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Weekly Watch

Latin

October 10, 2011
Economic Analysis

South America

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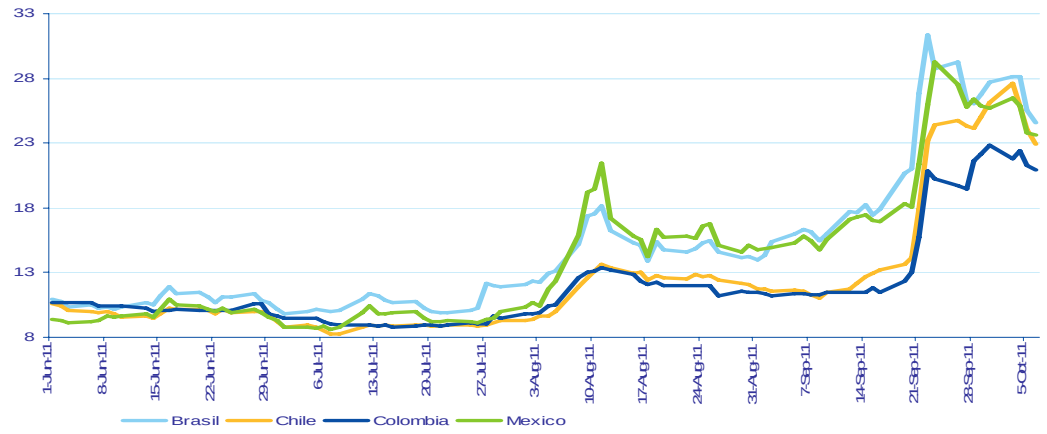
Inflation and depreciations could delay monetary easing

In most countries September inflation was higher than in previous months and above market expectations. This will not change the course of monetary policy in the short run, but in the event of new surprises in inflation, with weaker currencies and no clear signs of a slowdown in demand and employment, central banks will find difficult to lower interest rates.

Volatility remains high and Latin American assets are sensitive to global news

Although tensions in the financial markets have receded, they remain high, and currencies continue to fluctuate within broad ranges subject to news from Europe and the U.S. In particular, a favorable bias was observed at the end of the week in the BRL, MXN and PEN. These movements could continue, while, the CLP and COP were subject to their exposure to copper (global cycle) and local positioning.

Chart 1
LatAm: Implied 1-month exchange-rate volatility



Source: BBVA Research

Highlights

- The central banks of Colombia and Peru maintain their reference rates
- Some upward surprises in inflation
- Economic activity and employment continue strong in August
- Fewer foreign-exchange interventions this week
- Initial September indicators do not show any deterioration in confidence
- Energy: more problems in Venezuela, relief in Argentina

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Economic Analysis

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Markets

Volatility remains high as markets await resolutions in the euro zone.

After hitting highs for the year in the second half of September, implied foreign-exchange volatility stabilized, but at higher levels: over 20% for the main Latin American economies, compared with minimums this year of close to 8%. The exchange-rate crosses in the region have been sensitive to global factors such as announcements on sovereign risk and contagion to the European financial system. Among the significant factors was an announcement at the start of last week on the capital requirements of a Franco-Belgian bank (Deixa), Moody's downgrade of Italy and weakness in the manufacturing sector in the euro zone. The result was losses of close to -3% in the BRL, CLP and COP, but more moderate in the case of the MXN (-1.4%) and PEN (-0.3%).

