

Inter-American Dialogue

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Featured Q&A With Our Board of Advisors

Q Peru last week became the first of possibly three Andean nations to conclude a free trade agreement with the United States, but the deal is strongly opposed by Peruvian farm groups, which fear a flood of cheap US agriculture imports will wipe them out. Given local opposition to the trade agreement and upcoming elections in April, do you think Peru's Congress will approve it? What benefits would the FTA bring Peru? What problems does it present?

A **Guest Comment: Carlos Janada:** "The FTA with the US is a positive development for Peru. Non-traditional Peruvian exports, such as agribusiness exports, will have easier access to the most attractive market in the world, contributing to higher growth and more jobs. The process, however, may not be smooth, as there will be sectors that are negatively affected by the agreement. Peruvian authorities will have to monitor this process carefully to determine which sectors might be unfairly affected and estimate appropriate compensations. While approval of the FTA by the Peruvian Congress might face a bumpy road, I think either this Congress or the next one will ratify it. The major risks for the passage of this FTA lie with the American Congress, given its protectionist bias. As we know, CAFTA was barely approved at a time when the popularity of President Bush was still running high and the US trade deficit was lower. The FTA has also the potential to

facilitate drug eradication in Peru by promoting attractive alternative opportunities for Peruvian legal exports."

A **Guest Comment: Dennis Jett:** "My guess is that Peru's Congress will pass the FTA, but that it will not be without controversy. With elections slated for April, this will be a natural issue for some politicians to exploit. In the end, the benefits from more open markets will probably be seen as more important to Peru's economic future than the potential damage to some sectors. Also, those who oppose globalization and the so-

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PHOTO OF THE DAY



Argentine President Nestor Kirchner said yesterday that his country will pay back its entire \$10 billion IMF debt. See related story on page 2.

Photo: LaNacion.com

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NEWS BRIEFS

Cemex Earnings Up 63 Percent on Higher Sales

Mexico's **Cemex** said today it expected fourth-quarter earnings before interest, tax, depreciation and amortization at \$950 million, up 63 percent from a year earlier after a major acquisition boosted sales. The cement-making giant said revenues would be above \$3.9 billion in the October-December period, up 95 percent following the \$5.8 billion purchase of Britain's **RMC Group**, the world's largest ready-mix concrete producer.

Source: Reuters.

US Treasury Dept Denies Cuban Baseball Team Entry

Cuba will not be allowed to play in the World Baseball Classic next spring because the US Department of Treasury denied Major League Baseball the license required for the Cuban team to participate. The move came after Cuban-American members of Congress urged Treasury to veto the license application and asked Major League Baseball to drop the Cuban team from the tournament, saying the money team members could earn violated US law.

Source: The Miami Herald.

Colombian, US Navies Searching for Wreckage of Helicopter

The United States and Colombian navies will conduct a deep-sea search for wreckage of a US helicopter that crashed during an antidrug operation off Colombia's Pacific coast, killing all three American sailors aboard, officials said Thursday. Those killed were identified in a Navy statement yesterday.

Source: The Miami Herald.

Economic News

Argentina to Pay Entire \$9.8 Billion IMF Debt

In a move that surprised many experts, Argentina said yesterday it will pay back its entire \$9.8 billion debt to the International Monetary Fund this month, according to local daily *La Nacion*. The country will pay down the debt from its foreign reserves. Earlier this week, neighboring Brazil said it would pay back its entire \$15.5 billion in debt to the IMF. But the Argentine announcement contrasted from Brazil's in its bitter tone from Argentine officials, reflecting resentment over the IMF's tough-love treatment during the South American country's \$80 billion debt default in 2001. "We're leaving behind an irresponsible model of indebtedness that did nothing but isolate us,"

note this morning that he views the move as a possible liability as well. "We think the government may have prematurely discarded a still-valuable medium-term financing option," Werning said. Kirchner's posture of standing up to the IMF plays well at home, however, as many middle class Argentines lost their life savings in the devaluation that followed the 2001 recession. Many of these constituents blame foreign-owned banks, utilities and the IMF for their plight.

Mexico, US Seek Regional Agency for Infrastructure Projects

US Treasury Secretary John Snow and Mexican Finance Minister Francisco Gil said on Thursday they are seeking to establish an independent agency to rate the investment quality of large infrastructure projects in Latin America, Reuters reported. Snow and Gil said after a meet-

“We're leaving behind an irresponsible model of indebtedness that did nothing but isolate us.”

