

# In the Age of Disruption: Latin America's Domestic and International Challenges



Cynthia J. Arnson, Editor

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Cynthia Arnson  
October 2018



# Introduction

Cynthia J. Arnson

Disruption seems to be a defining quality of our times.

Innovators think of disruption in positive terms—leaps of imagination and invention that transcend the limits of what seemed possible. But in politics and international relations, disruption has also come to mean the shattering of norms and basic assumptions, becoming a source of anxiety, friction, and division. The verb “upended” seems to have entered our vocabulary as never before, conjuring images of a world turned upside-down at a dizzying and at times unfathomable pace. How is this disruption experienced in Latin America and what are its consequences? This report explores two sources of disruption: first, corruption scandals and their impact on the domestic politics of Latin American countries themselves; and second, the ways that the trade policies of the President Donald Trump administration have altered the calculus around regional economic integration.

In the first instance, a stream of corruption scandals has roiled Latin American domestic politics, with each day seeming to bring new accusations of official or corporate crimes. The poster child of these contemporary scandals is the Brazilian case known as *Operação Lava Jato* (Operation Car Wash). *Lava Jato* began in 2014 as an investigation by the federal police into money laundering run out of a local gas station. In the course of the investigation, police discovered a connection between these black market financial dealings and the state-owned oil company Petrobras. Pushed forward by crusading federal judge Sérgio Moro, *Lava Jato* soon mushroomed into a sprawling investigation of bribes, kickbacks, and other illegal activity that has ensnared hundreds of members of Brazil’s political and business elite.<sup>1</sup> Those convicted, indicted, or under investigation for crimes stemming from *Lava Jato* include prominent politicians from all of Brazil’s major parties—governors, senators, mayors, deputies, presidential chiefs of staff, and two former presidents—by 2017, over 140 trial-level convictions.<sup>2</sup> CEOs of leading Brazilian companies are serving unprecedented and lengthy jail sentences. *Lava Jato*’s casualties have included Brazil’s popular former president, Luiz Inácio Lula

da Silva, who had hoped to run for president in the country's 2018 elections but was banned from doing so based on his criminal conviction.<sup>3</sup>

If the *Lava Jato* scandal has profoundly marked Brazilian politics, just as important has been its impact outside the country. One of the companies investigated by Brazilian officials was construction giant Odebrecht, a major *multilati-na* with investments and infrastructure projects throughout Latin America and around the world. Because bribes and payoffs to foreign officials and political parties were laundered through U.S. banks, and because one of Odebrecht's subsidiaries, Braskem, was listed on the New York Stock Exchange, the U.S. Department of Justice (DOJ) claimed jurisdiction under the U.S. Foreign Corrupt Practices Act. DOJ revealed that Odebrecht had paid over three-quarters of a billion dollars in bribes in 12 countries, ten of them in Latin America (See Part I).<sup>4</sup> In December 2016, the company, along with Braskem, paid a record \$3.5 billion in fines, with the bulk of the funds repaid to Brazil in addition to the United States and Switzerland.

Prosecutors in Colombia, the Dominican Republic, Chile, and elsewhere have launched their own investigations into Odebrecht's illegal payments. Perhaps the most prominent casualty was Peruvian President Pedro Pablo Kuczynski. Kuczynski denied and then was forced to admit having benefited from business dealings with Odebrecht while serving as a cabinet minister under a previous government. Kuczynski resigned in 2018 following the leak of videotapes that purported to show his political allies trying to buy votes to stave off an impeachment vote by the Peruvian congress.

While the fallout from the *Lava Jato* and Odebrecht scandals has garnered wide publicity, a seemingly unending cascade of corruption revelations has rocked the hemisphere.

- In Guatemala, government prosecutors backed by the United Nations Commission Against Impunity in Guatemala (CICIG) uncovered tens of millions of dollars in customs fraud allegedly spearheaded by former president Otto Pérez Molina and his vice president, Roxana Baldetti. Following a wave of massive street protests in April 2015—the so-called “Guatemalan Spring”—the Guatemalan legislature voted to strip Pérez Molina's immunity from prosecution. He was forced to resign and remains in prison awaiting trial;<sup>5</sup> in October 2018, Baldetti was sentenced to fifteen and a half years in prison on fraud and other charges. In September 2018, however, current Guatemalan President Jimmy Morales, himself under investigation by the CICIG for alleged illicit

campaign financing, announced that he was ending the Commission's mandate when it expired in 2019. Morales then blocked the head of the mission, renowned Colombian prosecutor Iván Velásquez, from returning to Guatemala following a trip abroad. Although overruled by Guatemala's Constitutional Court, Morales refused to allow Velásquez to return to Guatemala.

- Corruption investigations in Argentina pushed forward during the administration of President Mauricio Macri have ensnared former officials of the Néstor Kirchner and Cristina Fernández de Kirchner governments, prominent members of the private sector, and Fernández de Kirchner herself. The most explosive and potentially far-reaching revelations involve the so-called “*Cuadernos de los Coimas*” (bribery notebooks), a set of journals kept between 2005 and 2015 by a driver for a senior official of the Planning Ministry. The notebooks detail cash payments worth tens of millions and perhaps billions of dollars, solicited from private companies and individuals as bribes and kickbacks in exchange for government contracts. The notebooks were first shared with a journalist for the leading daily, *La Nación*, in January 2018; he shared them with judicial authorities prior to making their contents public beginning in August 2018. Over a dozen former government officials and corporate executives have been arrested and face a variety of corruption charges.<sup>6</sup>
- Following a three-year investigation, InSight Crime, a research group that tracks organized crime in the Americas, identified the Venezuelan regime of President Nicolás Maduro as a “mafia state,” citing the levels of penetration of state institutions by organized crime, the “industrial scale” pillage of government coffers by members of the government, and the export of criminality to neighboring states, especially through drug trafficking, among other factors.<sup>7</sup> Since 2015, the U.S. Department of Treasury has sanctioned scores of senior Venezuelan officials for a variety of abuses, including corruption-related narcotics trafficking, money laundering, and the embezzlement of state funds. Those identified by the U.S. Treasury Department as “specially designated narcotics traffickers” include former Vice President Tareck El Aissami and former chief of financial intelligence Pedro Luis Martín Olivares.<sup>8</sup> In August 2018, investigators from the U.S. Department of Homeland Security filed a federal criminal complaint against eight former Venezuelan officials and businessmen for embezzling \$1.2 billion from the state-owned oil company, PdVSA, and laundering the funds through U.S. and other foreign banks and real estate

purchases in Miami and elsewhere. Press reports indicate that Maduro and three stepsons, who are not named in the complaint, are being investigated as part of the case.<sup>9</sup> Two nephews of Venezuelan First Lady Cilia Flores are in prison in the United States following their convictions on cocaine-trafficking charges. The United States sanctioned additional high-level officials, including the Vice President and the Minister of Defense in September 2018.

- The Mexican government headed by President Enrique Peña Nieto (2012–2018) was beset by corruption scandals and accusations of conflicts of interest involving him, his wife, cabinet ministers, and governors and former governors of the ruling party.<sup>10</sup> These included revelations by a prominent journalist in 2014 that Peña Nieto’s wife had purchased a \$7 million luxury home from a contractor who had extensive business dealings with Peña Nieto when he was governor of the State of Mexico;<sup>11</sup> accusations that the government used sophisticated surveillance technology sold to the government for security purposes to spy instead on opposition journalists and human rights and anti-corruption activists;<sup>12</sup> and the thwarting of an independent investigation into the disappearance of 43 students from a rural teachers’ college.<sup>13</sup> In response to the outcry in civil society over these and other corrupt acts, the Mexican government instituted a National Anti-Corruption System in 2015. But its leaders accused the Peña Nieto government of sabotaging their efforts.<sup>14</sup> In 2018, presidential candidate Andrés Manuel López Obrador tapped into popular disgust with ruling elites—a so-called “mafia of power”—by making the fight against corruption a hallmark of his campaign.<sup>15</sup> He won a landslide victory in the July 2018 presidential election.
- In Colombia, the head of the prosecutor-general’s anti-corruption unit was arrested in 2017, accused of taking bribes from an ex-governor and other political figures being investigated for corruption, in exchange for confidential information about their cases. A subsequent investigation uncovered a network of judges and lawyers, including several former Supreme Court justices—a so-called “Toga Cartel” (*Cartel de la toga*)—who allegedly took millions of pesos in bribes in exchange for throwing off and manipulating judicial proceedings against members of congress, governors, and other politicians. The tactics included evidence tampering and planting stories in the media to undermine the credibility of witnesses, all in the interest of favorable legal decisions for the accused. The former anti-corruption prosecutor, Luis Gustavo Morena Rivera,

was extradited to the United States in 2018 because one of the bribes was allegedly solicited in Miami. Another case that rocked public opinion involved the embezzlement by local authorities of close to \$200 million in funds for school meals for poor children. Among those arrested was the former governor of La Guajira, one of Colombia's poorest provinces. By the time of the presidential election in 2018, corruption ranked as the top concern of Colombian citizens. But an August 2018 anti-corruption referendum—the fourth time that year Colombians went to the polls—failed to obtain the required threshold of votes. Nonetheless, President Iván Duque pledged to support many of the anti-corruption reforms in the legislature.<sup>16</sup>

The list could go on and on, detailing accusations against three former presidents in El Salvador, a former president of Panama, and others. Corruption itself is hardly new in Latin America,<sup>17</sup> nor are corruption scandals that have driven Latin American presidents from office.<sup>18</sup> What does seem unprecedented are the sheer dimensions of the scandals; their transnational reach; the growing, albeit uneven efforts by justice ministries, the courts, and special anti-corruption units to prosecute corruption; and the levels of popular indignation each time a new scandal is uncovered. That latter factor—rising intolerance for corruption among citizens—appears to be part of a global phenomenon. As democracy scholars Thomas Carothers and Christopher Carothers argue, more than 10 percent of countries around the world “have experienced corruption-driven leadership change,” a reflection of citizens’ “growing unwillingness to put up with corrupt behavior and other forms of bad governance.”<sup>19</sup>

Explanations for this unique moment in Latin American history appear to be both structural and institutional. Structural reasons are rooted in the historic expansion of the region's middle class during the economic boom years of the 2000s, a period followed by years of mediocre growth, recession, and the resulting strain on public budgets. According to this logic, those who have escaped poverty—some just barely—are more demanding regarding access to and the quality of public services, and thus more intolerant of corruption that diverts scarce resources from public use to private gain. Changes in communications technology, such as the ability of social media to rapidly disseminate information and spur social mobilization, is also a structural feature of the current *coyuntura* (moment in history). Institutional factors include the growing independence and capacity of judges, attorneys general, and court systems overall to prosecute cases; the critical role played by independent media and investigative journalists in publicizing

corruption; and legal and penal code reforms, such as the introduction of plea bargaining, whistle-blower protections, and wiretap laws that help prosecutors gather evidence for criminal trials. In particularly extreme cases of state penetration by corrupt criminal groups, the international community has supported mechanisms to bolster judicial capacity and reduce impunity. The two most notable regional examples at the United Nations Commission Against Impunity in Guatemala (CICIG) and the Organization of American States-backed Mission to Support the Fight Against Corruption in Honduras (MACCIH),<sup>20</sup> both of which have encountered significant resistance in their respective countries to the fulfillment of their missions. Significant anti-corruption efforts have also been advanced by the Organization for Economic Cooperation and Development (OECD) through its Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, as well as the inter-governmental Financial Action Task Force (FATF), which combats money laundering. As the Brazilian case forcefully demonstrates, U.S. laws such as the 1977 Foreign Corrupt Practices Act have also been critical tools in exposing and prosecuting acts of corruption.

## Corruption and Its Meaning for Democratic Governance

While some of the developments cited above are salutary, it is clear that the scope of corruption has also hurt democratic governance in the region.<sup>21</sup> Corruption is not only a way of doing business; rather, as former president of Brazil Fernando Henrique Cardoso indicates in his introductory essay, corruption has become a way of governing, a “fundamental mechanism for a government to gain and retain power.”

Democratic institutions, he argues, are facing a particularly difficult moment:

At the core of those problems we find the widening gap between people’s aspirations and the capacity of political institutions to respond to the demands of society. The entire political system is seen as elitist, contaminated by corruption, oblivious to people’s daily concerns.

He continues:

People perceive parties and politicians as all being involved with corruption and as responsible for the inefficiency of public services. This gives rise to

an overall reaction of indignation and, more often than not, an attitude of cynicism regarding public life.

Empirical evidence tends to support the claim that citizens in Latin America are more dissatisfied than ever with democracy as a form of government. According to the Santiago-based polling firm *Latinobarómetro* in 2017, after five consecutive years of decline, only 53 percent of the region's citizens agreed that democracy was preferable to all other forms of government. Satisfaction with democracy has also declined steadily since 2009; only 30 percent of those polled reported being satisfied, while fully 65 percent said they were dissatisfied. While the drop in satisfaction with democracy paralleled a decline in the region's economies at the end of the commodities boom, satisfaction did not recover in tandem with modest increases in growth. Thus, concluded *Latinobarómetro*, political factors, not economic ones, had more to do with the decline in satisfaction with democracy.<sup>22</sup>

Is corruption at the root of declining faith in democracy? There is strong evidence to suggest that it is an important, but not the only factor. According to Transparency International, for example, since 2012 perceptions of corruption have worsened in almost two-thirds of Latin American and Caribbean countries; this despite the various initiatives by governments, civil society, and the international community to fight corruption.<sup>23</sup> Paradoxically, it is possible and even likely that the greater visibility of corrupt acts in Latin America—because of greater transparency and institutional strengthening—has led perceptions to worsen even as the situation itself has started to improve.

That said, according to the Latin American Public Opinion Project (LAPOP), citizens in the region continue to be victimized by corruption at an alarming rate. According to LAPOP's 2016–2017 *Americas Barometer*, on average one in five individuals is a victim of corruption in any given year; and the higher the rate of victimization, the higher the perception of corruption overall. Over 60 percent of individuals in an average country believe that the majority of politicians are corrupt. Perhaps most disturbingly, those most victimized by and aware of corruption have also become more tolerant of it, and such tolerance has steadily increased since 2010.<sup>24</sup> This suggests an important degree of resignation among citizens that the corruption to which they have been exposed—being bribed by a police officer or municipal official, for example—is the only way to “get things done” and that legal remedies, to the extent they exist, are non-effective.

Both *Latinobarómetro* and LAPOP demonstrate that corruption is but one challenge to the credibility and legitimacy of democratic regimes in the region.

While corruption has become the principal concern of citizens in Brazil and Colombia, in other countries, high levels of crime and insecurity, unemployment, and the poor quality of government services top the list of public concerns. The existence of corruption makes all of these issues harder to solve while also impeding economic development. A growing number of economists have noted that, rather than “greasing the wheels” to coax results out of cumbersome bureaucracies, corruption “sands the wheels” by discouraging investment and growth.<sup>25</sup> As managing director of the International Monetary Fund Christine Lagarde put it, “corruption does serious damage to economic growth, investment, FDI, and tax revenues—and to income distribution and inclusive growth too.”<sup>26</sup>

Estimates of the annual costs of corruption are staggering: in Mexico, \$26–\$130 billion, equivalent to between 2–10 percent of Mexico’s \$1.15 trillion GDP in 2015; in Colombia, \$17.5 billion, equal to almost 10 percent of the national budget; and in Peru, \$3.6 billion, equal to 10 percent of the annual national budget.<sup>27</sup> Corruption also deepens inequalities, draining public coffers of funds that could have been spent on improving services for the poor and those with modest incomes, who are more likely to depend on the public sector for health care and education. As noted by Panamanian lawyer and former ambassador Jaime Alemán in Part I, the poor pay the highest price when corruption is rampant.

What will only be clear with hindsight is whether the current salience of corruption in Latin America marks a turning point—a combination of citizens’ intolerance for corruption coupled with the availability of effective remedies—or whether the spate of judicial activism, media investigations, and pressure from civil society will provoke a backlash intended to preserve a culture of impunity. Some of the very weaknesses that allowed corruption to flourish—a politicized and compromised judiciary, for example, or threats aimed at intimidating those seeking an end to corruption—may undermine the search for greater transparency and accountability. Powerful elites have the ability to fight back, attacking anti-corruption efforts as the enemy of social peace and national security. Latin American countries differ significantly in terms of the political will and institutional capacity to confront corruption. As the discussion in Part I indicates, Latin America stands at a certain parting of the waters; making progress in the fight against corruption through a variety of legal, cultural, and institutional channels could greatly strengthen democracy. Conversely, the failure to do so will contribute to the further erosion of the legitimacy of democratic systems.

The second source of disruption examined in this report has to do with the turmoil in international trade relations occasioned by foreign economic policies

of the Trump administration. As a candidate in 2016 and continuing during his first 20 months in office, Trump harshly criticized free trade agreements as unfair to U.S. workers and excoriated long-time allies for not contributing their share of the costs of multilateral security alliances such as the North Atlantic Treaty Organization (NATO). In his inaugural address, President Trump pledged that:

From this day forward, a new vision will govern our land. From this moment on, it's going to be America First. Every decision on trade, on taxes, on immigration, on foreign affairs, will be made to benefit American workers and American families. We must protect our borders from the ravages of other countries making our products, stealing our companies, and destroying our jobs. Protection will lead to great prosperity and strength. . . . America will start winning again, winning like never before.<sup>28</sup>

The commitment to “putting the interests and security of the American people first”<sup>29</sup> resonated deeply with Trump’s electoral base, giving voice to a sense of grievance that U.S. leadership and alliances in the decades since the end of World War II had hurt rather than benefited the United States. Trump drilled down on this message throughout his months in office, telling the United Nations in September 2018 that “[w]e reject the ideology of globalism, and we embrace the doctrine of patriotism. Around the world, responsible nations must defend against threats to sovereignty not just from global governance, but also from other, new forms of coercion and domination.” The message was clear. In the words of conservative scholar Walter Russell Mead, “for the first time in 70 years, the American people have elected a president who disparages the policies, ideas, and institutions at the heart of postwar U.S. foreign policy.”<sup>30</sup> Proponents of America First insisted that it did not mean “America alone.”<sup>31</sup> Yet a host of initiatives, from the U.S. withdrawal from the Paris Climate Agreement to the public dressing-down of NATO allies, signaled a retreat from the global alliances and economic relationships promoted by the United States since the end of World War II and cemented with U.S. leadership.

In the Western Hemisphere, the retreat from multilateralism was far from total. The Trump administration and the president himself worked closely with regional allies to devise a unified response to the crisis in Venezuela. Strong bilateral relationships with leading democratic allies—Argentina, Chile, Colombia, Peru—continued, based on pragmatism and, in some measure, a desire of hemispheric leaders not to provoke a volatile and unpredictable U.S. president. “America First”

had its most immediate and visible effect in the economic arena. During the 2016 campaign, Trump had lambasted NAFTA as “the single worst trade deal ever approved in this country,”<sup>32</sup> launching a contentious effort to renegotiate NAFTA that finally concluded in late September 2018.<sup>33</sup> Similarly, on his first full day in office, President Trump withdrew the United States from the 12-nation trade pact known as the Trans-Pacific Partnership (TPP), which would have created a free trade zone among Pacific Rim countries in Asia and the Americas that together produced 40 percent of global GDP.<sup>34</sup> (President Trump later indicated that the United States might rejoin, but it was not clear that other signatories would agree to U.S. terms.) Trade tensions between the United States and Latin American and European allies escalated further in early 2018, when the Trump administration announced substantial tariffs on steel and aluminum imports on national security grounds. Tariffs on these imports from Mexico, Canada, and the European Union were delayed until June 2018, but nonetheless spurred retaliation against U.S. products as well as rancor in numerous foreign capitals. (Argentina and Brazil were subsequently exempted from the tariffs but subject to instead to export quotas.)<sup>35</sup> By far the biggest trade drama, however, unfolded between the United States and China, with hundreds of billions of dollars of new tariffs imposed on Chinese products in September 2018. The specter of an escalating and uncontrolled trade war between the world’s two largest economies carried “downside risks” for the countries of the hemisphere, according to the IMF, creating uncertainty that could undermine the region’s fragile recovery from several years of low growth and outright recession.<sup>36</sup>

The Trump administration’s emphasis on “securing the homeland... to make it harder for terrorists, transnational criminals, and other dangerous actors to reach our country,”<sup>37</sup> was a central aspect of “America First,” leading to “zero-tolerance” policies regarding migration. It is beyond the scope of this publication to explore the changes in U.S. immigration policy under Donald Trump or the impact of immigration on the U.S. economy overall. What is important for this discussion is the way that the harsh crackdown on immigrants, a politically-charged discourse equating Latin American migrants with violent crime,<sup>38</sup> stepped-up deportations, the cancellation of Temporary Protected Status (TPS) for some Central American and Caribbean immigrants, and the insistence on building a border wall impacted the U.S. image in Latin America and other parts of the world. According to a 2017 poll by the Pew Research Center, only 22 percent of those surveyed in 37 countries trusted President Trump “to do the right thing when it comes to international affairs,” a rating below that of Russian President Vladimir Putin

or Chinese President Xi Jinping. A Pew poll one year later reaffirmed the earlier findings about a plummeting U.S. image abroad.<sup>39</sup> The Santiago-based polling firm *Latinobarómetro* reported similar findings—that in 2017 President Trump ranked a 2.7 on a 10-point scale (with zero being “very bad” and 10 being “very good”).<sup>40</sup> Gallup, too, reported in 2018 that the approval rating of U.S. global leadership had fallen to a new low, down nearly 20 points from the last year of presidency of Barack Obama.<sup>41</sup>

On specific policy issues, the 2017 Pew poll showed that disapproval rates were especially high. Seventy-six percent in the 37 countries surveyed opposed plans to build a border wall between the United States and Mexico, with opposition in Mexico standing at 94 percent. Seventy-two percent disapproved of the withdrawal of U.S. support for major trade agreements, and 71 percent opposed U.S. withdrawal from global pacts on climate change. Trump’s ratings declined precipitously in NAFTA partners Canada and Mexico. According to Pew, Trump registered the lowest confidence rating—five percent—of any U.S. leader in Mexico since Pew began polling in that country. Canadians’ confidence in the U.S. president likewise dropped to its lowest point in fifteen years, a scant 22 percent, down from 83 percent in Obama’s second term.<sup>42</sup>

For U.S. allies in Latin America and the Caribbean, the Trump administration’s approach to NAFTA appeared to walk back decades of U.S. promotion of the value of free trade and open markets. Since the debt crisis of the 1980s and 1990s, the U.S. government and international development banks had admonished, if not directly pressured, countries of the region to liberalize their economies, privatize state enterprises, and open markets to foreign competition. The embrace of market reforms was not universal—South America’s largest economy, Brazil, retains significant tariffs to protect domestic industries, and the second-largest economy, Argentina, has vacillated for decades between policies of openness and protectionism. Countries of the Bolivarian Alliance for the Peoples of the Americas (ALBA), particularly Venezuela and Cuba, have remained not only outside the free trade consensus but also directly hostile to it.

