Latin American Weekly Spotlight

September 13, 2004

Dresdner Bank Lateinamerika AG
formerly Deutsch-Südamerikanische Bank AG

A company of the Allianz Group

Argentina:	Slowing GDP growth in the second quarter of 2004
Brazil:	S&P upgrades Brazilian government bonds
Chile:	Central bank revised its forecasts upwards
Colombia:	Government starts to cover next year's financial needs
Ecuador:	Government aims at IMF staff monitoring program
Mexico:	Investment ratio remains at a low level
Peru:	Production of manufactured goods increased faster than expected
Venezuela:	Risk premium on international bonds at new low

Argentina

GDP growth slowed to 0.5% (qoq, s.a.) in Q2-04 from 1.5% in Q1-04. The yoy-rate declined from 11.7% to 8.1%. Reflecting this weakening, the unemployment rate rose to 14.8% in Q2-04 from 14.4% in Q1-04. We expect qoq-growth rates to increase slightly again in H2-04. A first indication of this was visible in August, when growth of industrial production increased to 1.1%, mom, s.a. (10.6%, yoy). For 2004 as a whole we expect GDP to grow 6.5%. ---- The budget draft for 2005 contains a higher than expected primary surplus of 3.2% of GDP, 3% of which is earmarked for debt service (previously 2.7%). The government thus came closer to fulfilling IMF demands of a higher primary surplus (although the IMF is meant to have pressed for a figure of around 4% of GDP), which in turn is likely to have helped Friday's approval of the IMF board to extend US$ 1.1bn due until year-end. Argentina still needs to pay US$ 1.46bn to the IMF until the end of this year. ---- The two co-heads of the GCAB, Hans Humes and Nicola Stock, gave somehow contradictory statements on the state of debt restructuring. Whereas in Humes' view the positions of the GCAB and the Argentine government are not far apart and no substantial improvements of the offer are needed to reach an agreement, Stock stressed that there had been no progress and Argentina needs to improve its offer.

<u>Outlook</u>: Central bank President Alfonso Prat-Gay, whose term expires this week, resigned unexpectedly following President Kirchner's intention not to propose him for another term. His successor will be the present Deputy Foreign Minister and Secretary for Trade Negotiations, Martín Redrado. The change is likely to increase the government's influence on the central bank. ---- Mainly due to the import surge, the current account surplus of Q2-04 (around US$1.5bn) is likely to half compared to last year (Q2-03: US$3bn) (Tuesday). ---- The monthly GDP proxy EMAE (Wednesday) should have increased 6.5% (yoy) in August (July: 7.4%).

Brazil

Only a few days after the upgrade by Moody's, also the rating agency S&P changed their rating to BB- (from B+). Hence, Brazil is three notches from investment grade now. We remain confident that another upgrade is in the cards in the next year, as fundamentals have improved over the last years. ----- Continued positive poll data for the government: According to the latest Ibope poll, 55% of the interviewed are approving the government's work (in June this figure was at 51%). The confidence that they had in Lula increased even stronger, from 51 % to 58 %. This poll data could be reflected in the municipal elections which take place in two weeks. ----- The retail sales increased 12% yoy in July in real terms. In the period January to July of this year there was a gain of 9.7% yoy. The prospects for this sector are good. The consumer confidence index of Sao Paulo (IIC) rose 6.2% to 128.8 points in August (on a scale reaching from 0 to 200). ----- The August tax revenues were 22.4% higher in real terms than in the same month one year before. ----- According to the Brazilian treasury, the structure of the local debt improved further, as only 13% of the debt is linked to the dollar, while the fraction of fixed interest debt increased and now stands at 16.7%. Almost no progress was achieved with respect to the Selic-linked debt with a fraction of still above 50 % of the total.

