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Latin America Advisor

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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*

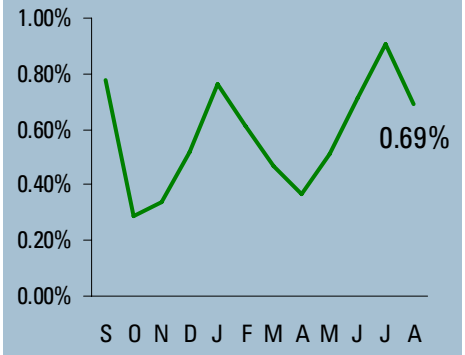
Q In his September 1 state-of-the-nation address, Mexican President Vicente Fox said he would continue to engage in dialogue with the opposition to achieve a consensus on political and economic reforms during the final two years of his six-year term. Are the prospects for reforms any better now than they were four years ago? How will Fox spend these next two years?

A Board Comment: James R. Jones: "Unfortunately, President Fox squandered his many advantages right from the start of his administration by not focusing on only two or three major reforms and keeping a laser beam of attention on those few issues until he succeeded in gaining congressional approval. His scattershot approach to issue reforms weakened his presidency and it's difficult to imagine a way in which he can gain political dominance again in the remaining two years. However, he could still be successful in passing many needed reforms if he exercises his leadership behind the scenes and gives the credit for success to others. My reading of the Mexican political polls is that the vast majority of Mexicans are highly dissatisfied with all three major political parties. In order to win the next presidential and congressional elections, the parties must demonstrate that they can respond to the wants and needs of the electorate. So that gives Fox a great opportunity to coordinate a self-effacing effort that lets all three party leaders become the heroes. The other thing he must do is energize Mexico's business leadership to get out front and use its muscle on all three parties' leadership to pass a meaningful reform program prior to the 2006 election campaigning. The year 2005 could be a very important year to get these things accomplished. It can be done. Although Fox cannot be the public face of those reforms, the presidency in Mexico is still the most important institution to make things happen. Fox must have learned many lessons of political leadership in the past four years. If he applies those lessons to the next two years, he may not

Continued on page 4

CHART OF THE DAY

Brazil IPCA Monthly Inflation
Sept 2003-Aug 2004



See related story on page 2.

Source: IBGE.

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NEWS BRIEFS

Bush Orders End to Support for Loans to Venezuela

US President George W. Bush on Friday ordered a withdrawal of US support for $250 million in loans for Venezuela from international organizations, citing the South American country's alleged role in the international trafficking or women and children for sexual exploitation. Venezuelan Information Minister Andres Izarra said the suspension of US support for the loans would damage already fragile relations between the two countries.

Source: Associated Press.

Mexican Central Bank Leaves Monetary Policy Unchanged

Mexico's central bank left the amount of money commercial banks must borrow at higher rates unchanged at 45 million pesos ($US 3.9 million) daily despite a higher-than-expected rise in consumer prices in August. August inflation was measured at 0.67 percent, raising the year's inflation growth to 4.82 percent. The bank expects the economy to grow as much as 4.25 percent this year, after a 3.9 percent year-on-year expansion in the second quarter, the fastest pace since 2000.

Source: Bloomberg News, Reuters.

Southern Peru Workers Return to Job, at Least For Now

Some 1,500 striking workers at **Southern Peru Copper Corp.** were expected to return to work today, but have threatened to renew the strike in 30 days if the company does not meet their wage and benefit demands. The workers suspended their 12 day-old strike, which they say has cost Southern Peru $1 million per day.

Source: Reuters.

Economic News

Hurricane Ivan Batters Caribbean, Heads for Cuba

Hurricane Ivan, one of the most powerful storms to ever hit the Caribbean, is expected to pass near or over Cuba's western end after hammering Jamaica and the Cayman Islands over the weekend. Some 1.3 million people in Cuba were evacuated from their homes, according to the Associated Press, as the Category 5 hurricane, whose winds have reached as high as 165 miles per hour, headed toward the island. The US National Hurricane Center said Ivan is the sixth-strongest hurricane recorded in the Atlantic basin, and is nearly as strong as Hurricane Mitch, which killed 10,000 people in Central America in 1998, Reuters reported. "It's definitely one of the most powerful hurricanes to have occurred in the Atlantic Ocean," said hurricane center meteorologist Gene Hafele. Ivan has killed at least 65 people throughout the Caribbean, including 39 in Grenada and 15 in Jamaica, and has destroyed or damaged several thousand homes, according to the Associated Press. Police killed two people in Jamaica amid looting and gunfights that erupted after the hurricane passed. Some 28 people were arrested. Ivan is projected to move into the Gulf of Mexico on Tuesday, and could strike the US anywhere between the Florida panhandle and Louisiana, hurricane center officials said.