But numerous countries of the region—twelve in all—ratified their commitment to open markets by signing bilateral or multilateral free trade agreements with the United States. As a region, the Americas accounted for the largest single share of all such agreements: 12 out of the 20 signed between 1985 and 2012.<sup>43</sup> The most consequential of these was NAFTA, which took effect in January 1994. More than 20 years later, by 2016, trilateral merchandise trade among the NAFTA signatories had more than tripled, reaching more than \$1 trillion annually. This

amount was greater than the value of U.S. trade with the European Union and almost double that of U.S. trade with China.<sup>44</sup> Canada was the largest destination for U.S. exports and Mexico the second largest.<sup>45</sup> Indeed, Mexico and the United States trade over half a trillion dollars in goods and services every year, about a million dollars in bilateral commerce per minute.<sup>46</sup>

The United States at one time had led the push for regional free trade—including by promoting the Free Trade Area of the Americas (FTAA) during the George W. Bush administration, aimed at uniting all economies of North, Central, and South America and the Caribbean, with the exception of Cuba. But the United States was not alone in these integration efforts. Governments of the left, right, and center in Chile, for example, concluded FTAs with at least 60 countries following the country's transition to democracy in 1990. And capitalizing on its geographical position as a Pacific Rim country, Chile was an early proponent of Latin America's efforts to link to the fast-growing economies of Asia. Chile was one of the original signatories, along with Singapore, New Zealand, and eventually Brunei, of the Trans-Pacific Strategic Economic Partnership (the forerunner to the TPP) in 2005. Eight more nations eventually joined these negotiations: Australia, Canada, Japan, Malaysia, Mexico, Peru, Vietnam, and the United States. The agreement signed in February 2016 reaffirmed the belief that economic integration and the liberalization of trade and investment was the surest path to “bring economic growth and social benefits, create new opportunities for workers and businesses, contribute to raising living standards, benefit consumers, reduce poverty and promote sustainable growth.”<sup>47</sup>

Parallel to this effort, and involving a distinct but overlapping constellation of countries, Chile, Colombia, Mexico, and Peru came together in 2012 to launch the Pacific Alliance (PA), an ambitious effort at sub-regional integration with the explicit goal of deeper integration with Asia. The PA countries constituted almost 40 percent of regional Gross Domestic Product and fully 55 percent of the region's exports; and in 2016, they grew at a rate more than double that of the rest of the region.<sup>48</sup> Looking to boost trade and investment flows, the PA admitted four non-Latin American countries—Australia, Canada, Singapore, and New Zealand—as associate members in 2017, opening a path to negotiate trade deals as a bloc, although progress on that front has been limited.<sup>49</sup> As indicated in Part II of this report, the countries of the Pacific Alliance are exploring “convergence” with the nations of Mercosur—Argentina, Brazil, Paraguay, and Uruguay.<sup>50</sup> Although together the trade blocs represent 80 percent of regional GDP and almost 85 percent of trade, intra-regional trade in Latin America is

among the lowest in the world, something that the UN Economic Commission for Latin America and the Caribbean (ECLAC, or CEPAL in Spanish) called “worrisome.”<sup>51</sup> What the Mercosur-PA “convergence” dialogue will achieve, and how rapidly, remains to be seen; this especially in light of presidential transitions in Mexico and Brazil in 2018 and Argentina in 2019.

As Fernando Henrique Cardoso and former Chilean Foreign Minister Hernando Muñoz note in their essays in this volume, the uneven fruits of integration and globalization and the failure to reduce glaring economic inequalities within societies have produced a backlash—from those left behind and from leaders who give voice to these inequalities. This issue came to the fore during the contested 2016 U.S. presidential elections, when, out of conviction (Trump) or fear of being punished by voters (Democratic Party candidate Hillary Clinton) repudiated the TPP from which the Trump administration eventually withdrew. Clinton herself had served as secretary of state during the Obama administration when the United States and 11 other nations originally signed the TPP.

Mexico, Brazil, and Argentina constitute Latin America’s largest economies, and the economic orientation of their leaders will have an outsized impact on the future of regional integration. That said, the drive for regional integration over the last decade stands in contrast to the inward-looking policies of the Trump administration. For example, following the Trump administration’s 2017 withdrawal from the TPP, the remaining 11 nations went ahead to conclude the agreement without the United States. Led by Chile and Japan, these 11 nations signed the Comprehensive Progressive Trans-Pacific Partnership (CPTPP) in March 2018 in Santiago, Chile, stripping out several provisions that the United States had insisted upon but which other members found onerous. Hence, while Washington ramped up a global trade war against China and with a successful renegotiation of NAFTA anything but certain, the countries of Latin America accelerated their connections with one another and with other regions (Asia as well as Europe), all the while focusing on the biggest prize—trade, financing, and investment from China.

China became a “big story” in Latin America during the first decade of the 2000s, and the extent of the relationship has been well chronicled.<sup>52</sup> As the Chinese economy grew by 9–14 percent a year, Chinese demand for the region’s commodities—copper, iron ore, oil, soy—soared. Although a handful of South American countries and a small number of primary commodities accounted for the vast majority of trade, the sheer volume of commerce between China and the countries of the region exploded by 2,500 percent between 2000 and 2013, growing from \$10 billion a year in 2000 to \$257 billion in 2013.<sup>53</sup> In South America,

the commodities boom fostered rapid growth that, together with domestic social policies, contributed to historic reductions in poverty and a 50 percent increase in the size of the middle class.<sup>54</sup> China's impact on economic growth in Latin America and the Caribbean has not been uniform; its exports have hurt domestic manufacturers in Mexico, Central America, and the Caribbean. Moreover, the region's exports to China are more heavily concentrated in commodities than are the region's exports to the rest of the world: 72 percent in the case of China versus 27 percent globally.<sup>55</sup> This has given rise to fears about the "deindustrialization" of the economies of the region and their excessive vulnerability to the boom and bust cycles that characterize commodity prices.

In fact, a slowing of China's growth rates, coupled with a slowdown of the world economy overall following the 2008 global financial crisis, contributed to an economic downturn in the region from which it is only slowly recovering.<sup>56</sup> The commodities super-cycle came to an end between 2013 and 2016, and the value of the region's exports to China dropped by 25 percent; this figure rebounded in 2017, growing by 16 percent.<sup>57</sup> But the composition and value of trade between China and the region is only part of the relationship. Chinese lending has also rapidly increased, particularly in the infrastructure and energy sectors. CEPAL estimates that between 2005 and 2016, China's loan commitments to Latin America and the Caribbean totaled more than \$141 billion, with about half that amount consisting of "loan-for-oil" arrangements with countries such as Venezuela, Brazil, Ecuador, and Argentina.<sup>58</sup> In certain years, Chinese lending to the region exceeded that of the World Bank, Inter-American Development Bank, and Latin American Development Bank (CAF) combined.<sup>59</sup> That said, the European Union as a bloc remains the largest source of foreign direct investment (FDI) to the region and the United States the largest single source FDI.<sup>60</sup>

During the Obama administration, U.S. officials competed with China for influence in Latin America by emphasizing the superiority of a rules-based trading order and by throwing full U.S. support behind the TPP, part of Obama's strategic "pivot toward Asia." By contrast, Trump administration officials have cast China as an exploitive imperial power whose interests are fundamentally antagonistic to those of the region.<sup>61</sup> The December 2017 National Security Strategy of the United States, for example, notes that:

China and Russia target their investments in the developing world to expand influence and gain competitive advantages against the United States.... China seeks to pull the region into its orbit through state-led investments

and loans.... Both China and Russia support the dictatorship in Venezuela and are seeking to expand military linkages and arms sales across the region. The hemisphere's democratic states have a shared interest in confronting threats to their sovereignty.<sup>62</sup>

The narrative positing Latin America as a place of great power competition between the United States, China, and Russia, privileges geo-strategic concerns. But for most countries of the region, economic considerations are paramount. Seen through that economic lens, China represents not a threat but an opportunity, a relationship to be managed, to be sure, but a country whose capital and investments can help the region address its development challenges. As former Chilean ambassador to China Jorge Heine notes in Part II, the links between Latin America and China represent the “most important realignment in the region's international relations in the past two centuries.” China's rapid advances in infrastructure and energy development within its own borders, Heine argues, could help Latin America overcome significant deficits in infrastructure and transform regional energy production and markets.

This optimistic view of China's role in regional development is not universally shared. Among the region's democracies, there is concern about the lack of competition among and transparency of Chinese firms, the pressure to accept Chinese labor for large infrastructure projects, and the impact of Chinese investments on environmental and labor standards. The learning curve in the relationship between China and Latin America has been steep on both sides of the Pacific.<sup>63</sup> But countries of the region vary significantly in their capacity to bargain with Chinese firms and lending institutions and to manage the relationship overall. At the same time, countries appear eager to benefit from Chinese loans and investments and the sheer size of the Chinese economy. This desire is behind a shift in the region's diplomatic allegiance from Taiwan to China, a pace that accelerated in 2017–18 when Panama, the Dominican Republic, and El Salvador recognized the People's Republic. Whereas in 2008 12 of the 23 countries around the world that recognized Taiwan were from Latin America and the Caribbean, by 2018 the 12 had fallen to nine.<sup>64</sup>

Now that the NAFTA negotiations have concluded, it is likely that the United States will reexamine other trade agreements with the hemisphere. The fact that the United States enjoys healthy trade surpluses with all FTA partners other than NAFTA should help to mitigate tensions. But the smaller countries of Central America and the Caribbean are especially vulnerable. Their exports represent a small proportion of regional commerce but nonetheless constitute a huge

percentage of the GDP in CAFTA-DR countries.<sup>65</sup> As Marisol Argueta notes in Part II, keeping CAFTA-DR strong while negotiating additional intra- and interregional agreements is vital for the future of a still largely impoverished region plagued by criminal violence.

Ultimately, there are more questions than answers about the region's ability to adapt to and even take advantage of the changing political economy of U.S.-Latin American relations. Will policy changes in the United States help accelerate the growing density of integration within and outside Latin America and the Caribbean? In light of the growing antagonism between the United States and China, are there opportunities for countries of the region to expand their own market shares?<sup>66</sup> Will growth in the U.S. economy boost regional economies, or will other features of U.S. economic policy—changes in tax policy and a rise in interest rates—undermine regional prospects? Quite apart from what the United States does or does not do, is the region prepared to harness and adapt to the forces of globalization, especially the rapid evolution of technology and communications, in pursuit of sustainable growth and social welfare? What does the region's greater relative autonomy in what Argentine diplomat José Octavio Bordón calls a “polycentric” global order portend for the future?

The following pages touch on these questions and others, offering partial answers and raising other issues central to the region's democratic future and prosperity. Disruption in domestic politics and international relations unleashes forces of destruction as well as creativity. Understanding those forces is a first step toward harnessing their positive potential.

## Notes

1. See, for example, “Handling Systemic Corruption in Brazil,” a conversation with Sérgio Fernando Moro, Brazil Institute, Woodrow Wilson Center, July 14, 2016, [https://www.wilsoncenter.org/sites/default/files/bi\\_rule\\_of\\_law-sergio\\_moro\\_finalv2.pdf](https://www.wilsoncenter.org/sites/default/files/bi_rule_of_law-sergio_moro_finalv2.pdf). Former president Dilma Rousseff, who was impeached in 2016 on technical grounds, had served as chair of the board of Petrobras during the time that much of the illegal activity was allegedly taking place. She denied knowledge of the crimes and no evidence was produced to link her to them. But the scandal caused her approval ratings to plummet and contributed to the political climate in which she was removed from office.
2. Presentation by Justice Luis Roberto Barroso, Brazil Institute, Woodrow Wilson Center, “Brazil's Institutional Challenge: Showing That Corruption Will Not Prevail,” September 8, 2017, <https://www.wilsoncenter.org/event/justice-luis-roberto-barroso-brazils-institutional-challenge-showing-corruption-will-not>. See also, Claire Felter and Rocio Cara, “Brazil's Corruption Fallout,” Council on Foreign Relations, April 24, 2018, <https://www.cfr.org/backgrounder/brazils-corruption-fallout>.

3. Former President Lula was banned from running based on the *Lei da Ficha Limpa*, a statute Lula signed into law in 2010, which forbids anyone convicted of a crime by a court of appeals from running for office. Many other senior politicians have also been implicated. In September 2018, Brazil's federal police recommended that President Michel Temer be prosecuted for allegedly taking bribes while he served as vice president. Previous corruption charges against Temer were blocked by the Brazilian Congress. Scarcely a month before the October 18, 2018, election, two other leading candidates, Fernando Haddad of Lula's Workers' Party (PT) and Geraldo Alckmin of the Brazilian Social Democracy Party (PSDB) were also accused of receiving illegal contributions for prior campaigns.
4. The Department of Justice's 29-page indictment is available at <https://www.justice.gov/opa/press-release/file/919911/download>. See also, "Brazil's Institutional Challenge," op. cit.; and Matthew M. Taylor, "The Odebrecht Settlement and the Costs of Corruption," Council on Foreign Relations, December 27, 2016, <https://www.cfr.org/blog/odebrecht-settlement-and-costs-corruption>.
5. For excellent overviews, see Francisco Goldman, "From President to Prison: Otto Pérez Molina and a Day for Hope in Guatemala," *The New Yorker*, September 4, 2015, <https://www.newyorker.com/news/news-desk/from-president-to-prison-otto-perez-molina-and-a-day-for-hope-in-guatemala>; José Elías, "How the Línea Corruption Scandal Toppled Guatemala's Government," *El País*, September 4, 2015, [https://elpais.com/elpais/2015/09/04/inenglish/1441373163\\_815497.html](https://elpais.com/elpais/2015/09/04/inenglish/1441373163_815497.html).
6. An interview with Diego Cabot, the reporter for *La Nación* who first exposed the existence of the notebooks, appears in "Los cuadernos de las coimas: así registraba el recorrido de los cobros el chofer de Baratta," *La Nación*, August 1, 2018, <https://www.lanacion.com.ar/2158187-las-pruebas-asi-registraba-el-recorrido-de-las-coimas-el-chofer-de-baratta...> See also, Daniel Politi, "A Gush of Graft Plea Bargains Rivets Argentina," *The New York Times*, August 26, 2018, <https://www.nytimes.com/2018/08/25/world/americas/argentina-corruption-notebooks-kirchner.html>. Since leaving office, Fernández de Kirchner has been implicated in a number of corruption cases and has attacked the investigations as politically motivated; she enjoys immunity from prosecution as a member of the Argentine Senate. Other members of her administration are in prison or have been convicted of corruption-related crimes. One, former secretary of public works José López, was arrested in June 2016 after being caught tossing bags stuffed with cash over the wall of a Buenos Aires convent. In an unrelated case, Amado Boudou, Fernández de Kirchner's vice president and former economy minister, was convicted of "passive bribery" related to attempts to buy a large share in a firm that did business with the government. Boudou was sentenced to almost six years in prison in August 2018.
7. "7 Reasons for Describing Venezuela as a 'Mafia State,'" InSight Crime, May 16, 2018, <https://www.insightcrime.org/investigations/seven-reasons-venezuela-mafia-state/>.
8. A compilation of U.S. sanctions, executive orders, and laws regarding Venezuela appears at U.S. Department of State, "Venezuela-Related Sanctions," <https://www.state.gov/e/eb/tfs/spi/venezuela/>. El Aissami and Martín Olivares were identified as drug traffickers under the U.S. Foreign Narcotics Kingpin Designation Act. See, for example, U.S. Department of the Treasury, "Treasury Sanctions Prominent Venezuelan Drug Trafficker Tareck El Aissami and His Primary Frontman Samark Lopez Bello," Press Release, February 13, 2017, <https://www.treasury.gov/press-center/press-releases/Pages/as0005.aspx>. Canada and the European Union have also sanctioned dozens of Venezuelan officials for violations of human rights and democratic freedoms.

9. Jay Weaver and Antonio María Delgado, “Ring Plundered \$1.2 Billion of Venezuelan Oil Money, Laundered It in South Florida, Feds Charge,” *Miami Herald*, July 25, 2018, <https://www.miamiherald.com/latest-news/article215493015.html>; and Jay Weaver and Antonio María Delgado, “Venezuela’s Maduro under Investigation in \$1.2 Billion U.S. Money-laundering Case,” *Miami Herald*, July 27, 2018; <https://www.miamiherald.com/latest-news/article215663355.html>.
10. Duncan Wood, “Fighting Corruption in Mexico: Taking It to the People,” *Foreign Affairs*, June 22, 2016, <https://www.foreignaffairs.com/articles/mexico/2016-06-22/fighting-corruption-mexico>; Denise Dresser, “Can Mexico Be Saved? The Peril and Promise of López Obrador,” *Foreign Affairs*, August 13, 2018, [https://www.foreignaffairs.com/articles/americas/2018-08-13/can-mexico-be-saved?cid=nlc-fa\\_twofa-20180823](https://www.foreignaffairs.com/articles/americas/2018-08-13/can-mexico-be-saved?cid=nlc-fa_twofa-20180823).
11. See Carmen Aristegui, “La Casa Blanca de Enrique Peña Nieto,” *Aristegui Noticias*, November 9, 2014, <https://aristeguinoticias.com/0911/mexico/la-casa-blanca-de-enrique-pena-nieto/>. Peña Nieto subsequently offered a public apology and his wife returned the mansion.
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13. Eric L. Olson, “Summit of the Americas: A Regional Strategy for Democratic Governance against Corruption in the Hemisphere,” testimony before the Senate Foreign Relations Committee Subcommittee on Western Hemisphere, Transnational Crime, Civilian Security, Democracy, Human Rights, and Global Women’s Issues, April 10, 2018, <https://www.foreign.senate.gov/hearings/summit-of-the-americas-a-regional-strategy-for-democratic-governance-against-corruption-in-the-hemisphere-041018>.
14. Azam Ahmed, “Mexico’s Government Is Blocking Its Own Anti-Corruption Drive, Commissioners Say,” *The New York Times*, December 2, 2017, <https://www.nytimes.com/2017/12/02/world/americas/mexico-corruption-commission.html>.
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17. See, for example, Alfonso Quiroz, *Corrupt Circles: A History of Unbound Graft in Peru* (Washington, D.C. and Baltimore: Woodrow Wilson Center Press and Johns Hopkins University Press, 2008); Joseph S. Tulchin and Ralph H. Espach, eds., *Combating Corruption in Latin America* (Washington, D.C. and Baltimore: Woodrow Wilson Center Press and Johns Hopkins University Press, 2000); and Stephen D. Morris and Charles H. Blake, eds., *Corruption and Politics in Latin America: National and Regional Dynamics* (Boulder: Lynne Rienner, 2010).

