Latin American Weekly Spotlight

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Argentina: Fitch raises rating of local currency debt
Brazil: Sovereign bonds and equities under pressure
Chile: Strong growth in economic activity expected
Colombia: The armed conflict remains a complex issue
Ecuador: Populism „ante portas"
Mexico: Surprisingly, Banxico raised the Corto
Panama: Torrijos wins presidential elections
Peru: 2006 election raises uncertainty
Venezuela: Government increases its influence in the Supreme Court

Argentina

The rating agency Fitch upgraded Argentina's long-term local currency rating of public debt from CC to B-. The rating applies to debt which was raised following the default and which the government is contractually servicing. Given the high primary surpluses we share this improved view. The long-term foreign currency rating of Argentine sovereign debt continues to be rated by Fitch in default class DDD. ---- With regard to the energy crisis, which is likely to worsen, the government announced a complicated program of price incentives to reduce energy consumption. Simple hikes of regulated prices likely would be more efficient. ---- As expected, construction growth in March came in strong (41.2 yoy; 1.3% mom, s.a.). ---- The cooling down of supermarket sales turned out to be more pronounced than expected (-0.8% mom, s.a.; +9.5% yoy). ---- In line with expectations, exports grew by 17% and imports by 81% (yoy) in March. Export growth was mainly driven by higher prices whereas the main reason for the strong import growth is the low base of comparison.

Outlook: According to official statements the revised offer for the restructuring of Argentine debt will be ready in June. However, its publication could take a few more months, as this would require the approval of US-American and Argentine entities. ---- We expect the increase in consumer prices in April (Wednesday) to have been only slightly higher than in March (0.6%, mom; 2.3% yoy). ---- Tax revenues in April (today) are likely to post another yoy growth in excess of 30% (March: 39.5%). ---- Economy minister Lavagna announced a reduction of the financial transaction tax from 1.2% to 1%, which will cost an annual US$ 350 mn. The IMF had demanded such measures as the tax is viewed to be distorting.

Brazil

Brazilian bonds continued under pressure last week as the good labor market figures in the US led to a renewed increase of interest rates at the long end. The EMBI+ Brazil rose by 60 bps to 662 bps, the highest level since October 2003. At the same time the Bovespa stock exchange lost 9% last week. In principle the fundamentals have not changed (continued high current account surplus, fiscal targets are not in danger; however, economic activity is still weak). ----- The current account surplus reached US$ 817 mn in March (lower than we had assumed on the basis of a central bank announcement last week), exceeding the March 03 amount by approx. US$ 650 mn. The FDI figures for March disappointed: registered inflows amounted to only US$ 700 mn instead of the expected US$ 1 bn. According to preliminary CB figures, April may turn out even weaker. ----- The unemployment rate increased unexpectedly strongly, from 12% in February to 12,8% in March. ----- According to the industrial association FIESP industrial sales increased by 30.7 % yoy in March. At the same time capacity utilization increased from 81.3% in February to 82.3% in March, thus pointing to a further upturn of investment demand. (Note: the publication of the INA industrial production index for São Paulo is suspended for some time because of changes in the methodology, informed FIESP). ----- The Lula administration decided to increase the minimum wage by BRL 20 to BRL 260. This came as a surprisingly low increase as the government is facing high political pressure and is only a few months ahead of the municipal elections. For public finances this moderate increase is fine.

Outlook: The car production will have increased further in April (Thursday). ----- The IPCA inflation (Friday) for April should stay at 0.4 % mom. We expect the central bank to cut the interest rates by another 25 bps on May 19. ----- The trade balance (today) should have a surplus of US$ 1.8 bn in April, below the amounts of recent months and more or less unchanged from April 03.

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Chile

Strong growth in industrial production (+7.8% yoy) and in industrial sales (+9 %) in March give further support to our forecast of a significant growth acceleration. Mining production posted its first growth in four months (2.2%). The labor market contributed to the positive picture despite a seasonal rise in the unemployment rate to 8.1% (March 03: 8.2%). The number of persons employed rose by 1.5% yoy.

Outlook: Following last week's positive production figures the overall IMACEC economic indicator should post a growth of 5% in March (Wednesday). This should lift the expansion in the first quarter of the year to 4.1 % yoy (Q4 03: 3.3 %). Together with accelerating growth inflationary pressure should increase, taking the CPI change in April to 0.2 % mom (tomorrow). Compared with April 2003, however, prices are expected to have fallen by 0.4%.

