

Latin

Weekly Observatory

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Economic Analysis

South America

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Markets

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Rising demand pushes prices up

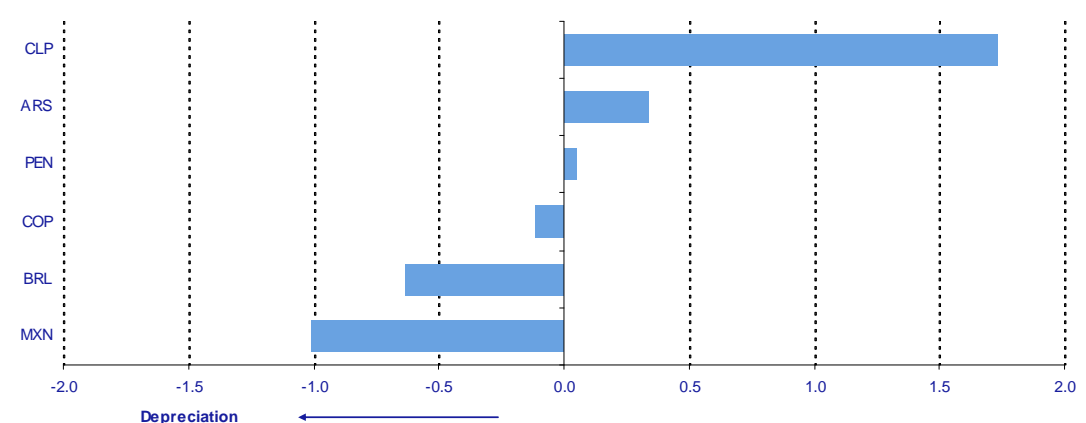
Economic activity remains strong in the region, boosted by buoyant domestic demand, with growth in Chile and a quarterly 0.5% expansion in the Brazilian GDP (6.8% y/y). Exports continue to grow as a result of high commodity prices, thus increasing inflationary pressure in Brazil, Colombia, Chile and Mexico. Employment grew in Peru and Mexico in line with growth, but remained weak in Venezuela. Meanwhile, although prices have risen, they are still being held in check. Central banks in Brazil and Peru therefore decided at their monetary policy meetings this week to maintain their reference rates at 10.75% and 3%, respectively.

Latin American markets close the week with slight falls, despite the greater appetite for risk in global markets

Except for the CLP, Latin American currencies ended the week down in response to the strength of the USD against the main currencies. The same was true of risk premiums and stock market indices, while the debt market is beginning to show signs of revival, mostly regarding international issues. If outflows of safe-haven assets were to continue, we could see positive movements in financial assets' prices in the region.

Chart 1

Variations in LatAm currencies (% , 7 days)



Source: Bloomberg and BBVA Research

Highlights

Economic activity exceeds expectations in Brazil, but underperforms in Chile

Employment growth at the start of the last quarter of the year

Commodity price rises boost exports

Pressure from domestic demand and some pressure from supply affect prices

Monetary policy decisions

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Economic Analysis

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Markets

General rise in USD with more favorable expectations for the U.S. cycle. If the appetite for risk continues, we expect positive moves in Latin American currencies.

Two elements determined currency movements in the region last week: 1) the approval of the Irish rescue package, which did not reduce global risk premiums, but contributed to lessen pressure on financial assets; and 2) expectations with respect to the U.S. cycle began to be revised upwards following the extension of the previous administration's tax cuts, as well as Bernanke's announcement of a possible additional injection of liquidity apart from that already planned in QE2.