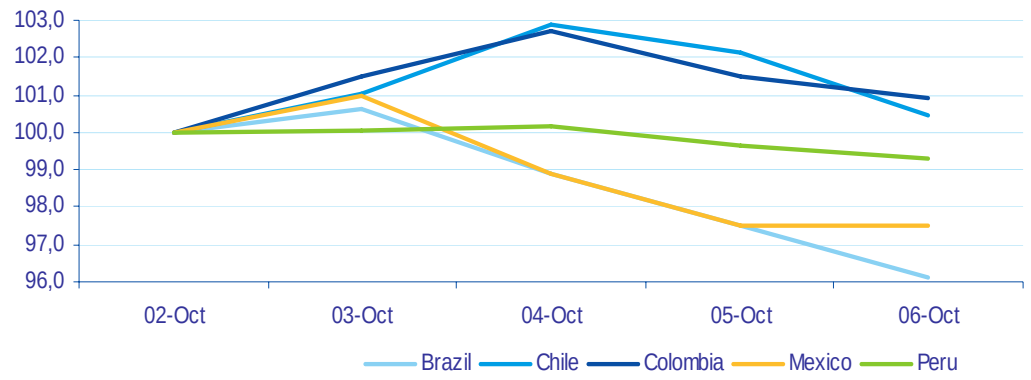
These currency movements in the region were reversed in reaction to a reduction in risk aversion associated to a number of news and policy reactions in Europe and the US by mid-week. The Latin American currencies reacted favorably to this scenario, with weekly appreciations in the BRL (+4.2%), the MXN (+2.6%) and PEN +0.8%); while there were slight losses in the COP (-0.9%) and CLP (-0.7%) as a result of movements in the copper price and positioning factors in local companies.

The difference between the currencies may be attributed to local factors, such as rumors of intervention in Brazil if the currency drops more steeply and statements by the Governor of the Bank of Mexico suggesting the MXN is undervalued. We expect the high currency volatility to persist, with fluctuations within a broad range, as long as there are no firm resolutions in Europe.

Latin American stock markets perform worse than developed economies; the markets will assess the corporate results in the U. S.

Global stock markets have been following European sovereign risk. Markets in developed countries performed slightly better than emerging markets and Latin America. The latter being affected by fears of contagion in the Asian continent, in particular China, and consequent worries over commodity prices. Over the coming weeks the markets are unlikely to change the focus of attention from sovereign risk to corporate results.

Chart 2
Latam: Weekly exchange rate performance (2-Oct=100)



Source: BBVA Research

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Economic Analysis

Highlights

The central banks of Colombia and Peru maintain their reference rates

The Central Bank of Peru kept its reference rate at 4.25%, and the Central Bank of Colombia at 4.50%. In both cases global uncertainty was a factor in their decision.

Some upward surprises in inflation

With the exception of Mexico and Venezuela, where inflation was lower than expected (0.25% m/m, 3.4% y/y; 1.6% m/m and 26.5% y/y respectively), there was a general, and sometimes surprising, increase in inflation. In Brazil, inflation was 0.53% m/m (7.3% y/y), countering expectations that it would begin to fall. In Chile the CPI was up 0.5% m/m (3.3% y/y), in line with our expectations. In Colombia, the CPI was up 0.3% m/m (3.7% y/y), more than expected. In Peru, inflation was 0.33%, 0.1 pp more than expected..

Economic activity and employment continue strong in August

In Chile, IMACEC for August rose 4.6% y/y. In Colombia the unemployment rate was 10.4% in August, a positive surprise for the analysts. In Mexico formal employment was up 4.0% y/y (0.28% m/m). In contrast, in Brazil industrial output fell by 0.2% m/m in August (1.8% up y/y), in line with expectations.

Fewer foreign-exchange interventions this week

The Central Bank of Brazil sold USD 3.4 billion through foreign-exchange swaps at the start of the week, while in Peru and Argentina the volume of foreign-currency sales fell in response to reduced pressure on the local currencies.