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21. Scholars of democratization in Latin America have long been concerned with the paucity of challenges faced by democracies following transitions from authoritarianism in the 1980s and 1990s. These democratic "deficits" include the weakness of political institutions—especially parties and legislatures; widespread impunity and the absence of the rule of law; persistent corruption and clientelism; and socioeconomic and political inequality. The impact of these structural deficits on the practice of citizenship and citizen attitudes towards democracy has been profound, perhaps best summarized in the word *desencanto* (discontent). There is a vast literature on democratic transitions in Latin America and the efforts to build democratic governance and the rule of law. Among the many works, see Guillermo O'Donnell and Philippe C. Schmitter, *Transitions from Authoritarian Rule: Tentative Conclusions about Uncertain Democracies* (Baltimore: The Johns Hopkins University Press, new edition 2013); Frances Hagopian and Scott Mainwaring, eds., *The Third Wave of Democratization in Latin America: Advances and Setbacks* (Cambridge, UK: Cambridge University Press, 2005); Jorge I. Domínguez and Michael Shifter, *Constructing Democratic Governance in Latin America* (Baltimore: Johns Hopkins University Press, 2013); and Organization of American States and United Nations Development Program, et al., *Nuestra Democracia* (Mexico: Fondo de Cultura Económica, 2010).
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23. "Corruption Perceptions Index 2017," Transparency International, February 21, 2018, [https://www.transparency.org/news/feature/corruption\\_perceptions\\_index\\_2017](https://www.transparency.org/news/feature/corruption_perceptions_index_2017); Alejandro Urizar and Luciana Torchiario, "Perceptions Remain Unchanged Despite Progress in the Americas," Transparency International, February 21, 2018, [https://www.transparency.org/news/feature/perceptions\\_remain\\_unchanged\\_despite\\_progress\\_in\\_the\\_americas](https://www.transparency.org/news/feature/perceptions_remain_unchanged_despite_progress_in_the_americas).
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38. In his first State of the Union address in January 2018, Trump invited the parents of two young women murdered by violent Central American gangs. He called on Congress “to finally close the deadly loopholes that have allowed MS-13, and other criminals, to break into our country,” alleging that “open borders have allowed drugs and gangs to pour into our most vulnerable communities.” Two recent studies however, dispute the linkage of migrants and crime. A study of four decades of immigration between 1970 and 2010 found that “immigration is consistently linked to decreases in violent (e.g., murder) and property (e.g., burglary) crime throughout the time period.” Another study found that “between 1990 and 2013, the foreign-born share of the U.S. population grew from 7.9 percent to 13.1 percent and the number of unauthorized immigrants more than tripled from 3.5 million to 11.2 million. During the same period, FBI data indicate that the violent crime rate declined 48 percent—which included falling rates of aggravated assault, robbery, rape, and murder. Likewise, the property crime rate fell 41 percent, including declining rates of motor vehicle theft, larceny/robbery, and burglary.” See Robert Adelman, Lesley Williams Reid, et al., “Urban Crime Rates and the Changing Face of Immigration: Evidence across Four Decades,” *Journal of Ethnicity in Criminal Justice*, 15:1, December 18, 2016, <https://www.tandfonline.com/doi/full/10.1080/15377938.2016.1261057?scroll=top&needAccess=true>; and Walter A. Ewing, Daniel E. Martínez, and Rubén G. Rumbaut, “The Criminalization of Immigration in the United States,” American Immigration Council, *Special Report*, July 2015, [https://www.americanimmigrationcouncil.org/sites/default/files/research/the\\_criminalization\\_of\\_immigration\\_in\\_the\\_united\\_states.pdf](https://www.americanimmigrationcouncil.org/sites/default/files/research/the_criminalization_of_immigration_in_the_united_states.pdf).
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41. Gallup, “Rating World Leaders: 2018,” 2, <https://news.gallup.com/reports/225587/rating-world-leaders-2018.aspx>.
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44. Testimony of Earl Anthony Wayne [former U.S. ambassador to Mexico] before the Senate Committee on Foreign Relations, “The Economic Relationship between the United States, Canada and Mexico,” January 2018, [https://www.wilsoncenter.org/sites/default/files/earl\\_anthony\\_wayne\\_testimony\\_before\\_the\\_united\\_states\\_senate\\_committee\\_on\\_foreign\\_relations.pdf](https://www.wilsoncenter.org/sites/default/files/earl_anthony_wayne_testimony_before_the_united_states_senate_committee_on_foreign_relations.pdf). Total trilateral merchandise trade is measured by the total of each country’s imports from its other two NAFTA partners. See “North American Free Trade Agreement (NAFTA)

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  46. Christopher Wilson, *Growing Together: Economic Ties between the United States and Mexico* (Washington, D.C.: Wilson Center Mexico Institute and Development Bank of Latin America [CAF], December 2017), 38, [https://www.wilsoncenter.org/sites/default/files/growing\\_together\\_economic\\_ties\\_between\\_the\\_united\\_states\\_and\\_mexico.pdf](https://www.wilsoncenter.org/sites/default/files/growing_together_economic_ties_between_the_united_states_and_mexico.pdf).
  47. TPP Full Text, Preamble, Office of the United States Trade Representative, (undated), <https://ustr.gov/sites/default/files/TPP-Final-Text-Preamble.pdf>.
  48. Guillermo Perry and Diego Auvert, *Financial Integration in the Pacific Alliance* (Washington, D.C.: Inter-American Development Bank and Woodrow Wilson Center, 2016), vii, <https://www.wilsoncenter.org/article/financial-integration-the-pacific-alliance>.
  49. Canada, for example, already has bilateral FTAs with all four PA countries and the benefits of reopening a multilateral negotiation are unclear. In addition, there appear to be tensions between domestic producers of agricultural goods in Colombia and exporters of similar products from the Associate member countries. It remains to be seen what posture the new president of Mexico, Andrés Manuel López Obrador, will adopt toward the PA. He did not attend the yearly PA Summit in July 2018. At the same time, South Korea opened talks about becoming an associate PA member during the annual PA summit in July 2018.
  50. Colton Wade, “Mercosur and Pacific Alliance Push for Integration in Moment of Convergence,” Think Brazil blog, Brazil Institute, Wilson Center, June 8, 2017, <https://www.wilsoncenter.org/blog-post/mercosur-and-pacific-alliance-push-for-integration-moment-convergence>.
  51. According to CEPAL, only 16 percent of exports by Latin American and Caribbean countries are to other countries of the region, compared with 50 percent in East Asia and North America and 64 percent in the European Union. See CEPAL, *La convergencia entre la Alianza del Pacífico y el Mercosur: Enfrentando juntos un escenario mundial desafiante* (Santiago: Comisión Económica para América Latina y el Caribe, 2018), 5.
  52. Key works include Margaret Myers and Carol Wise, eds., *The Political Economy of China-Latin America Relations in the New Millennium: Brave New World* (New York: Routledge, 2017); Ricardo Lagos Escobar and Enrique Iglesias García, *América Latina, China, y Estados Unidos* (Mexico: Fondo de Cultura Económica, 2015); Julia C. Strauss and Ariel C. Armony, *From the Great Wall to the New World: China and Latin America in the 21st Century* (Cambridge, UK: Cambridge University Press, 2012); Kevin P. Gallagher and Roberto Porzecanski, *The Dragon in the Room: China and the Future of Latin American Industrialization* (Stanford: Stanford University Press, 2010); R. Evan Ellis, *China in Latin America: The Whats and Wherefores* (Boulder: Lynne Rienner, 2009); and Rhys Jenkins and Enrique Dussel Peters, *China and Latin America: Economic Relations in the 21st Century* (Bonn and Mexico City: German Development Institute and National Autonomous University of Mexico, 2009).
  53. Cynthia J. Aranson and Jorge Heine, eds., *Reaching Across the Pacific: Latin America and Asia in the New Century* (Washington, D.C.: Woodrow Wilson Center Latin American Program, 2014), 10.

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56. "Latin America Faces Policy Dilemmas Post Boom," World Bank, April 12, 2016, <http://www.worldbank.org/en/news/press-release/2016/04/12/latin-america-faces-policy-dilemmas-post-boom>; "The World Bank in Latin America and the Caribbean," World Bank, last updated May 2, 2018, <https://www.worldbank.org/en/region/lac/overview>.
57. ECLAC-CEPAL, *op.cit.*, 39.
58. *Ibid.*, 23.
59. Boston University's Global Development Policy Center publishes annual reports on the trade, investment, and financing relationship between China and Latin America and the Caribbean. See: <http://www.bu.edu/gdp/initiatives/gci/latin-america-and-the-caribbean/>.
60. CEPAL, *La Inversión Extranjera Directa en América Latina y el Caribe* (Santiago: ECLAC/CEPAL, 2018), 12, <https://www.cepal.org/es/publicaciones/43689-la-inversion-extranjera-directa-america-latina-caribe-2018>. For an analysis of trends in China's FDI in the region, see Rolando Avendano, Ángel Melguizo, and Sean Miner, "Chinese FDI in Latin America: New Trends with Global Implications," Atlantic Council and OECD Development Center, 2017, <http://publications.atlanticcouncil.org/china-fdi-latin-america/>.
61. On the eve of a trip to Latin America, for example, Secretary of State Rex Tillerson had this to say: "China – as it does in emerging markets throughout the world – offers the appearance of an attractive path to development. But in reality, this often involves trading short-term gains for long-term dependency.... China's offer always come at a price – usually in the form of state-led investments, carried out by imported Chinese labor, onerous loans, and unsustainable debt. The China model extracts precious resources to feed its own economy, often with disregard for the laws of the land or human rights.... Latin America does not need new imperial powers that seek only to benefit their own people." Rex W. Tillerson, Remarks, "U.S. Engagement in the Western Hemisphere," University of Texas at Austin, February 1, 2018, <https://www.state.gov/secretary/20172018tillerson/remarks/2018/02/277840.htm>.
62. The White House, "National Security Strategy of the United States," December 2017, 51, <https://www.whitehouse.gov/wp-content/uploads/2017/12/NSS-Final-12-18-2017-0905.pdf>.
63. For an especially illuminating work on the management of China's role in extractive industries, see Cynthia A. Sanborn and Víctor Torres C., *La Economía China y las industrias extractivas: Desafíos para el Perú* (Lima: Universidad del Pacífico, 2009).
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Part I.

# Domestic Disruption: The Political Impact of Corruption in Latin America



# Corruption and Politics: A Sociologist's Viewpoint

Fernando Henrique Cardoso

The subject of my talk today will be the impact of global economic transformations on the crisis of Latin American representative democracy and the acceleration of that crisis due to corruption, with special attention to the case of Brazil.

## Twentieth-Century Transformations

In the 1970s, influenced by the seminal essay by Albert O. Hirschman, *A Bias for Hope*, I gave a talk here in Washington with the title, "A Bias for Democracy."<sup>1</sup> At that time, we endured the so-called *anos de chumbo* (years of lead) in Latin America. Our countries were torn apart by dictatorships and the logic of the Cold War. For good reason, the cause of my generation was economic development and the restoration of democracy.

In the 1990s, with the return of democracy, our passion became the fight against social inequality, a goal impossible to achieve without the stabilization of the economy. The world was changing. Great technological transformations were paving the way for robotization, the Internet, the revolutions in communication and transports. The transformations driven by the process of globalization enhanced the resurgence of neoclassical economy in academic life and of economic liberalism in politics.

This new world, structured around private multinational companies that were evolving into global companies, was bound to reduce the traditional functions of nation-states. A new ideology was on the rise, branded as "neoliberalism" by its critics. After the fall of the Berlin Wall, the Pax Americana coexisted with a Europe starting its process of integration and an emerging China, allied with global corporations.

In such a context, it is easy to understand why most of the Latin American left opposed globalization, understood as a threat to national independence and a

surrender of the elites to neoliberalism. In counterpoint to globalization and, to a lesser extent, to representative democracy—deemed formal or bourgeois—groups looked back and in some cases gave a new lease on life to the “national populism” prevalent in the 1950s and 1960s.

At the end of the 1990s and in the first decade of the 2000s, populism was born again in the Peronism of the Kirchners, the Bolivarianism or “Socialism of the Twenty-First Century” of Hugo Chávez—and even in Lula’s government in Brazil, although with a moderate tone in this case. In Venezuela, Chávez emerged as a superstar with his mix of verbal populism, distributive politics, and strong anti-American rhetoric, anchored in the Cuban experience and, more recently, in the economic and political interests of China and Russia.

This regressive trend did not become hegemonic in the region. Chile and Uruguay, countries with some tradition of social revolutionary movements, did not follow this path. The democratically elected governments of the *Concertación* in Chile and of the *Frente Amplio* in Uruguay were concerned with promoting sound economic policies as well as integrative social policies. The populist wave was also rejected by Colombia, where successive governments stood for democracy to deal with the threat posed by narco-trafficking and the revolutionary guerrillas. Even in Bolivia and Ecuador, politics of social inclusion were implemented together with more responsible economic policies.

It is within the framework of these uncertain but resilient democracies that a new crisis is now unfolding.

## Institutions under Stress

Before I qualify what occurs now in Latin America, let me stress that even in the regions where representative democracy is more deeply rooted—the Americas and Europe—institutions are facing a bad moment. At the core of those problems we find the widening gap between people’s aspirations and the capacity of political institutions to respond to the demands of society. The entire political system is seen as elitist, contaminated by corruption, oblivious to people’s daily concerns.

This phenomenon is neither local nor transitory. It is embedded in a broader economic, social, and moral transformation that affects society as a whole.

Some thinkers go as far as to speak of a “paradigm shift,” a “civilizational change.” It is one irony of our age that this deficit of trust in political institutions coexists with the rise of citizens’ increasing capacity to make the choices that shape their lives and the future of their societies. Shift, change, transformation, mutation

are key contemporary words. Everything seems to be in a state of flux, a situation fraught with risks but also with opportunities for reinvention.

When I was a university student and, a bit later, when I started to teach Economic History at the University of São Paulo at the beginning of the 1950s, it was fashionable to talk about change: social change, education for change, and so forth. There was passionate debate about the consequences—positive and negative—of what Eric Hobsbawm called “the era of imperialism.”<sup>2</sup> Despite amazing levels of human exploitation, the progress of industrialization and urbanization gave rise to a new culture based on secularization, separation between state and religion, and individualization.

On the negative side were the colonial expansion of Europe and the formation of an economically prosperous “center,” with control over technology and capacity to accumulate capital, in contrast to an immense “periphery,” dependent on the center when not colonized by it.

Throughout a long period, extending from the American Independence and the French Revolution to the Second World War and its political consequences in the fifties, the institutions of representative democracy gained ground in the West. Nazi fascism was defeated, Communism was contained. This is the world that is now being affected by the mutations that we have described as a “crisis.”

## The Communication Revolution

At the core of the civilizational change are technological transformations, to keep it simple: “the communication revolution” and its impact in society, economics, and culture. The classical distinction by Ferdinand Tönnies between “community” (the locus of people’s face-to-face experience with each other) and “society” (the kind of social organization in which people relate more formally through norms and contracts) needs to be revised.<sup>3</sup> Today the tribes formed in the Internet link people to each other without the intermediation of formal organizations. Like-minded communities of all kinds are created, transcending any barrier, including national frontiers.

On another level, the optimistic hope of Karl Mannheim, with his trust in planning and the positive outcomes of a rational world, is being replaced by a more pessimistic and particularistic culture.<sup>4</sup> The emphasis today is on race and culture differences. The politics of identity challenges the politics of class, contrary to previous expectations that social and economic differences would prevail over differences based on culture and race.

In this brief review we could also mention other classical thinkers such as Karl Marx, who stressed the connections between the forms of organization of production and the forms of sociability.<sup>5</sup>

Or David Émile Durkheim, concerned with the impact of demographic growth and industrialization over social cohesion.<sup>6</sup> And even Max Weber, who called attention to the power of rationalizing bureaucracies and the ability of charismatic leaders to challenge the oppressive monotony of bureaucratic routine.<sup>7</sup> All these categories need to be updated to help us understand the newness of contemporary societies.

## The Political Disconnect

Why, then, do we talk about the crisis of representative democracy when the mutation we are witnessing is much more profound?

The “world of yesterday”—based on the society of classes with its political institutions, parties, representing different class interests and values and embedded in ideologies—no longer exists as it existed before. Political parties are institutions born in the nineteenth century. As mass organizations that encompassed people “outside” the world of power, socialist and communist parties enlarged the legitimacy of democratic institutions. But the old forms of sociability and links of cohesion have been overturned by the fragmentation of society, the rise of new occupations, and the intense social mobility of contemporary societies.

These profound transformations in the fabric of contemporary society led to a disconnect between the political system (the parties) and society (the people). The cleavages, tensions, and conflicts in today’s globalized world are determined by a set of disparities of a different nature.

Twenty years ago, many in the so-called South feared that globalization would increase the distance between a rich North and a poor South. Not only did this not happen—it is enough to look at China’s world role or poverty reduction in several southern countries—but something totally unexpected did happen. Within each “rich” country, there are the “winners” and “losers” of globalization. The French sociologist Pascal Perrineau speaks of a new division between the “happy” and the “unhappy” with globalization.<sup>8</sup> That is, those who feel at ease in the new global environment and those who feel victimized by forces beyond their control, leading to a profound sense of personal and social loss.

Is this phenomenon not confirmed by the overwhelming pro-Trump vote in the U.S. “rust belt”? Or by the pro-Brexit vote in the depressed rural and industrial

regions of England? Or, conversely, the victory of Macron in France—was it not achieved with the massive support of the prosperous cities and regions which see the European Union as an asset not a threat? Who can deny that the working class and the union-based voters of the British Labor Party supported Brexit in the same way that the workers who voted for the Communist Party in France migrated in large numbers to Marine Le Pen?

## Neo-Populism

What united these voters? Old class consciousness or the new feeling of loss or gain with the transformations in their society?

New majorities are being formed around messages and leaders who vocalize them. One narrative (Trump, Le Pen) relies on fear, anger, and hate; another (Macron) on hope, competence, and self-confidence. This neo-populism based on fear of the future has a meaning that is quite the opposite of Latin American populism, which was nationalistic but wanted economic development and social inclusion.

Today's populism in Europe and the United States is also nationalist, but in the sense of a “regressive utopia,” the longing for the return to an idealized past. It also supports the social exclusion of minorities, immigrants, and all other kinds of people that do not conform to its adherents' moral prescriptions. In an unexpected twist of history, Arabs, “Mexicans,” Africans—all coming from regions torn apart during the era of colonial-imperialist expansion—now appear as the contemporary ‘barbarians at the gate’ of civilization. Walls and prohibitions are invoked to keep America for the Americans or France for the French.

In another paradox, the same web that connects corporations, flows of capital, and technology across the globe also connects terrorist cells, launders dirty money, and empowers cyber pirates.

In a nutshell: the crisis we are now living is the emergence of what could be called the “contemporary society,” or the “network society” that is driving away the “modern society” created by the Industrial Revolution. Of the world of yesterday, we see only the ruins. Of the emerging world, only the shadows.

## Contemporary Latin America: The Case of Brazil

This overall process of change evidently affects Latin American societies. But there are some specifics. Many of our countries, after getting rid of the military regimes of the Cold War period, tried to rebuild pre-existing democratic forms



## Of the world of yesterday, we see only the ruins. Of the emerging world, only the shadows.

whose structure reflected oligarchical societies. In some cases, there was a kind of fusion between previous democratic forms and populism, supported by the many who wanted a place in the sun in the urban-industrial society. In other countries, depending in part on the “volume and density” of societies, to quote from Durkheim, the relatively small number of those demanding access to modernity, mainly to universal social services provided by governments, facilitated the establishment of democratic rules in the European and American tradition.

Countries with large populations and those more affected by populism had much greater difficulty making this adjustment. All, however, suffer the effects of what I call “the rise of contemporary societies” and of globalization.

I now turn to the case of Brazil. In our country as in others, the overall crisis of politics is enhanced by a moral crisis arising out of the disclosure of a widespread system of corruption.

First, a statement: today’s collapse is the result of the persistence of a political culture based on patronage and corporatism, at the very moment that Brazil made the transition from modernity to contemporaneity. Patterns of electoral behavior and power mechanisms that were traditionally accepted now appear as dissonant and intolerable. An informed public opinion is now aware of the evidence of corruption at a systemic level.

The institutional framework of Brazilian democracy was established by the Constitution of 1988. A landmark in the transition to the rule of law, the Constitution was approved one year before the fall of the Berlin Wall. It incorporated several inconsistencies in the economic sphere while affirming political and civic rights, including in the social sphere. It granted full freedom for the organization of political parties and ensured their partial public financing. The president of the republic is elected by an absolute majority of at least 50 percent plus one vote. With 28 political parties represented in parliament,

the parties of elected presidents never got more than 20 percent of the seats in parliament.

