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THE FUTURE OF BRAZIL AND ARGENTINA

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## P R O C E E D I N G S

MS. GRAHAM: Welcome to Brookings. My name is Carol Graham. I'm a Senior Fellow here. I've been here for a long time working on all sorts of things from Latin American Economics to happiness and well-being. And we're here to talk about the intertwined economic and political fortunes in the southern cone, the future of Brazil and Argentina, and what seemed to be a happy story several years ago is getting a little more complicated. I remember having spent a lot of time during the reform era and watching Latin America for the most part really turn its macro economies around and having a certain amount of pride at looking at the region at the time of the financial crisis and noting that it was probably the region that suffered the least and that navigated the crisis the best of any. But now things are looking a little more complicated. Part of the story is obviously the global economy, a sort of demand story, prices for commodities -- all kinds of things that Latin American economies still have to navigate and worry about. But the other part of the problem or complication right now is the political story and here the two big southern cone countries, Brazil and Argentina are each in their own way, mired in some complicated political problems, which I certainly can't disentangle very well, but we have many people here who can. So without further ado, I'm going to turn it over to our panelists and then we'll have presentations, a panel discussion and then open it up for questions.

So I'd like to introduce the panel. We have Ernesto Talvi who is Director of The Brookings Global CERES Economic and Social Policy Initiative in Latin America and also directs CERES in Uruguay, Harold Trinkunas, who is Senior Fellow and Director of the Latin American Initiative in our foreign policy program, and the two initiatives coordinate quite closely. Then we have Raul Juste Lores, who is the Washington, D.C. bureau at Folha de Sao Paola and Silvia Pisani who is Chief Correspondent en La

Nación here in Washington, D.C. as well. So, we're going to start with Raul, if that's all right and then Silvia, then Harold, and then Ernesto. And we're going to hold you to eight minutes each, and I was just told that I have fame as a moderator, for being a real witch, which means I will hold you to eight minutes each. So there we go. Raul, over to you.

MR. LORES: Okay, good afternoon. Thank you very much for the invitation. Eight minutes, I must say that -- I mean, to describe the soap opera that Brazil is experiencing those days, I need properly the five seasons of Game of Thrones to describe all the juice and gruesome details of Brazilian politics. But I'll try to focus just on the present, since I don't have the Game of Thrones length here.

Until yesterday, the Minister of Finance of Brazil's Joaquim Levy was here in Washington for the IMF meetings. And he spoke freely about the adjustments, the new economic policies of Brazil, of how he is (inaudible) in all senses, the policies of the last four years. And he talked about education, social programs, environment, smoking -- everything you can imagine. I mean I've never seen a Minister of (inaudible) cabinet speak so freely in the last four years. So something has changed profoundly. Clearly, Levy is being treated as our savior. And I think there are certain reasons for that. First of all, Dilma was just reelected in October, in a very bitterly aggressive dispute election. And since then, her popularity has dropped a lot. And there was a poll last month that established that. Nine Brazilians in ten disapprove her governance and her job and even her personal favorability, is negative in 77 percent. That's a lot. So for the last 20 years, Brazil was extremely lucky to have two very political savvy presidents, Fernando Henrique Cardoso and Lula, who could manage a kind of consensus, and conservative economic policies and liberal social programs and social policies. And they could manage to rule the country where there are 28 political parties in Congress. So if you guys watch Congress and you see how hard it is to make two political parties to

create any kind of consensus, imagine trying to run with 28 political parties. And I would say most of them are not (inaudible) so you don't need only to present your policies and convince them, but most of the time, you need to distribute political favors, cushy jobs and part of your budget to make them happy. And I think President Dilma Rousseff clearly doesn't have the talent of Lula or Fernando Henrique Cardoso in doing that job. She doesn't mask her lack of interest in talking to Congress representatives, in talking to her own political party and also nothing new to Americans -- I mean presidents who seem to dislike profoundly Congress and talk to political parties. So we are experiencing the same problem but again, with 28 political parties. And the commodity boom that impacted a lot of Brazil, it wasn't the only responsible for the boom of Brazilian economy in the last decade. We had this kind of very strong social programs, of cash transfer of electricity and water for the poorest areas of Brazil, grants for students, affordable housing and so on. So there was a boom in the domestic consumption, but also, China helped us a lot. And since 2009 with China, is the most important trade partner of Brazil, by far, comparing either to the U.S. or to the European Union.

And this commodity boom is over. And during many years, this commodity boom has spoiled Brazilian policies in the way the government was able to hire even more public workers, and rising pensions, and rising public salaries and so one. And now it's the time of the tough choices. And I think (inaudible) made a very, very poor job in the last election. Nothing new about the lying during campaigns, but I think we overestimated the hope and the optimism of Brazilians saying that everything was fine. So it's very difficult after you say that you want to be re-elected without making any sacrifice. And if the opposition, the conservative opposition would be elected, adjustments would take place. And now you are elected and there are adjustments everywhere -- people are not happy. If you talk to some hardcore Brazilian leftists, you

try to paint the situation as the bad losers -- the conservatives and so on who are just crying because they didn't want to lose the last election. But we are not a country of 90 percent of rich people. So even poor Brazilians, middle class Brazilians, who are and were extremely grateful to the workers body social revolution, they are feeling gipped. They are feeling they were betrayed. And so that's a big challenge.

But as I started, and I don't know if seven minutes have already passed, but so -- one minute left, seven minutes okay. So Joaquim Levy, the new minister, is changing a lot of what's going on in Brazil. And not only him, Dilma appointed a minister of agriculture, and a minister of trade that are very business friendly. So in a way that's a changing policy. The problem is, and that's a big problem, is in politics.

Dilma knows that now she's extremely unpopular, political parties see that the President is bleeding in public. And you can see that it will be harder and harder to approve the reforms that are badly needed in Brazil. Our FBI fortunately is working a lot, and because it is working a lot, and properly, because Brazilian media is free, and because our judicial system is independent, we still have many, many politicians to send either to jail or to trial because of many corruption scandals. Many. So we don't know, and I don't have a crystal ball either, to realize if Levy can be successful, these (inaudible) economic policies while a good chunk of the government is just afraid if they will remain free until 2017. And that's the big question mark now. Thank you.