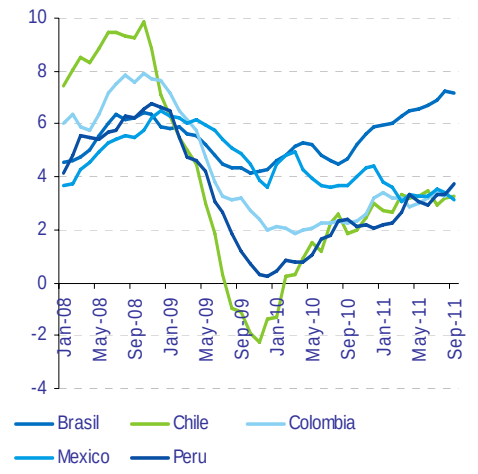
Initial September indicators do not show any deterioration in confidence

In Peru the index of business confidence increased by 2 points to 53 points in September, while the index of consumer confidence increased from 56 to 57 points. In Chile, new car sales accelerated to a growth of 12% y/y in September.

Energy: bigger problems in Venezuela, relief in Argentina

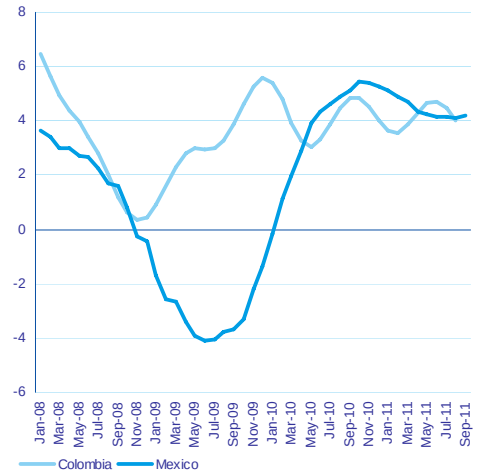
Unplanned electricity outages continue in Venezuela, with a negative impact on industrial production. In Argentina, final testing began in the nuclear power plant Atucha II. It is due to begin operating soon and supply power of 710 MW, equivalent to 2.5% of the total installed capacity in the power grid.

Chart 3
Inflation (Var.% y/y)



Source: BBVA Research

Chart 4
Employment rate growth, y/y %



Source: BBVA Research

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Calendar: indicators

Next Week: 10 - 14 October 2011

Argentina	Data	Period	Forecast	Consensus	Previous	Comment
Consumer Price Index	14-Oct	Sep 2011	0,9% m/m	0,8% m/m	0,8% m/m	
Wholsale Price Index	14-Oct	Sep 2011			0,9% m/m	
Cost Construction Index	14-Oct	Sep 2011			2,0% m/m	
Brazil	**Data**	**Period**	**Forecast**	**Consensus**	**Previous**	**Comment**
Retail Sales	11-Oct	Aug 2011		0.10% m/m	1.40% m/m	
Colombia	**Data**	**Period**	**Forecast**	**Consensus**	**Previous**	**Comment**
Imports	13-Oct	Aug 2011	38.0% y/y		32.8% y/y	We expect a moderation in the imports of durable consumption goods that it will be offset by purchases of capital goods.
Trade balance	13-Oct	Aug 2011	USD 193 millions		USD 545.7 millions	Despite the strength of domestic demand, the high international commodity prices could help to keep the trade surplus.
Building permits	14-Oct	Aug 2011	16.0% y/y		23.5% y/y	Growth of the building permits is moderated, but continue in highs in the year to date.
Mexico	**Data**	**Period**	**Forecast**	**Consensus**	**Previous**	**Comment**
Industrial Production	12-Oct	Aug 2011	0.1% m/m (3.7% y/y)	na	0.5% m/m (4.1% y/y)	Moderation in export manufacturing and automobile production point to low growth in the industry
Peru	**Data**	**Period**	**Forecast**	**Consensus**	**Previous**	**Comment**
Purchasing orders index	10-Oct	Sep 2011			50,0%	
Hiring index	10-Oct	Sep 2011			52,0%	

Source: BBVA Research

Calendar of events

Chile and Mexico: Monetary Policy Meeting (October 13 and 14, respectively)

Forecast: 5.25% (CL) and 4.5% (MX)	Consensus. 5.25% (CL) and 4.5% (MX)	Previous: 5.25% (CL) and 4.5% (MX)

We expect both countries to maintain their rates and give new signs with respect to future movements, particularly in terms of concern about exchange-rate fluctuations.

