



**Argentina:** Low inflation in August, but for seasonal reasons  
**Brazil:** Benign inflation figures in August  
**Chile:** Growth slow-down in July  
**Colombia:** Buyback of external debt announced  
**Ecuador:** Bond emission rescheduled  
**Mexico:** Fiscal austerity in the 2006 Budget Proposal  
**Venezuela:** Government prepares ground for debt buy-back

## Argentina

Consumer prices rose just 0.4% mom in August. The deceleration against July (+1%) was not an unexpected one for market participants (consensus: +0.5 %): tourism business activities registered a huge price decline in August, as the winter season is ending (-7.7% mom). Rising core inflation (+0.9% mom), however, shows that price increases continue on a broad base. With an annual rate of 9.7% in August, inflation was nearly twice as high as in August 2004 (5.3%) and this tendency is expected to continue. Once again, President Kirchner told supermarkets to refrain from excessive price increases, threatening with price controls. Yet these efforts will probably not result in dampening effects on prices, as inflation is primarily driven by the increasingly expansionary fiscal policy ahead of October's parliamentary elections and by the central bank's policy of unsterilized interventions on the currency market to counter the appreciation of the peso. We expect year-end inflation at 12.5%. ----- Real wages rose by 5.2% yoy in July. The level of real wages, however, is still significantly below the one of year-end 2001, when the currency board was abolished. ----- Amid expanding economic activity, tax and social security collection, at ARS 78 bn, was 18% higher in the first eight months of this year than in the corresponding period of 2004, with even increases in VAT (+16.9%) and income tax collection (+15.9% yoy). However, with exports on the rise, export taxes continue to support the budget (+24.9%). Social Security revenues rose by 25.9% amid wage increases and increasing employment in the formal sector.

## Brazil

Recently released inflation figures point to a lasting downward trend: The General Price Index (IGP), at -0.79% in August, was negative for the fourth consecutive month. According to FGV, this is the strongest decline in prices of the last 50 years. From January to August, the IGP accumulated an increase of only 0.32%. The main drop in the index occurred at the wholesale prices component (-1.0%). This should be passed through to consumer prices, which in turn should contribute to falling inflation expectations. Meanwhile, the IPCA index (which is the one used for inflation targeting

purposes) registered an increase of 0.17% in August, down from 0.25% in the previous month. In the last 12 months there was an increase of 6%, down from 8% in May and closer to the central bank's year-end target of 5.1%. ----- According to IBGE, after four consecutive months of growth, industrial production posted a higher-than-expected decrease of 2.5% mom (sa) in July. Compared with the same month last year, production was almost flat (+0.5% yoy). Nevertheless, we do not believe that this is the beginning of an enduring downward trend, since both the mom- and the yoy-bases of comparison were very high; vehicle production (+8.9% yoy) and new vehicle sales (+15% yoy) were strong in August; the significant real wage increases in July (1.3% mom sa; 9.3% yoy) suggest that non-durable consumer spending will continue. Against this backdrop, we expect the Central Bank to ease monetary conditions slightly on its meeting this week, with a likely 25 bps reduction to 19.5% to be announced on Wednesday.

## Chile

Economic activity slowed in July, with the IMACEC economic indicator posting growth of 4.4% yoy. This was below market estimates and can be traced back to the very weak performance of the mining sector, which contracted by 12.1% in July. Accumulated growth in the first seven months amounts to 6.05%, and some softening of economic expansion should take overall 2005 GDP growth to our forecast of 5.7%. ----- Inflation surprised on the downside in August: consumer prices increased by a lower-than-expected 0.3% mom (3% yoy), as transport prices did not increase as much as we had forecasted. A 0.2% mom (2.4% yoy) increase in core inflation, however, underlines the still present, albeit relatively modest, underlying inflationary pressure. In reaction to this and the still robust economic expansion which renders further monetary stimulus unnecessary, the CB lifted the monetary policy rate by 25 bps to 4%. We expect the CB to continue its gradual tightening policy and lift the monetary policy interest rate to 4.75% by year-end.