MS. PISANI: Thank you. Hello, I am Silvia Pisani. I am from Argentina. I was born in Argentina, raised in Argentina, and I have been the last fifty years trying to understand the country I love. So this is not the Game of Thrones, but more or less, so thank you, thank you so much for being interested in my country. I will try to explain to you in three very easy points, how do I see the things for the next future. Well not so easy.

As they say, I am the correspondent of La Nacion, which is one of the main newspapers in Argentina, one of the main opinion makers. But these opinions and these points of view are going to be only mine. So this is a good thing, if I am mistaken for sure, I will be, this is going to only be my fault and not the newspaper. So thank you for being here, as Raul said, Brazil and Argentina, we have a lot of things in common, and we tend to think that our fates are linked. But it's a difficult relationship between the two countries. And from the beginning, the main point that we have to understand is that while most of the problems and the scenario is the same -- for example what's going on with the commodities, the big change in the international scenario is more or less the same. The big difference between the two domestic scenarios is that Brazil is just starting a new period for Dilma. While in Argentina we are going to have elections in the next seven months. So that's the big difference between the two countries. So it also means that there is a big expectation of change which for sure will happen.

And so, everything that we talk about today is basic in April 2015, so in May it's going to probably be another scenario and in July it's going to be another one, so the things are getting very dynamic right now in Argentina.

So first of all, so the big difference is that we are going to face elections. Second, we have, and this is the second point, maybe we can focus then on this point for the conversation. The big challenges, this new scenario, open challenges, is going to open challenges in the economic field. Why? Because we are facing hard problems which are difficult to resolve. Inflation, have you ever heard about inflation in Argentina? Well, we are facing inflation, we are facing imbalance in the fiscal, we are facing restrictions in the monetary field. And, I don't know if you've heard about them, but we are having a lot of restrictions in the market because of the holdouts. Have you heard about them? Yes, okay. So that's the full scenarios that we are going to confront in the

economic field. And I will say that in my point of view if you ask, which are the most important, I would say that inflation, because that's linked with the political and the syndication, the unions and it's going to be difficult to deal with that, and also the holdouts. I think that there is a big expectation in the market about what's Argentina and the new environment going to do with the holdouts as you know -- Christina (inaudible) didn't want to pay or to negotiate with these holdouts, they called them the (inaudible) funds and that's a statement. So I think that's a bigger expectation of change after the elections.

And so the second point is the economic field, and then we have the political scenario. And this is very interesting because we are dealing with the (inaudible), which is a very interesting party and a movement. You can find a lot of books about this and I only have four minutes left, so I will try to do it shorter, but the first thing that we have to try to understand when you look at Argentina in the next months is how are going -- this is like when you break a marriage -- it's like a divorce. How are you going to deal with the other partner in a new scenario? So how it's going to be -- the new scenario with the (inaudible) after twelve years in power, out of power. And this is very interesting to see, and this is going to be a very strong conditioning for the next government. We have, who is going to be the next government? Do you know? Nobody knows, but we are going to know that on October 30. But the relationship between the (inaudible) out of power and the government is very different -- who is the winner, it depends on who is going to win. One scenario, if the winner is (inaudible) which is very more or less linked to the Casa Rosa, to the pink house, it's a very different scenario if the winner is (inaudible) which is now in charge of the city of Buenos Aires. And it's a very different scenario if the winner is Masa, which was years before with the president and now is in the opposition.

So this is very different scenarios, we can explore all of them if you want, but the main question is, what's going to do Christina? Christina is going to be a very strong player, and how is she going to play, and she is very good in mysteries so, we don't know still how she is going to play, but this is going to be a big question for sure.

And then, this is the big scenario, what's going in the international scenario and how that will affect the domestic, what's going to happen with our economy and the main problems. Then who is going to win the elections and how is going to be this new relation, between the winner and the government that is leaving the power. And then we have two more things to deal with and this is the new, also the new scenario that we have. We have some new problems in Argentina, we don't speak a lot about them, but for me they are a very big concern, which is when is the narco traffic, we are having a strong presence of that problem in Argentina -- stronger, stronger each day. Still it is in the policy pages of the newspapers, but I think it's entering in politics, in sports, in business, in everything. The other one is that we have a society deeply, deeply politicized, deeply divided, and so this is the scenario that we are going to face from October 30, which the elections and the new government which is going to be in power on December 10. We can be together if you want, on December 11, we can speak again. Thank you so much.

MS. GRAHAM: Thank you Silvia, and also, again for sticking to the time. So we'll have more time for discussion as well. Okay I'd like to turn it over to Harold, please.

MR. TRINKUNAS: Well thank you Carol, happy to be here to talk about Argentina and Brazil. I'm going to focus more on the implications of the present crises in the two countries on their foreign policy. Specifically what I'm going to be talking about is first of all, how their foreign policies and relations to each other are linked and have been

linked over the past decades. But also, look at how each country is using its foreign policy going forward to help address the present crisis each of them face and argue they have picked very different strategies as we look at the road ahead which I think will have implications for the relations with each other and also with other countries in the hemisphere and the United States.

So I think one of the things to keep in mind and I think we kind of lose sight of this, we've gotten so used to it -- when we think about South America as being sort of a peaceful region, a region at least in terms of relations among states, a region that is focused on regional integration -- creating new institutions such as Una Sur and (inaudible), is that really one of the most important changes I think in international relations for South America in the last century really was the resolution of the Argentine-Brazilian rivalry. Historically Argentina and Brazil were always rivals and concerned about each other's power, but their rapprochement in the 1980s really is what set the stage for many of the political changes that came after in the region and for creating the possibility of a regional integration project, and Argentina and Brazil very consciously for at least two decades worked on developing those institutions that supported that relationship, a new relationship between the two of them -- including not just Mercosur, the trade pact, but also in the security dimension. For example, agreeing to end each other's military and nuclear programs and create an inspection regime called ABACC that sort of showcased their new direction in foreign policy, their ability to trust each other, their ability to work together, and I think as we think ahead about what comes next for both countries, you have to keep in mind even though Brazil isn't really a country that has international allies, Argentina is one country that is always sort of in a special relationship with Brazil. It's one of the most important countries for its foreign policy and so everything that Brazil does as it looks out at the world, it always keeps one eye on what's

happening in Argentina.

