

# Weekly Observatory

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## Economic Analysis

South America

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Markets

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## Inflation is up

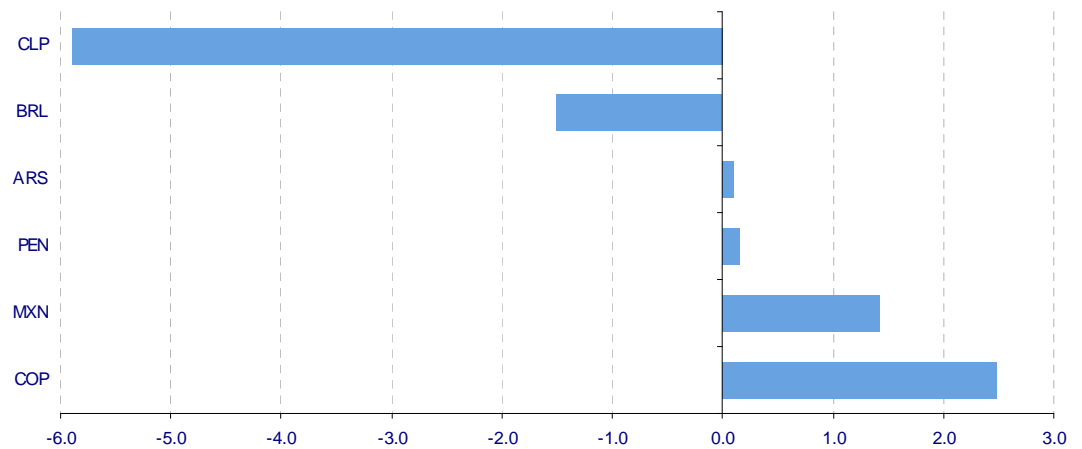
Inflation was higher than expected in Colombia and Venezuela due to supply shocks, as well as in Chile and Mexico. Economic activity continues strong in the region, boosted by buoyant domestic demand, with growth in Chile and expansion of credit in Colombia of 17.2% y/y. There was a surprising improvement in Brazil's trade balance in December. Meanwhile, both Argentina and Chile have ended the year with bigger fiscal surpluses than expected. Venezuela unified its dual exchange rate system, which ended at VEF/USD 4.30, while Brazil and Peru have continued to take measures to limit capital inflows and Chile joins the countries that are actively intervening in the foreign-exchange market by announcing a currency purchase program for USD 12 billion for this year.

## Measures to limit the appreciation of currencies in the region (Chile and Brazil), with short-term effects, could make the Mexican currency attractive

The announcement of accumulation of reserves in Chile and the reserve requirements for short positions in dollars in Brazil could be effective in the short term, but with questionable effects in the future. We believe that the increased attractiveness of the MXN could be a collateral short-term effect of this interventionism in the Southern Cone.

Chart 1

### Variations in LatAm currencies (% , 7 days)



Source: Bloomberg and BBVA Research

Markets



Highlights



Calendar



Markets Data



Charts



## Highlights

**Foreign-exchange measures in the region**

**Economic activity in Chile and Colombia remains strong**

**Inflation is up in most countries**

**Trade balance in Brazil**

**Positive indicators of fiscal solvency in Argentina**

**Peru: Official rates hike take most market players by surprise**

**Venezuela reconsiders tax increases**

**Economic Analysis**

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**Markets**

**Chile, Brazil and Peru establish measures to contain the appreciation of their currencies, with largely short-term effects**

The main events in markets in the region were the announcements on foreign-exchange policy in Chile (accumulation of reserves of USD 12 billion in 2011, amounting to nearly 45% of the country's international reserves) and Brazil (reserve requirements equivalent to 60% of the foreign-exchange position above either USD 3 billion, or their capital base, whichever is the lower). We believe that in both cases the measures will be effective in the short term to restrict the appreciation of the currencies and could even lead to an over-reaction of the USD (for example, the CLP has lost 6% over the week). The medium and long-term effects are more questionable. In Colombia, after a major depreciation in December due to similar measures to those implemented in Brazil (levels of 2,000 in the last days of the year), the currency registered strong gains last week and seems to be moving towards the 1,850 zone.

We believe that a collateral medium-term effect of this interventionism in the Southern Cone may be to increase the attractiveness of the MXN in the case of agents who want to capitalize on their commitment to the strength of emerging countries and the surprising upturn in the American cycle through foreign-exchange exposure. This is because the economic authorities in Mexico have clearly expressed their commitment to free flotation.

