peter Siavelis. "Why Victory for Bachelet in Chile is undeniable but bittersweet." *The Washington Post* (November 25, 2013). Available online at <http://www.washingtonpost.com/blogs/monkey-cage/wp/2013/11/25/why-victory-for-bachelet-in-chile-is-undeniable-but-bittersweet/>.
- ²² Alex Kaiser. "Is This the End of the Chilean Economic Miracle?" *Forbes*, October 28, 2013. Available online at <http://www.forbes.com/sites/realspin/2013/10/28/is-this-the-end-of-the-chilean-economic-miracle/>.
- ²³ See Cornelius Fleischhaker, "Peru: The Growing Pains of a Puma Cub," *No Se Mancha*, September 29, 2013. Available online at <http://semancha.com/2013/09/29/peru-puma-cub/>.
- ²⁴ "President Humala: Peru's foreign policy based on dignity and honor." *Andina*, September 24, 2011. Available online at <http://www.andina.com.pe/Ingles/noticia-president-humala-perus-foreign-policy-based-on-dignity-and-honor-379191.aspx>.
- ²⁵ In terms of Peruvian parties, Alberto Fujimori's 1990 *Cambio 90*, Alejandro Toledo's 2001 *Peru Posible* and Ollanta Humala's 2011 *Gana Peru* parties were all built by the presidential candidates themselves. Alan García ran on the populist APRA ticket in 2006.
- ²⁶ See "Humala Humbled: A lonelier president faces protests." *The Economist*, August 3, 2013. Available online at <http://www.economist.com/news/americas/21582580-lonelier-president-faces-protests-humala-humbled?zid=309&ah=80dcf288b8561b012f603b9fd9577f0e>.

Chapter 4

¹ Unweighted averages. Source: International Monetary Fund Data

² Trade is a sensitive subject in Latin America where exposure to global tailwinds has led to periods of dizzying booms and busts. Many 19th century patriots were inspired to take up arms against colonial Spanish rule to liberate the new world from restrictive trade policies. A subsequent era of trade climaxed between 1870 and 1914 when European demand for Latin American raw materials coincided with a boom in emerging market investment. During this period, Latin America outgrew the US in both GDP and per-capita GDP. See Francisco Gonzalez, *Creative Destruction: Economic Crisis and Democracy in Latin America* (Baltimore: The Johns Hopkins University Press, 2012), 47. This golden age of free trade dissolved during World War I. International dynamics would only worsen with the onset of the Great Depression. Caught in macroeconomic tides beyond its control, Latin American economists questioned the efficacy of export-led growth. These sentiments culminated in one of the region's notable contributions to economic philosophy, dependency theory, which held that free trade pigeonholed Latin America into exporting raw materials in exchange for ever-more expensive manufactured goods. The region transitioned to an inward-looking development model, raising prohibitive tariffs against imports while nurturing domestic manufacturers. This import-substitution industrialization (ISI) of the 1950, '60s and '70s distorted currencies, overvaluing exports and undervaluing imports; two factors that helped trigger the sovereign debt crises of the 1980s. Latin America underwent shotgun liberalization in the 1980s and 1990s under the guidance of the World Bank, the International Monetary Fund, and the US Treasury. Reformers often lacked a mandate: The governments that lowered trade barriers in Mexico, Peru and Chile had dubious democratic credentials, at best. Subsequent neoliberal politicians struggled at the ballot box in the 2000s, and many larger Latin American countries (but not the Pumas) began to unwind neoliberal reforms as part of the region's so-called "pink tide."

³ *Shaping the Future of Asia and the Pacific Latin-America and the Caribbean Relationship*. (Washington: Inter-American Development Bank, 2012).

⁴ Inter-American Development Bank (2012), 50.

⁵ Ibid.

⁶ Bertelsmann Foundation, Global Economic Dynamics Visualizer, 2013.

⁷ "China becomes Peru's main trade partner and a leading investor." *MercoPress*, September 23, 2011. Available online at <http://en.mercoPress.com/2011/11/30/china-becomes-peru-s-main-trade-partner-and-a-leading-investor>.