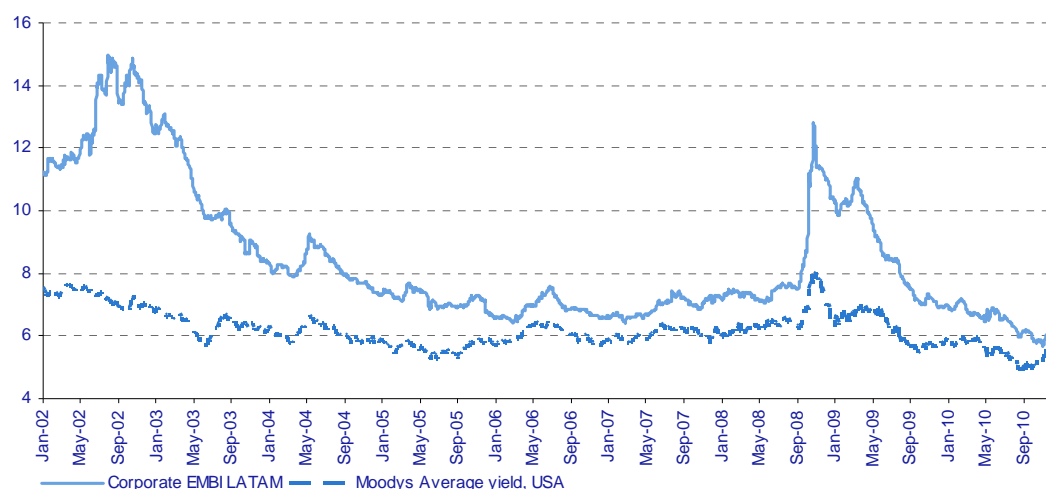
Although these elements resulted in a renewal in the appetite for risk in global markets, most of the currencies in the region closed with general losses (with the exception of the CLP, which appreciated by 1.7%, thanks to a rally in copper prices). These movements were a response to a strengthening of the USD against the main currencies (the DXY index was up 0.7% over the week). We consider that this trend could be reversed (particularly in the case of emerging economies) if safe-haven assets continue to flow out (10-year U.S. Treasury bond rates were up around 23 bps over the week). In addition, local elements are once more a factor of importance in some crosses (this week the market was responsive to monetary policy decisions in Brazil and Peru). This could act in favor of currencies in the short term (not counting the risk that authorities once more adopt an interventionist posture in foreign-exchange markets). In all, the risks continue latent, so in the short term we would expect a continuation of sideways movements within broad trading ranges.

Gradual return of Latin American issues to the international debt markets

There has been a gradual return of Latin American issues to the international debt markets, following the events surrounding the Brazilian Banco PanAmericano. The Brazilian state-owned utility Sabesp (BB/BB) made a 10-year issue of USD 350m with a coupon of 6.25%, a level considered adequate given its international rating. The telecommunications company Telmar (BBB-/Baa2/BBB-) also made a 7-year issue for EUR 750m at 5.12%. Finally, the Chilean utility E-CL (formerly Edelnor) announced its plans to issue USD 400m on the international market. This is despite the fact that corporate rates (YTM), as measured by the Corporate EMBI, have increased from 5.695% at the start of November to 6.146%.

Chart 2

Corporate EMBI LatAm (yield) vs. Moodys Average Yield



Source: BBVA Research

Highlights



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Economic Analysis

Highlights

Economic activity exceeds expectations in Brazil, but underperforms in Chile

In Chile, The Monthly Economic Activity Index for October was up 4.8% y/y, below market expectations, while the seasonally adjusted series was down 0.6% in the quarter. In contrast, the quarterly rise of 0.5% in Brazil in the third quarter was a positive surprise for the market (which expected 0.4%), although it is still limited compared with previous quarters due to the withdrawal of fiscal stimuli and the tougher monetary policy. We expect a recovery in the fourth quarter, with 2010 closing at an average growth rate of 7.5%.

Employment growth takes off at the beginning of the last quarter of the year

In line with economic growth, formal urban employment in Peru grew in September by an annual 5.2% rate, 0.1 pp up on the previous month. In Mexico, the sustained monthly increases of around 0.4% in recent months led to employment growth in November at rates similar to those in Peru. In contrast, employment is recovering less strongly in Venezuela, with a positive change of 2.4% y/y in September and an unemployment rate of 9%.

