



# Latin American Weekly Spotlight

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A company of the **Allianz Group**

<b>Argentina:</b>	Bondholder groups reject improved debt restructuring offer
<b>Brazil:</b>	Another record surplus in the trade account
<b>Chile:</b>	Rise in inflation in line with expectations
<b>Colombia:</b>	Solid GDP growth in Q1-04
<b>Ecuador:</b>	Finance minister Pozo stepped down
<b>Mexico:</b>	Possible tightening of monetary policy
<b>Peru:</b>	Mining royalties approved in congress
<b>Venezuela:</b>	Opposition apparently manages to get a referendum against Chávez

## Argentina

Should the official Argentine calculation proof right – verification will only be possible once all details will be released following the approval by regulatory bodies – that net present value (NPV) losses of the new debt restructuring offer amount to 75%, this would imply a significant improvement to Argentina's first offer which called for NPV losses of more than 90%. The improvement is mainly driven by the recognition of past due interest, which previously was not planned to be recognized. However, in comparison to other rescheduling experiences even the NPV loss of 75% appears excessive, particularly given Argentina's presently very comfortable fiscal situation. The main bondholder group (GCAB), which claims to represent 44% of bondholders, already rejected the offer. It remains doubtful if a sufficient participation ratio can be reached on the basis of the present offer. ---- With 0.7% (mom) the inflation rate in May came in slightly lower than our forecast. However, the figure confirms the upward trend in comparison to previous months. The yoy rate stood at 4.3% in May. For December this year we expect a rate of 8% (yoy), which would be inside the central bank's target range of 7%-11%. ---- On the back of the economic recovery, tax revenues continued booming in May (+73%, yoy).

Outlook: The UTDT indicator of consumer confidence compiled at the beginning of June (Wednesday) is likely to show stagnation or a slight decrease. The indicator is still in high territory with improving facts not visible and the energy crisis likely weighing on consumer sentiment. In May the indicator rose slightly (+0.6%) while there had been a strong decline in April (-11.4%).

## Brazil

The excellent trade balance data of June were another surprise as they showed a record high of US\$ 3.1 bn. Exports grew by 24.6% while imports increased by 25.1%, the latter indicating that internal demand is consistently increasing. ---- According to central bank data FX inflows recovered in May. The inflow amounted to US\$ 1.6 bn (net). Data show that banks have absorbed a big amount of these inflows. Hence the reason for the

weak real is not capital flight but the high (and in our view temporary) demand of Brazilian banks for US\$. ---- Car production increased by 7.6 % yoy in May, a sign that industrial sector growth remains well on track.

Outlook: The recovery of the industrial sector should have continued in April. However, the increase will not be as high as in March (11.9 %, yoy). We expect an increase of 3.8 % yoy (Wednesday). The May IPCA inflation rate will probably be 0.5% mom (5.2% yoy). For year-end we expect an inflation rate of 6.6% (Tuesday). - ---- After the approval by the lower house last week of the minimum wage increase by only BRL 20 to BRL 260, the senate should vote the issue this week. Good negotiation skills will be required from the government to push through this highly controversial bill (many senators – also from the ruling coalition – demand a higher increase).

## Chile

Consumer prices rose by 0.5 % mom in May, driven by higher transport costs. Annual inflation returned into positive territory (0.6 % yoy) after a few months of deflation. Although the CPI increase is pushed by high oil prices, it should be clear that their must no longer be fears of a phase of persistent deflation. We expect the beginning of a monetary tightening cycle by Q4-04.

Outlook: Solid growth should have persisted in May. We expect the IMACEC economic indicator to post a growth of 6.4 % yoy (Tuesday) ---- The trade balance should post another record surplus in May (US\$ 800 mn, Tuesday).

## Colombia

GDP increased by 3.8% yoy in the first quarter, slightly below our expectations. It was not only the construction and the mining sector that contributed to the good growth figure, but also the retail sector. This reflects that the recovery of consumption is continuing. ---- Surprisingly stable prices: inflation amounted to only 0.38% mom and 5.37% yoy in May ---- Voting the case of the



reelection bill of President Uribe: The third vote of eight in total was approved by the lower house commission. Another vote in the lower house has to take place until June 20 (the beginning of the recess in congress) if the time schedule is to be maintained. The next votes (after July 20, the end of the recess in congress) will be a long haul. We are skeptical whether the government will really be in a position to push this constitutional change through congress.