This situation made it imperative to form parliamentary alliances in order to govern. The seats of the three main parties, PT, PMDB, and PSDB—and they hardly ever join forces—combined account today for less than 200 out of 513 seats in the Chamber of Deputies. To succeed in approving legislation, governments depend on alliances between parties.

A political scientist, Sergio Abranches, calls this hybrid presidentialist formula “coalition presidentialism,” *presidencialismo de coalizão*.<sup>9</sup>

Given the persistence of patterns of patronage and corporatism—complacent, to say the least, with favor and privilege, the executive builds political alliances by sharing power through the nomination of politicians to public entities of the state and to public companies. When it was possible to form congressional majorities based on three or four large parties, this system seemed less corrupt. The parties composing the alliance were united, at least formally, in their support of the presidential candidate’s program before the election.

## Governing through Cooptation

The election of Luiz Inácio Lula da Silva coincided with two independent and positive developments.

First, the presentation prior to the election of a “Letter to the Brazilian People” in which Lula promised to follow the basic principles of the previous government in economic and financial matters: floating exchange rates, a system of targets to control inflation, and compliance with law of fiscal responsibility, which imposed limits on the expansion of public spending.

Second, the terms of trade in international commerce evolved in favor of the commodity-producing countries, insofar as China increased drastically its imports of foods and raw materials. The end result for Brazil was economic growth, high levels of investment, and the acceleration of social inclusion, which was already improving.

Missing this favorable opportunity to move ahead with an agenda of constitutional reforms was a mistake of Lula’s government, then enjoying a positive internal and external environment.

It chose to focus on strengthening its base of support inside and outside Congress. In so doing, it opened the doors of the state to a large and heterogeneous conglomerate of political parties, big and small, “rightist” or “leftist.” The

Lula government also ensured access to state funds for private companies arbitrarily designated as “national champions.”

Sooner rather than later, politicians realized the advantages of creating new parties, no matter how small in size or vague in ideas.

The first big corruption scandal—the so-called *mensalão*—erupted in the midst of Lula’s first term. A congressman denounced that dozens of members of parliament were receiving monthly illegal financial contributions in exchange for support for the government. This was the turning point, the beginning of a new phase, that of a ‘presidential system by cooptation.’

Certainly, corruption in Brazil is an ancient practice, as are nominations for government posts in exchange for political support. However, the misdeeds in the past were either individual acts or a mix of patronage with leniency, not a fundamental mechanism for a government to gain and retain power.

After the *mensalão*, corruption continued as if nothing had happened, reaching an all-encompassing level 10 years later with the so-called *petrolão*, the scandal initially centered on Petrobras. Over the last several years, investigation of the Operation *Lava Jato* (Car Wash), led by the Federal Police and the judiciary, gradually disclosed the systemic nature of corruption in Brazil. The consequences for the political, institutional, and moral fabric of the country are overwhelming.

## Public–Private Complicity

In a distortion of Antonio Gramsci’s idea of hegemony, the blind ambition to hold power for as long as possible paved the way for the ideological justification of the illegal financing of the Workers’ Party and its so-called allied parties.<sup>10</sup> This endeavor was facilitated by the expansion of the economy and the fraudulent manipulation of state funds. The government ensured a steady supply of cheap public credit to national companies investing in Latin America, Africa, and even globally.

This created a web of complicity between important sectors of the Brazilian economy and the parties in power. This interconnection, not to say connivance, between public and private interests was accepted by society at large. Lula’s programs of social inclusion somehow granted a kind of *urbe et orbi* absolution to any transgression.<sup>11</sup> At least for a while.

The proliferation of political parties, the transformation of electoral campaigns into costly “show business,” the personal corruption of political agents, the complicity of public and private companies, ultimately led to the endless series of scandals denounced by the judiciary and the media.



People perceive parties and politicians as all being involved with corruption and as responsible for the inefficiency of public services. This gives rise to an overall reaction of indignation and, more often than not, an attitude of cynicism regarding public life.

Some argue that the use of a “slush fund,” an undercover second cash account to finance electoral campaigns, allowing candidates and parties to receive funds not declared to the electoral authorities was a commonplace practice. Commonplace perhaps, but certainly not generalized. What is new is not only the amount of funds received, both as campaign donations and as money illegally diverted from contracts with the public sector. What is also new is the dissemination of this “system” throughout the public sector and the involvement of top members of the federal government in its organization and spread. To give one example: in the last electoral campaign, one single private company officially donated around \$100 million. And this same company (a meat processor and exporter) made official donations to several parties, including to parties in opposition to government.

As we speak, several top leaders of the Workers Party are in jail, and several more are either free on bail or awaiting trial. And note that the accused do not belong only to the PT. Leaders of almost all parties, including some from the opposition to the previous government, as is the case of my own party, are experiencing the same predicament.

From the standpoint of society, the impact of these malpractices is perceived as a moral disaster. People perceive parties and politicians as all being involved with corruption and as responsible for the inefficiency of public services. This gives rise to an overall reaction of indignation and, more often than not, an attitude of

cynicism regarding public life. The “moral question,” which seemed to be a concern of the educated middle classes, has now become a concern of the people at large.

## A New Political Algorithm

The interconnection between access to information and the demands for transparency and accountability will probably lead to substantive improvements in our democratic experience—starting with the disclosure of the corrupt foundation upon which political power was based (and perhaps still is).

Brazilian institutions have proved their resilience. The Federal Police, the attorney general, and the judiciary are acting with the autonomy and independence granted by the Constitution. Younger judges and prosecutors are well equipped to use new legal dispositions such as the plea bargain to foster their investigations.

Brazil is a signatory of the international conventions to fight organized crime, especially tax evasion and money laundering. The exchange of information with other countries has also helped to disclose crimes of corruption and bribery that in the past would have remain undetected.

Let me give one more example of how things have changed for the best despite the complexity of the present crisis.

In the past, confronted with a crisis like the current one, we Brazilians would be speculating about the attitude of the four-star generals. Today most of us do not even know their names, while the names of the 11 justices of the Supreme Court are household names. The Supreme Court, as guardian of the Constitution, has the final decision. It decides and that’s it.

The communications media—mainstream and social media—are fulfilling their role: they anticipate what is going to happen, and they criticize any and all acts of corruption or threats to the democratic process. Brazil enjoys full freedom of the press. Governments and parties dislike and criticize the media (as I did when in the presidency), but the media exercise their critical independence which is essential to the preservation of democratic values and of a climate of freedom.

The algorithm of politics has changed. It is time to reweave the threads between society and politics, citizen action and representative democracy, *demos* (the people) and *res publica* (the republic, or state).

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# Understanding the Historical Dimensions and Current Salience of Corruption in Latin America

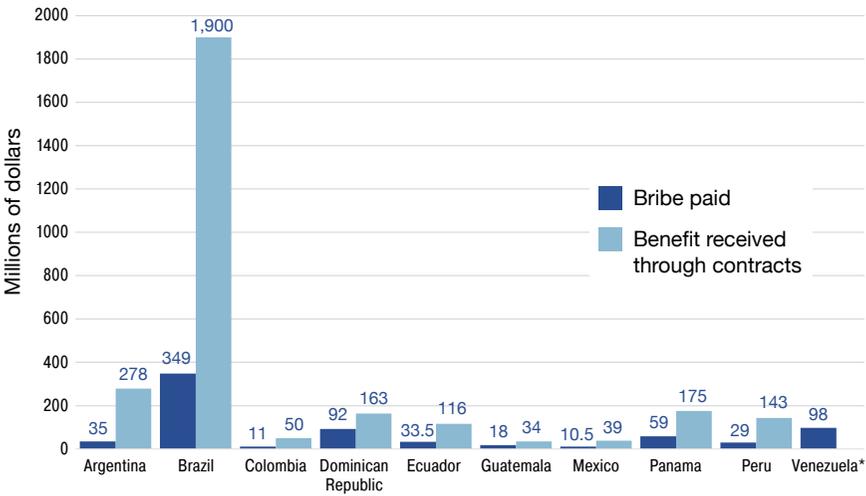
Daniel Zovatto  
Margarita López Maya  
Rafael Fernández de Castro  
Arturo Valenzuela

Why has corruption now emerged as one of the dominant political issue across Latin America? What are the implications for the region's still fragile democracies? Does the issue reflect or transcend partisan politics? How has the fight against corruption shaped regional politics?

These and other questions are addressed by four prominent Latin American political analysts: Daniel Zovatto, regional director for Latin America and the Caribbean of the International Institute for Democracy and Electoral Assistance (IDEA); Arturo Valenzuela, senior Latin American advisor for Covington & Burling, LLP, and former U.S. Assistant Secretary of State for Western Hemisphere Affairs, Margarita López Maya, professor emeritus at the Center for Development Studies, Central University of Venezuela; and Rafael Fernández de Castro, director of the Center for U.S.-Mexican Studies at the University of California, San Diego. We are grateful to Sarah Chayes, senior fellow with the Rule of Law Program at the Carnegie Endowment for International Peace, for her contribution to this exchange.

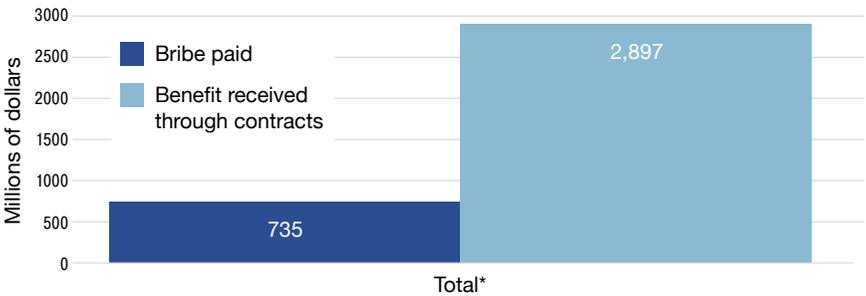
*Corruption is far from new in Latin America. Spanish colonial officials were famous for extracting resources both to benefit the imperial power and for personal profit. Scandals during the 1990s would lead to the ouster or criminal conviction of presidents in Brazil, Venezuela and Peru.<sup>1</sup> But since 2014, the issue has exploded, shaking governments across the region. The Odebrecht scandal alone—involving a Brazilian construction company that used bribery to secure billions in construction contracts—has*

**Figure 1. Odebrecht's Bribes and Benefits Received in Latin America, by Country**



\*Data on contracts not available for Venezuela.<sup>3</sup>

**Figure 2. Odebrecht's Bribes and Benefits Received in Latin America: Aggregate**



\*Total does not include bribes paid to governments in countries outside of Latin America (Angola and Mozambique). The totals including Angola and Mozambique are \$788 million in bribes paid and \$3.4 billion in benefits received.

Source (Tables I and II): United States District Court, Eastern District of New York. *United States v. Odebrecht S.A.*, December 21, 2016, <https://www.justice.gov/opa/press-release/file/919916/download>.

*tainted politicians and government officials in at least 10 Latin American countries, not including countries in Africa and Europe.*<sup>2</sup>

*What has changed in recent years? Is it the nature of corruption? Or Latin American tolerance for official malfeasance?*

**Daniel Zovatto:** First, we are talking about large-scale, grand corruption by both public and private actors at the highest levels. We are talking about a system that is much more complex and sophisticated, as well as more visible. According to Transparency International, *Latinobarómetro*, the World Bank, and others, levels of corruption as well as the perception of corruption vary a great deal from country to country, but the issue is increasingly viewed as one of the region's principal challenges.

Second, the issue is linked to the profound social transformations that Latin America has experienced over the last twenty years. Sixty to 70 million people have moved from poverty into the middle class as a result of the commodity boom that has now ended.<sup>4</sup> There is a new middle-class that is less tolerant and accepting of corruption and more demanding of transparency. Information is shared more widely as a result of social networks, and civil society itself is more mobilized. I think that for the first time the issue of corruption is making us feel ashamed as Latin Americans. The old notion that “he steals but he gets things done” (*roba pero hace*) is a thing of the past. This is a tremendously positive cultural change.

And third, for the first time, the issues of corruption, influence peddling, and conflicts of interest are being linked with the issue of the financing of political campaigns. In the past, these things were studied separately. But the cases of Brazil, Chile, Argentina, and Guatemala and many others demonstrate this interconnection.<sup>5</sup> We must examine corruption from a much more holistic perspective, relating the issue of the financing of campaigns with corruption, influence peddling, and conflicts of interest.

Odebrecht's financing of the political campaigns of a wide variety of political parties has raised issues that are completely new to Latin America. Odebrecht exported not only high-quality infrastructure projects; it also provided fundamental support to presidents of the right and the left in at least 10 Latin American countries, helping them in many cases to win elections.<sup>6</sup> After supporting the campaigns, the company would cash in. This regionalization of corruption requires us to adopt a new framework of understanding.

**Rafael Fernández de Castro:** There are three major problems, major obstacles to our welfare in Latin America: violence, social injustice or inequality, and corruption. The most oppressive problem today is corruption. That's the problem that depresses us most and that angers us most. Something has erupted in Mexico over the past two or three years—I would describe it as a kind of perfect storm of three major corruption cases that reached the presidency itself.<sup>7</sup>

Organized civil society has emerged as never before to say, “we have to do something against corruption.” Mexico’s General Law of the National Anti-Corruption System of July 2016 is very complex, but if put into effect could signify real change.<sup>8</sup> The law creates three important figures: a citizen committee to monitor compliance, an anti-corruption prosecutor, and an attorney general. Selection of the committee went very well—there will be leaders able to monitor everything within the system.<sup>9</sup> The anti-corruption prosecutor will be a very important figure, but he or she should have been named in 2014 and due to political gridlock, the incoming president will have to nominate a new anti-corruption prosecutor. The prosecutor general (*procurador general*) changes to an attorney general (*fiscal general*), but again, political polarization has hindered the process.

There is something very exciting going on in Mexico: civil society has said “*ya basta!*” The number one issue in Mexico’s 2018 elections was corruption. The elections were, in my view, some of the most important in Mexican history: not only the presidency was in play but also Congress, plus 30 of the 32 states had some kind of vote for local and state representatives and governors.<sup>10</sup>

*Latin American democracies are still relatively young; much of the region transitioned from military rule in the 1980s. Are the region’s political parties and government institutions strong enough to cope with these scandals?*

**Arturo Valenzuela:** In my opinion we are still facing the issue of democratic consolidation in Latin America. We should remember that between the 1930s and the 1980s in Latin America, about 40 percent of all changes in government came through *golpes de estado*. We should remember also that in the 1960s and 1970s, only three countries avoided the military authoritarianism of this period. We are still in the process of consolidating democratic institutions that are fragile in many places. In fact, the countries with least corruption are those that have a long history of democracy. Democracy itself contributes to the consolidation of rule of law.

Latin America has a governance problem. Eighteen presidents have not finished their terms in the post-Cold War era. Only two of these—[Jean-Bertrand] Aristide of Haiti and [Manuel] Zelaya of Honduras—were ousted in coups.<sup>11</sup> These governance problems arise to a large degree from the presidential system with separation of powers which forces minority presidents to buy—I'm just telling it like it is—the legislature. How do they buy the legislature? They turn to the private sector. And this effectively creates a monster. To return to Daniel Zovatto's point: we need to reform political financing plus electoral systems plus political parties. And recognize that some institutions—such as presidentialism in Latin America—are not working well.

*We tend to think of Latin American politics in terms of the left/right divide. Has corruption altered this construct for understanding Latin American politics?*

**Margarita López Maya:** I believe leftist governments have certain characteristics that we need to acknowledge. But Venezuela is a case that is so extreme that it departs from the rest of the region. The left, at least in my country, was profoundly anti-liberal. And that produced rhetoric during the eighteen years of *chavista* government against representative democracy. The government of President Hugo Chávez destroyed institutions that provided a counterweight to the concentration of political power. The *chavista* populist project also completely rejects handing over power. The idea of alternating political power is not in its DNA.

Corruption in Venezuela is different from what it was in the past, but it is also different in Venezuela than it is in other countries. In Venezuela it is a way of exercising power. The legacy of President Chávez's charismatic rule is of patrimonial control. When the charismatic leader leaves, he appoints his successor in an almost religious way. It is as if they are saying, 'We who govern Venezuela have the right to do so because we are the sons of Chávez, we are the disciples, we knew him, we interpret his legacy.' Public employees are selected for their loyalty to *chavismo*. The regime is non-modern, illegal, and irrational. The government has been apportioned among Chávez's relatives and military colleagues, who use and distribute state resources for their personal benefit. The military itself owns a conglomerate consisting of more than 20 companies ranging from mining, banks, construction, and agriculture.

The strength of the current government of Nicolás Maduro lies in the cohesion of this corrupt, mafia-like military-civilian leadership that enjoys not only vast

privileges but also impunity. Corruption is generalized and unrestrained, leading to obscene levels of enrichment that have erased the boundary between public and private gain. The political “tribes” that govern Venezuela have been transformed into criminal networks whose cohesion impedes divisions of the bloc in power as well as the possibilities for a democratic outcome.

Corruption allowed organized crime to penetrate the state. Crime is rampant. The situation of generalized violence is such that people fear leaving the house after 6 p.m. There are zones where the state is breaking into pieces.

Rafael Fernández de Castro’s observation about Mexico reminds me that, in Venezuela in the 1980s and 1990s, we were scandalized that corruption was implanted within our liberal representative democracy. As a result, representative democracy was discredited, providing fertile ground for the emergence of a charismatic leader. During those years the organized middle class, civil society, took to the streets demanding more transparency, a better quality of urban life. But in the end, in the late 1990s, we saw the emergence—through elections—of leftist populism.

**Rafael Fernández de Castro:** There was a great debate in Mexico in advance of the 2018 elections, in which the candidate on the white horse was Andrés Manuel López Obrador (AMLO), who led in all the polls. He is clearly an enormously polarizing figure. The polarization we see in the United States is also reflected in our own countries. The elite has turned López Obrador into someone worse than Hugo Chávez. At the same time, the verbal violence in AMLO’s ads was incredible—calling government officials “pickpockets” or “thieves.” But these ads were created with great intelligence, based on what focus groups were able to demonstrate: that people are very angry about what has happened over the six-year term [of President Enrique Peña Nieto]. Despite all the criticism and despite being depicted as Hugo Chávez, López Obrador won the presidency in good measure because he represents the fight against corruption.<sup>12</sup>

*Corruption scandals have erupted in most of Latin America, but the issue does not affect all countries to the same degree. What can be and is being done to hold officials accountable?*

**Daniel Zovatto:** Corruption is endemic to the region, but there is diversity among countries.

Venezuela, Guatemala, Haiti, and Nicaragua have the worst indicators. Argentina, Bolivia, Ecuador, and others are at the next level but still pretty bad.