Calendar of holidays

Argentina and Chile: October 10.

Brazil and Venezuela: October 12.

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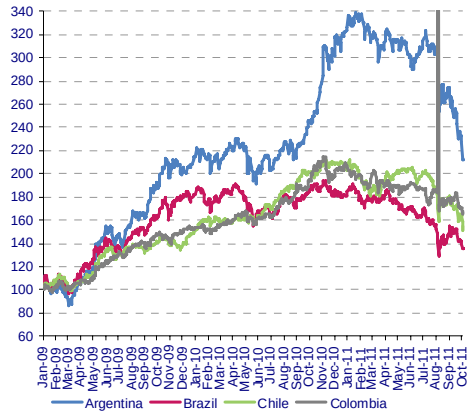
Market Data

			Close	Weekly change	Monthly change	Annual change
Interest rates (changes in bps)	US	3-month Libor rate	0.39	1	5	10
		2-yr yield	0.26	2	6	-8
		10-yr yield	1.99	8	-5	-40
	EMU	3-month Euribor rate	1.56	0	2	58
		2-yr yield	0.62	7	14	-16
		10-yr yield	1.94	6	4	-31
Exchange rates (changes in %)	Europe	Dollar-Euro	1.344	-0.1	-4.4	-3.4
		Pound-Euro	0.87	0.7	-1.8	-0.8
		Swiss Franc-Euro	1.24	1.7	2.3	-7.5
	America	Argentina (peso-dollar)	4.21	0.1	0.0	6.3
		Brazil (real-dollar)	1.78	-4.0	7.4	6.8
		Colombia (peso-dollar)	1948	1.2	8.8	9.1
		Chile (peso-dollar)	521	0.2	12.5	8.1
		Mexico (peso-dollar)	13.44	-2.7	7.7	7.9
		Peru (Nuevo sol-dollar)	2.75	-0.8	0.9	-1.4
	Asia	Japan (Yen-Dollar)	76.66	-0.6	-0.9	-6.4
		Korea (KRW-Dollar)	1180.00	-0.1	10.2	5.8
		Australia (AUD-Dollar)	0.981	0.9	-7.7	-0.4
Comm. (chg %)		Brent oil ($/b)	105.4	2.6	-9.0	25.5
		Gold ($/ounce)	1658.1	2.1	-8.8	23.1
		Base metals	537.5	0.3	-6.2	0.7
Stock markets (changes in %)	Euro	Ibex 35	8768	2.6	7.5	-18.2
		EuroStoxx 50	2258	3.6	5.0	-18.9
	América	USA (S&P 500)	1165	3.0	-2.8	0.0
		Argentina (Merval)	2361	-4.2	-17.9	-12.5
		Brazil (Bovespa)	52290	-0.1	-7.6	-26.2
		Colombia (IGBC)	12965	0.4	-4.3	-14.9
		Chile (IGPA)	18747	-0.3	-7.0	-14.8
		Mexico (CPI)	33280	-0.7	-5.4	-3.4
		Peru (General Lima)	17745	-3.2	-11.9	-5.9
		Venezuela (IBC)	99696	0.1	-0.1	50.4
	Asia	Nikkei225	8606	-1.1	-1.8	-10.3
		HSI	17708	0.7	-11.7	-22.8
Credit (changes in bps)	Ind.	Itraxx Main	189	-13	14	87
		Itraxx Xover	813	-26	95	344
	Sovereign risk	CDS Germany	97	-15	19	61
		CDS Portugal	1117	8	80	718
		CDS Spain	361	-21	-7	143
		CDS USA	51	-1	0	---
		CDS Emerging	348	-26	68	150
		CDS Argentina	1130	46	298	427
		CDS Brazil	188	-14	35	89
		CDS Colombia	190	-9	38	89
		CDS Chile	149	-5	48	84
		CDS Mexico	185	-12	34	82
		CDS Peru	191	-12	34	89