### **Ecuador**

Finance Minister Pozo stepped down last week, officially for personal reasons. We nevertheless see his demission as an attempt by the government to weaken rising social protests against the economic policy stance. Former CB president Mauricio Yopez was announced as the new minister of finance. Yopez is viewed as having, like Pozo, a liberal economic policy approach. We would therefore not expect a sharp reversal of economic policies. In turn, however, social protest should not calm down as well. --- -- The unemployment rate reached a 3-year high of 12.1 % in April (March: 11.9 %). Underemployment rose to 46.2 % from 42.9 % in March.

### **Mexico**

In April the public sector surplus, at MXN 27.7 bn came in slightly below expectations. This was due to the 8.5% real increase in expenditure. In the first three months of 2004 monthly expenditure on average only grew by 3.6% in real terms. ---- Consumer confidence rose strongly in May, to 99.9, which was due to the improving situation on the labor market.---- Private-sector inflation expectations for the end of 2004 were practically unchanged in May at 4.09 yoy, or 3.58% yoy for core inflation (see „outlook“ for implications on monetary policy)

Outlook: In March, gross fixed investment (Monday) probably had a big increase of 7% yoy, or 3.5% mom, on a seasonally adjusted basis. This would be the biggest increase in more than four years. ---- In April, industrial production (Friday) should have risen further compared to March by 0.2%. This translates into a yoy increase of 6.5%. Given the good data in the US, the outlook for industrial production in the months to come is still positive. ---- In May, consumer prices most likely fell by 0.2% due to seasonal factors (Wednesday). Given an annual rate of inflation of 4.3% - much higher than the inflation target of 3% - and the outlook for interest rate hikes in the US, it would not come as a surprise if the central bank would tighten its monetary policy again already this Friday.

### **Peru**

The rating agency Fitch raised the outlook of its long-term foreign-currency bond rating for Peru from "neutral" to "positive". Fitch stressed that Peru had managed to consolidate the public-sector budget in spite of a difficult political situation. ---- Congress approved the introduction of royalties in the mining sector, which, depending on the sales volume, will vary from 1% to 3% of a company's sales. This will probably dampen the still fragile interest of foreign investors.

### **Venezuela**

Inflation fell to 1.2% mom in May (April: 1.3%) due to price controls and increased apportionment of foreign currency for imports at the favorable official exchange rate. Year-on-year inflation dropped to 21.8%.

Outlook: Many observers, including ourselves, had no longer expected a referendum against president Chávez, but he surprisingly announced he accepted the signature verification result. The electoral authority had declared after the verification that the number of 2.44 million of valid signatures required for the referendum had been exceeded. So the referendum should take place if it is not legally contested. The date envisaged is August 15. However, should the referendum be delayed and only take place from August 19, a Chávez defeat would not result in new elections but rather in an automatic replacement of Chávez by the vice-president – which would be no real change of power. Yet we think president Chávez has a real chance of emerging the winner in the referendum. In coming weeks, government will probably increase expenditure in order to secure additional votes. According to polls, the president will be defeated, but we doubt that the polls are representative.



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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

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Exchange rate	date	last	one week	one month	one year	end 2003	ytd-change, %	end 2004f
Argentina	04.06.2004	2.97	2.96	2.92	2.81	2.81	-5.3	3.0
Brazil	07.06.2004	3.13	3.19	3.06	2.86	2.86	-8.5	3.1
Mexico	07.06.2004	11.41	11.45	11.58	10.66	10.66	-6.6	11.9
Chile	04.06.2004	645	640	638	717	717	11.2	600
Colombia	04.06.2004	2716	2739	2717	2819	2819	3.8	2800
Peru	04.06.2004	3.49	3.49	3.49	3.48	3.48	-0.1	3.5
Venezuela	04.06.2004	1918	1918	1918	1598	1598	-16.7	1918