Colombia

According to the media, the government will shortly launch a military offensive with up to 17,000 soldiers against the FARC. So far, no official statement has been given. At the same time, the disappearing of the leader of the biggest paramilitary group (AUC) gave reason for speculation over a failure of negotiations between the government and paramilitary groups. Overall we expect the armed conflict to remain a complex issue. ----- At the beginning of the week the government again intervened in the foreign exchange market in order to prevent the peso from appreciating beyond 2600 pesos/US$. Given expected increases of US$ interest rates, markets turned during the week and the peso lost some of its value (Friday close: 2658 pesos/US$). We expect a moderate increase in the US$ interest rate over the year and stick to our year-end exchange rate forecast of 2800 pesos/US$. ----- Growth of industrial production (6.1% yoy) as well as the increase in retail sales (7% yoy) confirm our positive economic outlook. While employment in the industrial sector decreased slightly (-0.3% yoy), the number of employed in the retail sector showed a healthy increase (4.1%).

Outlook: A senate commission approved the constitutional bill aiming at enabling president Uribe's reelection and the conservative party officially backed the planned constitutional change. Even though we do not rule out that the remaining votes for this legislative turn – until June 20th the plenary of the senate, a commission of the lower house as well as the plenary of the deputies have to approve the bill – will be successful, we do not expect Uribe to run for another presidency. The bodies mentioned have to vote again on this issue in the second half of this year and we expect resistance to rise in the upcoming months.

Ecuador

A policy change away from the current course of relative fiscal austerity becomes increasingly likely: On the one hand, voices calling for a relaxation of regulations concerning the buyback of public debt with funds accumulated in the FEIREP oil stabilization fund (reduction of the share earmarked for buybacks from 70% to 40%) are becoming stronger, and on the other hand, an overall hike in public sector remuneration seems imminent. This change of policy should cause the resignation (or at least a significant debilitation) of finance minister Pozo, up to now a stronghold of fiscal responsibility. As recently as last week in Washington, Pozo had pledged to retain the current policy course. ----- In the light of possible alternatives (including a toppling of President Gutiérrez), the recent change in policy seems to be the best outcome. We expect this view to prevail with the IMF as well, and expect the Fund to remain engaged with negotiations concerning a new Stand-By Arrangement (SBA), which should be softer concerning some of the sticky issues in Ecuadorian politics. Nevertheless, we do not expect a new agreement before June. ----- Consumer prices rose by a stronger-than-expected 0.65% in April, mainly due to rising food prices. Year-on-year inflation amounted to 3.6%. With consumer prices rising around 0.7% for the third month in a row, the disinflationary process achieved during the course of last year seems in danger. Due to Ecuador's dollarization scheme, price increases directly hurt the competitiveness of national producers (end-2004 CPI forecast: 5% yoy).

Mexico

In February, the "Global Economic Activity Indicator" – a proxy for the GDP – increased by 3.3% y-o-y, which confirmed our view of a only moderate economic upturn, even as the IGAE turned out to be somewhat stronger than expected.----Another development which supports a further economic recovery was the employment increase of 140,000 in March. Employment growth is a necessary condition for private consumption to continue to grow, as interest rates most likely will rise and real wage growth is currently very low. We continue to expect a GDP growth of 2.8% in 2004.---- In a surprise move, Banco de Mexico increased the corto to MXN 37 mn from MXN 33 mn, after it had left it unchanged at its regular meeting a week ago. Banxico said it was unhappy with the fall in money market rates, which according to the central bank was incompatible with the inflation target of 3%. After the monetary tightening cetes rates shot back up to 6%. We believe that the tightening move was a good one. Inflation was running at 4.2% in March, way above the inflation target, and the recent peso weakness could turn out to be a further source of inflationary concern. We expect that Banxico will have to tighten monetary policy again over the course of the coming months.

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Outlook: In April, consumer confidence, as measured by Inegi (today), should show only a small increase. This is due to the still high unemployment rate (and despite the recent improvement in the labor market, see above), which also contributed to a sharp slowdown in real salary growth.----Another economic activity indicator – gross fixed investment (Friday) – should have increased by nearly 5% y-o-y in February.---- The public finances (Tuesday) should show another surplus in March. This is not only due to seasonal factors, but also to a further oil price increase.---- The consumer price increase (Friday) should have been very low in April; the annual inflation rate should therefore fall to 4.1%. Nevertheless core inflation will have remained on a relatively high level of around 0.4%. In other words: no relief for the central bank!