<u>Outlook</u>: Overall we expect positive balance of payment data for August (Wednesday): The current account should have shown a surplus of US$ 1.8bn, thereby bringing the ytd surplus to an amount of US$ 8bn, twice that of the 2003-surplus. Foreign direct investment will not have reached the high level of July (US$ 1.6bn, our forecast for August: US$ 0.8bn), while net portfolio investments (ytd: Outflow of US$ 4 bn) might have shown a small outflow. ----- As employment in the industrial sector increased 0.2% M/M, the unemployment rate will have decreased only marginally to 11% in the same month (Thursday). For the same reason, we expect the consumer confidence index IIC to have improved only slightly. ----- In August, public sector debt should have decreased to 55% because of the appreciation of the real as well as high tax revenues. The primary surplus

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might amount to BRL 6bn meaning that the fiscal target agreed with the IMF continues not to be in danger. ----- The minutes of the last central bank meeting, where the overnight interest rate was raised 25 bps, should give some hints that at least one further interest-rate hike is in the cards, as inflation expectations lay clearly above the central bank inflation targets for 2004 and 2005.

Chile

At its September 2004 policy meeting, the central bank raised its growth forecast for 2004 and 2005 to an expansion of between 5.0 to 5.5% (DBLA 4.8%). The decisive factors for this decision are continuing strong exports and positive rates in mining output and industrial production. The central bank has increased its forecast for the 2004 trade to US$ 9.1bn from US$ 7bn (DBLA US$ 7.8bn). Dynamic export growth will remain in 2005.

Colombia

The central government issued a bond worth US$ 500mn (maturing 2014; yield: 8.5%) on the international capital market. Given that the government will make use of a still unused credit line by the central bank worth US$ 400mn, the money lent is most likely to be used for covering next year's financing needs. Altogether the government plans to issue US$ 1.5bn on the international markets next year. ----- We interpret the continuing rising energy demand (3.64% yoy in August) as a sign of a healthy upswing which is bound to carry on. ----- The government handed a slightly modified reform package to congress. A couple of measures (e.g. lifting the VAT rate from 16 to 17%, taxation of pensions) are scheduled to generate additional revenues worth 1.8bn pesos (0.7% of GDP). ----- A domestic bond swap announced at short notice, proceeded better than expected. Overall, the government managed to exchange more than 10% of domestic bonds maturing next year against securities maturing in 2007 and 2009. ------- As expected, the central bank left key interest rates unchanged on its monthly monetary meeting last Friday. Given a slight depreciation of the peso against the US$ and further interest rate hikes by the US central bank, we expect the Banco República to raise rates 50 bps in November.

Outlook: In July, imports should have risen just under 20%, about twice as much as exports. The trade balance is expected to have accounted for a slight deficit (about US$ 100mn). ----- Current data regarding industrial production, retail sales (both July) and the unemployment rate in August are to confirm our assessment of an ongoing economic upswing.

Ecuador

The IMF indicated that it will be sending a delegation to Ecuador in October to discuss a Staff Monitoring Arrangement (SMA) (Contrary to the Stand-by agreement, the SMA will not imply any disbursements). In this respect, Economic Minister Yepez´s journey to Washington, where he held discussions with IFIs in order to gain access to funding, could be described as a small success. But the difficulties that lie ahead in reaching a fast agreement with the IMF should not be underestimated. The IMF is likely to press for clarification on the government's plans for the oil sector, given the continued delays in passing a new hydrocarbon law. ---- The law remains the key to boosting oil production. Meanwhile, the current dispute between the government and Occidental Petroleum (Oxy) is a source of further uncertainty and sends a shadow over the operation environment facing foreign oil companies in Ecuador. The government alleges that the company Oxy has violated a number of contractual clauses, and is threatening to cancel its contract to exploit the Block 15 oilfield. Some industrial observers see a direct link to the recent adjudication by an international arbitration panel. The panel ruled against the government, saying Oxy was entitled to a US$ 75mn tax rebate.

Mexico

In July, industrial production rose by 0.8% mom in seasonally adjusted terms, after having fallen slightly for two months in a row. Compared to a year ago, industrial production was 3.8% higher. The data indicates that the economic upturn is still intact, but is dependent on US-demand. This is also confirmed by the figures on aggregate demand for the second quarter. Investment demand only rose 5.8% y-o-y in view of the low basis of comparison. Since 2000, the investment ratio has fallen from 24% to 19% of GDP. Should the ratio remain on this low level, the economy's medium-term growth potential will be limited to around 3%.

