

Weekly Watch

Latin

June 3, 2011
Economic Analysis

South America

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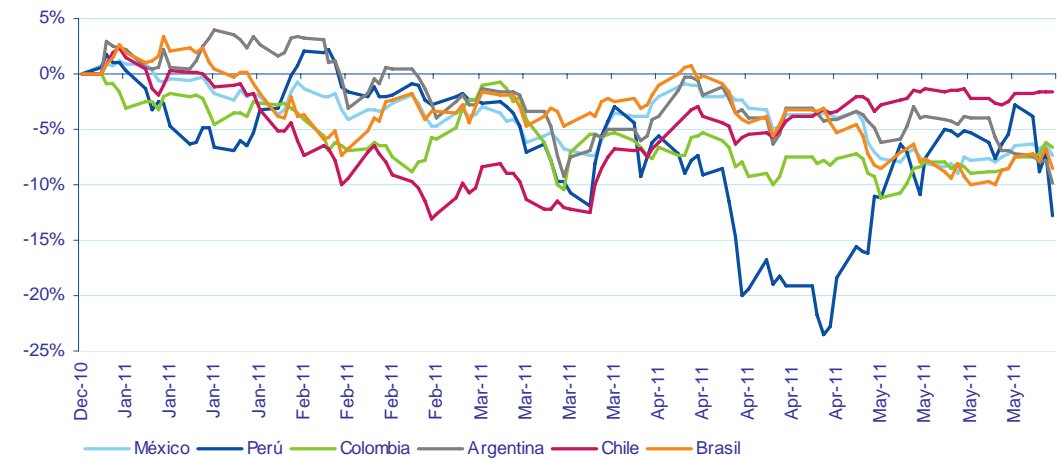
Signs of moderation

Economic growth figures for 1Q11 and advance indicators for April suggest there has been a moderation in the region over the last few months. Chile and Colombia have seen their unemployment rates fall in April. Argentina and Brazil have improved their fiscal balances, due to public spending control, also combined with increased revenues. The Central Bank of Colombia once more increased its reference rate in line with expectations and continues with its dollar purchase program. Finally, a week before the presidential elections in Peru there is still a technical tie between Humala and Fujimori.

Concerns about the global cycle increase risk aversion and lead to asset volatility in the region. Colombia boosted by rating upgrade

Fears about the cycle in the U.S. and Europe, particularly in employment and manufacturing, increased risk aversion over the week and led to greater asset volatility in the region. Currencies in the region fell back, except in Colombia, which stood out thanks to its upgrade. The launch of MILA as the second most important stock exchange in the region will help increase capital flows.

Chart 1
Latin American stock market prices (% YTD)



Source: BBVA Research

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Highlights

- Economic growth continues very strong in 1Q11
- Mixed industrial output results in Brazil and Chile
- Good employment results in Colombia and Chile in April
- Positive fiscal balances in Argentina and Brazil
- The Central Bank of Colombia increased its reference rate by 25 bps to 4.0%
- Technical draw only a few days before the second round in Peru

Economic Analysis

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Markets

Latin American currencies highly volatile due to an upturn in global risk aversion, with Colombia standing out on the positive and Peru on the negative side

Although at the start of last week there was a general appreciation in response to the possibility that Ecofin/IMF would grant a new aid package to Greece, as the days passed the feeling worsened due to uncertainty regarding the global cycle. The negative surprises in the manufacturing indicators in the U.S. and Europe and the ADP employment data in the U.S. (which revised down expectations for the payroll in non-farming businesses), combined with Moody's downgrading of Greece's credit quality, has led to a general phenomenon of risk aversion. The Latin American currencies affected were the BRL, MXN and CLP, which continued to move in line with economic indicators, commodity prices and risk premiums. Two stood out from the rest: 1) the COP benefited from the upgrade by Moody's; and 2) the PEN remained volatile, reflecting expectations surrounding the elections this weekend.