⁸ "NAFTA at 20: Deeper, Better, NAFTA." *The Economist*, January 4, 2014. Available online at <http://www.economist.com/news/leaders/21592612-north-americas-trade-deal-has-delivered-real-benefits-job-not-done-deeper-better>.

⁹ Source: IQOM Commercial Intelligence Data

¹⁰ An unwritten rule limits TPP participants to members of the Asia-Pacific Economic Cooperation (APEC), of which Colombia is not a member. A moratorium on APEC membership has prevented any new members from joining since 1998. (See: Barbara Kotschwar. "The Pacific Alliance, the TPP, and the RCEP: What does it all mean?" The Peterson Institute, 2013.) Analysts interpret the moratorium as a method to prevent India from joining.

¹¹ Adam Thomson. "Mexico: China's Unlikely Challenger." *Financial Times*, September 19, 2012. Available online at <http://www.ft.com/intl/cms/s/0/9f789abe-023a-11e2-b41f-00144feabdc0.html#axzz2dBfCfBNF>.

¹² *Statistical Yearbook for Latin America and the Caribbean*, 2000. (Santiago: United Nations Economic Commission for Latin America and the Caribbean, 2001), 504-505.

¹³ Thomson, 2012.

¹⁴ Source: World Bank Human Development Index

¹⁵ Claudia Avila Connelly. "Why 'Made in Mexico' Means Quality and Competitiveness." *Site Selection*, January 2012. Available online at <http://www.siteselection.com/issues/2013/jan/mexico.cfm>.

¹⁶ Theodore Kahn. "NAFTA at 20: A Good Deal for Mexico?" *No Se Mancha*, January 3, 2014. Available online at <http://semancha.com/2014/01/03/nafta-at-20-a-good-deal-for-mexico/>.

¹⁷ Emily Sinnott, John Nash and Augusto de la Torre. *Natural Resources in Latin America and the Caribbean: Beyond Booms and Busts?* (Washington: The World Bank, 2010), 33.

¹⁸ Christian Berthelsen. "Investors, Analysts See End of Commodity Supercycle." *The Wall Street Journal*, July 22, 2013. Available online at <http://online.wsj.com/article/SB1000142412788732414430457861967266497416.html>.

¹⁹ Ric Deverell. "Commodities' Forecast Update: the Return of Fundamentals." *Credit Suisse Securities Research & Analytics*, June 25, 2013. Available online at https://doc.research-and-analytics.csfb.com/docView?language=ENG&format=PDF&document_id=805424220&sourceid=emcmt&serialid=e0u%2foelAy4ymkowCA%2feznO5vq142utsd%2bWhhhYkcg%3d.

²⁰ Jack Farchy and Javier Blas. "Commodity traders call end of supercycle." *Financial Times*, June 26, 2013. Available online at <http://www.ft.com/intl/cms/s/0/d76d040a-de76-11e2-b990-00144feab7de.html#axzz2q27TmuQ8>.

²¹ Mauricio Mesquita Moreira and Danielken Molina. "Asia and the Pacific-LAC Trade: What Does the Future Hold?" In *Shaping the Future of Asian and the Pacific—Latin American and the Caribbean Relationship*. (Washington: Inter-American Development Bank & Asian Development Bank, 2012), 14.

²² Deverell, 2013.

²³ Mike Morris, Raphael Kaplinsky and David Kaplan. "One Thing Leads to Another – Commodities, Linkages and Industrial Development: A Conceptual Overview." *Making the Most of Commodities Programme Discussion Paper No. 12*, October 2011. Available online at [http://commodities.open.ac.uk/8025750500453F86/\(httpAssets\)/22498EAB8FBC93DE80257929002F2FA1/\\$file/MMCP%20Paper%2012%20\(revised\).pdf](http://commodities.open.ac.uk/8025750500453F86/(httpAssets)/22498EAB8FBC93DE80257929002F2FA1/$file/MMCP%20Paper%2012%20(revised).pdf).