EMBI+ Spread								
bps	date	last	one week	one month	one year	end 2003	ytd-change, bps	
Argentina	07.06.2004	4970	4921	4660	5049	5739	-769	
Brazil	07.06.2004	661	698	761	727	463	198	
Mexico	07.06.2004	209	205	229	228	199	10	
Colombia	07.06.2004	889	907	1013	1025	799	90	
Ecuador	07.06.2004	484	520	528	444	431	53	
Peru	07.06.2004	450	470	485	429	312	138	
Venezuela	07.06.2004	613	662	745	970	593	20	

Benchmark interest rates								ytd-change
%	date	last	one week	one month	one year	end 2003	%-points	end 2004f
Argentina, Overnight	03.06.2004	3.44	3.81	1.31	4.69	1.50	1.9	4.0
Brazil Selic	04.06.2004	15.76	15.78	15.77	26.27	16.33	-0.6	14.8
Mexico Cetes 28 days	04.06.2004	6.71	6.46	6.81	5.43	6.01	0.7	7.5
Chile 90 days, PDBC	03.06.2004	1.30	1.27	1.43	2.61	2.29	-1.0	2.8
Colombia Overnight	02.06.2004	6.97	6.90	7.04	7.41	7.49	-0.5	8.8
Peru Overnight	04.06.2004	2.60	2.55	2.55	3.88	2.50	0.1	2.6
Venezuela deposits 20 days	31.05.2004	10.58	10.02	10.35	15.18	13.20	-2.6	

Foreign exchange reserves								
US\$, bn	date	last	one week	one month	one year	end 2003	ytd-change	end 2004f
Argentina	02.06.2004	16.9	16.6	15.8	11.5	14.1	2.8	17.0
Brazil	03.06.2004	50.5	50.6	50.4	43.4	49.3	1.3	55.2
Mexico	28.05.2004	688.8	691.5	684.3	567.6	658.0	30.8	65.0
Chile	30.04.2004	16.0	na	16.0	15.9	16.0	0.0	16.6
Colombia	30.04.2004	11.4	na	11.3	10.6	10.9	0.5	11.5
Peru	30.04.2004	10.5	na	10.4	10.2	10.2	0.3	11.4
Venezuela (FEM&Gold incl.)	03.06.2004	23.9	24.4	24.4	16.7	21.3	2.6	

Economic activity				Inflation			GDP 2003, US\$ bn	
GDP (yoy, %)	2003e	2004f	2005f	% , year end	2003	2004	2005	
Argentina	8.7	6.5	3.8		3.7	8.0	8.0	127
Brazil	-0.2	3.5	3.5		9.3	6.2	5.2	492
Mexico	1.3	3.2	2.6		4.0	4.0	3.5	626
Chile	3.3	4.8	4.5		1.1	2.2	3.0	72
Colombia	3.7	4.0	3.7		6.5	6.0	6.5	78
Ecuador	2.7	4.8	2.9		6.1	5.0	0.9	27
Peru	4.0	3.8	3.7		1.8	2.3	2.2	61
Venezuela	-9.2	10.5	4.3		27.1	26.0	28.0	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	152	19.8	19.8	19.1	18.3
Brazil*	-5.2	-2.6	58	57	94.2	83.2	72.1	67.3
Mexico**	-0.6	-0.3	28	28	23	29	26	31
Chile***	-1.0	0.9	15	14	0.8	0.8	1.4	0.3
Colombia	-2.8	-2.8	60	60	6.2	5.3	8.4	7.9
Peru	-1.9	-1.6	48	48	1.1	1.5	2.3	2.5
Venezuela	-4.0	-3.5	45	40	4.7	6.3	8.0	9.7

\* 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	372	30	32.3	81	1.8	2.6	10.8	0.0	5.5
Brazil	226	12	67.4	68	0.7	3.9	27.0	11.5	6.8
Mexico	83	28	33.3	17	-1.6	-10.4	-7.8	15.0	3.5
Chile	134	18	6.8	21	1.1	1.0	6.0	1.5	6.1
Colombia	243	12	7.9	49	-1.3	-1.2	0.9	2.0	6.3
Ecuador	17	14	1.4	3	-0.4	0.4	6.4	-1.3	1.0
Peru	238	16	3.6	26	1.2	0.8	2.6	1.1	9.9
Venezuela	105	8	5.3	16	10.0	9.6	15.5	1.0	10.4