Let me talk briefly about Brazil and Argentina separately and sort of how they look at their foreign policies as they think about what comes next. Well from the Brazilian perspective, I think their ambition over the past decade has been to use the commodity boom, the resources that sort of powered their social revolution at home, to also power Brazil's rise in the world -- its ability to play a greater role in shaping the rules that governed the liberal international order. And at its core Brazil strategy was to use soft power -- by soft power we mean the power of attraction. The ability to lead by showcasing an attractive social, economic, political model at home -- and Brazil had that. In the sense of it had achieved economic growth, it achieved democratic consolidation, respect for human rights, a vibrant media, in higher levels of social inclusion the growth in the middle class -- this was an attractive narrative. And if you look at the Lula administration, Brazil deliberately tried to use this to project a greater national presence, I think President Lula probably opened more embassies, new embassies overseas than any Brazilian president before or since.

Now this was important because Brazil in a sense was showcasing an alternative to more authoritarian models of development that we'd seen in Asia. The problem now of course with the crisis at home it's not just that the economic growth has slowed down, which obviously undercuts the power of attraction of the existing sort of political and economic model, but the corruption scandal also undercuts Brazil's soft power. And I think what we're looking at going forward is that Brazil in a sense, its foreign policy is going to have to in fact retrench. In fact we've already seen retrenchment in the foreign ministry budget. Brazil is rethinking its foreign policy and in fact spending a lot more time trying to improve its relationship with the United States in the past few months as part of its way of thinking of how it can restart economic growth at

home.

So by contrast I think Argentina has always seen the regional integration project, its closeness with Brazil, as a way of changing its foreign policy so it can focus more on its own development to realize that it could no longer compete with Brazil. But instead Argentina focused, I think especially if you look back at the 1990s, at still playing an important role in the world stage but as a thought leader -- norms on human rights, on accountability, on its economic liberal modeling that sort of helped Argentina in a sense, punch above its weight when it came to international relations. That worked pretty well up until the financial crisis in the early 2000s. And since then Argentina has really taken quite a different path, it's turned much more inward, it's lost some of that global projection that it once had. And specifically during the government of President Christina Fernandez, it's really become much more antagonistic towards the liberal international order. The policy of being much more confrontational with the United States, with the United Kingdom, closer to China, and to Russia, in a sense that as part of that somewhat different international strategy of having a more confrontational demeanor abroad, in a sense perhaps as a way of distracting from some of the issues at home and justifying sort of the government's nationalism and sort of the best political actions that its taking at home.

So I think when we think -- Carol how am I doing on time?

MS. GRAHAM: Two more minutes.

MR. TRINKUNAS: If we think about what comes next in each of these cases, I mean Brazil really thinks about -- needs to think about how does it restart its economy and how does it solve its domestic political crisis, especially the corruption scandal around (inaudible). I think for Brazil to be able to recapture that soft power, it really needs to have a credible solution to the (inaudible) scandal and this probably

means allowing the federal police and the prosecutors to really pursue the case to its logical end. That would be an important message I think that Brazil that would transform the present scandal, and something that would show that Brazil's justice system has also matured and can solve problems -- very serious problems within institutional democratic context. And the other thing is to get its economy growing again. I think Brazil understands that -- Brazilians increasingly understand and Minister Levy understands that Brazil needs to export more, needs to be more productive, it needs to be more innovative, and that requires sort of a growing closeness to both Europe and the United States. But Brazil is still within the framework of Mercosur, its relationship with Argentina -- which in a sense, Argentina's very different international strategy means that Brazil faces with some obstacles to try and achieve its objectives of restarting economic growth. Or is Argentina simply not as interested in expanded trade with the European Union, or close relations with the United States? I think that how this gets resolved will have implications for Brazil and Argentine politics, and really this election that's coming up is really going to be an important part of resolving that. Because I think we see that both (inaudible) have talked about avoiding needless antagonism in the international relations and I think (inaudible) leaves more of a question mark when it comes to those kinds of issues. And I'll stop there.

MS. GRAHAM: Thank you Harold.

MR. TALVI: Okay, thank you, Carol. I'm going to try to look at the constant common patterns between Argentina and Brazil and some of the key differences, maybe wrapping up many of the things that have been already said.

So first, there was a very severe deterioration in the external environment for both countries -- the end of supersonic growth in China, the collapse in commodity prices. But something perhaps as important is the reassessment of risk in

emerging markets after the temper tantrum, and some potential accidents in the horizon with the crisis in Europe, Russia. And so that has had the consequences of a very sharp slowdown, I would say disappearance of short term capital influence, to the region, and to individual countries.

Second, there was an economic growth came to a total halt. In the last four years, both Brazil and Argentina grew on average below one percent a year. Third, there was a severe deterioration in the fiscal position. Since mid-2011 Brazil went from 4 percent of GDP primary surplus to a negative number for the first time since 2001. It has a seven percent of GDP overall surplus, overall deficit, I'm sorry. And Argentina went from close to balance to five percent of GDP deficit. Because expenditures continue to grow at boom rates while revenues slowed down and cooled off very significantly. Fourth, there is a severe deterioration in the external position of the countries. The current account deficit -- i.e. the excess of domestic expending over income that has to be financed by the rest of the world has increased dramatically, both in Brazil and in Argentina, that went from a surplus to a deficit position. Fifth, Argentina has experienced a very substantial acceleration in inflation rates while their inflationary pressures are also mounting in Brazil. Sixth, both countries, political and institutional climate has debilitated very significantly due, in the case of Brazil to the (inaudible) corruption scandal, in the case of Argentina to the loss of confidence in the government, in the judiciary, in the police, in the secret services that followed the mysterious death of Prosecutor Deniseman.

Now, all of these are common factors, how did governments react to very poor economic performance, and corruption scandals and social discontent? Brazil, reacted by going back to orthodoxy, fiscal adjustment, the rise in interest rates to try to contain inflationary pressures, and retain the capital that was leaving the country, and a

renewed effort among other things, as Raul was mentioning, to try to revamp investment and infrastructure.

What did Argentina do? Argentina went the way of heterodoxy, basically on strengthening heterodoxy -- inflationary finance of the deficit, tightening of exchange rate and capital controls, the tightening of restrictions on imports and the remittance of profits of foreign firms abroad, and the hardening of the non-negotiating position vis a vis, holder creditors.