**Capital markets in Latin America open the year on a positive note, but await monetary policy moves in Asia and local exchange-rate measures**

With the exception of Peru and Colombia, the main stock market indices in the region were positive in the first week of the year, due to improved cyclical expectations in the U.S. However, the surge at the start of the year moderated at the end of the week as fears increased of monetary measures in Asia (particularly China) to contain upward pressure on inflation. Another source of concern was the measures taken in some countries in the region to contain the appreciation of currencies.

Meanwhile, the Lima Stock Exchange and the Cavali central securities depository announced their return to the process of creating the Integrated Latin American Market (MILA) after the tax treatment of capital gains was brought into line.

Highlights →

Calendar →

Markets Data →

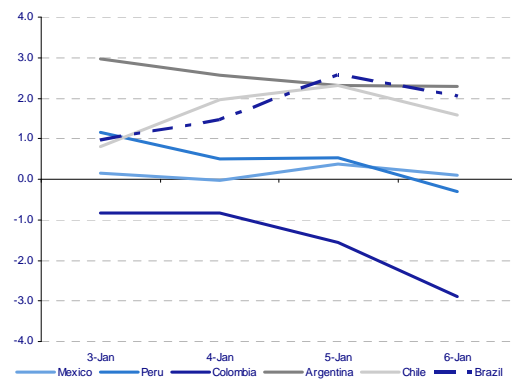
Charts →

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



Source: BBVA Research with data from Bloomberg

Chart 3  
**Latam: Stock Exchange Index (% var. weekly, vs. 30-Dec-10)**



Source: BBVA Research with data from Bloomberg

Economic Analysis

# Highlights

## Foreign-exchange measures in the region

Brazil added new reserve requirement, forcing banks to deposit 60% of their total short positions in dollars for the amount exceeding USD 3 billion dollars or the value of its capital base. Venezuela eliminated the preferential exchange-rate leaving the official rate at VEF/USD 4.3, with an implicit devaluation of 23%. In Chile the Central Bank announced the purchase of USD 12 billion of currencies in 2011, with a major impact on exchange rates and interest rates. In Peru, Congress approved the extension to the scope of income tax for earnings from financial derivatives with non-residents. In addition, set bank reserve obligations for branches of Peruvian banks abroad, while the government cut import tariffs.

## Economic activity continues strong in Chile and Colombia, but moderates in Brazil

In November, industrial output in Brazil fell less than expected (-0.1% m/m instead of -0.3%), reaching a standstill in the last quarter. In Chile the IMACAEC rose by 6.2% y/y (1.3% m/m). There was a strong increase in credit in Colombia (17.2% y/y), boosted mainly by commercial loans (18.3% y/y).

## Inflation is up in most countries

In Brazil, prices rose 0.6% m/m (5.9% y/y), while in Mexico inflation was higher than expected (0.5% m/m, 4.4% y/y), as happened in Chile too (0,1% m/m, 3,0 y/y). In Peru remained low in line with expectations (0.2% m/m (2.1% y/y). Inflation in Colombia (0.7% m/m, 3.2% y/y) and Venezuela (1,8% m/m, 27,2% y/y) was high, due to the impact of floods on food prices.

## Positive indicators of fiscal solvency in Argentina

Tax receipts were up 34.4% in Argentina in December, leading to a fiscal surplus of 0.3% of GDP in 2010. Public debt fell to 47.1% of GDP in 3Q10 and with the exchange of Brady bonds, some 95% of public securities are now no longer in default.

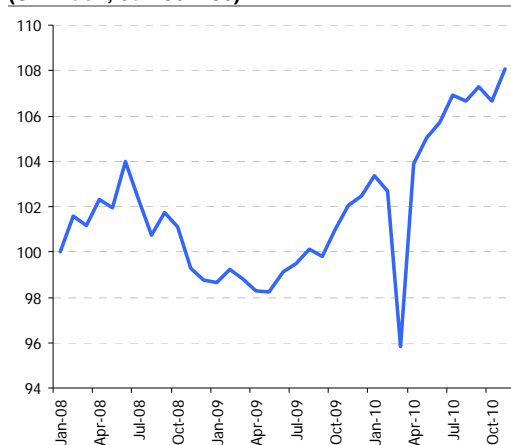
## Peru: Official rates hike take most market players by surprise

The Central Bank increased the reference rate by 25bps to 3.25%, surprising most market observers. This reflects the strong commitment with the inflation target.