²⁴ According to a World Bank background research paper, Latin American metals, for example, are differentiated enough "to create a high degree of intra-industry trade, implying the exchange of distinct varieties...[creating] the potential for specialization in, and upgrading to higher quality, higher values within product categories." (See: Sinnott, et al, 18.) Meanwhile, the *Banco Central de Reserva del Perú* argues that Peru has been effective in generating commercial linkages with local mines, citing the Yanacocha gold mine's spillover affects stemming from demand for local inputs. See: Fernando Aragón and Juan Pablo Rud. "The Blessing of Natural Resources: Evidence from a Peruvian Gold Mine." Banco Central de Reserva del Perú Working Paper, December 2009. Available online at <http://www.bcrp.gob.pe/docs/Publicaciones/Documentos-de-Trabajo/2009/Working-Paper-15-2009.pdf>.

²⁵ Esteban Pérez Caldentey. "Income Convergence, Capability Divergence and the Middle Income Trap: An Analysis of the Case of Chile." *Studies in Comparative International Development*, June 2012, Volume 47, Issue 2, 185-207.

²⁶ Raphael Bergoing, Alejandro Micco and Andrea Repetto. "Dissecting the Chilean Export Boom." *Cepal Review*, December 2011. Available online at <http://www.eclac.org/cgi-bin/getProd.asp?xml=/revista/noticias/articuloCEPAL/8/46378/P46378.xml&xml=revista/tpl-i/p39f.xml&base=revista/tpl-i/top-bottom.xml>.

²⁷ Simon Collier and William Sater. *A History of Chile, 1808-2002* (Cambridge: Cambridge University Press, 2004), 370.

²⁸ Bergoeing, et al., 5.

²⁹ Manuel Agosin and Claudio Bravo-Ortega. "The Emergence of New Successful Export Activities in Latin America: The Case of Chile." *Documentos de Trabajo del Departamento de Economía de La Universidad de Chile*, April 2007 (Santiago: Universidad de Chile). Available online at <http://www.econ.uchile.cl/uploads/publicacion/f5ba4950-b592-4285-8c58-decd6ea07234.pdf>.

³⁰ In May 2012 *Drinks International* found Concha y Toro to be the world's most admired wine brand. "Once again, Concha y Toro tops the Most Admired poll, a year on from its \$238mn purchase of Feter—a deal which had the potential to change the way in which the company was perceived on the international stage." See "The World's Most Admired Wine Brands." *Drinks International*, May 2012. Available online at <http://www.drinksint.com/files/Supplements/2012/Drinks-International-Most-Admired-Wines-2012.pdf>.

³¹ Mauricio Reina and Sandra Oviedo. "Colombia y Asia: Tratando de Recuperar el Tiempo Perdido." *FEDESARROLLO*, June 20, 2013. See also: Kahn (2013).

³² Mauricio Mesquita Moreira. "Too far to export: Domestic Transportation Costs and Regional Export Disparities in Latin America and the Caribbean." Inter-American Development Bank, 2013. Available online at <http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=38195718>.

Chapter 5

¹ The Economist attributes this quote to Felipe Larraín, Chilean Minister of Finance under President Sebastián Piñera (see <http://www.economist.com/news/americas/21578056-region-falling-behind-two-alternative-blocks-market-led-pacific-alliance-and>), but subjects referencing the Pacific Alliance as "the exciting thing happening in Latin America" has been common in interviews I have conducted with Mexican, Colombia, Peruvian, Chilean and US policymakers both in Washington and Latin America.

² Source: International Monetary Fund Data Base

³ Source: International Monetary Fund Data Base, Gross Domestic Product, Current Prices, US Dollars.

⁴ Socorro Ramírez. "Regionalism: The Pacific Alliance." *Americas Quarterly*, 2013. Available online at <http://www.americasquarterly.org/content/regionalism-pacific-alliance>.

⁵ Mexico, Guatemala, El Salvador, Honduras, Nicaragua, Costa Rica, Panama, Colombia, Ecuador, Perú and Chile.

⁶ Carlo Dade and Carl Meacham. "The Pacific Alliance: An Example of Lessons Learned." Center for Strategic & International Studies, July 11, 2013. Available online at <http://www.iadb.org/intal/intalcdi/PE/2013/12506.pdf>. It should be noted that Dade and Meacham place the Alliance's combined GDP at "just under US\$3 trillion," a higher figure than used in this study.