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Deadlocked EU-Mercosur Trade Talks to Resume Today in Brussels

Talks between trade negotiators from Mercosur and the European Union are set to resume today in Brussels, Belgium as the deadline for an agreement nears and the two sides remain deadlocked on key issues. After meeting with Brazilian Foreign Minister Celso Amorim yesterday, EU Trade Commissioner Pascal Lamy said the 25-country EU and Mercosur, which groups Brazil, Argentina, Uruguay, and Paraguay, would still try to meet an October 31 deadline for a free trade pact despite an impasse on trade in agricultural and industrial goods, according to Reuters. "The spirit is to try to meet the deadline we had in mind," EU Trade Commissioner Pascal Lamy was quoted as saying. "A lot of work needs to be done, but it is worth putting our people to work again." Both sides are expected to submit final offers on September 20. Mercosur wants the EU to improve market access for Mercosur farm goods, while the EU says it has not yet seen satisfactory offers in such areas as industrial goods, services, and government contracts. Last week, Brazil scored an important victory when a World Trade Organization panel ruled that EU sugar subsidies were illegal. The EU and Mercosur have been in talks for four years in an effort to increase the $40 billion in current trade between them. An agreement linking the regions' combined 680 million people would create one of the world's largest free trade areas.

Brazil's Inflation Slows in August, But Still Higher Than Expected

Brazil's monthly inflation rate slowed in August from July, but still posted a higher-than-expected increase, feeding growing speculation the Central Bank will raise interest rates this month. The IPCA consumer price index, which helps guide the Central Bank's monetary policy decisions, rose 0.69 percent in August, the biggest August increase in three years, although it marked a slowdown from a 0.91 percent jump in July. **UBS** analyst Victoria Wernick said in a research note this morning she expected the Bank's monetary policy committee (Copom) to raise its benchmark Selic interest rate a quarter point to

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16.25 percent this month in response to accelerating inflation. "... We are not expecting shock treatment because it is not an emergency and, therefore, the disinflation process required is much smoother than in previous occasions in Brazil's history," Wernick wrote. Inflation is projected to rise about 7.5 percent this year, more than the 5.5 percent target set by the Bank. The lowest interest rates in three years have boosted demand for cars and appliances, and put pressure on automotive manufacturers to raise prices as a result of rising costs and unions' increased demands for higher wages. Unemployment fell to a seven-month low in July as companies raised production in order to meet capacity. Cumulative growth in Brazil's industrial sector for the first seven months of 2004 was 7.8 percent and compared to the same period in 2003 growth was 9.6 percent.

Company News

Bankrupt US Airways Group Names Embraer as No. 1 Unsecured Creditor

US Airways Group, which filed for bankruptcy protection on Sunday, named Brazilian jetmaker **Embraer** as one of its largest unsecured creditors, Reuters reported. The Arlington, VA-based US Airways said it owes Embraer $1.47 billion for future aircraft commitments after having placed an order for 170 regional aircraft from Embraer and Canada's **Bombardier** last year. US Airways, the second-largest US airline, filed for bankruptcy protection for the second time in two years after it was unable to persuade unionized pilots, flight attendants, mechanics and others to make $800 million in labor concessions. The bankruptcy filing also came amid tough competition with low-cost rivals and skyrocketing fuel prices. Embraer, the world's fourth-largest manufacturer of civilian aircraft, posted second-quarter net sales of $924.3 million and net income of $80.2 million. Embraer is part of a consortium led by the US' **Lockheed Martin** that last month was awarded a US spy plane contract potentially worth $8 billion [Editor's note: see related Q&A in the August 11, 2003 issue of the *Latin America Advisor*.]

