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Subscribers may pose questions to the Board of Advisors for the Featured Q&A by contacting the Editor at rsimpson@thedialogue.org

Featured Q&A With Our Board of Advisors

Q Foreign investors are becoming increasingly frustrated with Argentina's apparent inflexibility in debt restructuring talks with creditors. What is Argentina's strategy in the restructuring talks? Can President Nestor Kirchner reach a compromise that both satisfies creditors and preserves his political standing in Argentina?

A **Guest Comment: Claudio Loser:** "It has been 27 months since Argentina stopped servicing its public debt owed to private creditors. While creditors complained, Argentina in practice obtained a grace period on these obligations, in support of its efforts to come out of the worst crisis of the country's recent history. Multilateral creditors continued to provide financing, and governments were sympathetic to Argentina. There was also an understanding that Argentina could not fulfill its obligations without a substantial debt 'haircut.' Today Argentina stands at a crossroads regarding its debt strategy. The economy has had a strong recovery (Argentina had the fastest rate of GDP growth in the region in 2003). At the same time, it has submitted a debt reduction proposal that could have been considered a good first offer. However, the government is insisting it is the only acceptable solution: a reduction of 90 percent in the effective value of debt, which is seen by creditors and an increasing number of foreign governments as vir-

tually confiscatory. The position is very popular internally, but can have dear consequences in the medium term, as foreign and local investors shun Argentina in light of this perceived intransigence and official loans are not renewed. Thus, President Kirchner would be well advised to have a more flexible position with regard to creditors if he wants to achieve sustained economic growth for Argentina."

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PHOTO OF THE DAY



**Brazilian Finance Minister
Antonio Palocci**

Source: Agencia Brasil.

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NEWS BRIEFS

**Colombia Just Misses
2003 Fiscal Deficit Target**

The Colombian government on Tuesday reported a consolidated fiscal deficit in 2003 equal to 2.9 percent of gross domestic product, narrowly missing a 2.8 percent target agreed to with the International Monetary Fund. The government aims to cut its fiscal deficit to 2.5 percent of GDP this year.

**Illegal Border Crossings Rise
After Bush Immigration Proposal**

The head of the union representing US Border Patrol agents estimates that illegal immigrant crossings have increased by 10-11 percent since President George W. Bush announced his immigration reform proposal last month. Union President T.R. Bonner attributed the increase to immigrants' belief they would receive amnesty as a result of the proposed reform. Bush has said he opposes amnesty for illegal immigrants.

**Rio de Janeiro State Governor
Raises Tax on Pipelines**

The governor of Brazil's Rio de Janeiro state, Rosina Matheus, has approved a law that could double taxes on pipeline operations. The tax increase is part of a campaign by Matheus to block construction of a pipeline that could prevent the state from hosting a new refinery and creating some 30,000 permanent jobs.

Telmex Q4 Profit Up 1.7 Percent

Telefonos de Mexico reported a net profit of 5.585 billion pesos (\$US 504 million) for the fourth quarter of 2003, up 1.7 percent from the same period of 2002. Revenues sank 1.23 percent to 30.183 trillion pesos.

Source: Reuters.

Political News

**Peruvian PM Offers Cabinet
Reshuffle for Opposition Support**

Peruvian Prime Minister Carlos Ferrero on Tuesday proposed a reshuffle of the cabinet in exchange for opposition support for President Alejandro Toledo's government amid allegations of corruption involving a former close advisor to the president, Reuters reported. "If we reached a basic deal with political groups on how to go forward together in the next two

“Ferrero admitted Tuesday 'the government has not acted with the firmness it should have in the face of isolated corruption cases'”

years ... if we could have a road map emerging from consultations which the president is conducting with the main political groups, and if we conclude that the climate is right to deal with the problem together, in that case [a cabinet reshuffle] should happen in February," Ferrero told reporters. Opposition politicians are demanding Toledo create a multi-party government, or include independent technocrats, following the release on Saturday of an audiotape of a December 2001 meeting in which the ex-advisor, Cesar Almeyda, is heard discussing pressuring and bribing judges with a principal operative in a corruption network led by jailed former spymaster Vlademiro Montesinos. Toledo has denied knowledge of the meeting, which he called an isolated incident, and has vowed to fight corruption in his government. Nevertheless, his popularity has sunk to a meager 7.3 percent in the wake of the scandal. Ferrero admitted Tuesday "the government has not acted with the firmness it should have in the face of isolated corruption cases" and said "there are probably people we should be watching carefully." Last Friday, Vice President Raul Diez Canseco resigned amid charges he authorized favorable tax status for a business belonging to the father of his girlfriend.