Panama

According to preliminary results of yesterday's presidential elections the expected change of government will take place. On the basis of 51% of votes counted, Martin Torrijos was well in the lead with 47%, followed by Guillermo Endara with 29%. Martin Torrijos, son of ex-dictator Omar Torrijos, will take office on September 1st this year. His campaign centered on promises to fight corruption and work for a more equal income distribution, at the same time criticizing the undemocratic presidency of his father. Being the most market-friendly of the main four contenders his victory is likely to be greeted positively by the business community.

Peru

The Minister of economy and finance agreed on a wage raise for state teachers by 115 soles per month. Even though the teacher's union criticized the wage increase as too low, we expect the recently tense relationship between the government and the unions to ease. ----- With a US 500 mn international bond emission (duration 12 years, coupon 8.375%) the Government completed the bond issuance volume planned for this year (US$ 500 mn had been pre-financed in November 2003). Given continuing favorable financing conditions and according to our estimates of a higher than budgeted deficit, we expect the government to issue further bonds on the international market worth up to US$ 700 mn this year (partly as pre-financing for 2005). ----- A recent poll reveals that the 2006 election (parliamentary and presidential) provides for uncertainty. Two ex-presidents, who both fled the country amid political crises, are heading the polls. While Alan Garcia (18%), whose presidency is linked to a macroeconomic crisis and a default on foreign debt, is again an active politician in Peru, Alberto Fujimori, who headed the polls with 19% lives in exile (Japan) and refuses to face up to the Peruvian judiciary.

Outlook: The government introduced a bill to congress which envisages an additional sales tax for all mining companies. Mining has attracted foreign investment worth several billions of US$ in recent years. A higher taxation of proceeds of this sector would therefore enhance the income situation of the government and at the same time discourage future investors. The bill should be a hot topic of discussion in the upcoming weeks and we expect it to be watered down (lower tax rate) before resolved.

Venezuela

Against the opposition's massive resistance, government parties approved in parliament the law concerning the Supreme Court's reorganization. Government may gain full control of the court by raising the number of judges from 20 to 32; this could also have a decisive influence on the referendum process. ----- Government decided that minimum salaries (valid for about 2.8 mn employees) will be increased in two steps by a total 30%, and thus more than expected. ----- The opposition movement has finally confirmed its participation in the verification process of 1.19 mn doubted signatures in favor of the presidential referendum. Yet it will have only three days instead of five for the process. Moreover, signatures given may also be revoked. To enable a referendum, about 60% of the signatures in question would have to be confirmed, which will be difficult. ----- There is the risk of new supply bottlenecks: Super markets threatened stop selling meat if the price regulation authority would not admit higher prices. Pharmaceutical companies are complaining about prices set much too low. ---- The foreign exchange control authority, Cadivi, canceled about 17,000 applications for currency apportionments which had not been requisitioned, thus reducing the overhang of unused currency approvals (> US$ 5 bn) by US$ 1.5 bn.

Outlook: April inflation figures are expected for the beginning of the week. As the impact of the February devaluation is still not showing fully in prices, the monthly rate should be only slightly higher than last month.

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Abbreviations:

mom = month-on-month
qoq = quarter-on-quarter
yoy = year-on-year
s.a. = seasonally adjusted
n.s.a. = not seasonally adjusted

Exchange rate	date	last	one week	one month	one year	end 2003	ytd-change, %	end 2004f
Argentina	30.4.2004	2.85	2.83	2.85	2.75	2.93	3.0	2.9
Brazil	30.4.2004	2.93	2.91	2.88	3.04	2.89	-1.4	3.1
Mexico	3.5.2004	11.44	11.28	11.15	10.19	11.23	-1.8	11.9
Chile	30.4.2004	623	612	603	698	593	-4.8	600
Colombia	30.4.2004	2658	2616	2668	2780	2780	4.6	2800
Peru	30.4.2004	3.48	3.48	3.46	3.47	3.46	-0.6	3.5
Venezuela	30.4.2004	1918	1918	1918	1598	1598	-16.7	2400

EMBI+ Spread							
bps	date	last	one week	one month	one year	end 2003	ytd-change, bps
Argentina	3.5.2004	4587	4471	4702	5034	5739	-1152
Brazil	3.5.2004	662	603	558	779	463	199
Mexico	3.5.2004	199	182	170	210	199	0
Colombia	3.5.2004	430	374	357	437	431	-1
Ecuador	3.5.2004	919	791	688	1042	799	120
Peru	3.5.2004	392	340	331	392	312	80
Venezuela	3.5.2004	686	652	636	1199	593	93