## The Venezuelan government reconsiders tax increases

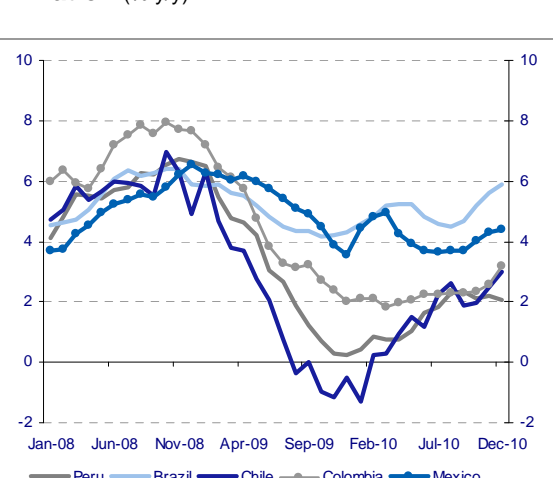
The government ruled out a rise in VAT and taxes on financial services, giving up revenues of 0.9% of GDP in the light of the oil bonanza.

Chart 4  
**Chile: Monthly Economic Activity Index**  
(SA index; Jan 08=100)



Source: BBVA Research

Chart 5  
**Inflation (% y/y)**



Source: INEI, INE, DANE

- Markets →
- Calendar →
- Markets Data →
- Charts →

## Calendar: Indicators

### Next Week: 10-14 January 2011

Country	Data	Period	Forecast	Consensus	Previous	Comment
<b>Argentina</b>						
	Cost of Construction Index	14-Jan	Dec 2010		0,5 m/m; 16,1 y/y	
	Consumer Price Index	14-Jan	Dec 2010		0,7 m/m; 11% y/y	
	Wholesale Price Index	14-Jan	Dec 2010		IPIM: 0,9 m/m; 14,9 y/y	
<b>Brazil</b>						
	Retail sales	12-Jan	Nov 2010	1.1% m/m	0,4% m/m	
<b>Chile</b>						
	Survey Economic Expectations	11-Jan	Jan 2011			
<b>Colombia</b>						
	Automobile sales	10-12 enero de 2011	Dec 2010	21163	30963	November sales are not sustainable by the presence of fair prices in that month, but it is expected that continued strong demand for automobiles in line with the growth of durable goods consumption.
	Consumer confidence	11-Jan	Dec 2010	28.0 s.a.	31.4 s.a.	Winter emergency impair the households confidence, but would remain at high levels.
	Industrial confidence	12-Jan	Nov 2010	5.0 s.a.	3.0 s.a.	Confidence could increase driven by the recent growth in industrial exports.
	Commerce confidence	12-Jan	Nov 2010	25.0 s.a.	28.8 s.a.	Impact of rainfall on consumption could moderate the confidence of traders.
<b>Mexico</b>						
	IGAE	10-Jan	Oct 2010	-0.08 m/m (4.2% y/y)	-0.3 m/m (5.0% y/y)	We expect slight drop in the monthly change in economic activity over last October following the fall in industrial production, services growth is maintained.
	Producción Industrial	11-Jan	Nov 2010	0.3 m/m (5.2% y/y)	-0.3 m/m (4.6% y/y)	We expect a slight recovery in industrial production influenced by U.S. manufacturing and continued construction recovery
<b>Peru</b>						
	Trade Balance	11-Jan	Nov 2010		USD 424 millions	
<b>Venezuela</b>						
	Car sales	10-Jan	Dec 2010	-2.3% m/m; 10.4% y/y	10.0% m/m; 13.0% y/y	With this result, the car sales fall 7.6% a/a in the 2010

Source: BBVA Research

## Calendar: Events

### Chile: Monetary policy meeting (January 13)

Forecast: 3.5%

Previous: 3.25%

At its monetary policy meeting next Thursday 13th, the Central Bank should increase its policy rate by 25 bps to 3.5%, due to the risk of inflationary pressures from domestic and external factors. However, most market observers expect there will be a pause.