Now, if we look at the financial thermometers of what orthodoxy brought to Brazil, it was a spiraling exchange rate, rising risk spreads, substantial decline in stock and bond prices. While heterodoxy brought to Argentina a reduction in the parallel exchange rate, a slowdown in capital outflows, and an increase in the prices of bonds and stocks.

So what is happening? And Silvia gave an advance, or a preview on this, and I think she made a very important point. What's happening here is that Dilma is at the beginning of a tenure and it appears that she has become a sort of lame duck president while she still has four years to go in a country that needs major surgery. So you need major surgery and you are without the surgeon. On the contrary, in Argentina Christina Kirchner's tenure is about to conclude and whoever succeeds her, is going to have a keen interest in solving the hold out problem, regaining access to international capital markets, being able to stop there for the inflationary finance of the deficit. Lower inflation, gradually remove capital and exchange rate controls, and gradually adjust the fiscal position to a sustainable one.

So, and with this I finish, Carol, although it is the severe deterioration in the external environment that in a sense deteriorated a week and very substantial economic fundamentals, it is actually the domestic political dynamics that is going to hold

a key for the future, and in that sense there appears to be a curious reversal of fortunes.

MS. GRAHAM: Ernesto, thank you very much. In fact I'm going to -- I very much like your pulling out the common challenges in the very differential responses and I'm going to build on that a bit. I'd like to start by posing some questions to Raul and to Silvia and then I'll cycle back to Ernesto and Harold. But in the scenario of large common challenges and then differential responses in both cases, there's the question of who's going to do the surgery and or kill the patient.

So I'd like to ask each of you, Silvia and Raul, to take that question a step further, Silvia you posed alternatives, that there are these very different political alternatives, and particularly on continuing with heterodoxy alienation from the international economic community or changing path. If you could just possibly spell out a little more about the competing scenarios and who you think might be more -- or who the public might be maybe more receptive to, to the extent that it's clear at this point. I think that may be very helpful. And Raul, given that you're describing and others have a situation where you have a lame duck president with four years to go, and yet need of major reforms, major surgery. What do you foresee happening? Is there somebody -- will Dilma change on this, is there someone else that will be leading the charge, or is it going to be muddling along, which would obviously not be a great outcome.

So maybe we could start with Silvia?

MS. PISANI: Okay, thank you. Great. I like this way to divide the things. Okay. So the question is, who is going to do the surgery and how should we do it to keep the patient alive? That's the question. Well in the case of Argentina, the doctor, the parents on the result of the payload -- of their elections, but I would say that the treaty with the major possibilities, more or less they are speaking about the same things. They are trying to -- maybe there is a difference in the speed in which they try to do the

surgery, but more or less they are thinking the same things, trying to be friends again with the world, be friends again with international markets -- capital markets. And also they know that they try to -- they need to fight inflation and to solve the fiscal deficit. I would say that the difference depends on the speed of the surgery, if it's going to be a shock or rapid. And that surely maybe it's going to be slower and the other two are speaking of doing the things faster.

But also, it depends on the political dynamic. Why? Because if after elections and after the new environment is in position, we don't know what's going to happen but if we have again one of those typical political battles in Argentina between one (inaudible) and another (inaudible), and you are not trying to kill each other -- maybe if that dominates the scenario, maybe the surgery has to deal also with this political dynamic. But I would say that the three of them, the three possible doctors are talking more or less of the same treatment, with different speed, with different kinds of shock, and if I can have one more minute -- for sure what's going to happen in Argentina is that it's going to be I think a great doses of expectations. I will think that the different actors are going to look with sympathy the new chapter in Argentina, and maybe if each one of the candidates, when they assume they can profit off that maybe we will have a good chance if they can profit from that good expectation of change.

MS. GRAHAM: Thank you very much. Raul?

MR. LORES: Too quite early, I mean to predict how the political parties are going to behave with (inaudible) weakness. But there is a positive change in that situation that for the last four years, Dilma almost managed the country by herself, she was the minister of the economy, she was the president, she was the chief of staff, and so on. And her constant meddling and micromanaging of not only the government but also the private sector who can't profit, who can't and so on, really, really hurt the

Brazilian economy. So now it seems, I mean the signals is we are witnessing the new education of Dilma Rousseff, allowing a minister of economy that was trained in Chicago, who is not a leftist in any sense, do his job. We are seeing that we are having a kind of semi-parliamentarianism taking place in Brazil where the speaker of the house, who belongs to her coalition but speaks as if he were in the opposition. He can literally force her to fire ministers or to hire other and so on. In normal times I think people would be scared, but many people in Brazil thinks that's good that Dilma is learning to decentralize and to have less power. So it's not a total disaster to see a weak president, because we saw a very strong president for four years and the results were not that convincing.

Because of the change in the economic policies, clearly the temperature, especially in the last two weeks has cooled down a little bit. So on April 12th, there were like the second national protests against Dilma asking for her impeachment, and the crowds were much smaller than in March, much, much smaller. And both expressed in front of the (inaudible) Cardoso last week, and Joseph Cera who was a presidential candidate against Lula in 2010 and also 2002, who was at Harvard this weekend, he also spoke against impeachment. So both (inaudible) Cardosa and Cera by all accounts are leaders of the opposition. They are saying that we don't have a strong reason or strong point just for her impeachment so they're trying also to call the mood and to try to let Dilma run.

We are missing just the final player of this soap opera. That's Lula. For the first time in my newspaper, we released the poll that for the first time showed how Lula himself was impacted by the unpopularity of Dilma. For the first time in a possible 2012 election between (inaudible) and Lula, Lula could lose to (inaudible). So I think Lula himself knows that he will need to act a lot to save his protégé and in a way, Lula can't just pretend to become a new opposition player. Oh, I mean she doesn't listen to

me, she doesn't pay attention to my advices and so on, but what he was trying to do for two or three months. She is too stubborn and so on, now Lula is feeling more and more responsible because the streets, the Brazilians are telling him he is responsible for her. So I think in a way (inaudible) Cardoso to Lula, I think grownups are returning to the table and that's positive.