⁷ Venezuelan President Hugo Chávez removed his country from CAN in 2006. Bolivia, a founding member of CAN but more recently a stalwart of the more statist ALBA coalition, did not join the Arc of the Pacific. In the more recent transition from the Arc of the Pacific (which has been inactive since 2010), the Pumas have consolidated their ranks: Ecuador and Nicaragua, for example, have neither joined nor observed the Pacific Alliance. See: Simone Baribeau. "Chávez: Venezuela to withdraw from Andean Community of Nations." *Venezuelan Analysis*, April 20, 2006. Available online at <http://venezuelanalysis.com/news/1706>.

⁸ Barbara Kotschwar. "The Pacific Alliance, the TPP, and the RCEP: what does it all mean." The Peterson Institute, October 2013.

⁹ "South America's Pacific Alliance Signs Deal to Scrap Tariffs." *Voice of America*, February 11 2014. Available online at <http://www.voanews.com/content/reu-south-america-pacific-alliance-deal-scrap-tariffs/1848724.html>.

¹⁰ Source: European Union statistics. Mexico is Colombia's fourth biggest trading partner.

¹¹ "Pacific Alliance is a 'marketing success' and no concern for Mercosur, says Brazil." *MercoPress* (June 22, 2013). Available online at <http://en.mercopress.com/2013/06/22/pacific-alliance-in-a-marketing-success-and-no-concern-for-mercursosays-brazil>.

¹² World Economic Forum. *The Financial Development Report 2012*. Available online at http://latamalternatives.com/Files/MEDIA_PRESS_1.pdf. http://www3.weforum.org/docs/WEF_FinancialDevelopmentReport_2012.pdf.

¹³ Firms such as Falabella and Cencosud (See: Diego Agudelo, Santiago Barraza, María Isabel Castro and Samuel Mongrut, *Liquidez en Los Mercados Accionarios Latinoamericanos: Estimando El Efecto del Mercado Integrado Latinoamericano* (MILA). (Centro de Investigaciones Económicas y Financieras, Universidad EAFIT, No. 12-21, 2012). Available online at http://repository.eafit.edu.co/handle/10784/657#Ue_nxY21H5E

¹⁴ Peruvian mining firms include Buenaventura, Hosch Shcil, Volcán, and Milpo. (See: Agudelo, et al.)

¹⁵ Colombian energy firms include Ecopetrol, Pacific Rubiales, ISA, and Colinvestores. (See: Agudelo, et al.)

¹⁶ Ndyá Gómez Ramirez. *El MILA y Su Impacto en el Sector Financiero*. (Nueva Granada: Univesidad Militar 2013), 28. Available online at <http://repository.unimilitar.edu.co/bitstream/10654/9966/1/GomezRamirezNidyaMercedes2013.pdf>. Also see: Andres Schipani. "Bourses: Uniting to build critical mass." *Financial Times*, November 21, 2012. Available online at <http://www.ft.com/intl/cms/s/0/10e97554-2808-11e2-afd2-00144feabdc0.html#axzz22nZIEIGZ>.

¹⁷ "MILA: Strengthening Financial Integration." Inter-American Development Bank. Available online at <http://www.iadb.org/en/topics/trade/MILA-strengthening-financial-integration,6839.html>.

¹⁸ Ramirez, 20. For a graph see <http://us.spindices.com/indices/equity/sp-MILA-40-index>.

¹⁹ In its insipient phase, and still without Mexico, MILA has captured the attention of international investors. "The Andean Region: Catching Up Fast" blared a headline from *Advanced Trading* in September 2012.

²⁰ "MILA Holding the Best Cards in a Long Game," read another from Latin American Investor. See Alice Botis. "The Andean Region: Catching Up Fast." *Advanced Trading*, September 27, 2012. Available online at <http://www.advancedtrading.com/exchanges/the-andean-region-catching-up-fast/24008007>, and "MILA Holding the Best Cards in a Long Game." *Latin American Investor*, July 4, 2013. Available online at <http://latinamericaninvestor.com/?p=123>. Meanwhile, a study conducted by the Centro de Investigaciones Económicas y Financieras (CIEF) in Colombia concluded that "the potential savings in transactions costs associated with a modest increase of 10 percent in trading activity ranges between 10 and 36 million dollars for the three countries." (See Agudelo, et al.)