Source: Bloomberg and Datastream

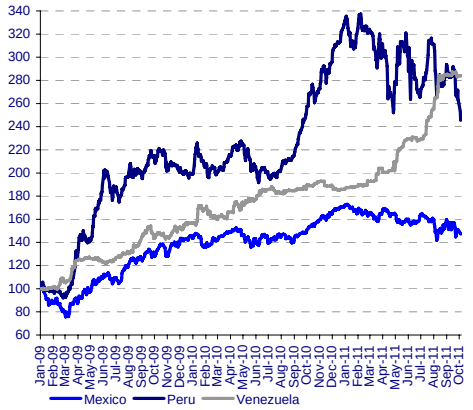
Charts

Chart 4
Stock markets (base index Jan09 = 100)



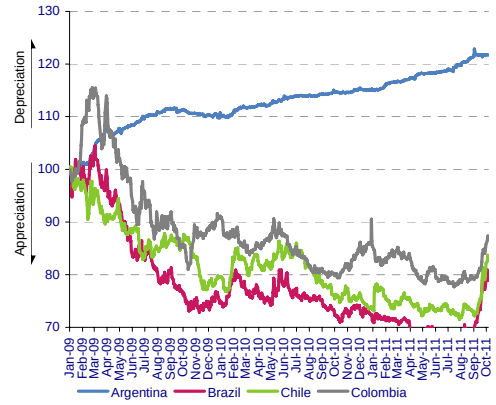
Source: Datastream and BBVA Research

Chart 5
Stock markets (base index Jan09 = 100)



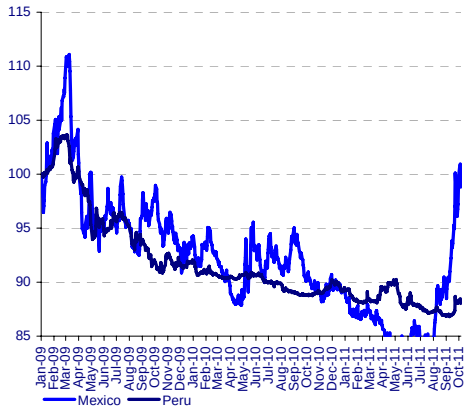
Source: Datastream and BBVA Research

Chart 6
Exchange rates (base index Jan09 = 100)



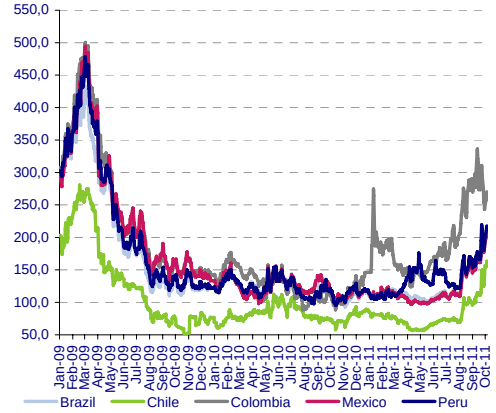
Source: Datastream and BBVA Research

Chart 7
Exchange rates (base index Jan09 = 100)



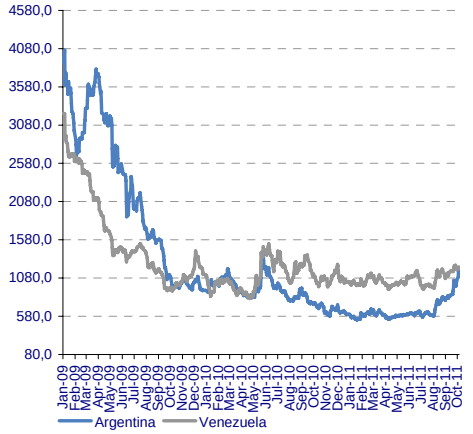
Source: Datastream and BBVA Research

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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