MS. GRAHAM: Thank you Raul. That is a positive story. So I want to continue with this theme about sort of common challenges and differential responses, but maybe take a longer term and more institutional view and ask both Harold and Ernesto to comment on different aspects of that. If you look at the two countries, beginning with Fernando Enrique Cardoso, Brazil has had sort of this usually very effective combination of a theoretically left leaning president adopting basically standard macroeconomic, Washington consensus style policies with also nice innovations, but really emphasizing on macroeconomic stability integration with the rest of the world and with a fair amount of success in terms of economic growth. This period seems to be a slight diversion from that, but the pushback suggests it's not.

On the other hand Argentina has, at least as seen from the outside, and I hope I'm wrong on this, but it seems to be consistently shooting itself in the foot. I mean consistently sort of taking this same sort of reaction, isolating itself, going back to inflation, going back to turning off the international community with some rationale perhaps, but it certainly hasn't helped its economic performance.

I'd like to ask Ernesto and Harold each in a different way to maybe comment a bit on whether its institutional differences or just a tradition of macroeconomic management or some sort of consensus on macroeconomic management that explains these differences, or is it an institutional thing. And Ernesto, in addition to that, you might comment on given these differences in macroeconomic approach, the extent to which

Mercosur now, which sort of creates a sort of tie between the two countries is sort of a burden or a plus. And Harold if you could comment perhaps a bit more on political and judicial institutions along these lines, and then also do these very different responses on the economic front make a difference to security cooperation.

MR. TRINKUNAS: Should Ernesto start or should I?

MS. GRAHAM: Go ahead.

MR. TRINKUNAS: Okay, I think that when we look at the two countries, I think the way you framed it was about right. I think with Argentina you've seen the biggest shift, the biggest swings in foreign policy and economic policy in a number of dimensions from the 1990s very much aligned with orthodoxy, democratic orthodoxy, human rights orthodoxy, economic orthodoxy, in a certain sense, to after the financial crisis, swinging sharply in the other direction. Much more aligned with the Bolivarian countries, with Hugo Chavez and support from Chavez the connections to Alba countries. But this is in a sense a return to -- I mean Argentina has gone back and forth this way many times in its history.

I mean we have to remember Peron's original government in World War II, Argentina was seen as sort of not part of the allied efforts, there was always a question mark around its foreign policy. The same thing during the 1970s, during the military government, it was seen even as a rogue regime -- pursuing sort of nuclear military nuclear program and rocket programs and so on and so forth -- missile programs. So Argentina has this kind of bigger oscillations and I think -- here's where Brazil's institutions, especially its foreign ministry, helps damp down some of that oscillation. We have seen somewhat of a split personality when it comes to Brazil vis a vis the region where definitely the PTs, the workers party, sort of more left oriented connections to other left wing parties in the region dominated its policies in that area versus its policies on the

international stage where I think you get much more of the traditional Brazilian criticism of the existing international order and make room for itself. Not challenging the basic rules but just to have a bigger say in what's going on, so much less variation I think on the Brazilian dimension. But this probably has more -- goes back to the domestic institutions. I think in Argentina you see the deterioration of some of the achievements that were made during the 1990s, and Brazil, I think we're seeing that the system is essentially working in a way. Sort of the response from the federal police and the prosecutors and so on and so forth, shows that institutions were available in Brazil to sort of try to address some of these issues.

MS. GRAHAM: Thank you for that.

MR. TALVI: I would like to comment on how do you translate governability, that didn't sound strange. I think Raul made a very interesting point on the fact that the weakening of Dilma might eventually improve the ability of the government to actually do the major surgery. So that's an extremely interesting point, I would like to translate the question to Silvia or to pass on the question to Silvia in the sense that, you told us whoever wins, is going to do a policy shift and the speed might differ but not the substance, my question is, in the governability.

MS. PISANI: No, that's the point.

MR. TALVI: Are they going to have the ability to do what they intend to do in any of these scenarios or they won't? That would be something I would be interested in hearing from you.

Regarding institutions I think, Carol, there's a big difference between Brazil and Argentina, and I think that actually the Petrobras scandal, versus the Nisman event really show the different institutional set ups of the country. I mean Brazil is going to end up jailing, as Raul said, the top politicians, top executives. I mean I always tell my

children that when you see corruption in the newspapers that can be actually be a signal of the strength of the system. Because you are rooting it out, because it was spotted and is being rooted out.

Argentina on the other hand, the Nisman episode brought a complete loss of confidence in the institutions. So Brazil, it is a loss of confidence in the political establishment but not on the institutions. I think in Argentina the problem goes deeper because it's a loss of confidence in the institutions themselves, it's not the current establishing the circumstance and the occupying the institutions.

And I think that's a very important difference and with this I end, and maybe I'll take some other thing afterwards, but the fact of what Raul is telling us in a moment of deep crisis, I mean the elders surrounding Dilma, protecting Dilma, for the interest of the system, not of Dilma Rousseff -- speaks millions about the institution and maturity. While in Argentina when the (inaudible) was in a very complicated situation, I mean the opposition actually created what was being the atmosphere in which we had de facto, an institution of coup d'état. That may be blunt in saying it, but so I think there's a huge difference between Argentina and Brazil in that sense, and I think that this is going to be important going forward in how the two countries react to --

MS. GRAHAM: Silvia do you want to take a couple seconds and try and answer the governability question before we open up --

MS. PISANI: Yeah, this is going to be one of the key points. I think we all here know that in Argentina we don't have political parties as we usually know them internationally. So the deep key, the main key for anyone who assumes power on December 10 is going to be how they build the government, their power, and a big difference is that they will try to do it very quickly. If the winner is (inaudible), this is going to be a big question because we never saw (inaudible) without anybody being his boss.

He's always been in power with somebody else. If he wins it is going to be the first time (inaudible) by himself. Maybe it is going to be a good opportunity to know who is (inaudible), because this is a big question. Somebody and here the bets are that -- I think that he's going to struggle for his position and he is going to try to know, to be a very strong president, but he has to deal with the Kirschners, so it's going to how to build that. That's the big question, and I think it's going to be more difficult for (inaudible), why?

