www.thedialogue.org

Monday, July 25, 2005

Inter-American Dialogue

LATIN AMERICA ADVISOR

Featured Q&A *With Our Board of Advisors*

Q Brazil last week announced the early payment of $5 billion of an IMF loan. Why did Brazil make this decision? How does it benefit Brazil? What are the chances that the IMF would have to step in to assist Brazil with a new loan program between now and next year's presidential election?

A Board Comment: Roger Scher: "External conditions are quite favorable for Brazil and other emerging markets right now. Global bond yields are low as are emerging market bond spreads. Risk aversion is high in the markets. In addition, Brazil's credit fundamentals are stronger than in the past, notably the performance of exports and the decline in such external debt indicators as net external debt to current external receipts, which should end this year at just above 100 percent, down from 128 percent in 2004. Foreign exchange reserves have risen. With this as a backdrop, efforts to reduce external exposure have been made, notably the reduction in dollar-indexed debt and the purchase of US$ by the central bank and the treasury. The paydown of obligations to the IMF should be understood in this vein."

A Guest Comment: Paulo Vieira da Cunha: "The Central Bank liquidated its debt under the Supplemental Reserve Facility (SRF) which carried a punitive rate of 8.9 percent pa vs. 3.3 percent pa (in $-terms) on the existing Stand By agreement. Since the rate charged on the SRF is clearly above the expected rate of return on reserves held by the central bank, it makes sense to liquidate the debt—especially when the outlook for the balance of payments is positive and robust, as it is today. Gross reserves of the central bank stood at $59.9 billion at end-June and the payment to the IMF will not change the net reserves position that remains at $40.5 billion. Our forecasts suggest that the trade account will close 2005 with a surplus of $35.3 billion (the 12 month total is now running at $38.1 billion) and the current account with a sur-

Continued on page 4

PHOTO OF THE DAY

Jose Sergio Gabrielli de Azevedo took over as CEO of Brazilian state oil company Petrobras on Friday. See profile on page 3.

Photo: PR Newswire Brasil.

Inside This Issue

NEWS BRIEFS

Amorim "Shocked and Perplexed" over Brazilian Killed in London

London Police chief Sir Ian Blair has apologized to the family of the Brazilian man shot dead by police in south London on Friday. He said the death of Jean Charles de Menezes was a "tragedy," but admitted more people could be shot as police hunt suspected suicide bombers. Mr Menezes was "completely unconnected" to Thursday's attempted bombings, Scotland Yard confirmed. Brazilian officials issued a sharp reaction to the news. "The Brazilian government and the public are shocked and perplexed that a peaceful and innocent person should have been killed," Brazil's foreign minister Celso Amorim said Sunday.

Source: BBC.

Mexican Steel Company Acquires Republic Engineered

Ohio-based **Republic Engineered Products Inc.**, the largest producer of specialty bar quality steel in North America, agreed to be acquired by **Industrias CH, S.A. de C.V.**, a steelmaker and processor based in Mexico City. Though terms have not been reported, ICH would acquire Republic in a stock purchase of all shares, including those owned by the majority shareholder, **Perry Capital**, which acquired Republic while it was in bankruptcy in 2003. Republic would become a subsidiary of **Grupo Simec** of Guadalajara, Mexico, of which ICH is the majority owner. Sergio Vigil, director and chief financial officer of ICH, said, "The addition of Republic to our family of companies will give us a presence in the United States for the first time."

Source: company release.

Political News

TeleSUR Begins Broadcast; Not Against American People, Head Says

TeleSUR, the new Caracas-based international television network, aired its first broadcasts Sunday. Funded by the governments of Venezuela, Argentina, Uruguay and Cuba, teleSUR touts itself as an alternative to the US' CNN en Espanol and Univision, and is being watched closely in Washington for its political tone and content. Last week, days before teleSUR's first broadcast, legislation was introduced in the US House of Representatives (see "Capitol Hill Watch" in the July 22 *Latin America Advisor*) to consider broadcasting Radio and TV Marti-type transmissions into Venezuela in order to offer "accurate news" to Venezuelans in the face of teleSUR's launch. "The United States has sent a message that we will not turn a blind eye as Hugo Chavez continues to snuff-out freedom and hijack Venezuela from its citizens," Florida Congressman Connie Mack said in a press release last week. In its first broadcast Sunday, the channel's president, Venezuelan Communications Minister Andres Izarra, told viewers that teleSUR was not directed against the people of the US. "It's an initiative against imperialism," Izarra said, according to the Associated Press. "That shouldn't be interpreted, however, as an initiative against the American people." Telesur's first news program began with a critical report on the failures of the mission in Haiti led by Brazil, followed by another on the plight of refugees in Colombia, according to the BBC. Venezuelan President Hugo Chavez in a phone link to the station said the broadcast yesterday was reaching five countries. The network aims to reach 23 nations eventually, according to reports. It is to be on the air four hours a day at first, and hopes to be on 24 hours a day. [See also http://www.telesurtv.net/]