Commodity price rises boost exports

In October, Colombian exports were supported by an increase of 24.6% y/y in oil sales and a moderate rise in non-traditional products (9.5% y/y). The trade balance in Chile registered a surplus of USD 1,577m (USD 12,729m in 2010). Whereas imports are expected to continue their strong growth in Colombia, in Chile a future deceleration of domestic demand could slow down their pace of recovery.

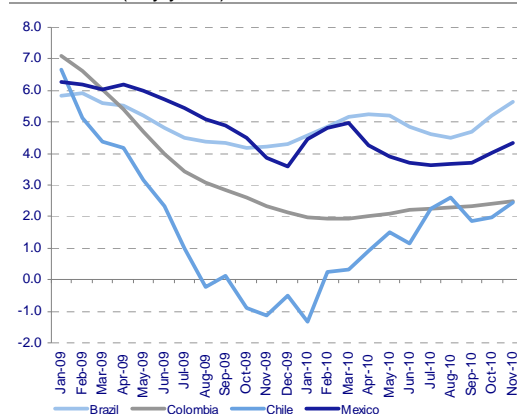
Pressure derived from domestic demand and some from supply affect prices

The region (except Chile) showed increasing inflationary pressure in November, exceeding market expectations. In Brazil, prices increased at a monthly rate of 0.83% (5.6% y/y), in line with expectations, while in Colombia the increase was 0.2% (2.6% y/y), explained mostly by the strong rains. In Mexico the monthly rise of 0.80% (4.3% y/y) consolidated the upturn in prices that began in October. Meanwhile, the inflation rate in Chile remained in check (0.1% m/m, 2.5% y/y), although the rise in the manufacturers' index (2.1% m/m, 10.4% y/y) suggests greater pressure in the coming months. In Venezuela, inflation appears to have stabilized, with a monthly increase of 1.5%, although it remains high (27.0% y/y).

Monetary policy decisions

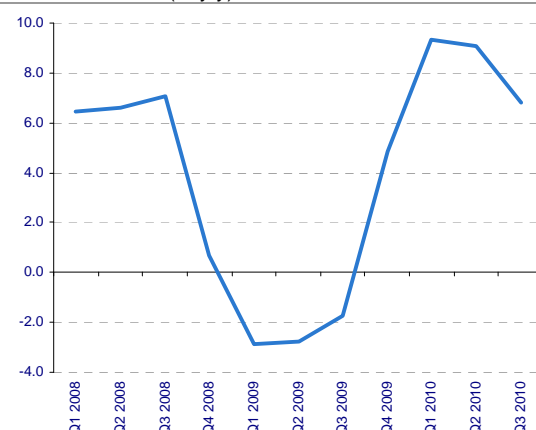
In Peru the governing board of the Central Reserve Bank maintained the reference rate at 3% due to the absence of inflationary pressures, while in Brazil the probability of an upward cycle of the SELIC has increased, although it was not changed in December. In Argentina, this month the Central Bank found it more difficult to sterilize monetary excess through the issue of bills and notes.

Chart 3
Inflation (% y/y; SA)



Source: BBVA Research

Chart 4
Brazil: GDP (% y/y)