(inaudible) is not a Peronist, and he's building his possibility of having the power with a very strange association with radicals, radicals in Argentina means moderates, no that's a -- you know that, don't think about -- that's the big -- so it's going to be civic radical, which means moderate. So it's a strange mixture of radicals, moderates, Peronists that are not happy with the Kirschners. So for (inaudible) it's going to be difficult because with the best win, I think that he is going to have the first minority in congress, and no more than that. With Masa, which is an ex-Kirschner maybe is going to, is also going to be difficult, but the difference is that maybe he's going to be able to at least enjoy all the extra Peronists and to build the power with them.

The main point also is that Argentina has not had a very strong experience I would think because it has no experience in building government agreements. So what you call a big agreement to try to think in political and long term policies. So it's going to be interesting to see, I think that each one of them has their particular conditions to try to build this association, these coalitions. It is going to be interesting to see that, but that is going to be the main point, how to build the coalitions. I don't know if I answered the question.

MS. GRAHAM: You did a great job, thank you very much. Now what I'd like to do is take advantage of our audience, I know there are lots of interesting people in the audience with plenty to say, or ask. What we ask is that once you get identified, if

you please identify yourself first, and before you pose a question, and you'll be handed a mike so that people can hear you.

So there's a question all the way in the back and there's a microphone right next to you.

SPEAKER: Hi, Alejandro Sanchez, I'm a senior fellow of the Council of Hispanic Affairs.

MS. GRAHAM: Would you mind standing up, just because it's hard for us to --

SPEAKER: They recently concluded some of America's (inaudible) a big, big (inaudible) for President Obama. He may (inaudible) Dilma, et cetera et cetera. But President Dilma also met with President Kirschner, very briefly, I'm just wondering how that meeting was reported in both your countries, if it was reported at all, and since the title of this event is about intertwined futures of both countries, what do you think about the future relations with both governments of your both two countries for the rest of the year and until the Argentine elections -- should we expect any kind of end of the year surprises before the Argentina elections or will it be just business as usual? Thank you.

MR. LORES: So I'm on the Brazilian side, but I can share a personal story. I was a correspondent in Buenos Aires, almost ten years ago, and when I went there it was like the honeymoon of Mercosur, had a good relationship and most of these stories I wrote were cover stories, a lot of space and so on. And I remember when I was living in Argentina in 2002, after the crisis while there was the president already, the space was shrinking. So the Obama-Dilma summit meeting, conversation, got all the attention, I don't remember, even my newspaper maybe dedicating a paragraph about what the Dilma and Christina were talking. And I very much doubt we had only two reporters there in Panama, but we were following Christina Kirschner, so I think there is

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this coupling, but of course I mean for the leftists in Brazil it's sad because they have been bashing so much about the original integration and now our future is together and so on, but see in reality, I mean from the business sector, should the media -- you're paying less and less attention to Argentina and to President Kirschner. So I think now in a way as people are talking in soccer, the ball is on the Argentinian side because I think we are waiting to see what happens next there.

MS. GRAHAM: The title of our event was clearly misconstrued.

MS. PISANI: Yeah the ball is in our field, you know why? Things are going to change, but I would say those are for the perspective of you know, if you want to have some inside information about how the meeting was treated and also -- you know we were expecting the meeting for the first day, what the two presidents were there in Panama and when it was the main point in the agenda of Christina Kirschner and suddenly they're saying the meeting is not going to be today. No? So what is she going to do here, who is he going to meet? So it's a different point of view you know. We don't have Dilma so what do we have? And so where is the story, where is the headline, and so that's the different point of view. I mean Argentina is looking around, and what are we going to have in the next month? I think that one of the main concerns in there -- there's a new slogan in Argentina, which is, we don't want Brazil to export their crisis to us. (laughter) That's the main -- we are very good in slogans.

MR. TRINKUNAS: Just wanted to add something, and I think this is one of the dilemmas for Brazil going forward, is that this institutional structure they built around Mercosur has really become almost a trap for them. They would like to have more free trade. They know that their probability of exporting to the U.S. or Europe is greater than to China, that's not really a market for them. But on the other hand, the Mercosur policy of not making the independent trade agreements, separately from the

other members or partners has really become sort of a straightjacket for Brazil. So Brazil doesn't want to break that aspect of Mercosur, but it also, it knows that it needs to move forward on free trade. So how does it resolve that? I don't think it resolves it before the next election, but I think the election could maybe open up some room for a different kind of thinking on free trade in Argentina. I don't know what the opinion on that is from the rest of the panel.

MR. TALVI: I think that the facts are resolving themselves out without Brazil and Argentina for the moment. I mean -- the world moves on. Basically with the (inaudible) kind of paralysis, we now have in the making to make tradings, one between the U.S. and Asia with ex-China, and the TPP, Trans-Pacific Partnership, the other one between the U.S. and Europe, the Trans-Atlantic Trade and Investment Partnership. And we have the Pacific Alliance in Latin America, and in Central American countries, the Dominican Republic, they all have bilateral free trade agreements with the U.S., nine of them have free trade agreements with the European Union. Seven of them have free trade agreements with Canada, and many of them have free trade agreements with Korea and Japan. So essentially, the future, who knows, this part of the region that is already highly networked and these mega trade -- they are either going to jump on the bandwagon, and actually Mexico, Chile, and Peru are already part of the TPP and the TTIP, or as we are pushing here from Brookings, we might even think of the possibility of creating a Trans-American Partnership, whereby these countries who already have ties with the U.S. and Canada can build an economic space by harmonizing the rules of origin that would be twice the size of China.

And when you look at them closer, I mean we have nothing, we are completely outside of the -- I mean it's not that the ball is in your field, I mean the ball is outside of the stadium, (laughter) we are completely out of -- we are playing in the

(inaudible) beside the stadium. I mean, Argentina's (inaudible) are very small little piece of land that we use to play soccer. And I think Brazil, the private sector of Brazil, correct me if I'm wrong Raul, understand this very well I mean and they have abandoned their usual protection instincts for a more integrationist policy because they see that it is in their interest to try to become a part of this movement.

Argentina is still highly insular in its instincts, at least circumstantially insular but as you once said Silvia, I mean you have this ability to change slogans and ways and that's the good thing about Peronism, that it's not ideological, if they see that the tide goes somewhere else, they might as well get on top of it. Just to summarize I think that the events are well ahead of us, and that I see clearly Brazil trying to jump on the bandwagon and if Brazil does it, Argentina will have to do it too.