²¹ This international partnering could have been done prior to and independent of MILA. However, experts such as the Inter-American Development Bank's Juan Antonio Ketterer believe that MILA encourages this process.

²² "MILA: A New Phase of Integration in Latin America." *Latin American Initiatives*, January, 2011. Available online at http://latamalternatives.com/Files/MEDIA_PRESS_1.pdf.

²³ Juan Antonio Ketterer. Interview by author. Washington, May 17, 2013.

Chapter 6

¹ "Latin America Geoeconomics: A Continental Divide." *The Economist*, May 18, 2013. Available online at <http://www.economist.com/news/americas/21578056-region-falling-behind-two-alternative-blocks-market-led-pacific-alliance-and>.

² Andres Oppenheimer. "While Pacific Alliance thrives, MERCOSUR withers." *Miami Herald*, May 25, 2013. Available online at <http://www.miamiherald.com/2013/05/25/3415192/andres-oppenheimer-while-pacific.html>.

³ This paper argues the Pumas' potential internal growth motor as an asset. But this motor is not enough to power development alone.

⁴ Andrés Malamud. "Overlapping Regionalism, No Integration: Conceptual Issues and the Latin American Experiences" EUI Working Papers, RSCAS 2013/20, March 2013. Available online at http://repositorio.ulb/bitstream/10451/8216/1/ICS_AMalamud_Overlapping_WORI.pdf. Edmar Luis Fagundes de Almeida and Nicholas Trebat. "The Argentine-Bolivia-Chile Crisis." In Paulina Beato and Juna Benavides (eds.) *Gas Market Integration in the Southern Cone* (Washington DC: Inter-American Development Bank, 2004), 250.

⁵ Gas consumption in the industry and mining sector jumped from 13 million cubic meters in 1996 to 310 million cubic meters. Recent estimates expect Chile to increase annual gas-fired electricity by 26 percent between 2011 and 2015. See Felipe Balmaceda and Pablo Serra. "Chile: Energy Dependence." In Paulina Beato and Juan BenAvides (eds.), *Gas Market Integration in the Southern Cone* (Washington, DC: Inter-American Development Bank, 2004), 122. Also see Robin Yapp. "Chile's Uncertain Renewable Energy Future." *Renewable Energy World*, April 9, 2012. Available online at <http://www.renewableenergyworld.com/rea/news/article/2012/04/chile-looks-to-renewables-as-its-grid-falters>.

⁶ In Bolivia gas finds accelerated in the 2000s, with proven and probable reserves increasing over 500 percent from 8.6 TFC in 1999 to 52.4 in 2004 representing the largest reserves in South America after Venezuela. See Vicent Fretes-Cibils, Marcelo Giugale and Connie Luff. Bolivia: Public Policy Options for the Well Being of All. (Washington: The World Bank, 2006). For its part, Argentina appears on the verge of a shale gas revolution. According to the U.S. Energy Information Administration, Argentina has 774 trillion cubic feet of technically recoverable shale gas reserves, placing it third globally behind China and the US (see Ogib Research Team. "Argentina on the Verge of Shale Gas Boom." *Oil and Gas Investments Bulletin*, December 14, 2011.)

⁷ In January of 2002, the Argentine Congress passed economic emergency laws that pegged end-user charges for electricity at one peso to one dollar, while freezing rates that transmission and distribution companies could charge. This emergency measure settled into a norm, and became a massive subsidy for Argentine gas consumption—the type of distortion which Puma economies have eschewed. Facing pricing ceilings, Argentine gas firms had little incentive to sell domestically. Attracted by higher spot values across the Andes, they preferred to serve the Chilean market. This momentarily fit Chile's needs, but the rules would soon change again. See Thomas Andrew O'Keefe. "Argentina." In Sidney Weintraub, ed. *Energy Cooperation in the Western Hemisphere: Benefits and Impediments* (Washington: Center For Strategic International Studies, 2007), 212.