Occidental Ready to Battle Ecuadorean Government in Court

US oil firm **Occidental Petroleum Corp.** said Sunday it would fight the Ecuadorean government in court over accusations the company breached a contract with state oil company **Petroecuador**, Reuters reported. In a statement, Occidental said it would turn to international law and treaties to energetically defend its rights in any court or forum. Last month, Ecuador's attorney general accused Occidental of breaching its contract with Petroecuador, primarily by failing to ask permission in 2000 before Canadian oil firm **EnCana** took a minority, non-operating stake in a parcel of land known as Block 15. The accusations against Occidental, which has said it complied with all of its obligations, have fueled speculation that the government is retaliating in response to Occidental's claims for a tax refund. In July, an international arbitration panel awarded Occidental a $75 million tax rebate on value-added taxes (VAT) it has paid since 2001, when the government declared VAT payments no longer qualified for reimbursement. The government, which is seeking to overturn the panel's ruling, denies that the two issues are related. Ecuadorean President Lucio Gutierrez has designated the energy ministry to judge the breach of contract case.

Subscriber Notice

Series of Economic Conferences:
"The Latin American Economy: Where Does it Stand? Where is it Headed?"

Session One: Macroeconomic Outlook for Latin America

Speakers:

Michael Gavin
Head of Latin America Research, UBS

David Malpass
Chief Economist, Bear Stearns

Thursday, September 16, 2004
8:30-10:00 a.m.
Inter-American Dialogue
1211 Connecticut Avenue, NW Suite 510
Washington, D.C.

RSVP to: rtrumble@thedialogue.org.

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Featured Q&A

Continued from page 1

get credit currently, but history will certainly redeem him."

Guest Comment: Andres Rozental: "It is highly improbable that President Fox will make any major headway in getting the opposition parties to agree to any of his political or economic reforms in the scant two years before the end of this administration. A clear sign of this is the reaction by the PRI and PRD to the 2005 budget proposal delivered by Fox to Congress last week. Although it contains only general proposals on changes to the value added tax regime—without any specific percentage proposals—there has already been a clear public indication that the opposition will fight against anything that doesn't strictly adhere to the consensus conclusions of the National Treasury Convention that met over the last year. As far as political reforms go, the proposal made by Fox to allow municipal mayors to be re-elected (which would be the first change to the blanket prohibition for elected local, state and federal officials to seek an immediate additional term) has also been negatively received by the PRI congressional leadership. Fox seems unable to garner any support for his by now quite modest reform agenda, mainly because of the constant confrontations between him and his cabinet on the one hand, and the opposition parties on the other. The threat of Mexico City Mayor Andres Manuel Lopez Obrador's loss of immunity and resulting disqualification as a candidate in the 2006 presidential elections has further poisoned an already unfavorable political environment for President Fox."

> "Fox seems unable to garner any support for his by now quite modest reform agenda ..."
>
> *- Andres Rozental*

Guest Comment: Tapen Sinha: "In the past four years, Vicente Fox has presided over a government that neither had a majority in the Chamber of Deputies nor in the Senate. With a very few exceptions, the opposition (both the PRI and the PRD) has taken advantage of the situation and blocked all kinds of reforms (ironically some of which the PRI had either initiated or supported in the past). The voting public has not taken this kindly. As the results of Oaxaca, Veracruz, and Baja California show, the reaction of the voters has been to lose sympathy with the current PAN government. Thus, the opposition will be in no mood for continuing the dialogue with the government at all. They believe (perhaps quite rightly) that if they can neutralize reform efforts, they will gain electorally in 2006. The government of Fox seems to have no idea on how to handle this impasse. The activities at present (for example, with the 2005 budget) seem to be geared toward muddling through the following two years. The only positive things that the current government seems to have done is to solidify the gains from democratization and not blown a big hole in the budget by trying to be populist."

James R. Jones *is a member of the* Advisor *board, Co-chair of Manatt Jones Global Strategies LLC, and was US Ambassador to Mexico from 1993 to 1997.*

Andres Rozental *is President of the Mexican Council for International Relations.*

Tapen Sinha *is ING Comercial America Chair and Professor of Risk Management at Instituto Tecnologico Autonomo de Mexico.*

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Subscription Inquiries are welcomed at freetrial@thedialogue.org

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