Latin American Weekly Spotlight

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Dresdner Bank Lateinamerika AG
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A company of the **Allianz Group**

Argentina: Still robust economic growth
Brazil: High current account surplus in July
Chile: Budget surplus at 2.9 % of GDP in the first half of 2005
Colombia: Central bank transfers international reserves
Ecuador: State of emergency declared
Mexico: GDP growth lower than expected in the 2nd quarter
Peru: PPK new prime minister
Venezuela: GDP expands by 11.1 % in the 2nd quarter

Argentina

The EMAE GDP proxy showed an increase of 9% yoy in the first half of the year, with the economic activity accelerating in the second quarter. In our opinion, this positive performance was induced by a beginning recovery in the construction industry, record harvests and improvements on the export side. Sustaining impulses, however, came also from the manufacturing industry, though this sector saw a decline in June of this year. For the second half of the year we expect a slowdown (yet from a high level), as production should reach its capacity limits. Economic activity was nearly stagnating in June in comparison to the previous month on a seasonally adjusted base (+ 0.1%). ----- We expect the government to launch a further long-term dollar bond issue in September which will be used for amortizing IMF maturities of around US$ 500 mn (due this month). Favorable conditions on the international capital market – high liquidity and low interest – make it easy for the government to place new issues. In contrast, negotiations on a new IMF program will probably progress only gradually. Such an agreement is to be expected rather in 2006. In the rest of this year, maturities of US$ 4.8 bn will still fall due. ----- The government continues to introduce measures to contain speculative capital inflows. Recently, it decided that residents in Argentina have to inform the national revenue authorities (AFIP) about capital income from abroad when these funds surmount US$ 50,000. The decision is retroactive, as capital inflows are subject to registration beginning with July 1st of this year. Since June of this year, foreign portfolio investors have already been obliged to keep 30% of their investment unremunerated with the Argentine authorities for a year.

Brazil

No end of the political noise is in sight. New revelations last week indicate that Rogerio Buratti, the former secretary of Finance Minister Palocci (when he was the major of Ribeirao Preto), is involved in corruption and money laundering. Mr. Buratti said that Palocci took bribes too, and the Veja magazine wrote in its weekend edition that it has documents confirming Palocci's involvement. Given the market nervousness (the BRL lost 2.1% against the US$ and the EMBI Brazil widened by 13 bps on Friday), Minister Palocci gave a long TV speech, denying all accusations and reaffirming the government's commitment to the current economic policy. Up to this point Palocci's position within the government remains still strong. Despite the dimension and importance of the political crisis, Brazilians still support President Lula, although at decreasing rates. According to the latest Datafolha poll, 63% of people interviewed do not see any reasons for an impeachment process against Lula. --- According to the latest central bank market survey, inflation expectations for 2005 and 2006 fell to 5.4% (from 5.5%) and to 4.98% (from 5%), respectively. Despite ongoing decreasing inflation expectations and inflation results - the IPC-S consumer price index fell by 0.2% mom in the four weeks ending Aug 15th, and the IGP-M fell by 0.49% - the COPOM left the interest rate unchanged at 19.75% in August. We believe the central bank will start cutting rates slightly in its next meeting in September. --- According to IBGE, retail sales rose by a higher than expected 5.3% yoy and by 1.2% mom in seasonally adjusted terms in June, accumulating growth of 4.6% in the first six months of this year. Yoy sales growth was particularly high in the sector "IT, office equipment and communication" (51.6%), which was boosted by the recent *real* strength that led to decreasing import prices. The second-best performer, the "furniture and electronic goods" sector (+21.4%), was driven by credit expansion. --- The current account registered a surplus of US$ 2.6 bn in July, the highest monthly result ever, as the trade surplus reached also a record of US$ 5 bn. This brings the current account surplus to US$ 7.9 bn ytd or 1.8% of GDP. On the other hand, the services and income account showed an increasing deficit of US$ 2.7 bn in July (January-July: US$ 18.8 bn, compared with US$ 14.1 bn in the same period last year), reflecting mainly the strong Brazilian currency. FDI totaled US$ 2 bn in July and US$ 10.6 bn ytd, a rise of 88%. As a result of the anticipated amortization of the IMF SRF credit line (US$ 4.976 bn), inter-

economics@dbla.com

national reserves declined by US$ 5 bn, to reach US$54.7 bn at the end of July.

Chile

At 2.9% of GDP, the central government's fiscal surplus in the first half of the year is a historical record. The good result is based on a significant growth in public revenues (+22.4% yoy in real terms), while expenditure growth remained subdued at 5.5% yoy. The extra monies the government obtains are used to replenish the Copper Stabilization Fund and to prepay public debt, mostly to the central bank. While Budget Director Marcel tried to keep expectations with respect to the overall 2005 performance in check, citing high tax devolutions and a lower copper price as principal reasons for the government's overall target of 3% of GDP. We expect the government to significantly exceed this target on the back of solid copper prices, forecasting a year-end surplus of 4% of GDP.