Outlook: Cetes rates could rise at Tuesday's auction in expectation of a Fed rate hike the same evening. In case the price pressure has eased a bit in the first two weeks of September (Thursday), the central bank should keep its monetary policy unchanged on its Friday policy meeting.----- In July, retail sales (Tuesday) probably rose 3%.---- In August, the unemployment rate (Wednesday) most likely remained at 3.8% for a the third month in a row.---- In August, the trade deficit probably fell compared to the same month a year ago, when it reached US$ 493mn due to higher oil prices.

Peru

The monthly GDP indicator, calculated by the statistical office, rose 3.8% yoy in July. Even though this constitutes a slowdown when compared with the first half of this year (on average 4.8% yoy), the increase in production of the manufacturing sector was the highest so far this year with 9% yoy. Due to the emerging recovery of domestic demand, we have raised our GDP growth forecast for this year to 4.2% from 3.8% before. ----- The consumer confidence index determined by the consulting firm APOYO reached 40 in September, so far the highest figure this year. Nevertheless, as the index can vary between 0 and 100, the current level remains disappointing.

Venezuela

President Chávez has transferred the direction of the three new ministries that were established by him after the referendum - “ministry for popular economy” (“Ministerio de Economía Popular”), ministry for housing construction and ministry for nutrition) - to persons who sympathize with the “Bolivarian Movement”. This is an indication that the government keeps holding strictly to its present course. ----- For the next year, the Chávez fraction is considering to present a motion to parliament aimed at abolishing the constitutional provision that restricts the president’s tenure in office to a maximum of two terms of six years each. The intended amendment which could be initiated with the simple majority of the Chávez fraction in parliament, would only become effective, if confirmed later on by means of a referendum. ----- The risk premium on Venezuelan foreign-currency bonds has hit a new low: as a consequence of persistently high oil prices, substantial foreign-exchange reserves as well as the clarification of the political situation, the EMBI+ spread fell below 500 bps. ----- The finance minister has been given the go-ahead by parliament for the issuance of new foreign-currency bonds in the amount of up to US$ 1.5bn; the revenues generated are to be used for the early repayment of domestic and foreign debts (among them, Brady bonds amounting to US$ 0.7bn). The new issues are scheduled to be launched this and the next week. ----- After the upgrading of the Venezuelan government bonds, Moody’s has now also improved the rating for the PDVSA foreign-currency bonds, from Caa1 to B2. ----- The opposition has presented a formal application to the Constitutional Court requesting to annul the referendum result because of a faulty evaluation. We expect this process to peter out as time goes by.

Outlook: For this week we are expecting the (overdue) figures on the production of the private-sector manufacturing industry for July to be published, which should confirm the continuation of the economic upswing at the beginning of the second half of the year.

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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	20.09.2004	2.99	3.00	3.01	2.91	2.91	-2.8	3.1
Brazil	20.09.2004	2.87	2.91	2.97	2.89	2.89	0.9	3.1
Mexico	20.09.2004	11.46	11.56	11.33	10.76	10.76	-6.1	11.9
Chile	17.09.2004	610	615	632	657	657	7.7	620
Colombia	17.09.2004	2543	2521	2597	2868	2868	12.8	2640
Peru	17.09.2004	3.35	3.36	3.38	3.48	3.48	3.9	3.4
Venezuela	17.09.2004	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	20.09.2004	5541	5328	5189	5121	5739	-198
Brazil	20.09.2004	454	508	525	637	463	-9
Mexico	20.09.2004	177	188	185	202	199	-22
Colombia	20.09.2004	792	843	822	1116	799	-7
Ecuador	20.09.2004	388	404	412	414	431	-43
Peru	20.09.2004	305	321	360	328	312	-7
Venezuela	20.09.2004	473	525	546	782	593	-120