**Table 1.** Corruption scores in Latin America

Country	Score	Global Rank	Factor 1. Constraints on Government Power	Factor 2. Absence of Corruption	Factor 3. Open Government
<b>Uruguay</b>	0.71	22	0.76	0.76	0.71
<b>Costa Rica</b>	0.68	24	0.79	0.68	0.72
<b>Chile</b>	0.67	27	0.71	0.69	0.71
<b>Argentina</b>	0.58	46	0.63	0.53	0.64
<b>Brazil</b>	0.54	52	0.58	0.46	0.61
<b>Peru</b>	0.52	60	0.65	0.38	0.56
<b>Panama</b>	0.52	52	0.53	0.45	0.59
<b>Colombia</b>	0.50	72	0.53	0.41	0.63
<b>El Salvador</b>	0.48	79	0.48	0.42	0.52
<b>Ecuador</b>	0.47	85	0.43	0.42	0.49
<b>Dominican Republic</b>	0.47	90	0.45	0.37	0.52
<b>Mexico</b>	0.45	92	0.46	0.31	0.61
<b>Guatemala</b>	0.44	96	0.54	0.35	0.49
<b>Nicaragua</b>	0.43	99	0.32	0.38	0.41
<b>Honduras</b>	0.40	103	0.39	0.34	0.43
<b>Bolivia</b>	0.38	106	0.36	0.26	0.45
<b>Venezuela</b>	0.29	113	0.18	0.30	0.30

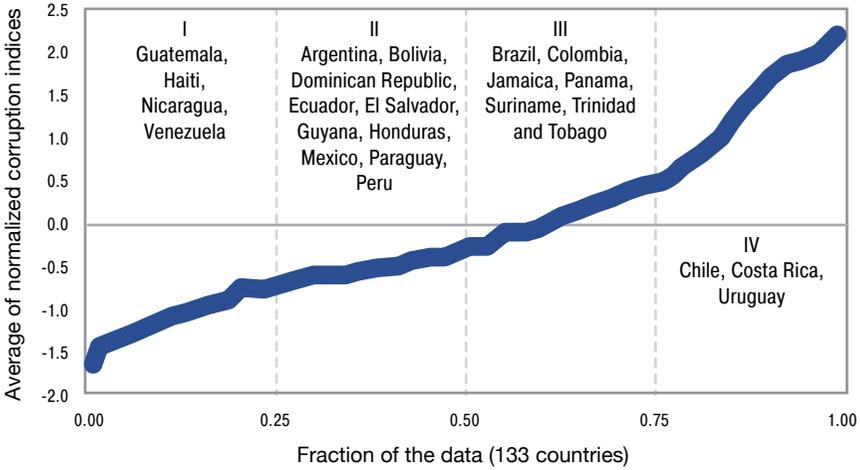
**Data is not available for Paraguay**

Source: Daniel Zovatto, using data from The World Justice Index, 2018

Country	Factor 4. Fundamental Rights	Factor 5. Order and Security	Factor 6. Regulatory Enforcement	Factor 7. Civil Justice	Factor 8. Criminal Justice
Uruguay	0.78	0.71	0.69	0.74	0.54
Costa Rica	0.78	0.69	0.64	0.63	0.56
Chile	0.73	0.68	0.62	0.63	0.56
Argentina	0.72	0.61	0.50	0.58	0.43
Brazil	0.57	0.65	0.52	0.53	0.37
Peru	0.65	0.64	0.50	0.44	0.36
Panama	0.59	0.67	0.52	0.48	0.33
Colombia	0.56	0.57	0.51	0.49	0.34
El Salvador	0.53	0.60	0.49	0.50	0.30
Ecuador	0.51	0.63	0.45	0.46	0.38
Dominican Republic	0.59	0.61	0.40	0.45	0.33
Mexico	0.52	0.59	0.44	0.40	0.30
Guatemala	0.55	0.58	0.35	0.35	0.30
Nicaragua	0.47	0.70	0.45	0.39	0.34
Honduras	0.43	0.61	0.37	0.41	0.24
Bolivia	0.46	0.58	0.41	0.34	0.21
Venezuela	0.36	0.47	0.22	0.33	0.14

Data is not available for Paraguay

**Figure 3. Corruption Varies Greatly Among Countries**



Sources: Transparency International; Verisk Maplecroft; and World Bank, World Governance Indicators database

At the third level are Brazil, Colombia, and others. And those with very low levels of corruption are Chile, Costa Rica, and Uruguay. The low levels of corruption in these three countries correlate with high levels of human development, high indices of governance, and the existence of anti-corruption measures. The past 40 years have seen the adoption of measures that are starting to pay off: public information laws, transparency laws, the creation of special prosecutors, etc. It is true that there are very dedicated judges like [Brazil's Sérgio] Moro and others.<sup>13</sup> But what would they do without laws that allow for plea bargaining, the strategic use of preventive detention, etc.?

The only way to solve these problems intelligently is through a public/private alliance in which the public and private sectors works together to strengthen institutions. These efforts must begin with the institutions that promote the rule of law and justice. Forty years since the beginning of the transition to democracy, most Latin American countries still do not have justice systems capable of combating corruption.

**Arturo Valenzuela:** This is not just a corruption crisis; it is a crisis of institutions that are still consolidating. The reason that three countries stand out [for

low levels of corruption] is because they were stronger democracies in the past. There is a path dependency that's quite clear. What is most needed to combat corruption? The strengthening of democratic institutions. That's why we need to be worried about populists that have succeeded in part because political parties have been severely weakened.

Civil society's rejection of politics can become part of the problem. If the public rejects politics, rejects parties, rejects institutions because all of them are bad, civil society becomes part of the problem. These things need to be fixed, not rejected.

**Rafael Fernández de Castro:** I would like to challenge Daniel on the notion of a public–private alliance to combat corruption. It is not so easy. There is a problem with Latin American elites. For some reason, elites—be they Honduran, Brazilian, or Mexican—have not yet decided to bet on the rule of law. They still want to preserve a status quo that has served them well. The elites in my country have not taken a stand on the issue of corruption. Those who have done so are social leaders and others in civil society, not the elites.

**Margarita López Maya:** Daniel sees a panorama that allows him to be optimistic. The dynamics in Venezuela do not let me feel optimistic. Quite the contrary. When corruption reaches an extreme in which transnational organized crime has penetrated the state and taken over state functions, the international community has more weight than national actors. We Venezuelans do not have the capacity at this moment to act alone against what is not just corruption but also violence, inequality, destruction of institutions, a state that can no longer fulfill basic social functions, a state that is heading towards collapse. For us it is imperative to have international support that is not just timely but also sustained. We need proactive international support coordinated with proactive internal democratic actors to reach a solution so that Venezuela can reconstruct or construct a democratic state and enter the twenty-first century with some guarantees of welfare and equality for its citizens.

**Daniel Zovatto:** I am delighted to be called optimistic. For an Argentine to become an optimist is an example of this profound process of social transformation we are now living through.

I see the past 40 years of democratic transition as a carriage with three horses: we are advancing very well in terms of political, electoral democracy; but we are way behind in terms of the second “horse”: constructing the rule of law. We need

to forge consensus within each country and the region to strengthen rule of law. The third issue is state capacity. We don't have capable bureaucracies. We need to keep on improving the electoral dimensions of democracy and make a push to catch up in terms of justice and institutional strengthening. These are the three issues that we must address to resolve the problem of violence, the problem of inequality, and the problem of corruption.

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# Strategies for Overcoming Corruption

Gabriela Hardt  
Claudia Escobar  
Gonzalo Smith  
Ricardo Uceda  
Jaime Alemán

Two very different Latin American countries offer contrasting models of how empowered prosecutors, backed by independent judges, can unravel complex criminal conspiracies within the state: Brazil, the region's largest country in area, population, and national income, and Guatemala, one of the smallest and poorest.

In Brazil, what began in 2015 as a seemingly simple money laundering investigation—into small businesses such as car washes, used to hide the profits of black-market moneychangers—morphed into what some call the largest corruption scandal in history.<sup>1</sup> Prosecutors working under Sérgio Mora, a federal judge in the southern state of Paraná, followed a money trail that led to the country's top elected officials as well as executives with Petrobras, the state-run oil company, and Odebrecht, a multinational construction company. Odebrecht's payments, detailed by the U.S. Department of Justice, have generated similar investigations in 11 countries, making the case also a model for international prosecutorial collaboration.<sup>2</sup>

Guatemala's anti-corruption crusade grew out of efforts to rid the country of illegal security networks that continued to operate within the state following the end, in 1996, of a brutal internal armed conflict dating back to the 1960s. Unable to investigate such powerful networks on its own, the Guatemalan government—under pressure from civil society—invited the United Nations to establish a commission with broad powers to investigate conspiracies within the state. The U.N. International Commission Against Impunity in Guatemala (CICIG) has worked alongside the country's public prosecutors to produce evidence leading to the arrest of a former president and vice president for customs fraud along with

dozens of other officials, lawmakers, politicians, and businesspeople in a series of high-profile corruption cases.

Jurists from each country provide insights into the strategies that have allowed their judicial systems to expose corrupt networks within the state and prosecute those responsible. First, *Gabriela Hardt*, a substitute federal judge in Curitiba, Paraná, explores the reforms that made Operation *Lava Jato* possible. *Claudia Escobar*, a former appeals court magistrate who resigned in protest of illegal interference with the judiciary, examines the achievements and challenges facing the judicial system in Guatemala. Both point out that while prosecutors have made high-profile arrests, these high-profile cases are still ongoing and face powerful domestic opposition.

There are also valuable lessons from the private sector itself, in terms of building internal safeguards and compliance systems within companies aimed at preventing corrupt practices and at protecting companies from liability for illegal behavior by staff or contractors. *Gonzalo Smith*, the chief legal and governance officer for S.A.C.I. Falabella, a Chilean multinational corporation, provides an explanation of how such efforts can help inoculate a company against corruption while also helping to fortify public institutions.

## Gabriela Hardt: Brazil's Window of Opportunity

For the past three-and-a-half years, I have been a privileged spectator of Operation *Lava Jato*, the largest criminal investigation into corruption and money laundering in the history of my country. The criminal scheme discovered is so large that investigations today have not only spread to various cities around Brazil, but have also spilled beyond national boundaries. According to the Federal Prosecutor's Office, as of August 31, 2017, more than 30 countries have requested documents from Brazilian officials to support investigations related to facts initially uncovered by the Thirteenth Federal Court of Curitiba.<sup>3</sup> Brazil has also requested documents from 39 different countries in connection with the same case.

Corruption has become a daily concern for Brazilians: It is now usually the first topic covered on national newscasts. In 2015, one year after the first phase of Operation *Lava Jato* began, Datafolha Research Institute surveys showed that—for the first time in the survey's history—Brazilians considered corruption to be the biggest problem in the country, ahead of other concerns such as health, violence, education, and unemployment.<sup>4</sup>

## *Long, Complicated Procedures*

As a rule, the Brazilian criminal system does not handle complex cases well, especially those involving white-collar crimes where, until recently, impunity often prevailed. The existence of three different appeals levels complicates criminal proceedings, which usually take more than 10 years to reach a final verdict. As a result, it was very common to have cases in which the initial trial judge imposed heavy sentences, upheld by the first court of appeals, but the defendants never actually served their sentences because the statute of limitations had run out before the final ruling.

Bilateral agreements signed by Brazil have quickened criminal investigations related to supranational crimes, which no longer depend on the lengthy procedures of *letters rogatory* [letters of request]. In the early 2000s, Brazil ratified important treaties to combat transnational crime, which not only involved Brazil in international efforts to combat certain types of crime, but also introduced several new investigative instruments already used internationally into national legislation. Two treaties of particular importance are the United Nations Convention against Transnational Organized Crime and the United Nations Convention against Corruption.

With these new tools at their disposal, investigators and prosecutors have been able to form solid criminal cases in connection to Operation *Lava Jato*. Judges handed down the first sentences just one year after the first indictments, confirming that the documents and testimonies behind these cases contained evidence of several crimes. Despite the initial efficiency of the investigations and criminal proceedings in the lower courts, only about a dozen of the more than 680 people implicated are serving sentences for crimes they committed. Because of delays in the countless appeals that reached the higher courts, which deal with an insane workload, and because sentences can only be served following a final decision, most of those implicated escaped punishment.

## *Privileged Jurisdiction*

Another factor that has hindered the fight against corruption in Brazil is the existence of numerous public officials with what is known as “privileged jurisdiction,” which means they can only be investigated and judged by upper-level courts. In Brazil it is estimated that more than 40,000 people have this prerogative, including powerful people involved in large-scale corruption schemes. The Supreme Court of Brazil—the highest court in the country—has special jurisdiction over

criminal cases involving high authorities, including the president, ministers of state, and members of the national congress. The Court's intense workload has effectively shielded such people from accountability. According to a study by the Association of Brazilian Magistrates, between 1988 and 2007, the Supreme Court did not convict any political figures.

A milestone in terms of holding high-level figures accountable was Criminal Action 470, also known in Brazil as the *Mensalão* [a slang term meaning big monthly payment]. In this case, the Supreme Federal Court condemned politicians directly linked to the sitting government, including a former presidential chief of staff, several members of Congress and other political leaders, and bank directors for corruption and money-laundering crimes. However, the case also highlights the complexity and difficulty of prosecuting these cases. Although the indictment was filed in 2005, it was not accepted by the Supreme Federal Court plenary until 2007 and not decided until 2012. The final judgment took 53 sessions, which almost paralyzed the work of the Court during four-and-a-half months. This in a case where only 40 people were indicted, 25 of whom were convicted.

Compare this with Operation *Lava Jato*: since 2014, over 280 people have been indicted in relation to 67 criminal cases in the initial trial courts.<sup>5</sup> As of September 2017, sentences had been handed down in 34 of these cases. For cases under the jurisdiction of the Supreme Federal Court (involving elected officials), although 450 people were investigated, there have been formal accusations in only five criminal actions. Three-and-a-half years into the investigations, as yet there have been no convictions.

### *Operation Lava Jato*

Operation *Lava Jato* initially began as one more investigation into crimes against the national financial system and money laundering. The evidence that emerged led to the discovery of a major corruption scheme spread through diverse spheres of the public administration. As Justice Teori Zavascki, the original rapporteur for the case in the Supreme Court, said “*cada vez que se puxa uma pena aparece uma galinha inteira.*” (Every time you pull a feather out [of the *Lava Jato* investigation], you get a whole chicken.)

At the end of the initial investigations, investigators, by mere chance, found that an operator on the black exchange market was involved with a former director of Petrobras, the state-owned oil company. Given this connection, investigators reviewed several large state contracts and collected evidence indicating

discrepancies in their value. The conclusion of the first plea agreements showed the existence of a great criminal scheme: people recommended by political parties in the government coalition were appointed to high-ranking positions on the Petrobras board of directors. Once in place these nominees diverted resources and funds back to these political parties and party leaders, taking a portion of the diverted funds for themselves. They covered up these kickbacks using administrative procedures that appeared lawful even as they agreed to inflated contracts worth billions of dollars signed with some of Brazil's largest companies, which acted in cartel-like fashion, dividing among themselves major works and contracts.

Operation *Lava Jato* was not a simple corruption scheme. Instead—as stated in the decisions handed down by Federal Judge Sérgio Moro—it was an issue of “systemic corruption” which has tarnished the image of Brazil and the self-esteem of Brazilians. It showed that corrupt practices had become a normal part of the public procurement process in Brazil. Bribery fees were paid based on pre-established rates before the amount to be contracted was confirmed; pre-defined payments were distributed among civil servants, intermediaries, and political groups, which were responsible for maintaining these officials in management positions at the state-owned companies and government agencies.

### *Paradigm Shifts*

Operation *Lava Jato* remains an ongoing investigation; new evidence continues to emerge every day, with denunciations presented in courts across the country. While it is not possible to conclude yet what its final impact will be—especially whether in the end it will change culture in the country's fight against corruption—it has been successful. Authorities have repatriated more than US \$700 million and blocked assets whose value exceeds 3.2 billion *reais* (approximately US \$1.03 billion), which is the most effective asset recovery operation in history.

This success stems from the following paradigm shifts in the Brazilian criminal process:

1. The Federal Police and the Public Prosecutor's Office established task forces with experienced professionals, some of whom had already worked on similar investigations in the past, such as Operation *Banestado*, which made it possible to avoid repeating previous mistakes.<sup>6</sup>

2. The Federal Regional Court of the Fourth Region, which has jurisdiction over the Thirteenth Federal Court of Curitiba, allowed Judge Sérgio Moro to work exclusively on cases related to the operation. As a student of the Palermo “maxi trial” of Italy’s great mafia bosses, Judge Moro believed one must prioritize the most serious cases.
3. Courts at the appellate level understood that the requirements for injunctions could be met not only in cases involving violent crime or drug trafficking—as was usually the case in Brazil—but also when “systemic” crime had been discovered, which clearly affects the public and economic order of the country.
4. There has been a fundamental change in the jurisprudence of the Supreme Federal Court that allows sentences to be executed if the appeals court upholds the initial trial court’s judgement. The court had previously required the exhaustion of all appeals. That allowed impunity to prevail in a country where the law allows an endless number of appeals at four different judicial levels.
5. The implementation of plea bargain agreements as established by Law 12,850/2013 constitute an important means to fully resolve cases involving criminal offenses committed by complex criminal organizations. In many cases, it is only possible to unveil their true *modus operandi* with the help of those who choose to collaborate.
6. Finally, the adoption of an electronic tracking system by the Federal Regional Court of the Fourth Region has increased the speed and public transparency of the process. After the end of the investigative phase, all steps, requests, and decisions become public and may be viewed immediately by any interested party, including, notably, the press.

### *A Window of Opportunity*

In a true democracy, public opinion, freedom of the press, and the transparency of the acts of public administration are fundamental for combating and avoiding acts of corruption. Without press coverage and without immense popular support, it would not have been possible to overcome the various obstacles that appeared during the investigation.

Operation *Lava Jato* is still an ongoing investigation, which has been and continues to be criticized. But some of its results are unprecedented. Never before had top executives of the country's largest companies been arrested, tried, and convicted. Several sitting members of Congress are under investigation and face prosecution before the Supreme Court; proceedings pending in the lower court involve a former president of the Chamber of Deputies, former cabinet ministers, a former governor, and several former members of Congress.

Brazil has continued to face new scandals. On September 5, 2017, we saw shocking images of the seizure of more than R\$51 million (approximately US\$16.5 million) in cash hidden in boxes and suitcases, illicit funds allegedly received by an ex-minister in the current government who has held important positions in the two previous governments. This demonstrates there has been a paradigm shift in the effective prosecution of criminal cases because of Operation *Lava Jato*, but it is not sufficient to change the culture of the country. It is a major step, but not enough.

The Public Prosecutor's Office has proposed legislative reforms, supported by more than 2 million signatures, to better prevent and prosecute this type of crime. Nonetheless, the bill passed by the Chamber of Deputies distorts the initial proposal, seeking instead to maintain the status quo. There are several bills underway in the National Congress that could reverse the progress already made in Operation *Lava Jato* and undermine the actions of investigators, prosecutors, and judges.

When fighting powerful forces, you must expect them to use every means at their disposal to keep their power. However, I have personally had the privilege of following closely the hard work of well-intentioned and well-prepared people who over the past three-and-a-half years have faced new battles every day. For all this, I hope that Operation *Lava Jato* serves as a real window of opportunity so that we succeed in building a stronger and more reliable country, one based on trust and the rule of law.

## Claudia Escobar: Guatemala's Uphill Struggle

The Guatemalan context is totally different from that of Brazil, not only because it is a small country but because of our unique circumstances. We suffered a prolonged civil war that divided the country for nearly 40 years. There are still unhealed wounds from that war and its legacy has been impunity, insecurity, and inequality. Ninety-eight percent of crimes go unpunished, turning Guatemala into

a paradise for criminal groups. There is a culture of fear and of silence along with extreme violence and enormous institutional weakness in all areas of political life. Criminal groups have co-opted many institutions.

In 2006 the government of Guatemala recognized its weaknesses and asked the international community for help. A number of international cooperation agencies have helped Guatemala with projects for institutional strengthening, especially in the areas of justice and security. The most emblematic effort is the International Commission Against Impunity in Guatemala (CICIG), which was created by the United Nations at the end of 2006 and began to operate in Guatemala in 2007. For the past 10 years, we have been able to count on the support of this important ally in the fight against impunity and corruption, which is responsible for complex tasks that the state recognizes it cannot carry out on its own.

### *CICIG's Mandate*

The commission has three main responsibilities: 1) to investigate illegal, clandestine security groups and networks—including political networks—operating in the illegal economy; 2) to work with state institutions to dismantle these networks and to further the prosecution of their members for crimes committed; and 3) to make recommendations to the state regarding public policies and legal reforms designed to eradicate and prevent the reappearance of these clandestine organizations and illegal security bodies.

One of the principal strengths of CICIG is its independence: it has the power to investigate without pressure from state entities or influential interest groups. Its work has exposed presidents, ministers, legislators, business people, military officers, and judges. It has also exposed others close to the circles of political power who have enriched themselves through a system of privileges.

In assessing the performance of CICIG, we should note that at beginning of its mandate, Commissioner Carlos Castresana pushed for the approval of laws that today constitute valuable tools for criminal prosecution. These include the law against corruption, the law on asset forfeiture, and the regulation of wiretapping. These important changes were key to the achievements in subsequent years.

Commissioner Iván Velásquez has exposed the degree of corruption within state institutions as well as political interference in the judiciary.<sup>7</sup> He also revealed illegal financing of political campaigns. He has touched the most sensitive nerves of a system that was designed to preserve impunity. In the process, he has earned powerful enemies.

## *Achievements and Challenges*

The achievements of CICIG and the progress in strengthening institutions are obvious and have been recognized throughout the world as one of the most successful efforts in the struggle against corruption. But there is still much to be done to dismantle the criminal networks that have co-opted the Guatemalan state. It is an uphill battle to eradicate these mafias and prevent their reappearance. This requires not only the joint effort of national actors but also political will, something that, sadly, does not exist in Guatemala at this time.

Corruption is the consequence of terrible institutional weakness. Underlying that weakness are the interests of powerful illegal groups that benefit from the absence of the state and engage not only in corruption but also in all sorts of illicit activities: trafficking in drugs and weapons, human trafficking, property theft, extortion, etc.

Those exposed by the Commission have become its unrelenting enemies and employ every means at their disposal to undermine the CICIG's work. In their zeal to defend the status quo—in which they were untouchable—they have allied themselves with international organized crime, which has unlimited economic resources and mechanisms to confront those who are fighting for the rule of law. (See the Introduction to this report.)

## *Guatemalans' Choice*

CICIG was not designed with the idea that it would replace public institutions or substitute for their functions. Its success in criminal prosecutions relies on the capacity of the Public Ministry [the public prosecutor's office]. To obtain convictions the CICIG depends on a judicial system that is still in need of deep reform. It is up to Guatemalans either to take advantage of the support of the international community reflected in the CICIG or to allow the mafias to continue governing us.