Colombia

As expected, the central bank left its key interest rate unchanged at 6.5% ----- Against a background of rapidly rising international reserves - currently amounting to US$ 14.9 bn -, the central bank is planning to transfer US$ 1.5 – 2 bn to the government. The central bank already sold US$ 1.25 bn to the government, which it used to prepay IADB loans, in April. The new operation comprises the issuance of TES in the local market. That is why the local TES market responded quite nervously to the announcement of the transaction last week. Another reason for volatility in the TES market last week was that local traders are concerned about the possibility of the central bank selling TES in the secondary market to sterilize its interventions in the foreign exchange market.

Ecuador

One political crisis is followed by the next. Only two weeks after the turbulences caused by the surprise step-down of finance minister Correa, last Thursday President Palacio had to declare a state of emergency in the two provinces Sucumbíos and Orellana in the Amazonas region. Protestors reportedly almost stopped the production of the state-owned enterprise Petroecuador and other private companies. On Thursday oil exports were interrupted. According to national newspapers the government is expecting losses of over US$ 200 mn. The demonstrators want the oil-companies to increase their investment in the region's infrastructure, more jobs and an increase of taxes and royalties.

Mexico

In the second quarter of this year, the Mexican GDP grew by a lower-than-expected 3.1% yoy (consensus forecast: 4%). Seasonally adjusted data showed a contraction of 0.42% compared with the previous quarter, as a reflection of contractions of 0.82% in the agricultural sector and 0.11% in the services sector. On the other hand, the industrial sector recorded a positive result of 0.3% qoq (sa). Despite the relatively weak second-quarter growth figures, the Ministry of Economy is still forecasting GDP growth of 3.8% for the year 2005 as a whole, based on better growth prospects for the second half of the year (DBLA forecast: 3.3 %). The central bank also seems to be optimistic: it left the Corto unchanged at MXN 79 mn in its latest monetary policy meeting last week, although there has been a declining inflation trend.

Peru

After Prime Minister Carlos Ferrero resigned and therefore the whole cabinet had to step down, President Toledo announced the former minister of economic affairs and Minister of Finance Pedro Pablo Kuczynski as new Prime Minister. Kuczynski's deputy Fernando Zavala will be the new head of the department of economic affairs. He is known to be an independent technocrat and it seams quite certain that he will not change the current economic policy. Due to the nomination of PPK as Prime Minister it seems unlikely that he will run for President in the elections next year. Should he wish to do so, he would have to step down from his current office by October 9. ----- Low output of the fishing industry caused slower than expected economic growth in June. At 4.63% yoy, growth was more than one percentage point lower than expected by the market consensus and the government. Nevertheless, growth reached 5.89% yoy in the first half of the year, bringing the government to raise its economic growth expectations for 2005 from 4.8% to 5.5%, in line with our adjusted growth forecast of 5.4%.

Venezuela

Fiscal figures published by the central bank exhibit the same picture for June as in the months before, with revenues expanding at a significantly higher pace than expenditure (106% and 21%, respectively, yoy in nominal terms). As a result, the central government's surplus amounted to Bolívares 4.5 trillion (some US$ 2 bn) in the first six months of the year. We expect the government to step up expenditure further in the second half, as congressional elections are approaching at the end of the year. ----- Driven by (mostly off-budget) public expenditure (+29.5% yoy) going to infrastructure projects, subsidized food markets and social handouts, the economic activity expanded by 11.1% yoy in the second quarter of the year. The oil sector continued its

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weak performance, rising a mere 2.5% yoy, while non-oil activities grew by 12.1%. In the first half of 2005 the economy grew 9.5% yoy, and against a backdrop of still increasing oil prices and the government's reinforced populist stance, including a strong spending spree, there is a significant upside risk to our already high overall 2005 GDP growth forecast of 6%.

Dresdner Bank Lateinamerika AG
Neuer Jungfernstieg 16
20354 Hamburg
Germany

Economics Dept.
Chief economist: Dr. Heinz Mewes
Tel.: (+49 40) 3595 3494
Fax: (+49 40) 3595 3497
E-Mail: economics@dbla.com
http://www.dbla.com

Abbreviations:

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

Exchange rate	date	last	one week	one month	one year	end 2004	ytd-change, %	end 2005f
Argentina	22.08.2005	2.91	2.88	2.86	3.01	2.97	2.2	2.9
Brazil	22.08.2005	2.40	2.33	2.40	2.97	2.66	10.6	2.4
Mexico	22.08.2005	10.73	10.59	10.65	11.41	11.15	3.9	11.0
Chile	22.08.2005	542	537	568	628	556	2.5	580
Colombia	22.08.2005	2309	2307	2315	2595	2355	2.0	2337
Peru	22.08.2005	3.25	3.25	3.25	3.38	3.28	0.8	3.3
Venezuela	22.08.2005	2147	2147	2147	1918	1918	-10.7	2150