Benchmark interest rates							ytd-change	
%	date	last	one week	one month	one year	end 2003	%-points	end 2004f
Argentina, Overnight	17.09.2004	2.50	2.56	2.50	1.94	1.50	1.0	3.0
Brazil Selic	17.09.2004	16.22	15.94	15.86	19.85	16.33	-0.1	16.5
Mexico Cetes 28 days	17.09.2004	7.26	7.26	7.16	4.23	6.01	1.3	7.5
Chile 90 days, PDBC	16.09.2004	2.35	2.42	1.62	2.84	2.29	0.1	2.3
Colombia Overnight	15.09.2004	6.88	6.87	7.07	7.33	7.49	-0.6	8.5
Peru Overnight	16.09.2004	2.65	2.70	2.75	2.73	2.50	0.2	2.6
Venezuela deposits 30 days	14.09.2004	10.94	11.37	11.55	13.41	13.20	-2.3	14.0

Foreign exchange reserves								
US$, bn	date	last	one week	one month	one year	end 2003	ytd-change	end 2004f
Argentina	15.09.2004	18.3	18.2	18.1	10.8	14.1	4.2	18.5
Brazil	16.09.2004	49.2	49.3	49.7	51.3	49.3	0.0	50.1
Mexico	10.09.2004	70.2	70.3	68.7	58.7	65.8	4.4	65.0
Chile	31.08.2004	15.8	na	15.9	15.3	15.9	-0.1	16.4
Colombia	31.08.2004	12.1	na	11.8	10.5	10.9	1.2	12.0
Peru	31.07.2004	11.1	na	10.9	10.0	10.2	0.9	11.4
Venezuela (FEM&Gold incl.)	16.09.2004	21.3	21.5	21.2	18.2	21.3	0.0	

Economic activity				Inflation			
GDP (yoy, %)	2003	2004f	2005f	%, year end 2003	2004	2005	GDP 2003, US$ bn
Argentina	8.8	6.5	3.5	3.7	7.0	8.0	127
Brazil	-0.2	4.5	3.9	9.3	6.9	5.8	492
Mexico	1.3	3.5	3.0	4.0	4.2	3.5	626
Chile	3.3	4.8	4.5	1.1	2.9	3.1	72
Colombia	3.7	4.0	3.7	6.5	6.0	6.0	79
Ecuador	2.7	4.8	2.9	6.1	2.3	0.9	27
Peru	4.0	4.2	4.0	1.8	4.0	3.9	61
Venezuela	-7.6	12.8	4.5	27.1	21.0	24.0	86

Public sector	Budget balance, % of GDP		Public debt, % of GDP		Amortization, US$ bn		Gr. financing needs, US$ bn	
	2003	2004f	2003	2004f	2003	2004f	2003	2004f
Argentina	1.3	3.1	140	154	19.8	19.8	19.1	16.3
Brazil*	-5.2	-3.1	58	57	94.2	82.1	72.1	66.2
Mexico**	-0.6	-0.3	28	28	23	29	26	31
Chile***	-0.4	2.5	13	13	0.8	0.8	1.4	-0.7
Colombia	-2.8	-2.8	56	52	6.2	5.3	8.4	7.9
Peru	-1.9	-1.5	48	46	1.1	1.3	2.3	2.3
Venezuela	0.2	0.5	45	35	10.8	4.6	10.7	4.1

* 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	378	39	32.3	80	1.2	1.7	10.0	0.0	5.8
Brazil	210	12	67.4	64	1.3	7.5	32.1	9.5	5.9
Mexico	80	28	33.3	17	-1.4	-8.7	-6.0	15.0	3.5
Chile	127	18	7.7	22	1.9	1.7	7.8	2.7	5.8
Colombia	242	12	6.9	41	-1.8	-1.7	0.4	2.0	6.3
Ecuador	17	14	1.4	3	-0.3	0.3	6.8	-1.1	1.1
Peru	225	16	3.6	26	-1.5	-1.0	2.4	1.1	8.6
Venezuela	87	8	8.1	22	12.3	12.4	19.7	1.5	9.2