Global stock markets, except Asia, performed negatively due to global cyclical fears. Colombia stands out positively

Despite some optimistic news (although not definite) on the sovereign risk front, reflecting proposed action on Greece, it was the fear about the movement in the global cycle that had most effect on the markets. In Brazil there was less concern about interest rates, although it was not a differentiating factor this time. Of particular note this week was the performance of Peru, where volatility linked to the elections was reflected in the stock markets and country risk indices; and, in the positive side, Colombia was favored by Moody's upgrade from Ba2 to Baa3, a rise of two notches that means the country's debt is now investment grade.

MILA is launched with a capitalization making it the second biggest capital market in the region

One of the highlights was the launch of MILA and the agreement reached with S&P to create families of indices based on the new integrated stock exchange. MILA is the second biggest market in terms of number of listed companies and market capitalization, after that of Brazil, and the third in terms of volume. We expect the integration to help improve the region's visibility and increase transaction volumes (see the note "MILA: more than the sum of its parts" on January 18).

Chart 2
Implied volatility of the BRL, MXN and CLP (%)



Source: BBVA Research

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Highlights

Economic growth continues very strong in 1Q11

In Peru GDP grew by 8.8% y/y in the first quarter (9.2% in 4Q10; 9.6% in 3Q10). The figure is consistent with an estimated quarterly growth of 1.3%. Private spending continued to expand significantly, while public expenditure slowed. In Brazil, GDP grew by 1.1% q/q in 1Q11 (0.7% q/q in 4Q10), as the strength of investment offset moderation in private consumption expenditure. In year-on-year terms GDP grew by 4.2% (5.0% in 4Q10; 6.8% in 3Q10).

Mixed industrial output results in Brazil and Chile

Brazil surprised the market, which expected industrial output to grow 0.2% m/m, with a contraction of 1.3% y/y and 1.1% m/m. This surprise supports the outlook for an economic slowdown in the second quarter. In contrast there were no surprises in Chile. In line with our expectations and those of the market, industrial output was up 9.5% y/y and 1.8% m/m in April.

Good employment results in Colombia and Chile in April

The unemployment rate fell in Chile and Colombia to 7.0% and 11.8%, respectively. The reduction is the result of employment increasing at a faster pace than the labor force, particularly in the manufacturing sector and retail trade. While self-employment in Chile was up 11.5% y/y, notably higher than the increase for salaried employment (5.4% y/y), in Colombia both types of employment grew at rates of around 4% y/y.

Positive fiscal balances in Argentina and Brazil

Tax revenues in Argentina picked up in May boosted by economic activity and inflation, to ARS 50.6 billion (28.7% y/y). By type of tax, there were big gains in Income Tax (up 22.4% y/y) and VAT (up 47.7% y/y). In Brazil, the primary surplus was 3.1% of GDP in April, as a result of high revenues and a greater control of expenditure. The government will adjust its spending for the rest of the year to achieve the target of a primary surplus of 2.9% GDP, but no more than that. In Venezuela, the President of the Republic has requested an extension of the debt law to double the planned debt in the national budget for the year.

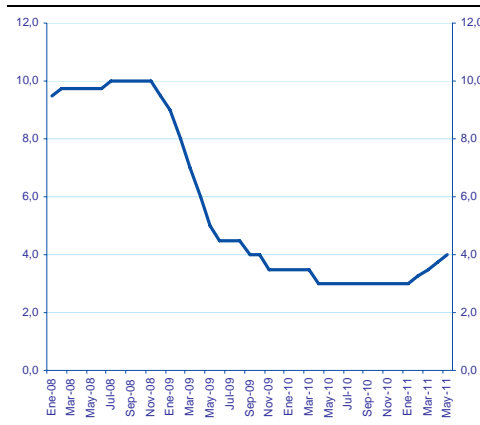
The Central Bank of Colombia increased its reference rate by 25 bps to 4.0%

The statement by the Bank of Colombia continued to suggest a less expansive monetary policy stance in the near future, in line with increases of 25 bps expected by BBVA Research in the benchmark rate over the coming months, and a year-end rate of 4.5%. The bank announced it would extend its dollar purchase program by at least USD 29m per day until (at least) September 30, 2011.