- Nestor Kirchner

President Nestor Kirchner said in a speech in Buenos Aires. Argentina took the decision after three years of economic growth have raised foreign reserves, and was aided by Venezuela's purchase this year of \$1 billion worth of Argentine bonds. Kirchner said the payment will save Argentina \$1 billion in interest and help sustain an economic recovery. But more than financial reasons drove the decision, according to analysts. The IMF loans typically came with policy guidelines and stipulations attached. Claudio Loser, a former IMF official and now senior fellow at the Inter-American Dialogue, told Bloomberg News yesterday that for Argentina, repaying the IMF will only increase its financing costs. The IMF charges lower interest than the government pays to borrow on debt markets. "It's going to end up costing Argentina a lot more money because they will have to seek other forms of financing that are more expensive," Loser told Bloomberg News. **JP Morgan Chase** analyst Vladimir Werning wrote in a research

ing they will ask other nations in the region to create a multilateral "Infrastructure Facility of the Americas" to rate the quality of project proposals, potentially under the auspices of the Inter-American Development Bank (IDB). "This rating system can help unlock large flows of private finance for infrastructure by improving investor information," the two finance leaders said at a news conference. "The idea is that this facility for investment is channeled through the private sector," Gil said, according to Reuters.

Political News

Court Orders Newspaper to Stop Reporting on Brasil Telecom Case

A Sao Paulo court has ordered the daily newspaper *Folha de S. Paulo* to stop publishing reports about the legal case involving **Brasil Telecom** and its investors. A Federal District Court judge last Friday

ordered the Sao Paulo-based newspaper, one of the largest in the country, to stop publishing reports about a pending court case involving alleged corporate espionage at Brasil Telecom. The order reportedly instructed the newspaper to "immediately cease any form of dissemination of information relevant to the facts and people involved in the proceedings in question, via newspaper, television, or radio news reports or via any other means of dissemination, including the Web site maintained by this company," according to reports. *Folha de S. Paulo* has said it would comply with the order and remove 165 pages of news reports on the case from its Web site, but it would also appeal the decision. The New York-based Committee to Protect Journalists condemned the ruling as "the latest example of judicial censorship in Brazil." "Brazilians have a right to know the details and the veracity of these serious allegations involving major corporate and government matters," CPJ Executive Director Ann Cooper said. Since 2004, *Folha de S. Paulo* has covered a corporate battle for control of Brasil Telecom. In July 2004, the paper reported that the investment firm Opportunity, which controlled Brasil Telecom, had hired US security company **Kroll** to spy on **Telecom Italia**, a competitor, as well as government officials believed to have influence over the business dispute. Federal police launched an investigation into the allegations and in April 2005 filed corruption charges against 15 businessmen, including the company's president, CPJ said in a release.

Company News

Ideal and Inbursa Win Mexican Toll Highway Concessions

Mexican companies **Ideal** and **Inbursa** won a 30-year concession on Thursday to build and operate a 223-kilometer (138-mile) highway on the outskirts of Mexico City, Reuters reported. Both are owned by politically-connected Carlos Slim, one of Latin America's wealthiest businessmen and philanthropists. The companies said they will spend 2.972 billion pesos to build the Arco Norte highway, and beat out four

The Dialogue Continues

A continuation of the December 14, 2005 Q&A

Q International money managers are pouring funds at a record pace into Latin America and other emerging markets, sparking fears that a sudden flight of capital could trigger a string of economic crises, just as in the past. How vulnerable are Latin American countries to capital flight? Are they better insulated from such shocks than in the past?

A **Guest Comment: Christian Stracke:** "The official balance of payments data show that most Latin American economies are much less vulnerable to a sudden reversal of capital flows than they were in the 1990s. Net portfolio flows into Brazil, for instance, have been minimal through most of 2004 and 2005, although the last few months have seen somewhat greater inflows. Mexico stands out with the largest net portfolio inflows in Latin America in recent months, but even those portfolio inflows have been smaller, both in absolute terms and as a share of GDP,

than they were in the 1990s. A classic turnaround in foreign portfolio investors' sentiment followed by huge outflows is therefore much less likely over the next year than it was in the 1990s. What is different, however, is the more widespread use of structured financial products whereby foreign investors are indirectly long local securities via offshore credit-linked notes and other structures. The foreign investors do not actually hold the local securities, but local financial intermediaries effectively transfer the risk of those securities via the offshore structured products. Many of these transactions do not appear in the official balance of payments data, so the true level of Latin America's exposure to portfolio flight capital may be difficult to gauge."