> "It's an initiative against imperialism. That shouldn't be interpreted, however, as an initiative against the American people."
>
> *– teleSUR President and Venezuelan Communications Minister Andres Izarra*

Colombia to Offer Cash for Coca to Farmers; Disarmament Law Passes

Colombian President Alvaro Uribe said in a speech late Saturday that his government is willing to offer cash to farmers in exchange for their coca—the key ingredient for the illegal drug cocaine—if they promise to quit farming the crop, the Associated Press reported. President Uribe, an ally of Washington who is popular at home for his efforts to deal with narcotrafficking rebel groups, said drug crop farmers should approach the nearest police or army commander without fear of arrest and hand over their crops, and the price would be negotiated at the point of sale. The program is so far only available in the central Meta region and to farmers who commit to stop raising coca, according to the Associated Press. Currently, farmers can make up to $800 for a kilogram of coca paste, according to a Reuters report, and there are no substitute crops that offer comparable return. In related news, President Uribe signed into law Saturday the war-weary country's much debated disarmament law, a bill that encourages right-wing paramilitaries to lay down their arms in exchange for limited amnesty, according to UPI. The Peace and Justice Law grants right-wing paramilitary leaders reduced sentences and other benefits. Offenders will receive no more than eight years in a minimum security prison, and as part of the law, the government agreed to create a temporary area in Narino department for disbanding the militants. [Editor's note: see related story on page 3 in the July 21, 2005 edition of the *Latin America Advisor*.]

Company News

Harvest Natural Resources Notified $85 Million in Venezuela Taxes Due

Harvest Natural Resources became the latest oil company operating in Venezuela to be notified of back taxes owed the government. Houston, Texas-based Harvest, which owns 80 percent of **Harvest Vinccler, C.A.** production company, was notified Friday that it owed $85 million in back taxes, according to Reuters. Earlier last week **Royal Dutch Shell** was told it owed $131 million in past due taxes. Both companies have been cooperating with the government, according to an agency official, who said the checks on Harvest and other companies were routine. The official told Reuters that at least one more foreign company would be notified next week of taxes due, and more could be announced, according to Reuters. "We have 16 more cases open," he said. Harvest has been at odds with the government in recent months over alleged delays in payments from Venezuela. In June, Harvest said in a release posted on its website that it received $27 million in US dollars and 58 billion bolivars as partial payment for its 2005 first quarter deliveries of oil and gas to **Petroleos de Venezuela, S.A. (PDVSA)**, shy of the $64 million due May 31, 2005. Harvest President and Chief Executive Officer, Peter J. Hill, said, "While we acknowledge the delayed partial payment, the payment shortfall and receipt of a portion of the fee in bolivars are not consistent with the terms of our operating service agreement." No reaction from Harvest to Friday's tax assessment was available by press time.

Advisor Profile

Jose Sergio Gabrielli de Azevedo

Editor's Note: On Friday, July 22, 2005 Jose Eduardo Dutra submitted his resignation as CEO, Board Member and President of Brazil's state-owned Petrobras, positions he has held since January 2003. Under his leadership, Petrobras achieved record levels of growth and boosted oil production in the country to its highest level ever. Dutra's successor is Petrobras CFO Jose Sergio Gabrielli de Avezedo.

Photo: Petrobras

Name

Jose Sergio Gabrielli de Avezedo

Career Highlights

Gabrielli, 55, is currently a full professor on leave from the Federal University of Bahia. He has been the CFO and Investor Relations Director of Petrobras since February 2003.

As CFO, he was responsible for the Executive Management of Accounting, Corporate Finance and Treasury, Project Finance, Investor Relations, Tax Administration and Financial Planning and Risk Management. He is a member of the Board of Directors of Petrobras Energia Participaciones S.A. (PEPSA) and Petrobras Energia S.A. (PESA).

From 2000 to 2001, he was a Visiting Research Scholar at the London School of Economics and Political Science until he moved back to Brazil. Gabrielli was deputy director of Research and Post-Graduate Studies, as well as director of the Economic Sciences Faculty at the Federal University of Bahia, before he became superintendent of the Foundation for Research and Extension Support (Fapex) in Brazil.

Academic Background

Received Bachelor's and Master's degrees in Economics from the Federal University of Bahia, as well as a Doctorate from Boston University in Economics.

Notes

Dutra quit the CEO post to run for the senate next year. Gabrielli's promotion has been viewed positively by some market analysts.