Technical draw only a few days before the second round in Peru

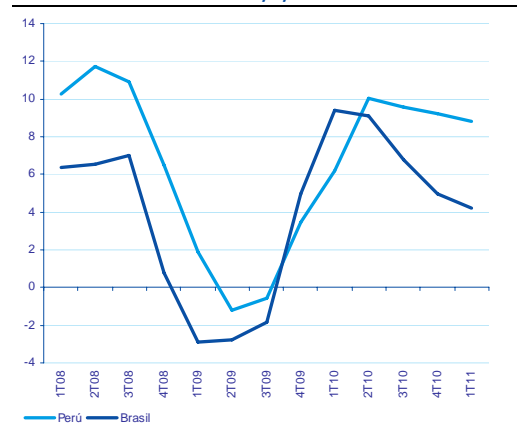
In the Ipsos-Apoyo poll carried out on May 29 Keiko Fujimori's share of the vote fell by two points to 41%, while Ollanta Humala maintained his at 39%. Fujimori's fall coincides with a rise in blank and undecided voters. The gap between the two is within the margin of statistical error (+/- 2.2%), so there is still a technical draw. The second round will be on Sunday, June 5.

Chart 3
Bank of the Republic of Colombia interest rate (%)



Source: BBVA Research

Chart 4
GDP Peru and Brazil (% y/y)



Source: BBVA Research

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Calendar: indicators

Next Week: 6 - 10 June 2011

Brazil	Data	Period	Forecast	Consensus	Previous	Comment
Inflation	7-Jun	May 2011	0.45% m/m	0.55% m/m	0.77% m/m	Due to seasonal factors and lower pressure from commodities, inflation should moderate this month.
SELIC target	8-Jun		12.3%	12.3%	12.0%	There is a generalized consensus that the CB will increase the SELIC by 25bps. The monetary authority could signal extra hikes in forthcoming months.
Retail sales	10-Jun	Apr 2011			1.2% m/m	
Chile	Data	Period	Forecast	Consensus	Previous	Comment
Monthly index of economic activity	6-Jun	Apr 2011	6.6 % y/y	6.7% y/y	15.2% y/y	
Inflation	8-Jun	May 2011	0.3 % m/m	0.3 % m/m	0.3 % m/m	
Economic expectations survey	10-Jun	Jun 2011				
Colombia	Data	Period	Forecast	Consensus	Previous	Comment
Credit	10-Jun	Apr 2011	21.7% y/y		21.9% y/y	Forecast has a downward bias due to Easter period, although this effect is temporary.
Mexico	Data	Period	Forecast	Consensus	Previous	Comment
Inflation	9-Jun	May 2011	CPI -0.64% (3.33% yoy) Core 0.12% (3.06% yoy)	-0.63% mom	-0.01% April (3.36% yoy)	Because of the downwards surprise during May's first fortnight, inflation has stopped the expected rise in annual terms for the 2Q11, and due to this the inflation outlook for the year has improved considerably. The negative monthly rate that will be observed in May is caused by the usual reduction in electric fees during the warm seasons, and very intense reductions in farm produce prices. Core inflation remains firmly under control in all of its components except for the prices processed foods.
Peru	Data	Period	Forecast	Consensus	Previous	Comment
Monetary policy rate	9-Jun	Jun 2011	4.5%	4.5%	4.3%	Inflation and expected inflation around the upper limit of the Central Bank's target suggest that the monetary policy stance would continue normalising. This, however, is subject to how markets internalise the electoral result on June 5th

Source: BBVA Research

Calendar of events

Brazil and Peru: Monetary Policy Rate (June 8 and 9, respectively)

Forecast: Brazil 12.25%; Peru 4.5% **Consensus: Brazil 12.25%; Peru 4.5%** **Previous: Brazil 12%; Peru 4.25%**

In Brazil there is a general consensus on a rise of 25 bps. The central bank statement may give a signal on possible additional rises in the SELIC. In Peru, inflation and its expectations are at the upper limit of the Central Bank's target range, suggesting a continued return to normal in the monetary stance. However, this will depend on how the markets take the election result on June 5.

Calendar of holidays

Colombia and Venezuela: June 6.