Economic News

**Venezuelan Government Orders
Banks to Increase Farm Lending**

Venezuela's finance and agriculture ministries on Tuesday raised commercial banks' compulsory minimum credit level for agriculture to 16 percent of their loan portfolios from 12 percent, as part of President Hugo Chavez's campaign to increase farm financing, Reuters reported. The hike, which applies to 34 commercial banks—including two state-owned banks

—will be implemented gradually, reaching the new 16 percent minimum by the end of July and remaining in effect through the end of the year. Non-compliant banks would face fines and other sanctions. Last month, Chavez demanded that the Central Bank release \$1 billion of its \$22 billion in international reserves to help finance a planned \$2.4 billion agriculture program this year. The Bank's directors have resisted and instead negotiated a compromise by cutting reserve requirements for banks that lend to farmers, freeing up \$325 million in funds. The Bank also aims to offer \$875 million through other commercial financing. Analysts say the demand for credit from Venezuela's farmers remains low, and recommend efforts be aimed at technical assistance and land owning rights. [Editor's note: look for related Q&A on this topic in next Monday's issue of the *Latin America Advisor*.]

**US Official Expects Argentina to
Make March IMF Payment**

US Treasury Undersecretary for International Affairs John Taylor said Tuesday he expects Argentina to make a \$3 billion loan payment due March 9 to the International Monetary Fund (IMF), Reuters reported. In response to a question

about what the US would do if Argentina failed to make the payment, Taylor said, "I'm assuming that Argentina will pay the amount due so that's a hypothetical question." Argentine President Nestor Kirchner has said his government would not make the payment if the IMF's executive board does not approve a second review of the country's \$13.3 billion loan program in March. Approval of the review would free up cash needed to make the payment. However, the IMF has grown increasingly critical of Argentina's ability to comply with the conditions of the loan agreement, which require that the government negotiate in good faith a debt restructuring agreement with holders of some \$88 billion in defaulted sovereign debt. In a rare show of displeasure with Argentina's slow progress on debt talks, eight members—mostly from European countries—of the International Monetary Fund's executive board abstained last week from a vote approving a first review of the IMF's loan to Argentina.

Brazilian Minister Predicts Further Interest Rate Cuts in 2004

Brazilian Minister of Finance Antonio Palocci on Tuesday predicted the Central Bank would continue to lower its benchmark Selic interest rate in 2004 despite the Bank's decision last month to hold rates steady, Reuters reported. "The Copom (the Central Bank's monetary policy committee) temporarily suspended the process of rate cuts, it did not change the perspective of a downward trend," Palocci told reporters. According to the minutes of the last month's Copom meeting, which were released last week, the Bank held the rate at 16.5 percent because of its concern about a possible accelerating inflationary trend. Before last month, the Bank had cut the Selic 10 percentage points over a period of seven months. Palocci also on Tuesday dismissed concerns about financial markets' recent jitters, asserting there was no economic crisis on the horizon.

Peru to List Shares of State-Owned Companies

Peruvian Economy Minister Jaime

The Dialogue Continues

A continuation of the February 2, 2004 Q&A

Q Recent months have seen currencies strengthen in several Latin American countries, including Brazil, Mexico, Argentina, Chile, and Colombia. Should these countries be concerned that their currencies are too strong and pose a risk to exports? To what extent should authorities in these countries intervene to control their currencies' rise?

A **Guest Comment: Graciana del Castillo:** "I am certainly not in favor of intervention. However, I disagree that a depreciation of the Mexican peso will help the economy gain competitiveness. Only structural reform would do

that (particularly in the energy, pension and labor sectors). In fact, the depreciation of the peso during past years has resulted in an increased foreign debt burden, despite efforts in the budget at zero net foreign borrowing. Foreign debt, as a percentage of GDP, has been growing since 2001. The data on Mexican debt shows an increase from 12.2 percent in 2001 to 13.5 percent in September 2003. Further devaluation will make things worse. Given that domestic debt has increased by about 35 percent since 2000, it would be worrisome."

Graciana del Castillo is Managing Director of the Macroeconomic Advisory Group.