⁸ In 2004, La Casa Rosada sought to limit gas exports to Chile in response to a domestic shortage in Argentina. Supply restrictions held exports to Chile below 66 percent of the normal amount, jeopardizing daily Chilean operations. At some future point, Buenos Aires will likely roll back domestic gas subsidies, thus obviating suppliers' desires to export abroad (see O'Keefe, 223).

⁹ Evo Morales rose to power spearheading a rejection of plans to build a private pipeline that would move Bolivian gas to Chilean ports where it would be condensed and shipped to North America. In an astute reading of public temperament, Morales and his Movimiento al Socialismo (MAS) unleashed a string of protests and blockades in 2003 that paralyzed parts of Bolivia. The notion that neoliberals sought to "sell Bolivian gas to Chile," broadened into the No al Gas movement: a rejection of neoliberal policies that would see two presidents chased from power and a third, Evo Morales, renationalize the hydrocarbon industry.

¹⁰ Charlotte Karrlsson-Willis. "Bolivia to finally bring Chilean dispute to Hague this Wednesday." *The Santiago Times*, April 22, 2013. Available online at <http://santiagotimes.cl/bolivia-to-finally-bring-chilean-dispute-to-hague-this-wednesday/>.

¹¹ Alexandra Ulmer and Fabian Cambero. "Bachelet, ahead in Chile polls, eyes LNG to keep lights on." *Reuters*, October 1, 2013. Available online at <http://www.reuters.com/article/2013/10/01/us-chile-election-energy-analysis-idUSBRE9900ZE20131001>.

¹² Suelen Emilia Castiblanco Moreno. "El Paradigma de Internacionalización en las Relaciones Comerciales Colombo – Venezolanas, Una Mirada desde las Cadenas Productivas." *Suma de Negocios*, Vol. 2 N. 1, June 2011, 79-92.

¹³ "Dinámica Comercio Exterior: Colombia- Venezuela, 2004 – 2008." National Bureau of Statistics of Colombia (DANE) (April 2008). Available online at http://www.dane.gov.co/daneweb_V09/files/investigaciones/boletines/exportaciones/bolesp_exp_04_08.pdf.