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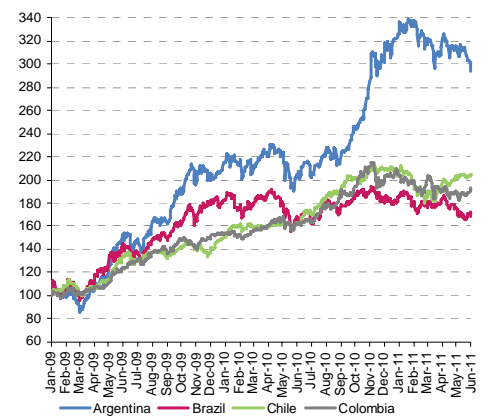
Market Data

			Close	Weekly change	Monthly change	Annual change		
Interest rates (changes in bps)	US	3-month Libor rate	0.25	0	-2	-28		
		2-yr yield	0.46	-2	-13	-27		
		10-yr yield	3.01	-6	-20	-19		
	EMU	3-month Euribor rate	1.44	1	2	73		
		2-yr yield	1.66	10	-25	119		
		10-yr yield	3.02	4	-28	44		
Exchange rates (changes in %)	Europe	Dollar-Euro	1.449	1.5	-2.4	20.5		
		Pound-Euro	0.89	2.6	-1.2	7.1		
		Swiss Franc-Euro	1.22	0.2	-4.5	-12.6		
	America	Argentina (peso-dollar)	4.09	0.0	0.3	4.2		
		Brazil (real-dollar)	1.58	-1.4	-2.1	-14.8		
		Colombia (peso-dollar)	1784	-1.8	0.7	-9.2		
		Chile (peso-dollar)	467	0.1	0.4	-13.4		
		Mexico (peso-dollar)	11.64	0.2	0.1	-9.7		
		Peru (Nuevo sol-dollar)	2.76	0.2	-2.2	-3.1		
		Japan (Yen-Dollar)	80.62	-0.2	0.1	-12.1		
		Korea (KRW-Dollar)	1078.80	-0.4	0.4	-11.9		
		Australia (AUD-Dollar)	1.067	-0.4	-0.8	29.0		
		Comm. (chg %)	Brent oil (\$/b)	115.1	0.0	-5.1	59.6	
			Gold (\$/ounce)	1533.2	-0.2	1.1	25.7	
Base metals	611.9		0.8	-0.6	30.4			
Stock markets (changes in %)	Euro	Ibex 35	10283	0.2	-4.0	15.2		
		EuroStoxx 50	2791	-1.0	-5.4	9.3		
		USA (S&P 500)	1313	-1.4	-2.6	23.3		
	América	Argentina (Merval)	3150	-3.5	-6.0	44.4		
		Brazil (Bovespa)	64218	-0.1	0.9	4.1		
		Colombia (IGBC)	14443	0.7	2.6	18.2		
		Chile (IGPA)	22981	0.3	1.8	27.3		
		Mexico (CPI)	35416	-1.1	-0.3	14.3		
		Peru (General Lima)	21736	-2.9	5.1	57.3		
		Venezuela (IBC)	80614	0.7	9.3	27.4		
		Asia	Nikkei225	9492	-0.3	-5.1	-4.1	
			HSI	22950	-0.7	-1.6	16.0	
		Credit (changes in bps)	Ind.	Itraxx Main	105	1	8	-22
				Itraxx Xover	381	8	25	-208
Sovereign risk	CDS Germany		39	-1	-1	-10		
	CDS Portugal		691	11	68	338		
	CDS Spain		254	0	28	-3		
	CDS USA		48	-2	5	---		
	CDS Emerging		217	0	16	-77		
	CDS Argentina		622	7	39	-550		
	CDS Brazil		107	0	3	-39		
	CDS Colombia		101	-4	2	-68		
	CDS Chile		69	0	11	-36		
	CDS Mexico		104	-1	7	-40		
	CDS Peru		146	20	-1	1		