## Calendar: holidays

### Colombia and Venezuela: Monday, January 10

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## Market data

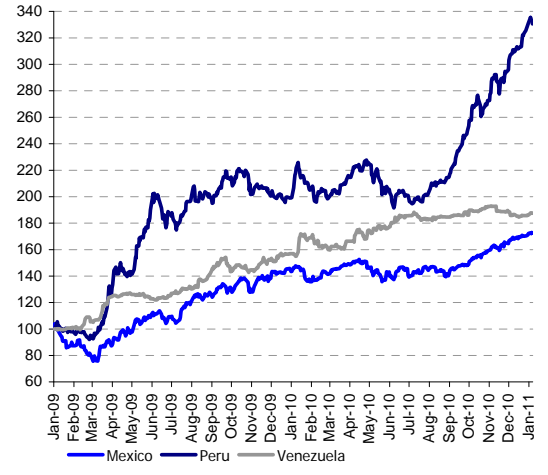
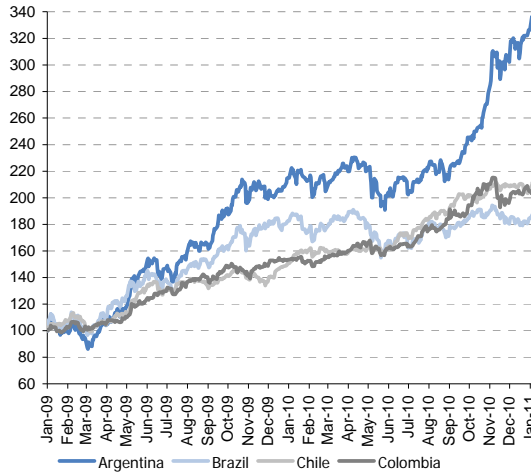
			Close	Weekly change	Monthly change	Annual change
<b>Interest rates</b> (changes in bps)	<b>US</b>	3-month Libor rate	0.30	0	0	5
		2-yr yield	0.62	2	-1	-36
		10-yr yield	3.38	9	11	-45
	<b>EMU</b>	3-month Euribor rate	1.00	-1	-3	31
		2-yr yield	0.88	2	-12	-36
		10-yr yield	2.90	-6	-11	-48
<b>Exchange rates</b> (changes in %)	<b>Europe</b>	Dollar-Euro	1.297	-3.0	-1.9	-9.9
		Pound-Euro	0.84	-2.5	-0.3	-7.0
		Swiss Franc-Euro	1.25	0.4	-4.3	-15.2
	<b>America</b>	Argentina (peso-dollar)	3.97	-0.1	-0.2	4.6
		Brazil (real-dollar)	1.68	1.2	-0.8	-2.8
		Colombia (peso-dollar)	1855	-3.3	-1.5	-5.7
		Chile (peso-dollar)	497	6.2	4.2	0.7
		Mexico (peso-dollar)	12.20	-1.2	-2.1	-3.9
		Peru (Nuevo sol-dollar)	2.80	-0.1	-0.5	-1.6
		<b>Asia</b>	Japan (Yen-Dollar)	83.16	2.4	-1.3
	Korea (KRW-Dollar)		1120.70	-0.4	-1.9	-0.4
	Australia (AUD-Dollar)		0.998	-2.5	2.1	8.1
	<b>Comm.</b> (changes in %)	Brent oil (\$/b)	93.9	-0.9	3.4	15.4
		Gold (\$/ounce)	1366.9	-3.8	-1.1	20.1
		Base metals	582.5	-0.2	2.0	16.9
<b>Stock markets</b> (changes in %)	<b>Euro.</b>	Ibex 35	9593	-2.7	-4.8	-21.1
		EuroStoxx 50	2826	1.2	0.3	-6.3
	<b>America</b>	USA (S&P 500)	1273	1.2	3.7	11.2
		Argentina (Merval)	3616	2.6	5.5	53.7
		Brazil (Bovespa)	70344	1.5	3.2	0.1
		Colombia (IGBC)	15050	-2.9	-2.6	29.2
		Chile (IGPA)	23410	1.9	1.2	36.2
		Mexico (CPI)	38611	0.2	2.6	17.4
		Peru (General Lima)	23290	-0.4	6.3	49.0
		Venezuela (IBC)	65794	0.7	0.5	21.0
	<b>Asia</b>	Nikkei225	10541	3.1	3.0	-2.4
		HSI	23687	2.8	2.6	6.2
	<b>Credit</b> (changes in bps)	<b>Ind.</b>	Itraxx Main	109	4	3
Itraxx Xover			429	-8	-27	35
<b>Sovereign risk</b>		CDS Germany	56	-2	6	30
		CDS Portugal	507	7	75	415
		CDS Spain	348	-2	43	240
		CDS USA	40	-2	0	---
		CDS Emerging	201	0	-12	-36
		CDS Argentina	564	-38	-72	-411
		CDS Brazil	107	-4	-2	-9
		CDS Colombia	108	-5	-2	-24
		CDS Chile	81	-4	-2	22
		CDS Mexico	110	-3	1	-13
		CDS Peru	108	-5	-6	-8

