

Weekly Observatory

February 07, 2011

Economic Analysis

South America

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Markets

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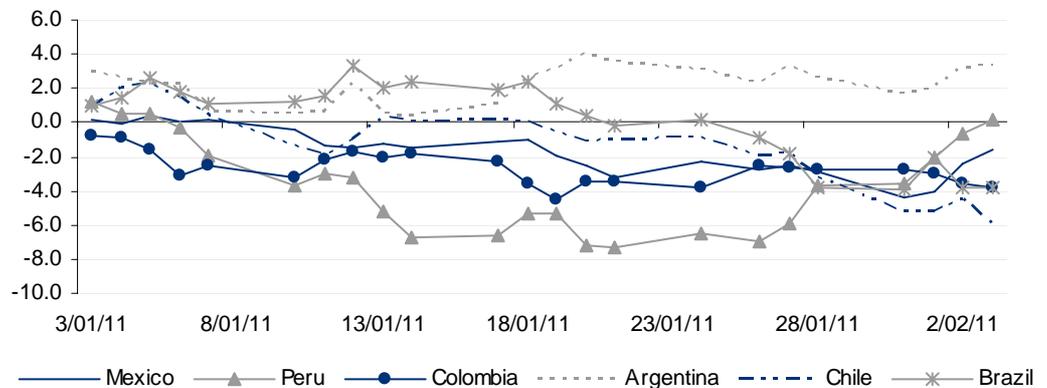
Currencies continue to appreciate

Mixed closed in the manufacturing sector: Argentina and Chile expand, while Brazil resent the end of the fiscal plan, and in Mexico the decrease in Manufacturing Confidence could indicate a slowdown in production. The dynamic economy and the effect of foreign prices are causing inflationary pressures in the region; the monetary policy remains expansive, but the stimuli continue to be withdrawn gradually. This way, the appreciation of local currencies is again under pressure.

In line with the majority of risk assets, Latin American currencies and share indices performed positively during the week.

Recent financial news from the United States resulted in a recovery of regional currencies compared to the previous week, though it was limited by the geo-political conflicts in the Middle East. The stock markets closed with gains, but they were lower than their global peers in response to various factors related to local monetary policies and more moderate easing in LatAm risk premiums. Solid demand can still be observed in the corporate credit market

Chart 1
LatAm Stock Market Monitor (3M)



Source: Bloomberg and BBVA Research

Highlights

- Inflation begins to accelerate in Peru**
- Monetary policy adjustments**
- Bank credit in Chile maintains its upward trend**
- Mixed closures for the region's manufacturing sector**

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Economic Analysis

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Markets

A busy week for financial news resulted in a generalized appreciation of LatAm currencies

Last week was laden with economic information and events that impacted the dynamics of the region's currencies. The flow of US economic data (personal spending, the ISM manufacturing index and employment) resulted in a positive bias in the majority of exchanges, which were, however, somewhat limited by the geo-political conflicts in the Middle East. Furthermore, a less hawkish than expected statement, together with the decrease in the debt rating of Ireland and Angela Merkel's declaration regarding the purchase of European Stabilization Fund bonds, provoked profit-taking in the euro share price, which then transferred somehow to all LatAm exchanges. Thus, the currencies in the region reported an average appreciation of 0.5% at the close of Thursday, which also responded to a correction of the dramatic fall recorded last Friday for the majority of risk assets. Against this backdrop, the CLP's performance was noteworthy, broking the support of 480 down with the rally in copper prices. Also, exchange rate interventions on the domestic front have shown to be less effective and moved to the second degree.

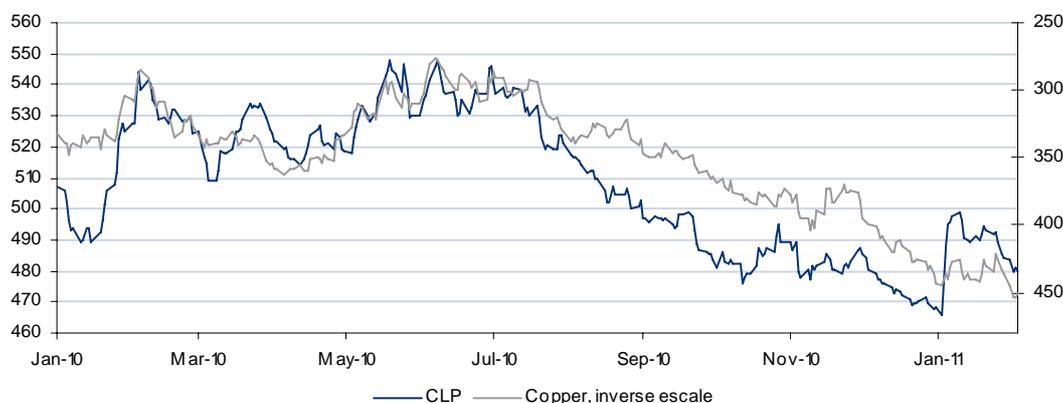
Lower performance of LatAm share indices as compared to their global peers, though the growth remains attractive.