Quijandria said Monday the state will post 10 percent of the shares of its firms on the Lima Stock Exchange to encourage their operations' transparency, Reuters reported. President Alejandro Toledo's government has been encouraging private investment, which slowed last year after the privatization of some state-owned companies were canceled in the face of deadly local protests. "The idea is to list on the Exchange a small portion of all shares in state firms, a very minor percentage of some 10 percent ... with the purpose of giving them more transparency," Quijandria explained, emphasizing that the move would not result in more privatizations. "The government has no intention whatsoever of creating a sort of backdoor privatization strategy. That's not the idea," Quijandria told local radio. Peru has reported only \$13.5 million in privatization-generated revenues for 2003, having cut in August its yearly target to \$174.9 million from \$400 million. Fifteen state-run firms are already on the Lima Stock Exchange and give quarterly financial reports to stock market regulator Conasev.

Peru will list oil refiner **Petroleos de Peru, Egasa,** and **Egesur**—the two electricity groups whose attempted privatization last year provoked protests in Arequipa—six of the 16 maritime ports, and other assets.

Company News

America Movil Estimates 11 Percent Subscriber Growth in 2004

Regional mobile phone giant **America Movil** said Tuesday it projects 11 percent subscriber growth in Mexico this year and plans to invest up to \$600 million in network upgrades in the country, Reuters reported. "We are budgeting 2.5 million [new] subscribers [this year in Mexico] and I hope to have a little bit more than that," Chief Executive Daniel Hajj Aboumrad stated. The projected growth in subscribers in Mexico would follow a 17 percent expansion in the country during 2003 to 23.44 million customers, who account for more than half of America Movil's total regional subscriber base. The

Featured Q&A*Continued from page 1*

A **Guest Comment: Federico Thomsen:** "Argentina's strategy in the restructuring talks is the same as the one it is applying to the revision of utility rates, which have been frozen since the 2002 peso devaluation: delay as much as possible any decision that could have a negative impact on President Kirchner's popularity. While in the case of utilities the risk of bottlenecks in the energy sector sets a limit to this strategy, the government

“President Kirchner has been pursuing an aggressive approach to 'negotiations' with the outside world that's kind of a good-cop/bad-cop routine, but without the good cop.”

— *Michael Gavin*

does not perceive any such limitation in the case of its debt in default. The improvement in sovereign creditworthiness that would follow a successful Argentine restructuring is not much of an incentive for an administration that is enjoying having money for social programs amid strong economic growth (real GDP up by 8 percent in 2003 and probably by over 6 percent this year). The glitch in this strategy is that the IMF, under pressure from some its members, including a growing number of G7 countries, is increasingly unwilling to continue its standby program with Argentina unless there is at least a semblance of a 'good will' negotiation between the country and its creditors.

company plans to grow existing businesses this year, after the \$1.65 billion spent on acquisitions last year made America Movil the world's sixth-biggest mobile company. America Movil said Monday the addition of 4.2 million new subscribers through acquisitions had

Soon Kirchner will need to show more flexibility in the talks with bondholders. This may involve more changes in packaging than in content; although a higher primary surplus is possible for 2005-06, a sovereign debt restructuring that is feasible politically and sustainable financially will still produce a huge haircut for private investors."

A **Board Comment: Michael Gavin:** "President Kirchner has been pursuing an aggressive approach to 'negotiations' with the outside world that's kind of a good-cop/bad-cop routine, but without the good cop. So far he's won big, most notably when his brinkmanship in the IMF yielded him 'victory' in the form of a very undemanding IMF program. This aggressive behavior will continue until it stops working for him politically, and that is likely to be some time coming. When (or if) the US and Spain become a little less accommodative, and the Argentine public starts to get used to the idea that they have something to lose in remaining an international financial outcast, then the Kirchner government may take a different approach to their negotiations with bondholders. But don't hold your breath."

Claudio Loser is a Senior Fellow at the *Inter-American Dialogue* and former *Head of the International Monetary Fund's Western Hemisphere Department*.

Federico Thomsen is *Head of E.F. Thomsen economic consultancy*.

Michael Gavin is a member of the *Advisor board* and *Head of Latin America Economic Research* at UBS.

doubled its fourth-quarter net profit and boosted revenue by 56 percent. Hajj also predicted America Movil would invest between \$300 and \$350 million in Brazil—the company's number two market—in 2004, and would upgrade its network to GSM technology.

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