- ¹⁴ María del Pilar Esguerra Umana, Enrique Montes Uribe, Aarón Garavito Acosta and Carolina Pulido González. "El comercio colombo-venezolano: características y evolución reciente," *Apuntes del CENES*, Vol. XXIX, No. 69, 123-162, June 2010.
- ¹⁵ Ewan Robertson. "Trade Between Venezuela and Colombia Back on Track." *Venezuela Analysis*, February 11, 2013. Available online at <http://venezuelanalysis.com/news/7727>.
- ¹⁶ Mark Weisbrot and Jake Johnston. "The Gains from Trade: South American Economic Integration and the Resolution of Conflict." Center for Economic and Policy Research, November 2010. Available online at <http://www.cepr.net/documents/publications/gains-from-trade-2010-11.pdf>.
- ¹⁷ Umana, et al.
- ¹⁸ "La lejanía entre Colombia y Venezuela." *Semana*, July 27, 2013. Available online at <http://www.semana.com/nacion/articulo/la-lejania-entre-colombia-venezuela/352263-3>.
- ¹⁹ Luisa Gómez Rodríguez (Editor, Portafolio). Interview with author. Bogotá, July 15, 2013.
- ²⁰ Source: UN Comtrade, OECD/European Commission. See <http://stage.stocks-flows.de/edit/180?lang=en>. Audi, Acura, Volkswagen, Nissan and BMW are five of many automobile companies that produce in Mexico.
- ²¹ "Two ways to make a car." *The Economist*, May 10, 2012. Available online at <http://www.economist.com/node/21549950>.
- ²² *The Wall Street Journal* report that a Mexican-made Volkswagen Jetta sold for US\$19,342, while the same car in Brazil sold for US\$28,072. See Laurence Iliff and Gerald Jeffris. "Mexico and Brazil Fix Trade Spat on Cars." *The Wall Street Journal*, March 15, 2012. Available online at <http://online.wsj.com/article/SB10001424052702303863404577284060757942448.html>.
- ²³ Ibid.
- ²⁴ From 2007 to 2011, 78.78 percent of Mexico's average annual exports were destined for the United States (2007-81.2 percent; 2008-78.9 percent; 2009- 79.5 percent; 2010-78.3 percent 2011-76 percent). Source: UN Comtrade, OECD/European Commission.
- ²⁵ Hermino Blanco Mendoza, Jaime Zabludovsky Kuper, Adalberto García Rocha and Sergio Gómez Lorz. "Brazil's Dutch Disease and the Auto Trade War with Mexico: Stylized Facts." Center for Economic Policy Research, June 14, 2012. Available online at <http://www.globaltradealert.org/gta-analysis/brazil%E2%80%99s-dutch-disease-and-auto-trade-war-mexico-stylised-facts>.
- ²⁶ Buoyant exports to Canada and the US over the same time span suggest a correlation between the restrictions and the decline. See Brandon Case. "Mexico Car Exports Drop 11% as Brazil, Argentina Limit Shipments." *Bloomberg*, March 6, 2013. Available online at <http://www.bloomberg.com/news/2013-03-06/mexico-car-exports-drop-11-as-brazil-argentina-limit-shipments.html>
- ²⁷ "Two ways to make a car." *The Economist*, May 10, 2012. Available online at <http://www.economist.com/node/21549950>.
- ²⁸ *The Wall Street Journal* report that a Mexican-made Volkswagen Jetta sold for US\$19,342, while the same car in Brazil sold for US\$28,072. See Laurence Iliff and Gerald Jeffris. "Mexico and Brazil Fix Trade Spat on Cars." *The Wall Street Journal*, March 15, 2012. Available online at <http://online.wsj.com/article/SB10001424052702303863404577284060757942448.html>.
- ²⁹ Ibid.
- ³⁰ From 2007 to 2011, 78.78 percent of Mexico's average annual exports were destined for the United States (2007-81.2 percent; 2008-78.9 percent; 2009- 79.5 percent; 2010-78.3 percent 2011-76 percent). Source: UN Comtrade, OECD/European Commission.
- ³¹ Hermino Blanco Mendoza, Jaime Zabludovsky Kuper, Adalberto García Rocha and Sergio Gómez Lorz. "Brazil's Dutch Disease and the Auto Trade War with Mexico: Stylized Facts." Center for Economic Policy Research, June 14, 2012. Available online at <http://www.globaltradealert.org/gta-analysis/brazil%E2%80%99s-dutch-disease-and-auto-trade-war-mexico-stylised-facts>.
- ³² Buoyant exports to Canada and the US over the same time span suggest a correlation between the restrictions and the decline. See Brandon Case. "Mexico Car Exports Drop 11% as Brazil, Argentina Limit Shipments." *Bloomberg*, March 6, 2013. Available online at <http://www.bloomberg.com/news/2013-03-06/mexico-car-exports-drop-11-as-brazil-argentina-limit-shipments.html>.

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- ¹ Source: Eurostat, Global Solutions
- ² Using figures from the IMF's World Economic Outlook Databases
- ³ See Samuel George. "Behind the Brazil-USA Beef." *No Se Mancha*, September 23, 2013. Available online at <http://semancha.com/2013/09/23/behind-the-brazil-usa-beef/>
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¹⁷ In 2009 a 21-year-old construction worker was shot dead as protesters attempted to occupy Shougang land. The fact that the shooting did not lead to any criminal charges remains a sore point for the community and has lent credence to the notion that Shougang operates beyond the control of Peruvian law enforcement. See Simon Romero, "Tensions Over Chinese Mining Ventures in Peru." *New York Times*, August 14, 2010. Available online at <http://www.nytimes.com/2010/08/15/world/americas/15chinaperu.html?pagewanted=all>

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Samuel George
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Global Economic Dynamics

Bertelsmann Foundation
1101 New York Avenue, NW, Suite 901
Washington, DC 20005
USA
main phone +1.202.384.1980
main fax +1.202.384.1984

www.bfna.org