Guatemalans must push for legal reforms, invest in a judicial system that can regain citizens' trust, and train public officials so they can be appointed on their merits, not on the basis of their political connections.

Constructing a genuine rule of law is not easy. We will face enormous challenges. Yet I would like to be optimistic and consider this an opportunity for change. Despite all the difficulties there are devoted public servants in the justice system who are ready to defend judicial independence and act impartially. There are citizens who are more informed and aware of the costs of corruption.

That, too, can drive change. There is—to a certain extent—freedom of the press and an important role for the media. In these moments of crisis, all of these things can help a small country like Guatemala face its enormous challenges in fighting corruption.

## Gonzalo Smith: Corporate Anti-Corruption Strategies

First, I will provide a perspective on the impact that new rules and regulations against corruption have had on companies in Latin America, specifically *multilatinas*. Second, I will offer a sense of what seems to be working well on the corporate side, for example, in my company, Falabella, in the fight against corruption and suggest what further steps could contribute to further progress.<sup>8</sup>

### *International and Domestic Law*

The systematic fight against corruption is fairly recent. Indeed, the Inter-American Convention against Corruption was only adopted in 1996.<sup>9</sup> A few Latin American countries are still not signatories, but almost all signed and ratified the convention between 1996 and 2004. In addition, the Organization for Economic Cooperation and Development's (OECD's) Convention on Combating Bribery of Foreign Officials in International Business Transactions was adopted in 1997 and entered into force in 1999.<sup>10</sup> Mexico and Chile are the only two Latin American members of the OECD. But the good news is that the OECD convention has been adopted by eight non-OECD countries, four of which—remarkably—are Latin American: Argentina, Brazil, Colombia, and Costa Rica.

Virtually all countries in Latin America have started adapting their laws to fulfill the commitments contained in these conventions. Naturally, some seem to have done so with greater zeal than others. It is important to bear in mind that these adaptations have not, for the most part, criminalized bribery. That is because bribing a government official has been a crime in most Latin American countries since the *Códigos Penales* (criminal codes) were first written.

There are two aspects of these recent changes that are truly novel compared to what existed before:

The first consists of making legal entities legally capable of a crime. While this sounds almost trivial, it was only after much debate by legal scholars, and a fair amount of intellectual pain, that it was admitted that a legal entity could be capable of committing a crime. Because legal entities lack a will of their own, it was

hard to argue that they are capable of criminal intent. This technical debate was never truly resolved, but it became irrelevant from a practical standpoint. That is because, from a public policy perspective, legislators deemed that the goal of fighting corruption made it worthwhile to overlook the technical issue of whether you could attribute intent to legal entities.

The second legislative change is remarkable, though it has not been adopted by all signatories to the Inter-American and OECD conventions against corruption. This adaptation involves creating a safe harbor against criminal liability for legal entities who can show that they exercised proper diligence prior to the acts that could result in criminal liability, through the adoption and implementation of systems to prevent the occurrence of crimes.

In other words, if you have an effective anti-crime compliance system within your organization, your company can dodge criminal liability. Chile is one of the countries that has adopted this change. Because of that and because of my familiarity with the Chilean case, my subsequent comments refer mostly to Chile.

### *How the Safe-Harbor Model Works*

Safe harbor from criminal liability translates into a model for the prevention of crimes within legal entities. This model consists of a series of structural, behavioral, and procedural measures and steps within companies that, when properly applied, make it much harder for a crime to occur within the organization.

Bribery is one of those crimes but not the only one. In the case of Chile, corporate criminal liability can exist relative to the bribery of government officials (at home or abroad), money laundering, financing of terrorism, and knowingly trading in stolen goods. The potential for criminal liability for money laundering and financing of terrorism requires the adoption of preventive measures for a series of other crimes related to them.

There is a long list of measures that must be adopted in order for a crime prevention system within an organization to be effective. Some of the most important aspects include:

1. The appointment of an officer in charge of the program who has direct access to the CEO, monitors the system day-in day-out, reports to the company's board at least twice a year, and has sufficient resources relative to the size and complexity of the organization;

2. Implementation of methods to prevent crimes, such as risk assessments of processes and procedures vulnerable to corruption; the establishment of protocols, rules, and procedures for these at-risk procedures; accounting and financial controls to prevent financial resources from being used to commit crimes; and helplines for the reporting of potential criminal activity;
3. Certification of systems or models by independent, specialized agencies and at regular intervals, something that provides an extra layer of protection from an evidentiary perspective.

Clearly, the list of measures for an effective system is much longer and includes such things as third-party intermediary due diligence, business partner due diligence, specific contractual provisions against bribery in all contracts, protocols for communicating with government officials, etc.

### *Why It Works*

The true merit of the safe harbor mechanism is how it impacts corporate culture. It creates an incentive to change not only what is done, but also how it is done. Corporate culture is something that companies do well and are used to managing on a daily basis. When compliance is based on culture, the behavior no longer feels like an obligation. Instead, there is an internal drive to follow process and procedure, something that companies know how to do.

Too little time has gone by to measure the true effectiveness of the changes put in place. But they do have the merit of keeping everyone on his or her toes, to ensure that the model for prevention of crimes is working effectively.

Another positive aspect of the safe harbor system is that, because it mandates specific actions, the model is comparable across companies of similar sizes. Thus, the standard is open to continuous improvement, as no company can afford to be the laggard.

### *Lessons for the Public Sector*

From a corporate perspective, what further steps could be taken to strengthen the fight against corruption? I believe there are two things that would be enormously effective.

First, as we all know, bribes are paid because bribes are taken. Every bribe has someone who offers and someone who accepts, a payer and a payee. Neither

side is a victim. When a bribe is offered, paid, solicited, or taken, both parties are responsible.

Seeing how the safe harbor system has caused systematic changes within companies and has institutionalized responsibility, I cannot but think that similar institutional incentives within the public sector could go a long way in preventing corruption. (This is distinct from criminal sanctions applied directly to a corrupt public official.)

The system devised for private companies cannot be applied in mirror image to the public sector. There are important differences: the ultimate price to be paid by a company for corruption—its dissolution—is not something that can necessarily be applied to the public sector. Other penalties, such as fines, should also be different. When someone within a company pays a bribe, it is usually for the benefit of the company; but when someone in the government takes a bribe, it is usually for personal or political gain.

Despite these differences, I see no substantive reason that the public sector and its leaders should not be held institutionally accountable for failing to implement systems to prevent corruption. Institutional incentives in the public sector could and should make the organization and its leaders liable if corruption occurs. This is how pliers work, by applying pressure on both sides.

Simply banning bribery did not work for a very long time, over 200 years. Now that active, preventive obligations seem to be working in the private sector, it seems only natural that the same approach should be adopted in the public sector. Imagine how different things would be if liability for taking a bribe fell on a public institution or its leaders, unless there were an effective model for preventing such crimes in place.

### *Private Corruption*

Second is the big issue of commercial or private bribery and corruption. Not having proper legal tools to prosecute private bribery or corruption within companies is a deeply frustrating experience for companies themselves. Legal scholars have traditionally argued that, in the absence of another crime such as embezzlement, private bribery is not a crime, not only because there is a lack of public interest, but also because there is no strict cause and effect between the voluntary payment of a bribe by a third party and damages to an entity whose employee took a bribe. The traditional perspective has been to view such matters as a management problem.

This seems to be a narrow and outdated perspective. Though there may be no public economic involvement in privately-held companies, this cannot be said of publicly-traded corporations, which receive public funds either in the form of equity or debt. The creation of corporate cultures based on integrity should be considered a matter of public interest. The fact that corrupt payments have very dissimilar legal treatments depending on who receives the bribe does not help at all. It is very difficult to explain within an organization why certain actions involving a government official can land you in jail, but are almost impossible to prosecute when the other party to a corrupt act is a private client, supplier, or contractor. This dichotomy is extremely damaging and constitutes a major obstacle to the implementation of effective control environments within organizations. Legislators are starting to consider the criminalization of private corruption in Latin America. However, I believe that the issue of private corruption is not yet regarded as an integral part of the fight against corruption in the public sector. Public and private should go hand-in-hand.

### *The Right Incentives*

Over the last 20 or so years, there has been crucial and meaningful progress. Having more laws and regulations is not what has truly made a change. Rather, it is having the right laws, regulations, and incentives. Drawing on elements that are innate to corporate life has been crucial.

Nothing has been more effective than requiring specific actions regarding structure, process, and procedure in order to provide for adequate monitoring and an effective system for prevention. These actions must be coupled with incentives for making the measures work. Implanting a corporate culture of preventing corruption has been key.

A corporate culture of cleanliness keeps the food industry running well; a culture of maintenance keeps planes in the air; a culture of safety keeps miners out of harm's way. A culture of integrity is an integral part of the fight against corruption. Safe harbor systems based on prevention have provided the right incentives to go beyond what has been done in the past.

Extending this kind of active diligence to the public sector and completing the picture by criminalizing private corruption would be extremely useful in furthering the fight against corruption.

## Notes

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7. "Iván Velásquez, 'el retador del poder' que desata crisis en Guatemala," *El Tiempo*, August 27, 2017, <https://www.eltiempo.com/mundo/latinoamerica/quien-es-ivan-velasquez-colombiano-que-desata-crisis-en-guatemala-124244>. [Ed.]
8. Falabella, headquartered in Santiago, Chile, has operations in Argentina, Brazil, Chile, Colombia, Mexico, Peru, and Uruguay. Falabella's holding company is the largest corporation traded on the Santiago stock exchange, with a market cap in excess of \$23 billion. The company grew out of a small family-owned business founded in the late nineteenth century and the majority of the company's current controllers are relatives of the founding family. Falabella operates department stores, home improvement stores, supermarkets, financial service companies, banks, travel agencies, insurance brokers, an insurance company, shopping malls, and other commercial real estate. The company has 107,000 direct employees and consolidated revenues in 2016 totaled \$12.8 billion. [Ed.]
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## Ricardo Uceda: Peru's Decades-long Struggle

The aftershocks of the Odebrecht scandal continue to rattle the highest levels of the Peruvian government. Ongoing investigations into the company's pay-to-play schemes have brought down one serving president and implicated three others. Pedro Pablo Kuczynski (2017–2018) resigned in March 2018.<sup>1</sup> This was after videos emerged purportedly showing his allies trying to buy votes to avoid impeachment for allegedly profiting from Odebrecht contracts while serving as a cabinet minister in the early 2000s. Former presidents Ollanta Humala (2011–2016) and Alan García (2006–2011) are both accused of taking illegal campaign contributions from the company.<sup>2</sup> Alejandro Toledo (2001–2006) faces an international arrest warrant; he is reportedly living in the United States while Peruvian courts seek his extradition on charges of laundering up to \$20 million in Odebrecht bribes.<sup>3</sup> Keiko Fujimori, daughter of former president Alberto Fujimori, has also been accused of receiving illicit funds from Odebrecht to finance her 2011 and 2016 presidential campaigns.

However, the Odebrecht scandals represent but one effort to combat high-level corruption in Peru. As an investigative reporter and editor in the 1990s, Ricardo Uceda, executive director of the Instituto Prensa y Sociedad (IPYS), helped uncover the corruption and human rights scandals that eventually brought down the authoritarian government of President Alberto Fujimori (1990–2000).<sup>4</sup> During Fujimori's presidency, the country "was swimming in corruption," according to Uceda. High-level officials across the government—from judges to military officers to ministers to members of parliament—charged for their services. Even the owners of the big television networks accepted payments from the intelligence services.

A combination of journalistic and judicial courage eventually brought the Fujimori era to a close.<sup>5</sup> Investigations into the activities of intelligence chief Vladimiro Montesinos—including leaked footage of videos showing him bribing opposition lawmakers, judges, and military officials—forced Fujimori to appoint a special prosecutor. When these investigations got too close to his own presidency, Fujimori asked his justice minister to fire the prosecutor. Instead, the minister stood his ground, telling the president, "If he goes, I go."

Fujimori fled to Japan in 2000, sending Congress his resignation by fax. He remained abroad until 2007 when Chile extradited him to face trial on corruption and human rights charges. (Although sentenced to 25 years in prison, Fujimori was granted a controversial humanitarian pardon in December 2017 in what critics say was an attempt by Kuczynski to avoid impeachment with the help of factions of the imprisoned president's party.)<sup>6</sup>

Special prosecutor José Ugaz and his team went on to investigate hundreds of corrupt officials.<sup>7</sup> Their efforts showed that “even under Fujimori, justice could work,” Uceda said. But graft remains endemic in Peru, despite the use of special prosecutors and sweeping reforms that have transformed the justice system from a largely inquisitorial to an accusatory model. Though significant, these measures have not been enough. “Leadership is necessary,” Uceda said. “Leadership plus aggressive or radical transparency. Because this is what allows the people to fight those who are corrupt.”

Investigations by Peruvian journalists once again came to the forefront of Peru’s anti-corruption struggles in July 2018, when IDL-Reporteros, led by renown Peruvian journalist Gustavo Gorriti, made public over a dozen leaked audio recordings in which judicial officials—from the Supreme Court, the Superior Court of Callao, the National Council of Magistrates, and others—are heard engaging in the rigging of sentences in exchange for bribes and other forms of influence-peddling. The revelations led to the resignation of the justice minister, the head of the Supreme Court, and at least four members of the Council of Magistrates. The Peruvian congress declared a three-month state of emergency in July 2018 and the Institute for Legal Defense (IDL), one of Peru’s premier human rights organizations, called the revelations “unprecedented” and “one of the greatest crises of our democratic system.”<sup>8</sup>

In response to the crisis and to the massive outpouring of popular indignation the audio recordings provoked, Peruvian President Martín Vizcarra (who took office following Kuczynski’s resignation) pledged a thorough reform of the judicial system. Those efforts are ongoing and have generated significant political tensions between Vizcarra, who sought reforms via a referendum, and the opposition-controlled Congress. A referendum on anti-corruption reforms is to take place in December 2018.

## Notes

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## Jaime Alemán: A Roadmap for Combatting Corruption

When newly elected President Ricardo Martinelli offered Jaime Alemán the position of Panama's Ambassador to the United States, he accepted the offer gladly from a leader he considered a "good friend," someone who was "smart," and "full of energy." Martinelli, a supermarket mogul who boasted of his \$400 million network, ran on a "platform that he would eradicate corruption," Alemán said.

Less than a month into his ambassadorship, however, Alemán began hearing reports of bid rigging and other corrupt acts by a president who would eventually become yet another casualty of the Odebrecht bribery scandals. Martinelli, who sought political asylum in the United States after his party lost the 2014 elections, was arrested in Miami and extradited back to Panama in June 2018. He is charged with embezzling millions of dollars of public funds and conducting the illegal surveillance of more than 150 rivals.<sup>1</sup> Alemán said that Martinelli's presidency was "a total catastrophe" that set Panama back generations in its fight against corruption. Martinelli remains popular within his own party, however, and plans to run in the country's 2019 elections.

Alemán said that there are concrete steps that countries such as Panama can take to battle corruption and build a government based on rule of law. He laid out a "roadmap" of 15 essential measures for countries of the region as well as the international community.

### *Latin American governments should:*

1. Create strong and independent attorney's general offices;
2. Build a strong and independent judiciary, from top to bottom;
3. Protect independent media (television, radio, newspapers);
4. Encourage a proactive civil society, including the presence of organizations such as Transparency International, which are focused on fighting corruption;
5. Approve modern public procurement legislation, in order to prevent the rigging of the adjudication process before bids are even presented or opened;
6. Revoke the licenses of banks (such as the Banca Privada D'Andorra, BPA) that knowingly open accounts for corrupt corporations and/or corrupt government officials;
7. Impose hefty fines and long jail terms for corporations and individuals found guilty of corruption;
8. Lengthen the statutes of limitation so that corrupt officials do not escape possible indictment and prosecution;

9. Prohibit companies indicted for or convicted of corruption from participating in public projects in the future;
10. Encourage the use of social media (e.g., Facebook, Twitter, WhatsApp, etc.) to denounce corruption and call for public demonstrations as necessary;
11. Organize seminars, conferences, and ad campaigns, to raise awareness of the dangers of corruption.

*The United States and others in the international community should:*

12. Implement measures proposed by the inter-governmental Financial Action Task Force (FATF) to combat money laundering and by the Organisation for Economic Cooperation and Development (OECD) to combat tax evasion, including protocols for automatic multilateral exchange of information;<sup>2</sup>
13. Vigorously implement such laws as the U.S. Global Magnitsky Human Rights Accountability Act, to revoke visas and freeze assets owned by foreign nationals engaged in corrupt activities;<sup>3</sup>
14. Exercise tighter due diligence controls of real estate purchases, to stop public officials from using such investments to launder ill-gotten funds (such as the case of New York apartments bought with funds stolen from the Malaysian wealth fund);
15. Enforce extradition treaties and implement the UN Convention against Corruption (UNCAC), to facilitate asset recovery.<sup>4</sup>

## Notes

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Part II.

# Adjusting to Disruption in the International Arena



# The New Directions of Regional Integration

Heraldo Muñoz

This reflection addresses how Chile, a middle-income country, dealt with the current regional and global challenges, particularly regional integration, during the administration of President Michelle Bachelet (2014–2018).

During this period, Chile's performance in foreign affairs was among the best in modern times. The country became a world leader in ocean conservation by organizing the "Our Ocean" conference in Valparaíso in 2015, by linking ocean conservation to combat climate change in a declaration known as "Because the Ocean," an initiative led by France, Monaco, and Chile, and, most importantly, by creating more marine-protected areas than in any period of our history.

Chilean South-South cooperation, centered particularly on Central America and the Caribbean, jumped to almost US\$30 million since 2015. Chile was an accompanying country in the peace process between the government of Colombia and the Revolutionary Armed Forces of Colombia (FARC).<sup>1</sup> In 2018 Chile has several dozen personnel in the new stage of the United Nations verification mission and became a guarantor in the conversations between the government and the National Liberation Army (ELN).<sup>2</sup> After 13 years in Haiti, we withdrew our troops from the UN peacekeeping mission, but left a police contingent and shifted our efforts to development cooperation.

And, at long last, 27 years since the recovery of democracy, Chileans abroad could vote in primaries and presidential elections, after approval of a complex constitutional reform and implementing legislation, a task led and carried out by the Foreign Ministry. Likewise, after 27 years of failed attempts at modernizing Chile's Foreign Ministry, we were able to negotiate in Congress and approve, without one vote against, the Law of Modernization of the Foreign Ministry of Chile, promulgated by President Bachelet during the last week of her mandate.

Last but not least, our defense of democracy and human rights placed us as one of the facilitating countries for the possible negotiation, hosted by the government of the Dominican Republic, of a political outcome to the deep Venezuela crisis. Unfortunately, this effort failed and the presidential election took place, unilaterally called by the Maduro government, in May 2018, without the minimum guarantees of a free and fair election, and without the participation of most of the opposition. The Group of Lima recognized the efforts of Chile and Mexico and condemned the lack of governmental political will to find an electoral solution to the Venezuelan crisis.

There is much more to be said about what we achieved in recent years, but I will focus my attention—as requested—on regional integration and trade. Before getting into the new directions of regional integration, allow me a few observations on the global context.

## A New Era of Discontent

Many years ago, former U.S. Secretary of State Dean Acheson published a masterly analysis of the emergence of the post-World War II international order, under the title *Present at the Creation*. Recently, the prestigious and influential journal *Foreign Affairs* used the title, “Present at the Destruction?” for its May/June 2017 issue.<sup>3</sup> I would instead use a title like “Present at the Diffusion,” because power has spread as never before.

The Brexit vote, President Donald Trump’s election, and the withdrawal of the United States from the Trans-Pacific Partnership (TPP) and the Paris climate agreement seem to mark the beginning of a new era. There appears to be a new age of citizen dissatisfaction, of discomfort with the asymmetrical fruits of globalization, with the balance of winners and losers stemming from the unstoppable process of technological innovation.

The opening of trade, interconnectivity, and technological acceleration moved millions of people out of poverty and created new middle strata. According to the World Bank, the number of people living below the poverty line fell from 35 percent in 1990 to 10.7 percent in 2013, despite the fact that the number of inhabitants of the planet increased by almost 2 billion in that time. However, the benefits have gone disproportionately to few privileged groups, leaving many behind and creating a growing number of malcontents.

Latin American and Caribbean countries continue to lead inequality indices, despite efforts to revert the situation. According to the UN Economic

Commission for Latin America and the Caribbean, the Gini coefficient in 2015 showed an average value of 0.47 for 17 Latin American countries, a level considered high. Although the index of inequality showed improvement until 2012, the rate of decline fell in recent years. Today, 11 of the 20 most unequal countries in the world are in the region.