The region's stock markets followed the performance of their global peers, though, in relative terms, their performance continues to be inferior. We attribute this to the following: 1) the risk premiums in other markets have recently eased and were not as high as in LatAm; 2) though the expected economic performance is significantly better in emerging markets, the positive surprises have remained higher in developed markets; and 3) the Brazilian stock market is still affected by the uncertainty of the magnitude of the restrictions in the monetary policy. Within the region, Mexico and Peru stand out, and the first, to date, reported few mixed results in 4Q10. In the coming weeks, performance will be more closely linked to the results reporting seasons. If our expectations are realized, we will continue to observe attractive growth that could support the current valuations and even act as a catalyst.

The appetite for the corporate credit market is maintained.

International investors continue to respond positively to the non-investment grade issues from Latin American corporations. Over the week, the Mexican construction company ICA (B+/Ba3) auctioned off a 10-year note for US\$400m and coupon at 8.9%, in addition to the CEMEX 7NC4 for US\$1,000m. Companies in the energy, primary and financial sectors of all LatAm countries also report a strong response from international investors.

Chart 2
CLP v/s Copper



Source: BBVA Research with data from Bloomberg

Highlights →

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Highlights

Inflation begins to accelerate in Peru

In January, inflation rose to 0.39% m/m (2.2% y/y), marking its fastest rate since October 2008. Although this result was primarily due to seasonal factors (increase of some food prices) and one-off factors, which were linked to an increase in international oil prices and resulted in the adjustment of electricity and fuel rates, the market has begun to correct its inflation expectations upwards.

Monetary policy adjustments

The Central Bank of Peru (BCR) increased banks' reserve obligations, while Colombia, even when the policy rate remained unchanged (3.0%), sent a message with a more restrictive tone. Against this backdrop, the pressures on local currency appreciation resumed, and the BCR took up its exchange rate interventions once again. Moreover, starting next week, the Bank of Mexico will begin publishing the minutes of its monetary policy meetings.

Unemployment rates in Chile and Colombia fall. As of December 31, 2010, unemployment rates in Chile and Colombia stood at 7.1% and 11.3%, respectively. In Chile, payroll employment increased, while, for the second consecutive quarter, self-employment declined. A total of 369 thousand jobs were created in the 13 metropolitan areas of Colombia in 2010; 56% of them were salaried.

Bank credit in Chile maintains its upward trend

Total nominal credit grew 8.62% in 12 months. In terms of margin, only commercial loans declined as of December 2010. Activity, measured by the real change of loan placements, fell 0.07% in the month and expanded 5.12% in twelve months. The value of the Provisions for loan losses index in December stood at 2.49%, which marked the third consecutive month of decreases in the margin.

Mixed closures for the region's manufacturing sector

In Argentina, the manufacturing sector grew 5.6% m/m in December and 9.8% in 2010. In Brazil, however, industrial output surprisingly fell back 0.7% m/m in December, though it grew 10.5% in 2010 due to the strong expansion in the first half of 2010. Industrial output in Chile fell 0.5% m/m in 2010, due to the 15.7% decrease of the sectors affected by the earthquake. In Mexico, Manufacturing Confidence decreased (-2.1% m/m) in January.