Source: Bloomberg and Datastream

# Charts

Charts 6 & 7

## Stock exchanges (base index Jan09=100)

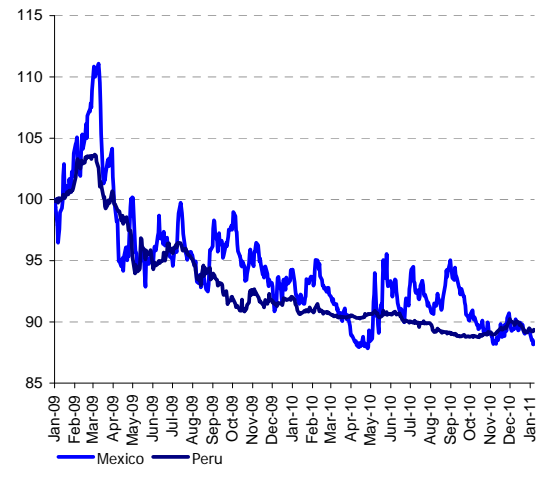
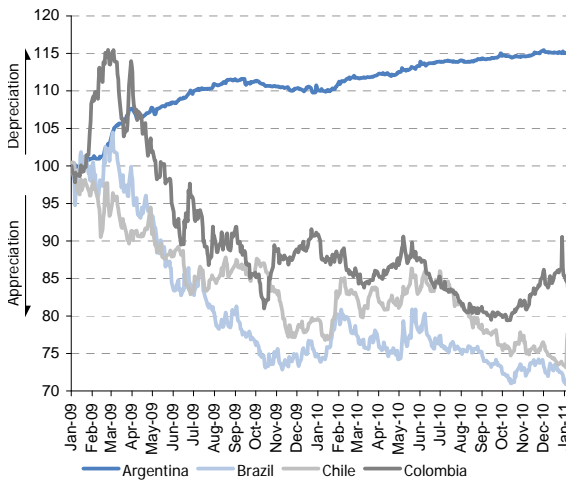


Source: Bloomberg

Source: Bloomberg

Charts 8 & 9

## Exchange rates (base index Jan09=100)

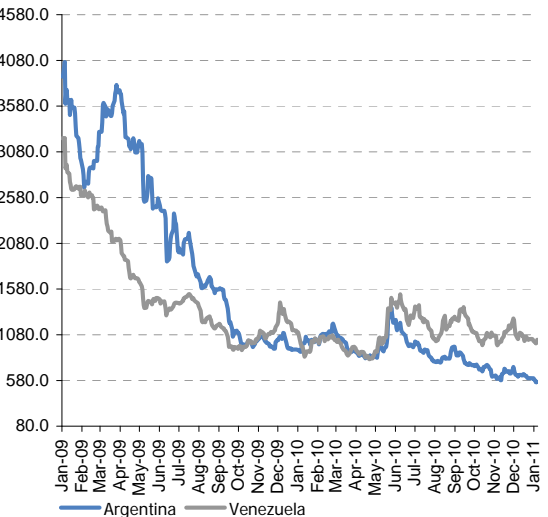
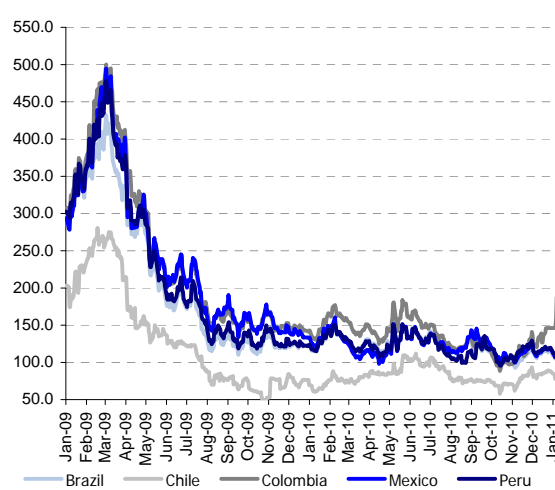


Source: Bloomberg

Source: Bloomberg

Charts 10 & 11

## Credit Default Swaps (levels)



Source: Bloomberg

Source: Bloomberg

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