## Social Gains at Risk

At the same time, we have experienced an economic slowdown and a steep fall in the prices of most commodities, the centerpiece of the export strategy of most Latin American economies and the main source of national income. This has created low growth and, in some cases, recession. Considering a much tougher macroeconomic environment than that of the previous decade, the ensuing “belt tightening” has also placed social gains at risk. Recent economic recovery leading to increases in regional exports do not yet constitute a firm trend. This is particularly the case as trade wars appear in the horizon.

China’s new position as a main market for our region’s goods and China’s economic shift from investment in infrastructure to investment in consumption have been partly responsible for the end of the commodities boom. The “new normal” for Latin America would seem to be low economic growth. In fact, according to the Economic Commission for Latin America and the Caribbean, Latin America registered modest growth of 1.3 percent in 2017, behind the growth of other regions, including the economies of developing East Asia and Pacific, which are projected to expand at 6.2 percent in 2017 and 6.1 percent in 2018, according to the World Bank.<sup>4</sup>

To make things worse, in Latin America and the Caribbean, we are witnessing the frightening impact of climate change such as rising sea levels and warmer oceans, which, scientists agree, make storms and hurricanes far more destructive than they would have been in previous decades. Natural disasters are particularly burdensome for middle-income regional countries, since due to their income per capita, access to development cooperation from traditional donors is severely restricted.

Chile and other middle-income countries in our region have pointed out the blatant contradiction between the spirit of the multidimensional 2030 Agenda for Sustainable Development—adopted by world leaders in September 2015—and the “graduation” of aid recipient countries by traditional donors, based solely on the criteria of income per capita. We believe there is an urgent need to rethink

this issue, as it seems impossible to meet the UN's Sustainable Development Goals without technical assistance or financing for development.

## Regional Tensions

Regional integration has been an important part of the historical discourse of most if not all Latin American and Caribbean countries. However, achievements have been scarce and geopolitical rivalries endure. In recent years Latin America and the Caribbean exhibit more political and ideological diversity than just about any other time. The tensions are reflected in weakened regional organizations like the Organization of American States, the Union of South American Nations (UNASUR), and the Community of Latin American and Caribbean States (CELAC).

Chile believes that regional integration and open markets are fundamental for creating the right conditions for more innovation, diversification, and integration into international value chains, all fundamental for national economic growth. Our integration into the international community has been characterized by an open trade policy. This policy has boosted trade and allowed increased investment flows, which have guaranteed sustained economic growth. As a result, Chile went from US\$5,846 per capita income in 1990, to US\$23,969 in 2016, and poverty decreased from 39 percent to 11.7 percent in the same period.

Today, Chile has 26 trade agreements with 64 countries, representing over 60 percent of the world's population and over 85 percent of global GDP. We are also associate members of Mercosur, the South American trade bloc, and collaborate closely with the Caribbean Community (CARICOM) and the Central American Integration System, or SICA. Of course, the Pacific Alliance (Chile, Peru, Colombia, and Mexico), launched in 2011, is the cornerstone of our approach to the region. Furthermore, our interest in Asia-Pacific integration led us to get involved in the five-year negotiation of the Trans Pacific Partnership Agreement (TPP). I will refer to this later. We have even taken the first steps towards a trade agreement with the Eurasian Economic Community, composed of Russia, Belarus, Kyrgyzstan, Tajikistan, and Kazakhstan.

But we believe that the regional market is the most appropriate for export diversification. It is the most important market for exports of manufactures and services and for most companies that export, especially small and medium-sized enterprises (SMEs). In addition, our region is the natural space for the growth



Chile has 26 trade agreements with 64 countries, representing over 60 percent of the world's population and over 85 percent of global GDP.

of *multilatina* enterprises and the creation of multinational production chains. Investments crisscross our region in a silent private sector integration that has stimulated government action. We are seeing more cross-border roads, tunnels, pipelines, energy trade, and connectivity—aside from retail stores and other entrepreneurial activities—than at any other period in modern history.

However, while intra-regional trade in Europe is 69 percent, in Asia 52 percent, and in North America 50 percent, it is only 26 percent in South and Central America. Nevertheless, for the vast majority of Latin American and Caribbean countries, intra-regional trade is qualitatively better than their raw material exports to other markets.

It is clear that we have some important outstanding tasks. We must boost productivity, increase innovation, adapt our economies to new technologies, and diversify our exports.

## Pacific Alliance and TPP

From the outset of President Bachelet's second term in 2014, we became concerned about the clear political and economic distancing between the Pacific Alliance (AP, for its Spanish initials) and Mercosur. We decided to seek a “convergence in diversity,” that is, to engage in a dialogue to explore common actions despite the differences between the two integration schemes. There was skepticism and we heard a number of distortions—for example, that Chile sought the merger of the two blocs, that Chile was opting for rapprochement with lesser partners that would slow down if not stop the AP's progress. But we insisted, arguing that Chile has strong interests in the Pacific but also in the Atlantic, and that the region



## Pacific Alliance members made a qualitative leap forward, by agreeing not only to continue to deepen the integration among the four, but also to initiate high-standard trade negotiations with Asia-Pacific countries

needed a stronger international voice and larger trade flows. And we did not want a geopolitical divide between the AP and Mercosur.

The Pacific Alliance became our regional integration hub towards the Pacific Rim and a bridge towards our Atlantic neighbors. Alliance and Mercosur ministers of foreign relations and trade met in April 2017 and agreed on a concrete plan of action—a road map—that constitutes the only palpable evidence of integration between two different regional economic blocs in the region. The action plan includes trade facilitation, regional value chains, customs cooperation, trade promotion, and SMEs, non-tariff barriers, and facilitation of trade in services. Each objective has its corresponding implementation activities and dates. Progress is reflected in the decision to hold the first summit in Mexico, in July 2018, between both economic blocs at the presidential level.

Following the departure of the United States from the TPP, Chile held a successful ministerial meeting in Viña del Mar in March 2017, with high-ranking officials from 15 Pacific Rim countries. The main objective was to reiterate our commitment to free trade and integration. The 11 remaining signatories of the TPP agreed to continue exploring how to implement the partnership, an agreement that we all considered would be beneficial for our countries. After months of negotiation, 11 countries signed the Comprehensive and Progressive Trans-Pacific Partnership (TPP 11) in Santiago in March 2018.

Since the Trump administration decided to renegotiate the NAFTA agreement—and we wish a positive outcome for all three countries involved—we

expect that the signing of the CPTPP will provide more flexibility and economic alternatives for Mexico, Peru, and Chile, the three Latin American signatories of the TPP 11.

But continuing the TPP negotiations after the U.S. withdrawal was not the only result of the March 2017 meeting in Viña. The members of the Pacific Alliance made a qualitative leap forward, by agreeing not only to continue to deepen the integration among the four, but also to initiate high-standard trade negotiations with Asia-Pacific countries. The Pacific Alliance is presently negotiating as a bloc with each individual country chosen: Australia, Canada, New Zealand, and Singapore; once these negotiations are completed, each partner will become an “associated state” of the Alliance, a new category created for this purpose. Thus, the Pacific Alliance will become a powerful alternative platform for larger Asia-Pacific regional integration, along with the Free Trade Area of the Asia-Pacific (FTAAP) and the Regional Comprehensive Economic Partnership (RCEP), the first under advanced study and the latter under negotiation.<sup>5</sup>

Furthermore, the Pacific Alliance and the Association of Southeast Asian Nations (ASEAN) also negotiated a Framework for Cooperation between the two integration mechanisms, adopted in September 2016. The Framework prioritizes four strategic areas: economic cooperation; education and person-to-person contact; science, technology, and innovation; and sustainable development.

In sum, the Pacific Alliance has proven a success. To the additional protocol that freed 92 percent of all trade among the four member states, we should mention: 1) the implementation of the Entrepreneurial Capital Fund, 2) the creation of the Pacific Alliance investment facilitation initiative, 3) the integration of the stock markets of the four countries (*Mercado Integrado Latinoamericano*, or MILA), and 4) the consolidation of the Student and Academic Mobility Platform, among others.

What makes the Pacific Alliance successful is perhaps that it avoids the errors of other integration schemes. The AP has no secretary general, no headquarters, and no permanent bureaucracy, allowing for flexibility and action-oriented initiatives.

## Bilateral Agreements

At the same time, we must also persist in our bilateral approaches to economic integration. Thus, Chile negotiated a free trade agreement with Uruguay and modernized our longstanding and successful trade agreement with Canada, introducing in both cases new issues, such as a gender chapter, focused on empowering

women economically. We concluded the modernization process of our trade agreement with China (the first one ever by China with a single country); we agreed to update our trade deal with South Korea; and we signed at the end of 2017 a new free trade agreement with Indonesia. At a different level, we hope to complete the modernization of our association agreement with the European Union, since all EU members provided the mandate to launch negotiations. Formal negotiations began in November 2017 and are expected to conclude during the second semester of 2018.

Integration with our neighbors has been and will be a key goal of our foreign policy. We must take advantage of the possibility to cooperate fully. Chile does not benefit from the instability or lack of progress of our immediate neighbors.

With Peru, relations have focused on a common future agenda. We are working closely on a number of fronts, including energy interconnectivity, migration, security, trade, and investment. In July 2017, for the first time in our history, we held a binational Cabinet of Ministers headed by then-presidents Michelle Bachelet and Pedro Pablo Kuczynski, an occasion on which we signed 15 agreements and decided to pursue 120 common projects.

With Bolivia, things have been less than optimal. Despite acrimony, Chile has carried out what we call a “silent integration.” Trade and investment have increased; there is a new Bolivian airline authorized to operate in Chile; Chile provides cooperation to Bolivia in the medical field (we recently celebrated the ten-year anniversary of cooperation by the Exequiel González Cortes in Chile and the Children’s Hospital of La Paz); Bolivians, mostly graduate students, attend our universities, many with scholarships funded by the Chilean government; and Bolivians continue to immigrate and settle in our country. At the governmental level, in July 2017 our Joint Border Commission met for the first time since 2013 and technical authorities at various levels will continue to meet in the near future. All of this while Bolivia argued, inconsistently, in the International Court of Justice of The Hague about a fully sovereign access to the sea through Chilean territory—in clear violation of the 1904 Treaty of Peace and Amity that fixed borders between the two countries in perpetuity—or calling simply for a return to a table of conversations, while President Evo Morales campaigned against Chile, and in favor of his political future, in inflammatory Twitter attacks.

With Argentina, we forged a very intense relationship, while also engaging in joint regional initiatives. We agreed on strategic points of action for the coming years, including physical connectivity, energy exchanges, integration into global value chains, and migration. We also signed a major trade liberalization

agreement, which will surely boost bilateral trade and investment. We have even launched a 2030 Strategic Forum, which is defining how both countries could face or imagine a preferred future.

## New Directions

All the actions I have described, plus our active participation in the Asia-Pacific Economic Cooperation (APEC) forum and in other initiatives, have positioned Chile as a strong promoter of economic integration in Latin America, the Asia-Pacific, and globally.

These are some of the new directions of the present and the future of regional and global integration.

To make progress toward sustainable development, however, we need to find answers and new ways to solve these national, regional, and global challenges of the twenty-first century. We need to benefit all citizens and focus on tackling the many inequalities that remain in our countries, not just in terms of income.

It will not be easy. That said, we have no other real option but to work with each other to build the new regional and international structures to confront these new realities.

## Notes

1. Norway and Cuba were facilitators, while Chile and Venezuela were accompanying countries of the process. All four, however, made important contributions at critical moments of the negotiation. [Ed.]
2. Scant progress was made in peace talks the ELN during the administration of President Juan Manuel Santos and their future under the new government of President Iván Duque remains uncertain. [Ed.]
3. “Present at the Destruction? Assessing Trump in Practice,” *Foreign Affairs*, June 29, 2017, <https://www.foreignaffairs.com/press/2017-06-29/present-destruction-assessing-trump-practice-new-foreign-affairs>. [Ed.]
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# The Changing Patterns of Regional Integration

Jorge Heine  
José Octavio Bordón  
Marisol Argueta de Barillas  
Caroline Freund

## China and Latin America: Jorge Heine

China is a key—yet often poorly understood—subject in Latin America’s international relations. I wish to offer 10 propositions about Sino-Latin American relations in the twenty-first century from an international political economy perspective.

**First Proposition:** The links that have emerged between Latin America and China in the course of the past 20 years or so signify the most important realignment in the region’s international relations in the past two centuries, especially for South America.

For most if not all of its 200 years of independent history, our nations have looked to the United States and to Western Europe as their main international reference points. Yet, in the course of the present century, this has changed dramatically. For Brazil, Chile, and Peru, China is their top trading partner and for many of the other countries it is their second largest trading partner. In the case of my own country, Chile, we export twice as much to China as we do to the United States. Chile runs a trade surplus with China, as opposed to the trade deficit we have with the United States. One quarter of all our exports go to China, a higher share than that of any other country in Latin America.

In terms of financial flows, in the past few years those from China to the region have been higher than those from the World Bank, the International Monetary Fund, the Inter-American Development Bank, and the Latin American Development Bank (CAF) combined. If this does not entail a major realignment of

the region's international political economy, I don't know what does. Nonetheless, this essential fact has not yet been fully internalized in the region, and we are still a long way from doing so.

**Second Proposition:** Contrary to the conventional wisdom, these links between China and the region are not new.

It is true that the rise of China and India in the new century constitute perhaps the defining fact of our time. And the notion that this only brings us back to the situation *ex ante*, that is, the one obtaining until the late eighteenth century, when China and India were the world's largest economies, is also quite widespread. What is less known is that actual trade between China and Latin America started as far back as the sixteenth century, so that the current trade boom between China and the Latin American and Caribbean (LAC) region repeats a pattern initiated four-and-a-half centuries ago.

Amazing as it may sound, the current flow of metals and agricultural products from the Americas to China and that of all sorts of textiles, from clothing to bed linens back to the Americas, had an earlier incarnation in the early days of the Spanish Empire, lasting roughly from 1565 to 1815, for 250 years, with remarkable duration and continuity.

**Third Proposition:** Globalization, in the sense of establishing regular exchanges between at least four of the world's five continents, was actually kickstarted by these links between China and the New World.

Specifically, by the regular trips of what is known as "*El Galeón de Manila*" (the Galleon of Manila) between Manila and Acapulco. As Peter Gordon and Juan José Morales have shown in their recent book, *The Silver Way*,<sup>1</sup> with the *tornaviaje*—that is, the return trip from the Americas to Asia across the Pacific—the Manila galleon provided the missing link in the world's global trade network, connecting for the first time all maritime routes in both directions. Gigantic ships of over 2,000 tons would bring to the Americas the rich silks of China and other parts of Asia, and bring back silver and other products from the Viceroyalty of Lima and elsewhere. From Acapulco, the cargo would go on to Mexico City, and then on to Veracruz, from where it would cross the Atlantic all the way to Seville.

For two-and-a-half centuries, Sino-LAC trade flourished, improving the standard of living of people in the Americas, making Mexico City into the first global city, and contributing to the financial and economic stability of China, for which silver was a key ingredient. The numbers are telling: a vast amount of the world's silver came from the New World, and about a third of that ended up in China. Those who are surprised about the boom in Sino-LAC trade in our time, should not be. If this commerce flourished in the sixteenth century, with transport and communications technologies very different from those available to us, it would appear only natural that it has once again come into its own in the twenty-first century.

**Fourth Proposition:** The pattern of exchanging raw materials for manufactured products was established early on, and continues to this day, with China selling industrial products and Latin America, commodities.

The real question is what can be done about this pattern. The irony is that often those who are in the forefront of denouncing this pattern of trade, saying it is harmful for the region, are also the most vocal opponents of anything that resembles industrial policy, a term that in fact has been practically banned from the vocabulary of many government economists in the region. One cannot have it both ways, arguing, on the one hand, that trade with China is harmful because it perpetuates an export profile based on mining and agriculture, but on the other hand opposing any effort at promoting industrialization, because that would amount to “picking winners and losers.” There are two different issues here: one of them is the increasing demand for commodities from China; the other is whether Latin American governments actively promote domestic manufacturing. To conflate the two is unhelpful.

**Fifth Proposition:** Denouncing trade with China as tantamount to promoting deindustrialization is to put the cart before the horse.

For ten years, roughly from 2003 to 2013, the “China boom,” in the words of political economist Kevin Gallagher,<sup>2</sup> was highly beneficial to regional economies, mostly in South America. Two questions come to mind: what was done with all the rents that were triggered by that boom? And second, did the rate of investment in the region increase as a result? The answer, in most cases, is that yes, debt was paid down, foreign exchange reserves increased, and social policies

were able to diminish poverty and income inequality, at least somewhat. But in terms of productive investment, as a rule, the rents from the China boom were not invested to diversify the productive structure or otherwise prepare the various economies for the days when the boom would turn to bust. In the first decade of the new century, the investment rate barely budged, growing by only 1 percent, to 19 percent from the 18 percent it had been in the nineties. This stands in stark contrast with the Chinese investment rate, higher than 40 percent.

**Sixth Proposition:** During the “China boom” years, the main driver of Sino-LAC links was trade, which increased 26 times from 2000 to 2013, when it reached \$265 billion. Since then, trade has flattened or even fallen and investment and financial cooperation are now moving to center stage.

Investment and financial cooperation require a more proactive role of governments than does trade. According to the traditional view, once China ceased to require such massive amounts of commodities, it would lose interest in Latin America and turn its attention elsewhere. Yet that has not been the case. Chinese banks are moving with great force into the region—in Chile there are two, the China Construction Bank and the Bank of China, and a third one is waiting in the wings. And the Chinese policy banks, like the China Development Bank and China Eximbank are keen to disburse funds to worthy projects.

In other words, there are a variety of Chinese entities willing and able to move into Latin America to finance a variety of different projects. The Chinese are especially interested in financing regional or sub-regional projects, of which there are precious few. I would argue that we are at a turning point in Sino-LAC relations. But whether we will be able to move into the next stage, with much higher Chinese investment and financial flows, will heavily depend on what Latin American governments are willing and able to do, both individually and collectively.

**Seventh Proposition:** China in LAC is no longer just about buying oil, iron, copper, and soybeans. China in LAC today is also about development.

The One Belt, One Road Initiative is an international development proposal that extends to the Global South (and to Europe) the formula that has worked well for China: build them, and they will come. As opposed to the notion that all

countries have to do is balance their accounts and keep inflation low in order to achieve growth, China believes that infrastructure and connectivity hold the key to growth and development. That is what China has done, and it has done so fairly well. For example, in the three-year period between 2011 and 2013, China consumed more cement than the United States in the entire twentieth century.

Consider that in 2008, when President Barack Obama was first elected, he was keen to rebuild U.S. infrastructure, including the building of bullet trains. In eight years in office, however, he was not able to build even one mile of a high-speed railway network. In those same eight years, from 2008 to 2016, China built 21,000 kilometers of high-speed rail, and today has more miles of high-speed railway lines than the rest of the world combined. The country that comes after China, Japan, has 2,500 kilometers of high-speed rail.

In my own country, Chile, we have been agonizing for decades about building or not building a tiny, two-kilometer-long bridge from Puerto Montt to Chiloé, a bridge that is still not in place. In 2017 China inaugurated a 50-kilometer, US\$10 billion bridge from Zhuhai to Macao and Hong Kong, in an effort to build up connectivity in what is known as the Greater Bay Area, in the Pearl River Delta, and create a competitive cluster of metropolises, including Guangzhou, Shenzhen, Hong Kong, and Macao.

China's success is not simply a function of its size. It is about a certain mindset, a capacity not just to plan, but to execute. China is more a continent than a country, and for thousands of years its rulers tried, mostly unsuccessfully, to integrate its vast territory, strewn with enormous rivers and high mountain ranges. Over the past decade, China has managed to achieve integration through a) mobile telephones, and b) bullet trains. Chinese citizens now travel with great ease across their country in great comfort on the fastest trains on Earth, and communicate with each other through the 1.3 billion mobile phones, their 800 million WeChat accounts, and the 750 million Internet users. We could do the same in South America if we had a different mindset.

**Eighth Proposition:** Latin America's infrastructure could benefit tremendously from Chinese investment, which could do wonders to integrate our own vast expanses, especially in South America.

Many of our economies are export-oriented, yet our infrastructure leaves much to be desired—this is the case even in Chile, widely deemed to have made much progress in this field. Whereas within the OECD countries logistics and

transport make up around 8 percent of the final cost of an export product, in Latin America this goes as high as 13 to 17 percent, thus affecting our competitiveness. Argentina, Brazil, and Chile supply around 20 percent of all the food imported by China, and all indications are that this will continue to rise in years to come. A significant investment in bi-oceanic corridors, trans-Andean tunnels, railways, highways, and mega-ports in the Southern Cone would do much to change this, and position all of us much better vis-à-vis Asia, which by 2050 will represent half of the world's product.