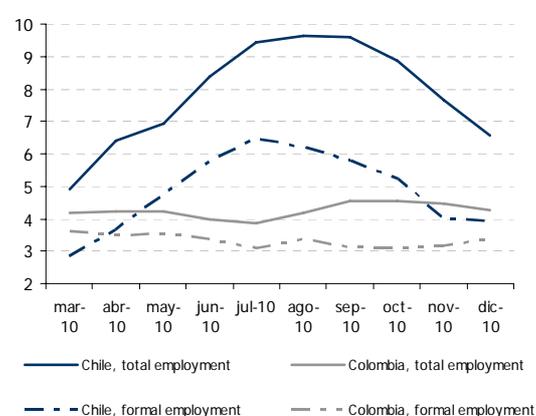
Chart 3

Argentina, Brazil and Chile: Industrial Output (y/y % change)



Chart 4

Chile and Colombia: Growth of Employment and Payroll Employment (y/y % change)



Source: BBVA Research with data from Indec in Argentina, Ibge in Brazil and Sofofa in Chile. Source: BBVA Research with data from INE in Chile and Dane in Colombia

Markets →

Calendar →

Markets Data →

Charts →

Calendar: Indicators

Indicators next week 7- 11 February 2011

Country	Indicator	Date	Period	Forecast	Consensus	Previous	Comment
Argentina							
	Terms of Trade	10/2/2011	4th Q'10	4.0% y/y		-0.5 % y/y	Improve in commodities export price
	Consumer Price Index	11/2/2011	January	1,5% m/m	1,3% m/m	0,8% m/m	Seasonal increase impact
	Construction Cost Index	11/2/2011	January			2,7% m/m	
	Whole Sale Price Index	11/2/2011	January			0,9% m/m	
Brazil							
	Inflation	8/2/2011	January	0.7% m/m	0.8% m/m	0.6% m/m	Inflation is expected to move up in January due to seasonal factors, but also due to the strenght of the domestic demand and commodity prices. The figure will have an impact on interest rate future markets and on agents' inflation perspectives.
Chile							
	Monthly Economic Activity Index	2/7/2011	December	6.2% y/y	6.2% y/y	6.2% y/y	
	Earnings Index	2/7/2011	December				
	Consumer Price Index CPI-PPI	2/8/2011	January	0.3% m/m		0.1% m/m	Inflation expectations have increased. There is the risk of decoupling from the Central Bank inflation target.
	Tenders and Maturities Calendar	2/8/2011	February				
	Financial Operators Survey	2/9/2011	February				
	Economic Expectations Survey	2/10/2011	February				
Colombia							
	Loan and resources	02/7-10/2011	December	Loan 16.3% YoY, resources 11.2% YoY		Loan 17.2% YoY, resources 8.9% YoY	Strong dynamism of the commercial portfolio at the end of the year, which could moderate in the first half of 2011 by removing the tax system favors investment.
	Automobile sales	2/9/2011	January	24000 units		25556 units	Low interest rates and peso appreciation maintain low prices in the sector. Expected to reinforce the signs of a gradual exit from the monetary stimulus in upcoming months.
	Monetary Policy Meeting Minutes	2/11/2011	January				
Mexico							
	Inflation	2/9/2011	January	0.55% m/m (4.03 % y/y)	0.0051	0.005	Inflation will continue reducing in annual terms, thanks to the comparison effect against January 2010. Core inflation will raise 0.46% driven by the prices of cigarettes caused by the higher IEPS tax, and tortillas due to pressures in corn prices.
	Industrial Production	2/11/2011	December	0.3% m/m (3.4% y/y SA)	NA	0.2% m/m (4.2% y/y SA)	Industrial production continued with moderate growth at the end of last year, slightly above the previous month. As has been in previous months, the main driver will be the outer cycle through the manufacturing sector.
	Private Formal Employment	During the week	January	0.4 m/m (5.3% y/y SA)	NA	0.5% m/m (5.3% y/y SA)	The employment continued growing with almost 749 000 new jobs over the previous year. New employment in construction sector will be important, which had fallen behind and look good share of manufacturing and services.
Peru							
	Policy rate	2/10/2011	February	0.035	0.035	0.0325	Robust domestic demand and inflation expectations that are starting to increase would lead the Central Bank to continue monetary policy tightening
	Trade balance	2/11/2011	December			USD 557 millions	
Venezuela							
	Consumer Price Index	2/10/2011	January	1.9 m/m		1.8 m/m	This figure could allow to observe the impact of FX adjustment on prices in line with our scenario.

Calendar: Events

Peru: Monetary Policy Meeting (February, 10)

Forecast: 3.5%

Consensus: 3.5%

Previous: 3.25%

The monetary adjustment will continue in February in a context of robust dynamism for domestic demand and inflationary expectations that are beginning to be adjusted upwards.