Source: BBVA Research

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Calendar: Indicators

Next Week: 13-17 December 2010

Argentina	Data	Period	Forecast	Consensus	Previous	Comment
Consumer Price Index	15-Dec	Nov 2010	0,7% m/m	0,8% m/m	0,8% m/m	Slight seasonal slowdown.
Construction Price Index	15-Dec	Oct 2010			16,0% y/y	
System of wholesale price index	15-Dec	Nov 2010			15,1% y/y	
Industrial Monthly Estimate	17-Dec	Nov 2010	8,0% y/y	8,5% y/y	8,4% y/y	Verify slight slowdown.
Brazil	Data	Period	Forecast	Consensus	Previous	Comment
Retail Sales	14-Dec	Oct 2010			0.4%	
COPOM Monetary Policy Meeting Minutes	16-Dec	Dec 2010				The Central Bank is expected to signal the future path of the SELIC. Markets are currently betting on a new monetary tightening while government officials comment on interest rates cuts.
Unemployment rate	17-Dec	Nov 2010			6.1%	The unemployment rate should come under the 6% rate for the first time since the beginning of the series.
Formal job creation	13-17 dic 2010	Nov 2010			204804	
Colombia	Data	Period	Forecast	Consensus	Previous	Comment
Trade balance	13-Dec	Oct 2010	USD 20 millions		USD -491.8 millions	Increased commodity prices and slight rise in nontraditional exports will stop the deterioration in the trade balance.
Industrial production	17-Dec	Oct 2010	1.8% y/y	3.1% y/y	2.8% y/y	A strong heterogeneity due to the recovery industry.
Retail sales	17-Dec	Oct 2010	15.3% y/y	15.3% y/y	18.6% y/y	Low interest rates and peso appreciation explain strong domestic demand.
Mexico	Data	Period	Forecast	Consensus	Previous	Comment
Industrial Production	13-Dec	Oct 2010	0.42 m/m (5.1 y/y)	5.5 y/y	-0.12 m/m (6.3 y/y)	Recovery in the industry influenced by good data in the U.S., affecting manufacturing and gradual improvement in the construction sector.
Peru	Data	Period	Forecast	Consensus	Previous	Comment
GDP	15-Dec	Oct 2010	9.4% y/y	9.7% y/y	10.4% y/y	In October, GDP keep growing at high rates due to the positive performance of the primary sectors. However, it would moderate with respect to previous month due to a weaker Construction sector.
Venezuela	Data	Period	Forecast	Consensus	Previous	Comment
Banking Lending	17-Dec	Nov 2010	4.0% m/m; 14.9% y/y		6.0% m/m; 13.7% y/y	Credit grows due to a seasonal impulses of consumption.
Banking Deposits	17-Dec	Nov 2010	4.1% m/m; 16.2% y/y		0.5% m/m; 14.4% y/y	Bonus payments (public and private) boost the deposits in the banking system.

Source: BBVA Research

Calendar: Events

Chile and Colombia: Monetary Policy Meeting (December 16 and 17, respectively)

Forecast: Chile, 3.25%; Colombia, 3.0%

Previous: Chile, 3.0; Colombia, 3.0%

In Chile, the last GDP and inflation figures have increased the probability of a pause in the normalization of the monetary stimulus. However, considering the monetary policy horizon, we maintain our forecast of an increase of 25 bps at the December meeting. In Colombia, with inflation in the lower part of the target range the interest rate can remain unchanged.

Calendar: holidays

No holidays in the region.