## Colombia

The government is going to buy back up to US\$700mn in Dollar- and Euro-denominated bonds, financed with the funds originating from the transfer of forex reserves from the CB to the government. Taking advantage of the positive capital market conditions, the government wants to improve its debt profile and reduce its dependence on changes in currency exchange rates. The buyback will reduce foreign debt from 42% of GDP to 40% of GDP, and especially bonds with maturities in 2006 and 2008 are very likely to be cleared before the elections next year. ----- Imports continue to grow strongly due to solid economic growth and the strong Peso. In July, imports reached US\$ 1.67mn, taking accumulated imports in the first seven months up 28% ytd. Especially imports of capital goods (+44.9% yoy) grew strongly, highlighting the solid state of domestic investment. This bodes well for economic activity, underlining our 2005 GDP growth forecast of 4%.

## Ecuador

President Palacio wants to renegotiate the contracts with private oil companies to increase the government's share of the oil revenues to 50%. At present, the government gets 20% of the revenues of private oil companies. The additional revenues are intended to be used for higher social benefits in the oil-producing regions where strikes almost stopped the production last month. It remains to be seen whether the government succeeds with its plan. Any use of regulatory force would certainly hurt investment in a sector which is vital for the country's public finances. ----- The political turbulences are taking their toll on the economy: The unemployment rate in July rose from 9.9% last year to 11.1%. Inflation is increasing as well, and was with 2.48% yoy (0.24% mom) in August higher than expected. The Central Bank admitted increasing inflationary pressure, adjusting its 2005 year-end inflation forecast from 2% to 2.9%. ----- The ministry of finance postponed the new issuance in the external markets from September to January 2006. Minister Barreiro reaffirmed the government's intention to raise the US\$500mn in the external markets, but pointed to the crisis in the Amazonian oil regions as a factor to postpone the issuance until the situation has finally calmed down. According to Barreiro, Venezuela will keep its promise to buy 60% of the debt issuance.

## Mexico

The government's budget draft for 2006 sent to Congress last week aims at fiscal austerity, proposing a surplus of 0.2% of GDP for the year (2005: proposed deficit of 0.22% of GDP). With realistic assumptions for economic growth (3.6%) and inflation (3.0%), overall expenditure should remain roughly unchanged in real

terms as compared to 2005, despite the elections in July 2006. The budgeted average Mexican oil price was set at US\$31.5 pb, significantly lower than the current price of around US\$50; therefore, strong lobbying in Congress for an increase in the proposed oil prices and thus for more spending should be expected. ----- According to the latest central bank survey, market expectations for economic growth registered a drop to 3.11% for this year, down from 3.54% in the July survey (DBLA: 3%). Inflation expectations for end-2005 fell to 3.68%, the lowest level since February 2004 (3.82% previously). Meanwhile, the Consumer Price Index showed a lower-than-expected increase of 0.12% mom in August, which took the annual rate (3.95%) into the central bank's year-end target range of 2 to 4%. We expect the CB to lower the corto soon, and to allow the overnight rate – currently at 9.5% - to drop further.

## Venezuela

Rodrigo Cabezas, head of the Finance Commission of the National Assembly, announced a government plan to reduce the external debt stock by 25%, but without giving further details or a time horizon. His declaration, however, can be assumed to be a correction of President Chávez' recent comments, who ruled out any issuance of public debt for the foreseeable future due to the government's comfortable liquidity situation. Liability operations could take place, however, in the short term, since the government has more than ample cash as the transfer of a total of US\$6bn in international reserves to the government-controlled FONDEN fund is due to begin during the current week (with several tranches until the end of the year). ----- Congress approved last week the reform of the FEM oil stabilization fund. The FEM, which should receive above-average oil revenues to be saved for rainy days, has not been replenished for three years now despite oil prices at record highs. The new framework provides the government with full discretion with respect to how much it saves in or takes out of the FEM. ----- In line with its increasingly interventionist policy stance, the government announced that it will expropriate some 700 companies deemed to be operated in an inefficient way. The companies shall be transferred to cooperatives formed by current or former workers of the companies. The constitutionality of such a measure seems to be more than doubtful, but such considerations have not hampered the government's actionism in the past. ----- Car sales increased by 71.6% yoy in August, a further indication of high handouts of hard currency on part of the CADIVI FX-authority and increasing availability of credit. ----- According to a government official, the number of price-regulated products and services is likely to increase. A final list, which still has to be discussed in the cabinet and be approved by President Chávez, is likely to be announced by the end of the month.