Calendar: holidays

Mexico: Monday, February 7

Markets →

Highlights →

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Charts →

Market data

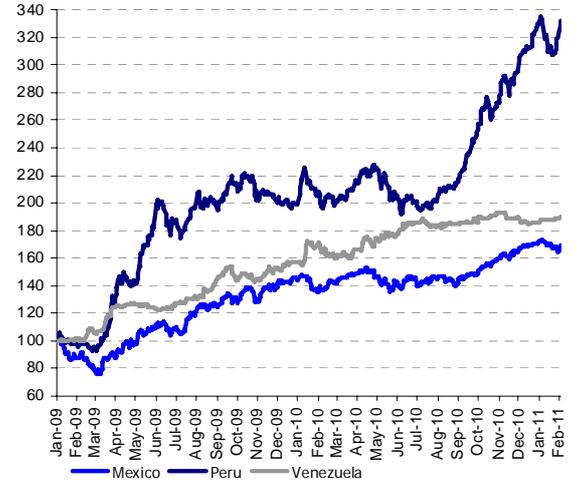
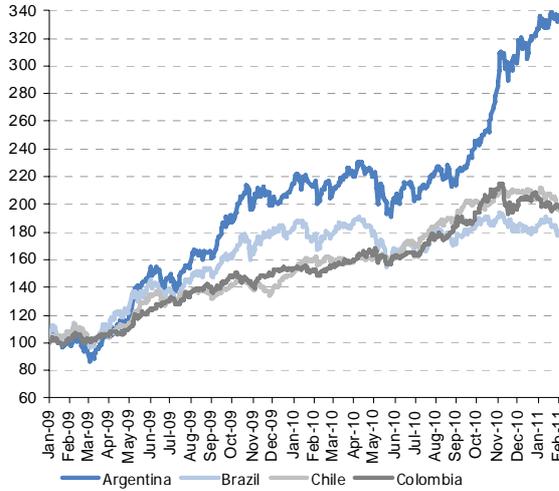
			Close	Weekly change	Monthly change	Annual change
Interest rates (changes in bps)	US	3-month Libor rate	0.31	1	1	6
		2-yr yield	0.70	17	0	-6
		10-yr yield	3.55	23	8	-2
	EMU	3-month Euribor rate	1.09	2	9	42
		2-yr yield	1.38	2	48	39
		10-yr yield	3.24	9	30	12
Exchange rates (changes in %)	Europe	Dollar-Euro	1.364	0.2	3.5	0.1
		Pound-Euro	0.84	-1.7	-0.7	-3.2
		Swiss Franc-Euro	1.29	0.6	1.6	-12.0
	America	Argentina (peso-dollar)	4.01	0.3	1.1	4.4
		Brazil (real-dollar)	1.67	-1.0	-0.4	-11.4
		Colombia (peso-dollar)	1862	-0.4	-1.0	-6.4
		Chile (peso-dollar)	480	-1.0	-3.1	-11.4
		Mexico (peso-dollar)	12.00	-1.4	-1.8	-9.0
		Peru (Nuevo sol-dollar)	2.77	-0.2	-1.2	-3.4
		Asia	Japan (Yen-Dollar)	81.58	-0.7	-2.0
	Korea (KRW-Dollar)	1102.50	-1.7	-1.9	-6.7	
	Australia (AUD-Dollar)	1.019	2.5	1.8	18.1	
Comm (changes in %)		Brent oil (\$/b)	101.5	2.1	6.3	45.8
		Gold (\$/ounce)	1349.6	1.0	-2.1	26.6
		Base metals	612.8	1.1	5.1	31.5
Stock markets (changes in %)	Euro	Ibex 35	10838	0.8	10.6	7.3
		EuroStoxx 50	3005	1.7	6.1	14.2
		USA (S&P 500)	1307	2.4	2.4	22.6
	America	Argentina (Merval)	3639	1.6	1.0	68.1
		Brazil (Bovespa)	66765	0.1	-6.1	6.4
		Colombia (IGBC)	14851	-1.4	-2.7	32.3
		Chile (IGPA)	21828	-1.9	-7.0	27.0
		Mexico (CPI)	37739	2.4	-2.5	23.2
		Peru (General Lima)	23724	5.3	1.0	71.1
		Venezuela (IBC)	66677	0.9	1.3	15.5
	Asia	Nikkei225	10544	1.8	1.6	4.8
		HSI	23909	1.2	0.6	21.6
Credit (changes in bps)	Ind.	Itraxx Main	97	-3	-5	6
		Itraxx Xover	408	-11	-9	-88
	Sovereign risk	CDS Germany	56	-5	-1	12
		CDS Portugal	398	-57	-100	174
		CDS Spain	227	-39	-116	67
		CDS USA	47	-3	8	---
		CDS Emerging	211	-14	15	-77
		CDS Argentina	586	-26	29	-489
		CDS Brazil	114	-8	10	-35
		CDS Colombia	115	-8	9	-61
		CDS Chile	77	-9	-5	-3
		CDS Mexico	117	-7	10	-35
		CDS Peru	108	-8	1	-43