Markets



Highlights



Market Data



Charts



Market data

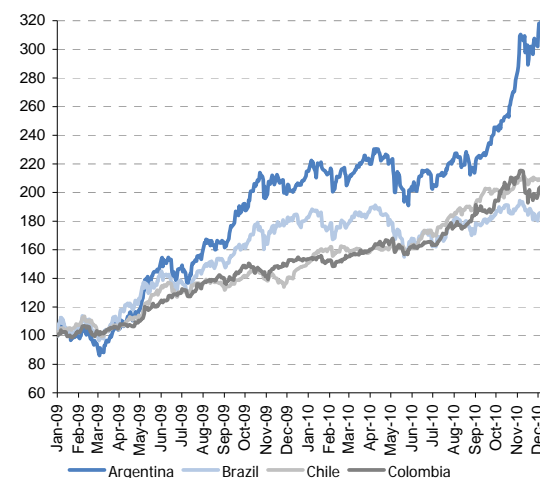
			Close	Weekly change	Monthly change	Annual change
Interest rates (changes in bps)	US	3-month Libor rate	0.30	0	2	5
		2-yr yield	0.61	14	19	-19
		10-yr yield	3.27	27	63	-28
	EMU	3-month Euribor rate	1.03	0	-2	31
		2-yr yield	1.06	20	11	-21
		10-yr yield	2.96	11	53	-25
Exchange rates (changes in %)	Europe	Dollar-Euro	1.321	-1.2	-3.2	-9.7
		Pound-Euro	0.84	-1.5	-1.3	-7.1
		Swiss Franc-Euro	1.30	-0.5	-2.6	-14.1
	America	Argentina (peso-dollar)	3.98	0.0	0.4	4.6
		Brazil (real-dollar)	1.71	1.5	-0.3	-2.7
		Colombia (peso-dollar)	1918	1.9	3.2	-3.9
		Chile (peso-dollar)	475	-1.1	-1.2	-4.5
		Mexico (peso-dollar)	12.48	0.9	1.6	-2.7
		Peru (Nuevo sol-dollar)	2.83	0.2	1.0	-1.8
	Asia	Japan (Yen-Dollar)	83.91	1.4	1.7	-6.0
		Korea (KRW-Dollar)	1141.90	0.9	2.7	-2.0
		Australia (AUD-Dollar)	0.986	-0.2	-1.1	8.1
Comm. (changes in %)		Brent oil (\$/b)	91.2	-0.2	2.7	26.9
		Gold (\$/ounce)	1378.0	-2.6	-2.2	23.5
		Base metals	572.5	0.9	0.7	20.2
Stock markets (changes in %)	Euro.	Ibex 35	10107	0.9	-0.4	-13.0
		EuroStoxx 50	2840	2.1	0.3	-0.8
	America	USA (S&P 500)	1236	0.9	1.8	11.7
		Argentina (Merval)	3384	-1.1	1.3	55.4
		Brazil (Bovespa)	68101	-2.4	-4.3	-1.7
		Colombia (IGBC)	15399	0.1	-0.4	33.5
		Chile (IGPA)	23069	0.3	-0.5	43.8
		Mexico (CPI)	37588	0.5	3.5	17.8
		Peru (General Lima)	21825	0.8	6.0	53.9
		Venezuela (IBC)	65460	0.4	-3.3	21.5
	Asia	Nikkei225	10212	0.3	3.6	1.0
		HSI	23163	-0.7	-6.2	5.8
Credit (changes in bps)	Ind.	Itraxx Main	106	-1	1	25
		Itraxx Xover	452	-15	-10	-35
	Sovereign risk	CDS Germany	52	6	13	29
		CDS Portugal	449	26	-30	377
		CDS Spain	325	31	47	232
		CDS USA	41	2	-1	---
		CDS Emerging	214	4	10	-69
		CDS Argentina	638	-10	4	-412
		CDS Brazil	110	5	8	-15
		CDS Colombia	111	4	9	-38
		CDS Chile	77	2	-6	1
		CDS Mexico	110	1	1	-32
		CDS Peru	114	3	-1	-13

Source: Bloomberg and Datastream

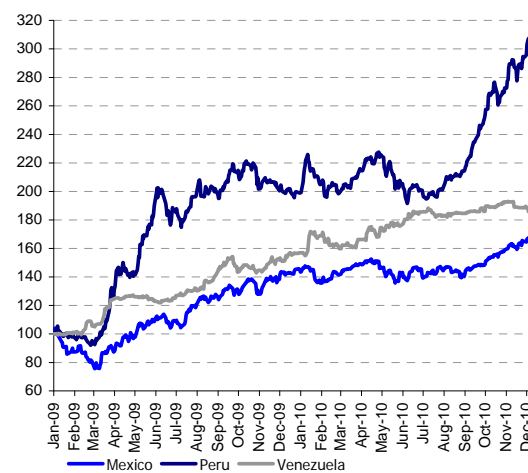
Charts

Charts 5 & 6

Stock exchanges (base index Jan09=100)