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](mailto: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

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Exchange rate	date	last	one week	one month	one year	end 2004	ytd-change, %	end 2005f
Argentina	12.09.2005	2.91	2.91	2.88	3.00	2.97	2.0	3.0
Brazil	12.09.2005	2.32	2.33	2.37	2.91	2.66	14.5	2.5
Mexico	12.09.2005	10.70	10.67	10.64	11.56	11.15	4.2	11.0
Chile	12.09.2005	535	535	537	615	556	3.9	570
Colombia	12.09.2005	2309	2295	2307	2521	2355	2.0	2388
Peru	12.09.2005	3.29	3.33	3.25	3.36	3.28	-0.2	3.3
Venezuela	12.09.2005	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	12.09.2005	407	393	416	5302	4707	-4300	
Brazil	12.09.2005	385	406	401	500	383	2	
Mexico	12.09.2005	134	144	152	186	167	-33	
Ecuador	12.09.2005	708	715	705	844	691	17	
Colombia	12.09.2005	271	301	311	391	333	-62	
Peru	12.09.2005	144	169	162	317	220	-76	
Venezuela	12.09.2005	387	395	422	522	412	-25	

Benchmark interest rates							ytd-change	
%	date	last	one week	one month	one year	end 2004	%-points	end 2005f
Argentina, Overnight	09.09.2005	4.50	4.63	4.25	2.56	2.31	2.2	5.0
Brazil Selic	12.09.2005	19.74	19.73	19.76	15.94	17.75	2.0	18.5
Mexico Cetes 28 days	12.09.2005	9.36	9.48	9.60	7.26	8.61	0.7	9.5
Chile 90 days, PDBC	08.09.2005	4.19	4.28	3.19	2.04	2.24	2.0	4.8
Colombia Overnight	07.09.2005	6.37	6.41	6.37	6.88	6.24	0.1	7.5
Peru Overnight	12.09.2005	3.10	na	3.03	2.70	3.03	0.1	2.5
Venezuela deposits 30 days	07.09.2005	10.59	10.35	10.68	11.37	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	09.09.2005	25.6	25.5	25.0	18.2	19.6	6.0	21.5
Brazil	08.09.2005	55.3	55.3	54.7	49.2	52.8	2.5	62.0
Mexico	02.09.2005	72.8	73.1	70.5	69.1	71.6	1.2	66.1
Chile	30.06.2005	16.6	na	17.4	15.8	15.8	0.8	16.7
Colombia	31.07.2005	13.9	na	13.7	11.8	13.5	0.3	15.5
Peru	31.07.2005	15.3	na	13.8	11.1	12.6	2.7	13.5
Venezuela (FEM&Gold incl.)	07.09.2005	32.4	32.0	30.8	21.7	24.2	8.2	28.5

Economic activity				Inflation				GDP 2003, US\$ bn
GDP (yoy, %)	2003	2004	2005f	% , year end	2003	2004	2005	
Argentina	8.8	9.0	6.0		3.7	6.1	11.9	127
Brazil	0.5	4.9	3.4		9.3	7.6	5.4	506
Mexico	1.4	4.4	3.0		4.0	5.2	3.8	626
Chile	3.7	6.1	5.7		1.1	2.4	3.6	74
Colombia	4.1	4.0	3.8		5.5	5.2	4.8	97
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	17.4	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	2.2	13	12	0.8	0.8	1.1	-1.2
Colombia	-1.2	-2.5	52	51	10.0	11.2	11.2	14.2
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	396	35	32.3	75	2.2	3.3	13.3	3.9	5.8
Brazil	200	12	65.6	58	1.9	11.7	33.7	18.2	6.1
Mexico	79	21	37.5	18	-1.2	-7.9	-8.6	17.4	3.3
Chile	112	18	7.2	18	1.4	1.3	9.0	6.7	5.0
Colombia	200	12	7.1	36	-0.1	-0.1	2.3	2.8	7.1
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