Source: Bloomberg y Datastream

Charts

Charts 5 & 6

Stock exchanges (base index Jan09=100)

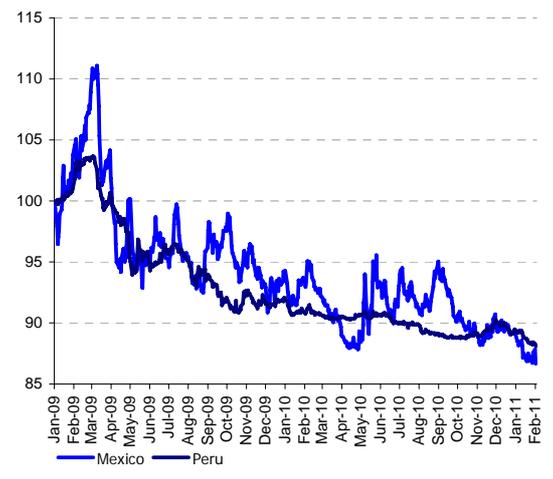
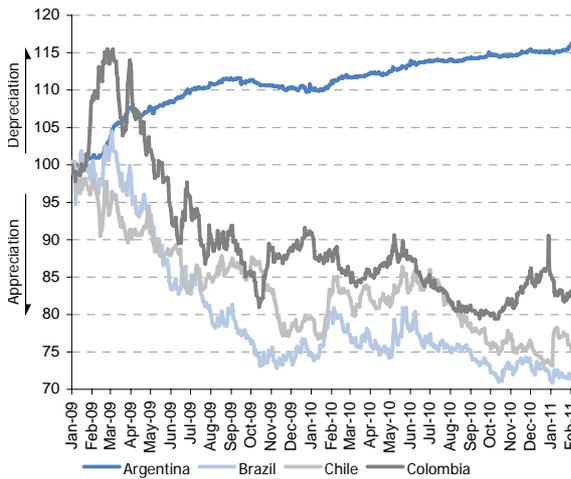


Source: Bloomberg

Source: Bloomberg

Charts 7 & 8

Exchange rates (base index Jan09=100)

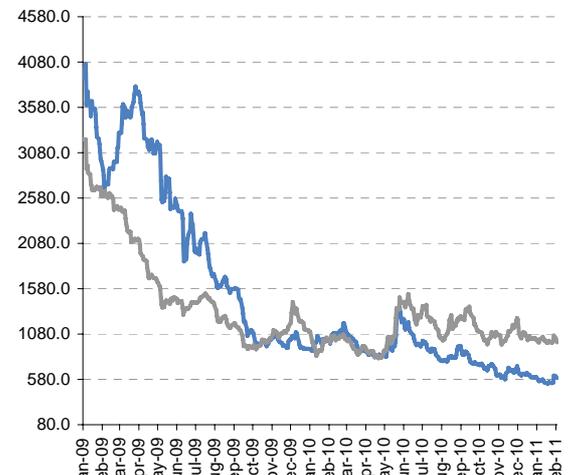
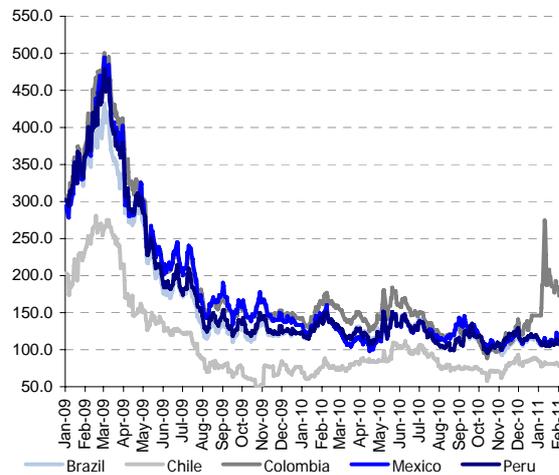


Source: Bloomberg

Source: Bloomberg

Charts 9 & 10

Credit Default Swaps (levels)



Source: Bloomberg

Source: Bloomberg

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