Yet this kind of investment in infrastructure is not taking place. Our mindset is exactly the opposite of the Chinese one. Our great fear is to build a two-kilometer bridge that will end up as a white elephant, underutilized and wasted. Therefore, it is best not to build it. The population numbers are, of course, quite different. But that hardly explains the lack of progress in regional infrastructure, where not only are we making little progress, but also in some cases going backwards. This is the case with the *Ferrocarril Transandino* (Trans-Andean Railroad) from Chile to Argentina, built in the early years of the twentieth century and closed in the 1980s, with no attempt to reestablish it in the past 30 years.

I once saw a caption showing the number of subway lines in Rio de Janeiro in 1993, which were two, and the number of such lines in Shanghai, which were zero. Fast forward 20 years: Rio still had the same two, and Shanghai had 14, with over 500 kilometers of subway lines. In Chile we are very proud of the Santiago subway, yet it has taken us 50 years to build 100 kilometers of subway—that is an average of 2 kilometers a year. In Shanghai they built 500 kilometers in 20 years, an average of 25 kilometers a year. It is called “China speed.”

Why does China grow so fast? There are many reasons, but at least one of them is because China does things quickly.

**Ninth Proposition:** Much as in infrastructure, Latin America's energy matrix could benefit considerably from Chinese cooperation and investment.

The conventional view is that in matters pertaining to energy, all China wants is our oil. Again, this is a distorted view of a much more complex reality. It is absolutely true that Chinese companies are interested in Latin America's oil. But they are also keen to invest and be part of the regional energy scene. The Chinese firm State Grid, the biggest energy company in the world, has made major investments in Brazil, where it has about half of its investment abroad. State Power Investment

Company (SPIC) is in Chile, with some US\$1 billion in assets, and is looking at investing another US\$2 billion in energy projects. The total Chinese investment portfolio in Argentina right now is around US\$30 billion, much of it in energy, including hydro and nuclear plants.

Yet, in some ways the most exciting Chinese energy project is the Global Energy Interconnection Development and Cooperation Organization (GEIDCO), an entity that arose from a 2015 proposal by President Xi Jinping. Its main purpose is to facilitate efforts to meet global power demand with clean and green energy alternatives, by emphasizing interconnectivity, co-construction, and sharing, as new ways for fighting climate change. The basic notion is that having a power system that is as interconnected as possible is just as important as building new energy sources and energy-saving technology. All help to accelerate the development of clean energy and promote the energy transition from carbon-based sources.

We all know how fragmented Latin America's energy systems are—even within countries. China, through GEIDCO, underscores how much there is to be gained by integrating and interconnecting those systems, something for which the Chinese bring both capital and expertise. China leads the way in renewable energy sources—both in solar and in wind, in terms of volume and cutting-edge technology—and is in an excellent position to make a significant contribution to the region.

**Tenth Proposition:** At this time, there is a basic convergence of interests between China and Latin America in terms of development priorities.

Some confusion is generated by the fact that China often uses the somewhat old-fashioned language of South-South cooperation to refer to matters that correspond quite straightforwardly to its national interest. Carlos Moneta and his colleagues in Buenos Aires have argued in their recent book, *La tentación pragmática (The Pragmatic Temptation)*<sup>3</sup> that Chinese infrastructure proposals for the Southern Cone are nothing but a ruse to get products from the sub-region faster and more cheaply to China for the benefit of the Chinese consumer. And that because such priorities have nothing to do with South America's own policy priorities, they should be disregarded.

I could not disagree more. Of course, it is in the interest of China to get products faster and in a more efficient way to its own market. But so it is for our own

countries. There are 200 countries around the world, and all of them want a piece of China these days. Competition is fierce and cutthroat. Latin American countries should be the most interested in safeguarding and expanding those pieces of the Chinese market they have already managed to secure.

A key statistic to keep in mind is that China has 19 percent of the world's population and only 7 percent of the world's fresh water reserves and 7 percent of the arable land. This means that it will always have to import food. Latin America, whose own equation in these matters is just about the reverse, is well-positioned to be China's main food supplier. But many others want that as well, and it is not possible to stay for long in that position if you aren't competitive.

The art and science of foreign policy rests on aligning one's own interests with those of others in such a way that both benefit: in a favorite Chinese expression, "win-win cooperation." China is not promoting the infrastructure and energy development of Latin America out of its love of humankind. It does so because such a policy serves its own interests. As it happens, I do think that building up our infrastructure and our energy matrix and interconnectivity is a very good thing, and would be of great benefit to all our countries. If we could integrate South America digitally and physically the way China has integrated its own mainland in the course of the past decade, "*otro gallo nos cantaría*" ["A new day would dawn"].

## José Octavio Bordón: South American Integration in a Global Context

The end of the Cold War brought, on the one hand, greater relative autonomy to the countries of Latin America, as the world system became more polycentric. This period also witnessed, especially at the dawn of the twenty-first century, the explosive economic growth of China and its greater presence in our region. Chinese demand for commodities generated large trade surpluses for the countries of South America, while manufacturing exports were less dynamic and even stagnant.

At the same time, the technological revolution produced major changes in the functioning of the global economy; and parallel changes in communications had a significant impact on political systems. Processes of economic change brought about a certain decoupling of investment and the expansion of the financial sector, something unusual for the region. And reductions in poverty and a better quality of life for many of the region's inhabitants went hand-in-hand with an increase in inequality.

The increased presence of China at the global level was accompanied by a growth in Brazil's regional and global presence and greater expectations regarding its economy. Scarcely five years ago it was impossible not to consider, as part of a reconfiguration of the global economy, the phenomenon of the BRICS (Brazil, Russia, India, China, South Africa). Today, however, the BRICS are no longer part of the discussion. The same is true of ALBA (Bolivarian Alliance of the Peoples of the Americas), an alliance led by Venezuela that has all but disappeared. Several years ago there was also a tendency to speak of a Latin America divided between the countries of the Pacific coast, characterized by liberal economies and open trading systems, and the Atlantic coast countries of Mercosur.

Now we are in a different moment—characterized not only of the renegotiation of NAFTA but also Brexit and the recession in Brazil (from which, I am confident, the country will emerge, as it always does.) Just as significant is the dynamism in the dialogue between the Pacific Alliance and Mercosur, what Chilean Foreign Minister Heraldo Muñoz has dubbed, “convergence with diversity.” The relationship between Argentina and Chile has contributed greatly to this new context. For example, Chile not only has about \$30 billion invested in Brazil, but also \$18 billion of investment in Argentina, something we believe will grow. We also hope to increase the amount of Argentine capital invested in Chile. Since 2014 and accelerating in 2017, there have been a number of meetings at the ministerial and vice-ministerial level to explore questions of integration between Mercosur and the Pacific Alliance. There have been very specific discussions in the concrete areas of customs cooperation, certification of origin, and regional value chains. This dialogue is ongoing.

This new dynamism is unfolding without confrontation and in search of new ways of responding to changing circumstances. At the economic level, institutions such as the Inter-American Development Bank (IDB), the Latin American Development Bank (CAF), and the UN Economic Commission for Latin America and the Caribbean (ECLAC or CEPAL) are functioning well. But other regional institutions appear stuck. The OAS works on traditional political issues, but important majorities clearly cannot make decisions. UNASUR has been without a secretary general since January 2017. This is worrisome.

We must approach issues with neither naïve optimism nor tragic pessimism, but rather, with a complex but optimistic realism. As Abe Lowenthal said years ago, we must avoid the intellectual and political laziness of being overly optimistic when things are going well, and overly pessimistic when there are difficulties. The “golden age” for many commodities has ended and will not return. But this



## Strengthening democracy within republicanism is fundamental to the process of integration and economic development.

does not mean that growth is impossible or that there will be a global recession. For those (largely in the Asia-Pacific) who have grown in the past to continue growing, and for those who haven't been successful to succeed in the future, we need a new model of market economies within democracy. We need more and better investment and more and better jobs. None of this will be simple or easy. Argentina chairs the G20 meeting at the end of 2018. Argentina must work with the other Latin American members of the G20, Mexico and Brazil, to shape an agenda that addresses the challenges facing the entire region, challenges which no country can confront on its own.

I conclude with a reflection about democracy, which at one level is unrelated to the economy but at a more fundamental level has everything to do with the economy. We have short memories regarding the anti-democratic republics in the region and we should worry about those who, in the name of democracy, dismiss republicanism or the need for checks and balances. Or, about those who in the name of participation dismiss representation, or in the name of representation dismiss participation.

We should see to it that more democracy generates stronger republics—that is, more checks and balances—and that more such balances generates more democracy.

We face the challenge of generating more investment and better jobs and of reducing the gap between Latin America and emerging countries in other regions. In our region, we should not forget that strengthening democracy within republicanism is fundamental to the process of integration and economic development.

## Marisol Argueta de Barillas: Central America and CAFTA-DR

These are exciting times. We need to actively promote the integration that is now finally taking place in Latin America. Mercosur (Argentina, Brazil, Paraguay, and Uruguay) accounts for over 38 percent of inter-regional trade. The countries of the Pacific Alliance (Chile, Colombia, Peru, and Mexico) account for a little more than 50 percent. Trade represents a tremendous opportunity to unleash the potential of domestically-led economic growth. Latin America should not forego this opportunity to promote more integration, more productivity, and more competitiveness.

In the World Economic Forum's 2017 *Global Competitiveness Report*, only three Latin American countries ranked in the top 50. Chile remains first in Latin America and in the thirty-third position overall. Costa Rica increased seven positions, climbing to the forty-first position. And Panama remains stable in the fiftieth position. These figures need to improve. Productivity must be part of the Latin American agenda. If we are not productive, if we are not competitive, we will not be able to insert our region into global value chains.

This analysis is not news. We are lagging in institutions. We are lagging in the efficiency of goods and capital markets. We're also lagging in labor market efficiency and innovation. I emphasize innovation because competitiveness will no longer be driven by the traditional factors that we have used to measure it over the past 20 or 30 years. Innovation and technological readiness will be true drivers of change and productivity. Latin America has an important potential here because of our demographic dividend (the high percentage of the population that is of productive age and who can contribute to economic growth). If we create the right ecosystems for the youth of Latin America to be creative, to be able to innovate and to foster entrepreneurship, we can make a big step toward our region's development.

Foreign Minister Muñoz and Ambassador Bordón shared information on the Pacific Alliance and Mercosur. I will focus on a region that should not be forgotten: Central America.

Central America should not be isolated from the patterns of integration into which South American countries are injecting new dynamism. Central America initiated its integration efforts in 1951, with the creation of the Organization of Central American States. That was the first attempt at integration in all of Latin America. In 1960 the Central American Bank for Economic Integration (BCIE) was created. Then we had the so-called Soccer War between Honduras and El

Salvador in 1969. But soccer was not the cause of that war. In reality that conflict was caused by the absence of norms to regulate the transit of goods and people from El Salvador to Honduras. And then in 1979, as we all know, more conflicts arose in Central America. These internal armed conflicts stalled integration efforts until 1991, the year that saw the creation of the Central American Integration System (SICA), and 1993, when the institutional process of Central America's integration system was launched.

The Central American nations include El Salvador, Guatemala, Honduras, Nicaragua, Costa Rica, and Panama. Belize joined SICA in 2000 and the Dominican Republic in 2004. These countries together constitute a market of 55 million people, a market that is a little smaller than Italy's but larger than that of Colombia, Venezuela, or Peru. Central America has a chance to become part of the very promising process of integration that is underway elsewhere in the region. Central Americans should be encouraged to become part of this process and others in the region should not forget that very vulnerable region in the center of the Americas.

Of course, the Central American and the European Union association agreement has injected dynamism into our integration process and has achieved some very important political and economic agreements.<sup>4</sup> And the Central America-Dominican Republic-United States Free Trade Agreement (CAFTA-DR) has been a useful tool for Central American integration, as we negotiated together as one bloc.<sup>5</sup>

CAFTA-DR opened the opportunity for increased trade. Today Central America exports to the United States are worth \$18 billion. This sum might seem marginal in comparison to exports from Mexico to the United States. But the figure represents a large percentage of Central America's GDP and a very large percentage of the sub-region's total exports, while the trade balance is also beneficial for the U.S. Keeping CAFTA-DR on the agenda and allowing the agreement to continue is extremely important for the sustenance of Central American economies.

In order to enhance productivity it is also important to introduce new elements, such as digital markets and the digital economy. Their expansion would be positive for trade with Central America as well as for hemispheric trade overall. All businesses—whether a small company or a large multinational—that use an online platform need a dynamic, agile framework in which to operate.

Changes in this new era of the fourth industrial revolution are taking place very fast and constitute a different set of factors as we think about how to advance

integration. We need to create an environment that allows a new, more innovative digital economy to thrive in the hemisphere.

Technology and communications are changing our societies, our economies, and us as individuals. We're moving from an inter-connected world to a hyper-connected and completely interdependent world. We need to understand how power structures are changing and assess the impact that technology and communications have on those changes. We also need to understand the effect of technological changes on the environment. We are the first generation to feel the impact of climate change and we are the last generation with the real potential to prevent a global ecological calamity.

Finally, we need to develop new ways of thinking in order to adapt our integration model to the changing realities. New regulations, more agile protocols, and better-aligned payment systems are only some of the factors to be explored. It is imperative that we do not look at integration through the traditional lens of the past.

## Caroline Freund: The Future of North America

As late as 2016, trade discussions focused on mega regional agreements: the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (T-TIP). Trade seemed to be going in just one direction: toward big regional agreements. In part, these agreements were a way to deal with China, which was excluded from them. They represented a way to rewrite the rules so that as the agreements expanded, they would help a country like China potentially change some of its behavior.

The fundamental question now is whether the world is moving toward more regionalism or less. The NAFTA renegotiation was certainly part of the trend toward less regional integration. The negotiation—at least from the U.S. perspective—was not focused on increasing trade, but rather on balancing bilateral trade, which is very different. The goal from the U.S. perspective has been to reduce the trade deficit. Such an approach is very contradictory with the way supply chains are formed and function.

There are three main areas of tension that arose out of the NAFTA agreement. One has to do with the fact that NAFTA integrates two very advanced countries with a developing country. There is a North-South tension that arises because wages are lower in Mexico, and labor and environmental standards are different.

The second area of tension concerns regional supply chains. NAFTA trade is about supply chains; and in some ways the functioning of supply chains seems

like trade on steroids. Supply chains are not just about trading goods that are produced more efficiently in the United States with goods produced more efficiently in Mexico. They involve looking at the whole chain of production and saying: “you (Mexico) produce the wiring harness for the car, which is really labor intensive, and we (the United States) will produce the transmission, which is much more technical.” Trade takes place not just between firms but within large multinational firms that have establishments on both sides of the border. The whole production process becomes more efficient as a result of their development, but there are adjustment costs, as part of the production process—and the associated jobs—are moved across the border.

The third tension arises around issues of national sovereignty. Trade agreements increasingly include some provisions that constrain domestic rulemaking. Investor–state dispute settlement (ISDS), for example, allows foreign companies to sue a domestic government in a neutral forum over changes in regulations that discriminate against their established businesses. What seems wrong or unfair to people in the host country is the idea of a company—and a foreign company, no less—suing a government. The purpose of ISDS is to prevent disputes and expand investment, but there are genuine concerns about “fairness.”

International data flows raise a host of new regulatory issues that also impinge upon sovereignty. Should personal data be stored abroad? Is the source or host country government entitled access to data? How can countries protect their citizens’ privacy? Harmonizing product standards is another new area that makes people nervous. Concerns came out strongly in the T-TIP negotiations, where, for example, Europeans worried about being forced to accept chicken meat rinsed in chlorinated water. While governments want control over domestic regulations that serve their populations, in many cases it is better and more efficient to have common international standards.<sup>6</sup> At the extreme, imagine a world of self-driving cars, where American cars cannot communicate with Japanese self-driving cars, which cannot communicate with European self-driving cars. This would be both inefficient and dangerous.

All of these issues tread on sovereignty because they impact the ability of individual countries to write and enforce their own laws and regulatory frameworks. New trade agreements will have to devise ways to handle these kinds of issues in a way citizens perceive as fair. Renegotiating NAFTA should be focused on these new economy and deeper integration issues. But, instead, it has been focused on balancing trade, which means it is largely about U.S.-Mexico trade, and largely about autos, where the main trade imbalances lie.



There are much better ways to deal with the problems that are affecting workers, most of which come from simple structural change and technology. We can deal with that through labor adjustment policies. Going backwards on trade is not the right way.

### *Focusing on NAFTA*

NAFTA was supposed to help with the issue of the convergence between North and South. One of the major disappointments with NAFTA is that convergence among Mexico, the United States, and Canada has not occurred.

In terms of per capita income growth, Mexico has the same rate of growth as Canada and the United States. Mexico has not grown faster since NAFTA went into effect. This means that NAFTA cannot have hurt the United States all that much. If NAFTA led to rapid Mexican industrialization at the expense of Northern deindustrialization, we should see Mexico growing faster than the United States and Canada. That has not happened.

Perhaps the biggest gain from the NAFTA agreement was a long period of friendly relations between the United States and Mexico.

While Mexico did not grow faster than the United States or Canada, the tensions having to do with the development of supply chains have been especially pronounced. Supply chains highlight wage differentials because jobs are created (or destroyed) by the same firm across borders.

The question arises, “If Ford builds a plant in Mexico, could those jobs have been created in the United States?” But that line of thinking is erroneous: the fact that there’s a Ford plant in Mexico producing certain parts, and a Ford plant in the

United States producing other parts means that the industry itself is more competitive. More cars can be produced at a lower cost, thereby raising the demand for Ford cars as opposed to autos from other producers in Asia or Europe. NAFTA has also brought investment from Asia and Europe into North America because of the auto industry. So instead of importing cars, we're producing them in the region.

Supply chains have benefitted from regional integration. They most likely would have developed to a certain extent anyway, because trade costs and distance matter a great deal. But having a trade agreement gives investors a sense of security about trade policies. Policy predictability has facilitated trade, benefiting certain industries, which has been good for the United States and good for Mexico as well. To be sure, some industries and workers have lost because of expanding trade, but the gains more than compensate the losses.

Protectionism will not address the kinds of issues arising in today's new and more integrated economy. Without competitive regional supply chains, products from North America will not be competitive with products from Europe and Asia. North American factories and workers will lose. There are some challenges of labor adjustment, but governments should address the challenges and move forward. There are ways, for example, to deal with problems that are affecting workers, most of which come from simple structural change and technology. We can deal with that through labor adjustment policies. Going backwards on trade is not the right path. The world has experienced a long period of growth and prosperity—and most importantly peace—as regional and global integration expanded.

## Notes

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## Biographies of Contributors

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**José Octavio Bordón** is ambassador of Argentina to Chile. He previously served as the director of the Center for Global Affairs at the Universidad Nacional de Cuyo and is a former deputy, senator, and governor for Mendoza Province. He is also a member of the board of directors of the Argentine International Relations Council (CARI) and president of the advisory council of the Center for the Implementation of Public Policies for Equality and Growth (CIPPEC). Bordón was elected governor of Mendoza Province in 1987 and stepped down in 1991. The following year he was elected to the Argentine Senate. He previously served as Minister of Culture, Education, and Sciences for the province of Buenos Aires and as ambassador of Argentina to the United States from 2003 to 2007. He graduated from the Universidad del Salvador (USAL) with a degree in Sociology.

**Fernando Henrique Cardoso** is a Brazilian sociologist, teacher, and politician who was president of Brazil from 1995 to 2003. In 1997, voters approved an amendment to the constitution that allowed the president to hold consecutive terms, and in 1998 Cardoso became the first Brazilian president to be reelected for a second four-year term. Barred constitutionally from seeking a third consecutive term, Cardoso left office in 2003. Cardoso entered politics in 1986 when he was elected senator from São Paulo. In 1988 he cofounded the center-left Brazilian Social Democratic Party. In 1992, after President Fernando Collor de Mello was impeached for corruption, Cardoso resigned his seat in the Senate to become foreign minister. In May 1993 he served as finance minister, overseeing negotiations that produced a number of anti-inflation measures. Cardoso became a professor of sociology at the Universidade de São Paulo in 1958, but the military government that took power in 1964 blacklisted him from teaching in the country's university system. He went into exile, teaching

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**Claudia Escobar** is a former magistrate of the Court of Appeals of Guatemala. Reelected in 2014 to a second term, she resigned due to executive and legislative interference in the judiciary and relocated to the United States because of intimidation in Guatemala. She is a respected legal scholar, who has taught at Guatemalan universities. She is founder of the Judiciary Institute as well as the Association for the Development of Democratic Institutionality and Comprehensive Development for Central America (Asociación FIDDI), organizations dedicated to promoting the rule of law in Guatemala. Escobar earned law degree at the Universidad Francisco Marroquín in Guatemala and obtained her PhD at the Universidad Autónoma de Barcelona. She was a fellow at Harvard University from 2015 to 2016, becoming the first Central American to be awarded a fellowship at the Radcliffe Institute for Advanced Study.

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