Benchmark interest rates							ytd-change	
%	date	last	one week	one month	one year	end 2003	%-points	end 2004f
Argentina, Peso 7 days	29.4.2004	1.63	1.63	1.69	7.94	1.81	-0.2	4.0
Brazil Selic	30.4.2004	15.80	15.82	15.80	26.32	16.33	-0.5	14.0
Mexico Cetes 28 days	30.4.2004	6.31	6.26	6.31	5.93	6.01	0.3	6.5
Chile 90 days, PDBC	29.4.2004	1.50	1.50	1.57	2.67	2.29	-0.8	2.8
Colombia Prime Rate	9.4.2004			11.13	10.63	11.32		7.5
Peru Overnight	30.4.2004	2.55	2.55	2.55	3.80	2.50	0.0	2.6
Venezuela Prime Rate								

Foreign exchange reserves								
US$, bn	date	last	one week	one month	one year	end 2003	ytd-change	end 2004f
Argentina	28.4.2004	15.6	15.3	14.9	10.9	14.1	1.5	17.0
Brazil	29.4.2004	50.3	50.5	51.3	41.4	49.3	1.1	54.2
Mexico	23.4.2004	68.4	67.8	67.6	57.5	65.8	2.6	65.0
Chile	31.3.2004	16.0		16.03	16.50	16.50	-0.5	15.9
Colombia	31.3.2004	11.33		11.29	10.62	10.62	0.7	11.5
Peru	29.2.2004	10.5		10.6	10.1	10.19	0.3	10.9
Venezuela (FEM&Gold incl.)	29.4.2004	24.4	24.015	23.19	24.02	21.30	3.1	-6.4

Economic activity								
GDP (yoy, %)	2003e	2004f	2005f	Q303	Q403e	Q104f	Q204f	GDP 2003e, US$ bn
Argentina	8.7	6.5	3.8	10.2	11.3	8.8	6.8	127
Brazil	-0.2	3.5	3.5	-1.5	-0.1	2.4	5.2	492
Mexico	1.3	2.8	2.6	0.6	2.0	1.8	3.7	614
Chile	3.3	4.8	4.5	3.1	3.3	4.4	4.8	72
Colombia	3.7	4.0	3.7	4.1	4.5	5.1	3.4	78
Ecuador	2.7	4.8	2.9					27
Peru	4.0	3.8	3.7	3.5	2.8	2.9	2.3	61
Venezuela	-9.2	6.0	5.0	-7.2	9.0	26.3	3.4	82

Public sector	Budget balance, % of GDP		Public debt, % of GDP		Amortization, US$ bn		Gr. financing needs, US$ bn	
	2003e	2004f	2003e	2004f	2003e	2004f	2003e	2004f
Argentina	1.2	1.6	140	150	19.8	19.8	19.1	18.2
Brazil*	-5.2	-2.6	83	79	94.2	83.2	72.1	67.3
Mexico**	-0.6	-0.3	28	28	23	29	26	31
Chile***	-1.0	0.2	16	14	0.8	0.8	1.4	0.8
Colombia	-2.8	-2.8	63	61	6.2	5.3	8.4	7.9
Peru	-1.9	-1.8	39	40	1.1	1.5	2.3	2.7
Venezuela	-3.6	-4.5	42	47	4.7	6.1	7.7	10.0

* Amortisations only federal debt, including short term debt ** Amortisations without Cetes *** debt, amortization and financing needs: central government only

External Sector 2004f	External debt		Debt service		Current account		Trade Balance	FDI (net)	Import cover
	% of exports	s.t., % of total	US$ bn	% of exports	% of GDP	US$ bn	US$ bn	US$ bn	months
Argentina	374	30	32.3	82	2.2	3.3	11.5	0.0	5.6
Brazil	237	12	64.0	69	0.6	3.3	26.3	13.0	7.1
Mexico	83	28	33.3	17	-1.8	-11.0	-7.8	14.0	3.5
Chile	135	18	6.9	21	1.6	1.4	5.8	1.5	5.9
Colombia	228	11	9.1	52	-1.3	-1.2	0.9	2.0	6.3
Ecuador	226	14	2.6	35	-2.0	-0.6	0.1	1.2	1.2
Peru	238	10	3.6	28	0.0	0.0	1.7	1.1	9.4
Venezuela	122	6	5.0	18	10.3	8.9	14.4	1.4	11.5