Source: Petrobras, OilVoice, Bloomberg News.

Economic News

S&P Raises Credit Ratings for Trinidad & Tobago

Standard & Poor's said last Thursday that it raised its credit ratings for Trinidad & Tobago, citing the Caribbean nation's strong fiscal and external accounts, its insulation from external shocks, and its efforts to diversify its oil and gas-dependent economy. In a statement, S&P said it raised Trinidad & Tobago's long-term foreign currency sovereign credit rating to "A-" from "BBB+" and its long-term local currency sovereign credit rating to "A+" from "A". S&P analyst Roberto Sifon Arevalo said the upgrades reflect the government's increased policy flexibility as a result of continued surpluses in fiscal and external accounts, the buffer against economic shocks provided by the growing Heritage and Stabilization Fund (HSF), and efforts to diversify the economy and increase local participation in the energy sector. Sifon Arevalo noted that Trinidad & Tobago's economy is projected to record double-digit growth in 2006, following growth of more than 6 percent per year since 2002. The country should also enjoy a 50 percent capacity increase in natural gas production, S&P said.

Featured Q&A
Continued from page 1

plus of $10.5 billion. Presently there is an overall surplus in the balance of payments, after capital account transactions, of over $10 billion—and it is this excess supply of dollars together with the strong structural surplus in the external accounts that sustains the outlook for a strong currency, notwithstanding the major political volatility. It is very unlikely that Brazil will be forced to access the IMF in the near future. On the contrary, the outlook is for accelerated net repayments to the IMF with a buildup in reserves through judicious dollar purchases by the central bank from the local market."

A **Guest Comment: Larry Krohn:** "The early repayment will save Brazil about $82 million in interest. If it needed the dollars, Brazil might be well advised to simply pay on schedule. But gross foreign exchange reserves are very ample (about $60 billion) and Brazil will not miss the $4.98 billion (at Friday's SDR rate) in principal plus some $0.12 billion in accrued interest that it intends to repay as early as today. The loans in question, drawn under the Supplemental Reserve Facility negotiated under the September 2002 Stand-by Agreement, bear an interest rate of 8.9 percent, much higher than the 4.0 percent Brazil pays the IMF on its Credit Tranche, providing an obvious motivation for the move. After the repayment, Brazil will owe the Fund about $15.75 billion. Since Brazil has pre-financed its 2005 external obligations, its near-term claims on the central bank's reserves will be minimal. Even with the continued political turbulence as a result of the corruption scandals and with national elections only 15 months away, investors are not deserting Brazil. The risk, therefore, that foreign investor recalcitrance might oblige the Treasury to significantly draw down reserves before next October is very low. And a Brazil petition before next October for new IMF financing to replenish reserves is too remote to consider."

A **Guest Comment: David F. Rogus:** "Brazilian authorities were prudent in deciding to repay $5 billion of the country's IMF loan early. This move should serve to calm some of the jitters in international markets resulting from the ongoing political scandals and demonstrate to investors that despite those irregularities, the economy is strong and the integrity of government accounts has been uncompromised. Brazil benefits by being seen a model creditor and by earning greater confidence and ultimately higher ratings in the markets. Given the array of positive economic indicators today, it would come as a shocking surprise if Brazil were to require a new IMF program between now and next year's elections."

A **Guest Comment: Claudio Loser:** "Brazil's announced early loan repayment to the IMF is a good example of the proverbial 'two birds with one stone.' It repays the most expensive portion of the IMF debt, and it gives a positive signal about the country's financial strength. Before the payment, Brazil was the largest debtor to the IMF, owing about $21 billion. After the payment is made, it falls to second place, after Turkey."

Roger Scher *is a member of the* Advisor *board and Head of Latin America Sovereign Ratings at Fitch Ratings.*

Paulo Vieira da Cunha *is Chief Economist and Head of Research, Latin America, at HSBC Securities, Inc.*

Larry Krohn *is an Economist covering Latin America with IDEAglobal.*

David F. Rogus *is President of David Rogus & Associates and a consultant to Lockheed Martin Overseas Corporation.*

Claudio Loser *is Senior Fellow at the Inter-American Dialogue.*

Latin America Advisor
is published every business day by the Inter-American Dialogue, Copyright © 2005

Erik Brand,
General Manager, Publishing

Robert Simpson,
Editor

Devin Finn,
Reporter

Danielle Jetton,
Computer Services Coordinator

Subscription Inquiries are welcomed at freetrial@thedialogue.org

Latin America Advisor is published every business day by the Inter-American Dialogue
1211 Connecticut Avenue, Suite 510
Washington, DC 20036
Phone: 202-822-9002 Fax: 202-822-9553