EMBI+ Spread bps	date	last	one week	one month	one year	end 2004	ytd-change, bps
Argentina	22.08.2005	428	412	421	5189	4707	-4279
Brazil	22.08.2005	409	394	416	525	383	26
Mexico	22.08.2005	151	148	158	185	167	-16
Ecuador	22.08.2005	732	695	734	822	691	41
Colombia	22.08.2005	299	302	327	412	333	-34
Peru	22.08.2005	150	149	188	360	220	-70
Venezuela	22.08.2005	420	411	443	546	412	8

Benchmark interest rates %	date	last	one week	one month	one year	end 2004	ytd-change %-points	end 2005f
Argentina, Overnight	19.08.2005	4.31	4.25	5.63	2.50	2.31	2.0	5.0
Brazil Selic	22.08.2005	19.74	19.76	19.72	15.85	17.75	2.0	18.5
Mexico Cetes 28 days	22.08.2005	9.58	9.60	9.67	7.21	8.61	1.0	9.5
Chile 90 days, PDBC	18.08.2005	4.03	3.96	2.96	1.57	2.24	1.8	4.3
Colombia Overnight	17.08.2005	6.37	6.59	6.38	6.99	6.24	0.1	7.1
Peru Overnight	19.08.2005	3.10	na	3.00	2.75	3.03	0.1	2.5
Venezuela deposits 30 days	17.08.2005	10.60	10.47	10.78	10.92	11.92	-1.3	14.5

Foreign exchange reserves US$, bn	date	last	one week	one month	one year	end 2004	ytd-change	end 2005f
Argentina	19.08.2005	25.2	25.1	24.0	18.1	19.6	5.5	21.5
Brazil	18.08.2005	54.7	54.9	59.5	49.7	52.8	1.9	62.0
Mexico	12.08.2005	70.6	70.5	70.2	68.7	71.6	-1.0	66.1
Chile	31.05.2005	17.4	na	17.0	16.1	16.1	1.2	16.7
Colombia	31.07.2005	13.9	na	13.7	11.8	13.5	0.3	16.0
Peru	30.04.2005	13.6	na	13.6	10.5	12.6	1.0	13.5
Venezuela (FEM&Gold incl.)	18.08.2005	31.4	31.1	29.7	21.1	24.2	7.2	28.5

Economic activity				Inflation				
GDP (yoy, %)	2003	2004	2005f	%, year end	2003	2004	2005	GDP 2003, US$ bn
Argentina	8.8	9.0	6.0		3.7	6.1	12.5	127
Brazil	0.5	4.9	3.4		9.3	7.6	5.7	506
Mexico	1.4	4.4	3.3		4.0	5.2	3.7	626
Chile	3.7	6.1	5.4		1.1	2.4	3.6	74
Colombia	4.1	4.1	4.0		6.5	5.5	5.4	80
Ecuador	2.5	7.0	3.5		6.1	1.9	2.7	27
Peru	3.8	5.1	5.0		2.5	3.5	2.0	61
Venezuela	-7.7	17.9	6.0		27.1	19.2	18.0	84

Public sector	Budget balance, % of GDP		Public debt, % of GDP		Amortization, US$ bn		Gr. financing needs, US$ bn	
	2003	2004	2003	2004	2003	2004	2003	2004
Argentina	1.3	4.2	140	126	19.8	19.8	19.1	16.1
Brazil*	-5.2	-2.7	56	52	94.2	84.3	72.1	68.4
Mexico**	-0.6	-0.3	28	27	23	30	26	32
Chile***	-0.4	2.1	13	12	0.8	0.8	1.1	-1.2
Colombia	-2.7	-1.2	56	52	10.6	10.0	12.8	11.2
Peru	-1.9	-1.3	48	46	1.1	1.3	2.3	2.2
Venezuela	0.2	0.0	46	39	10.8	9.0	10.7	9.0

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

External Sector 2004	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	397	35	32.3	75	2.2	3.3	13.3	3.9	5.8
Brazil	203	12	65.6	59	1.9	11.7	33.7	18.2	6.2
Mexico	78	21	37.5	18	-1.2	-7.9	-8.6	15.0	3.3
Chile	128	18	7.2	21	1.5	1.4	9.0	6.7	5.6
Colombia	205	11	7.3	39	-1.3	-1.2	1.0	2.6	6.8
Ecuador	17	9	1.4	3	0.3	0.9	6.8	1.1	1.1
Peru	195	10	3.7	25	-0.2	-0.1	2.7	1.8	9.3
Venezuela	111	22	8.3	21	12.7	13.8	21.4	1.3	9.0