MR. LORES: I think I mean this contradiction is already happening inside the Brazilian government, that's the question mark, which side is going to win. Both the new minister of agriculture of Brazil who was -- she was the president of the agro-business association (inaudible), and the new minister of trade who was the president of the national association of industries. Both have created sides of the Mercosur in the past, so you have like two so called enemies of Mercosu. And some of the most important ministers in Brasilia. I don't remember Levy talking about Mercosur. He doesn't look a fan either.

And when Levy, I mean by the way, not only talking about education, social adjustments, and social programs here in Washington, he also talked about new infrastructure projects, new concessions -- concessions now are the euphemism of profitizations in Brazil. And he talked freely about concessions, so we have three ministers who already are in the other stadium and not a competitor, so the question is, how the hard liners of the previous Dilma administration will react to these new comers,

because either the new comers are the saviors, and the surgeons, and they will have a say also in foreign policy -- or who have this kind of two head government, and that's complicated.

SPEAKER: (inaudible)

MR. LORES: I think you mean -- (inaudible) has been so weakened and most of all because the president is so not that interested in foreign policy, so (inaudible) has been weakened in power, in politics, and budget and so on. She clearly has advisors, I think Mercosur is more important than anything. There are hardcore leftists, with a kind of south, south agenda that's better to be the leader of the poor than to be in the bottom of the line with the rich partners. But that group is losing the battles, and I mean I think unlike Argentina, we are turning to our previous conversation, I mean Brazil was colonized by Portuguese. Extremely pragmatist people, who could survive between Spain and the U.K. -- I mean that's quite an achievement. So pragmatism in Brazil is very, very important, while I mean -- and my family is from Spain, so I can talk freely about it. I mean -- Spain loves the wars and battles with all its neighbors, so our culture values a lot of pragmatism, and that's why I think for Fernando Henrique Cardoso and Lula, for 20 years, despite all the rhetoric, despite all the sound bites, basically they kept the policies from each other. So I think that's a big difference comparing Peronism that you're literally almost create like coups, and I mean like (inaudible) Argentina with Peronists in the opposition.

MS. GRAHAM: Well thank you, that was really a great conversation. I would like to again see if there's anyone else in the audience. Okay, let's go right here, and again if you could please identify yourself.

SPEAKER: Bernardo Rico, World Bank, IFC. Could you comment on, I guess this question is for Silvia, a little bit the psychology of the private sector today in

terms of what the expectations are for this election and what if Argentina doesn't turn the corner three or four or five years from now. What happens to the private sector in Argentina, and also if you could expand just quickly a little bit on the narco trafficking situation and how bad you think it will actually get.

MS. PISANI: Quickly, what I would say is -- this is my personal opinion, that in the same scenario, we will -- with the same problems, and the same challenges, we will like, Brazil now, without the possibility of elections in seven months, I would say the situation in Argentina will be deeply different. This is for answering you, which one is the psychology of the private sector then, they say wait, wait and see because we need a change. It is very difficult to do business in Argentina right now because the rules change constantly. And when I say that, I really mean that, I mean for example, I will try to explain this in my English so, try to be patient.

But for example, if you need to export and so when you export you receive dollars. For example, (inaudible) try to imagine this -- you're an exporter, you're selling, I don't know why, glasses to China. So you put the glasses on the ship and you send them, and there they go. So they are going to pay you with dollars. And so the dollars go to the central bank of Argentina, the central bank of Argentina transforms that into peso, and they give the peso to you. So you don't see a dollar, you see a peso. That's in the system.

So they change all the time how much the currency, so you don't know how many pesos are you going to receive for each dollar, but also they can change from one day to another. In how many times, how much time do you have to give the central bank the money for the glasses you sell? And maybe the glasses are still selling to China, but as the central bank needs money, they say, we want the dollars in 30 days, and you say no. My glasses are still selling to China, they didn't pay me, they didn't

arrive. Ah, we need the dollars right now. So you say, my God you go to China, (laughter) how do you do that? And you are trying to sell glasses, when you have people around the world producing glasses around the world and they can wait one year because they understand that's how the international market works, so they can wait for six months, one year. So with this stupid example of the glasses, I try to explain to you how the situation to do business now, and at the same time you have a government asking you to export, because exporting is important.

So they are waiting and they are waiting to have a more clear environment and a more pro-business environment and a more rational environment. You know. Trying to understand that one bureaucrat in one ministry can spoil your life or your business and that's no good. So they are waiting, they are waiting. And about the narco traffic, this is a very new challenge. I know that all the politicians are talking about that, with this, I don't know how they are going to deal with that. They are worried about it, I don't know if they have the know-how to go against it, and I don't know if they -- I mean I think they are just dealing in the very beginning steps of the problem, but if they don't know, if they don't do anything, my opinion is that in the next three or four years we are going to have a deep very strong problem with that if they don't deal with that right now.

MR. TRINKUNAS: Carol, just wanted to add on the narco trafficking issue. I think one of the key things, it's an issue we've looked at here at Brookings, we have a project on improving global drug policy which I'm drawing on -- to make these comments. Basically what's changed in the region is that it's no longer -- Argentina is no longer a transit country for drugs, it's increasingly a production and consumption country as well. Production of synthetic drugs, and growing consumption of narcotics, although the data is not very clear, at least according to the sources such as the UNODC, cocaine

consumption per capita in Argentina and actually in Brazil is approaching levels you see in the United States, and so this is a major shift. So this means there's a lot more money in the narcotics industry and also the way that narcotics traffickers are paying for their local service providers in Argentina to help them move products and drugs, which then they resale on the local market which contributes to the consumption problem.

And this is creating a problem for the police which no longer have the same capacity to shape the criminal environment and prevent violence. I think traditionally police strategy in Argentina was to control the violence associated with crimes so that Argentina would feel like a safe country even though there was quite a bit of crime going on. But it was non-violent. And what the police are losing the capacity to do is to prevent that violence that they used to be able to do. I think that's a very worrying sign, the police no longer have that upper hand that they used to have in relation to criminal organizations.

MS. GRAHAM: Building on both those points, and the very good example of how difficult it is to export glasses from Argentina, to the extent that's what you're trying to do. You don't have to be a deep historian to recognize that the harder it is to do normal business in countries, the more incentives there are for people to do illicit kinds of activities, particularly lucrative ones like narco trafficking. So anyway, from the audience, I know there was someone in the middle back there, go ahead.