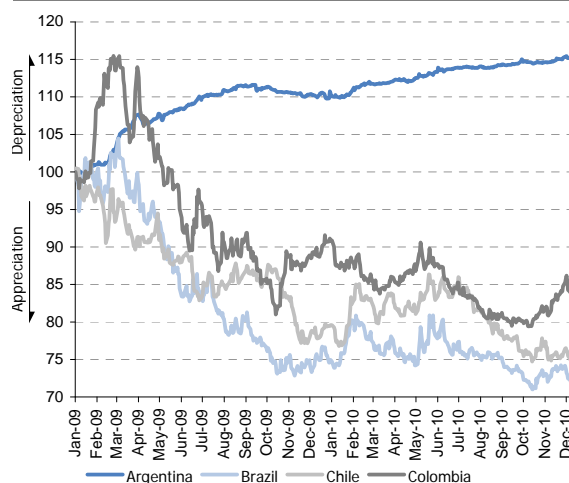
Source: Bloomberg



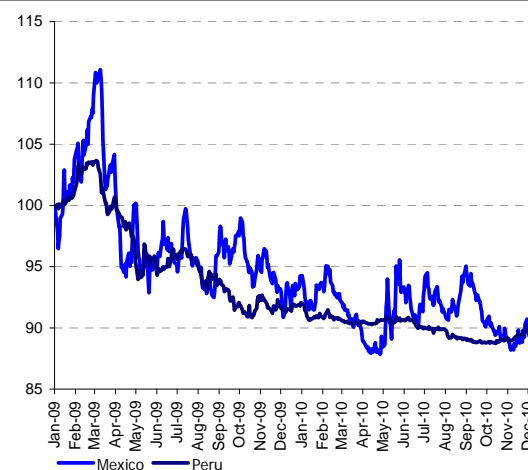
Source: Bloomberg

Charts 7 & 8

Exchange rates (base index Jan09=100)



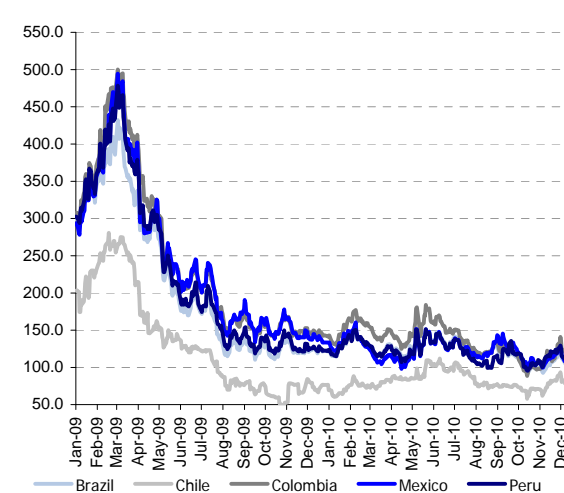
Source: Bloomberg



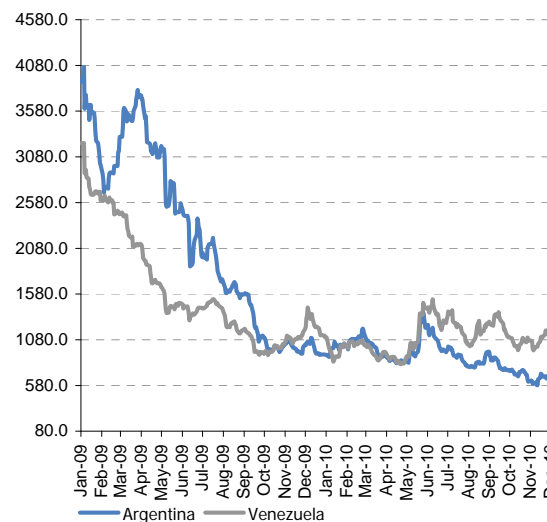
Source: Bloomberg

Charts 9 & 10

Credit Default Swaps (levels)



Source: Bloomberg



Source: Bloomberg

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