Source: Bloomberg and Datastream

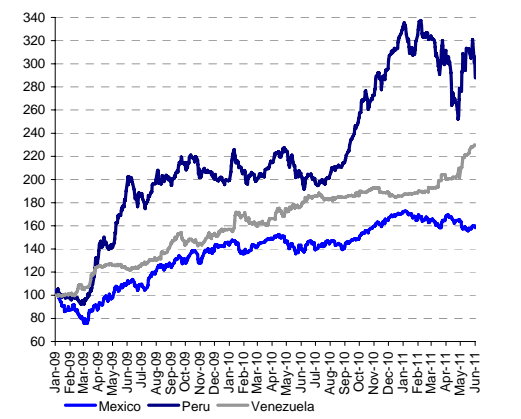
Charts

Chart 4
Stock markets (base index Jan09 = 100)



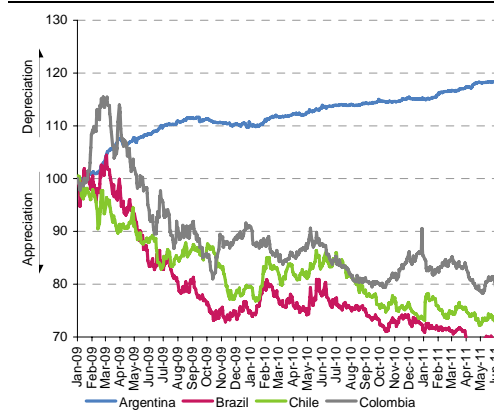
Source: Datastream and BBVA Research

Chart 5
Stock markets (base index Jan09 = 100)



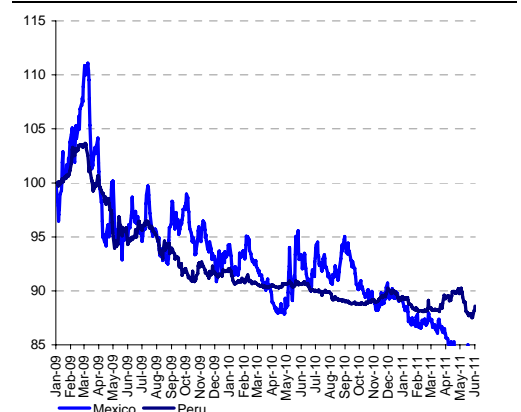
Source: Datastream and BBVA Research

Chart 6
Exchange rates (base index Jan09 = 100)



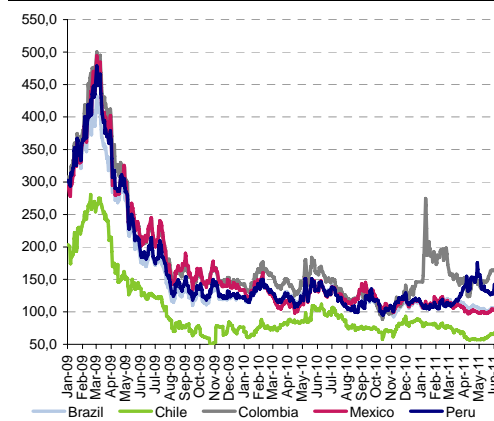
Source: Datastream and BBVA Research

Chart 7
Exchange rates (base index Jan09 = 100)



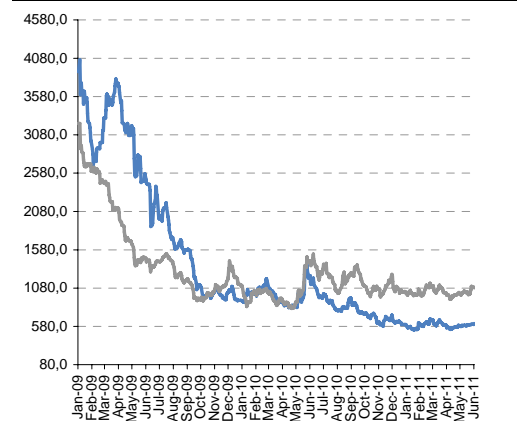
Source: Datastream and BBVA Research

Chart 8
Credit Default Swaps (levels)



Source: Datastream and BBVA Research

Chart 9
Credit Default Swaps (levels)



Source: Datastream and BBVA Research

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