SPEAKER: Hi there, Gary McCune, Deloitte Consulting. Apologies to kind of piggyback some more economic questioning for Argentina. It's fine whoever wants to take it, on the holdouts, I was just interested in the comments that there might be change in that after the elections, and I was interested to hear what you think the domestic support is for changing that policy. From outside it seems like there's a lot of nationalist support in favor of the current policies, I don't know if that's just what we're

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seeing from outside, so just interested to hear what the domestic situation would be like in terms of supporting a change in policy there.

MS. PISANI: About the holdouts, what I will say is, nobody is speaking, not one of the candidates is speaking too much about that. My impression is that the three of them will try to find some way to solve the situation, and as you said, it's going to be -- I mean now it's difficult because it's a very strong rhetoric in the government against it. I think that they will do -- my impression is that they will try to reverse that and try to find a solution and they will negotiate. I will say that the three of them, maybe they will try to find a way to find a solution because the situation is getting more and more complicated, and I think that they will try to find any solution and the sooner the better.

MS. GRAHAM: So we have time for one more last question, Margaret Delahage.

SPEAKER: Thank you, Margaret Delahage. We've talked a lot about getting the fiscal house in order, but I think both countries and probably a lot of countries in the rest of Latin America have a lot of other things they need to do in order to really be competitive in the global marketplace. Raul you mentioned the (inaudible) Levy had talked a bit about education. But there's major infrastructure projects, all of these are going to take a long time and a lot of investment it would seem. And so how do you see in the two countries' governments which face a lot of political challenges, attacking, addressing these longer term competitiveness issues?

MS. GRAHAM: Well with that simply question, I'm going to ask each of the panelists to take about one minute to either address that or say a last remark before we wrap up. Why don't we start at the other end with Harold.

MR. TRINKUNAS: I think that, I mean it strikes me that the climate in Brazil as you said, Raul, with this issue of concessions as being the new way of speaking

about attracting investment, Mr. Levy is very open to that and I think he is really trying to structure things in such a way as to facilitate this kind of involvement and in fact he was meeting here in Washington, he was talking about how open he was trying to make it for outside investors to be able to come into Brazil. I mean I don't see that climate at all in Argentina the way the current government is talking, but I do think that could easily change after the election, especially if as Silvia says, the new government sort of tries to address some of these issues that are sort of blocking them out of international capital markets, dealing with the holdouts, so on and so forth, you could see that as part of that things could take a pragmatic turn, and we already saw that, I think there's a lot of pragmatism for example associated with the (inaudible) attracting, setting up the rules for outside investment in shale in southern Argentina, even under the current government they were quite pragmatic about it, how to set that up in an attractive way. So I think we're going to see there's room for improvement in both.

MS. GRAHAM: Raul, either a final remark or answer Margaret's question.

MR. LORES: Well sure, I think I would try transfer. I mean I think we used to be a turtle in the right path, always slow but always improving, for decades. Unlike other countries with big booms and then they go back and so on. In education clearly we are on the right path, but much slower than other emerging markets. We're not like China that in one generation has created almost a kind of Ivy League, and is literally hiring teachers here, investing billions in our universities and so on. Brazil has reduced a lot of the illiteracy, it's great. Internet becoming more easily, more available from the amazon to the northeast, I mean the education to train teachers takes generations. To get better schools, to make parents aware that they are part of education, and not only public teachers, takes generations.

So I think we are on the right path, but it takes a while. But I think in this current wave of pessimism, we need to remember that we're all God blessed here. I mean stadiums would collapse, and airports would collapse, there would be mass murderers, and so on only to be a disaster. And actually the disaster was the only one that the press didn't predict, and that was our national team being so bad. And so education and innovation in other fields, we are improving. The problem is the world is not waiting for us. So especially when we see some Asian countries, you see that they are in a hurry. They are sending their children to study here in the U.S. They are spending a lot of innovation and so on, and we are doing a little bit, I mean slow motion, thank you.

MS. PISANI: Thank you for the question, for thinking back to the common sense. And I couldn't agree more with which has been said here. I would like to finish with two positive notes. For sure I think, I'm sure, I'm positive about this, that we are going to have a new climate, a new environment in Argentina in the next month, so it will be easier to think, and I hope to think in the long term, maybe, hope. And I would like to invite you, because we didn't speak about this, but there's a secret new player in the Argentinian political, and it's try to guess who. You don't know? The Pope. So maybe, no really I am speaking seriously. I think that now he's trying to help to finish this period and his tenure. My impression is that maybe, look at him, just pay attention. Maybe he will also try to help to invite the new government to think about in the long term. But for sure what we will have, I don't know that's a question for the Pope, but for sure what we're going to have is a new climate and maybe that would help a little bit to think in the long term.

MR. TALVI: So God is Argentinian after all? (laughter) I am going to finish on a positive note too, and I think in a sense also answering Margaret's question

which I think is very important and to the point. I mean just let us take a little bit of perspective on where are we. I mean let us think in the early 80s, early 80s, like Latin America was plagued by dictatorships. I mean and in fact the kind of crisis that we are seeing -- institutional crisis in Brazil and Argentina, would have amended the dictatorship. That's not happening. Not a single country in the continent had single digit inflation, not one. Fiscal deficits and debt were rampant. If at that time, they would have told us, by 35 after we would have -- I mean imperfect, but pretty solid democratic institutions and systems that single digit inflation was going to be the norm and not the exception that fiscal poverty by Chicago trained economists in the left of central government -- I mean it would have been unthinkable. So let us not underestimate how much did we do in the last 35 years, and maybe now this is a historical juncture in which the challenges that we now face is not only preserving what we conquered but becoming more competitive, more integrated, better educated, better than everything that comes together with all those needs, and perhaps five years from now, we will be saying, look, I mean that the turtle somehow reached the finish line. (laughter)

MS. GRAHAM: Those comments remind me of this great old joke of these two old diplomats playing cards or something and one of them says to the other, "Do you think we'll ever have world peace?" And the other one say, "No, it'll never happen, you'd have to wait for the American president to be black and for the pope to be from Argentina." (laughter)

Anyway, well thank you very much to our panelists, to a good audience, and an optimistic end to it all.

(Applause)

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