Christian Stracke is Senior Analyst, Emerging Markets Strategy at *CreditSights*.

other bids. None of the bidders asked for public funding, although the project includes at least 2.35 billion pesos to be spent by the federal government on public works, ministry officials said.

Telesp Celular Plans to Cut Capital Expenditures in Coming Years

Brazilian wireless company **Telesp Celular Participacoes**, the largest company within the joint venture of **Telefonica Moviles** and **Portugal Telecom**, plans to cut capital expenditure (capex) in 2006 and 2007, according to a Dow Jones report, citing a filing with the US Securities and Exchange Commission. The large amounts of capital invested by wireless companies in emerging markets like Brazil have helped buoy their economies and stock markets in recent years. Telesp said in the filing that it

aims to lower capex to 891 million reais (\$1=2.259 real) in 2006 and 674 million reais in 2007. According to the filing, Telesp's capex should peak at just over a billion reais this year. Telesp is currently being merged with the other four Brazilian operators under the **Vivo** brand, and expects the process to be completed by February. According to the SEC filing, Telesp expects its margin of revenue to earnings before interest, tax, depreciation and amortization, or EBITDA, this year to be 28 percent, down from 35 percent in 2004 and 42 percent in 2002 and 2003. In 2006 and 2007, it forecasts margins to contract again, to about 26 percent, before recovering to 30 percent by 2008. After the merger, Telesp will be listed on the **New York Stock Exchange** and the **Sao Paulo Stock Exchange**.

Featured Q&A*Continued from page 1*

called neoliberal economic model are not as strong in Peru as in some other countries. The challenge will be to find an effective way to compensate the losers and help them adjust and compete in a more open economy."

A **Guest Comment: C. Mateo Paz-Soldan:** "With the first round of presidential elections scheduled for April 2006 and the two leading candidates, Lourdes Flores Nano and Ollanta Humala, at opposite ends of the political spectrum, the debate surrounding approval of the USATPA (US-Andean Trade Promotion Agreement) and its impacts on Peru's future should be one of the primary political topics during the next three to four months. However, polls indicate that a large majority of Peru's population supports the FTA, and while the debate will be intense, the Congress should ultimately approve it. The USATPA will consolidate and augment the benefits that Peru has seen in the past 14 years since the approval of the ATPA in 1991 and its successor, the ATPDEA, in 2002. The US has become the destination for over 40 percent of Peru's manufactured exports and nearly 30 percent of its total exports, and it is estimated that over 1 million people in Peru are employed thanks to trade with the US. Growing non-traditional exports such as textiles and apparel (over \$1 billion in exports in 2004), and agricultural products such as asparagus, artichokes, paprika, onions, mangos and others have contributed to full employment in areas of Peru such as Ica and La Libertad and to a reduction of nearly 40 percent in extreme poverty levels, according to some estimates, in those same areas. The key to assuaging the concerns of the opposition is the level of commitment of future governments to the so-called 'agricultural conversion program' and other compensation mechanisms by which the sensitive agricultural sectors will be assisted by the state in making the adjustments necessary to remain competitive with commodity imports from the US or convert

to more promising agroexport sectors. Given previous governments' records, there is much skepticism about present commitments. However, if one considers that only seven percent of Peru's total

“... Only seven percent of Peru's cultivable land is presently dedicated to the agro-export sector.”

- C. Mateo Paz-Soldan

cultivable land is presently dedicated to the booming agro-export sector, then the magnitude of Peru's potential transformation in coming decades becomes clear."

A **Guest Comment: Liliana Ruiz:** "Considering there are only a few farm products with a risk of losing market, and that the Minister of Economy has made public his commitment to financially compensate farmers for possible losses, I think local opposition does not have solid ground to reject a treaty that, for the most part, will help to modernize Peruvian institutions. By focusing Peruvian state procedures and actions on competitiveness, this agreement will trigger necessary investment to grow and increase employment. Most Peruvian citizens have viewed this agreement with some sympathy since the start of the negotiations, and the final outcome will convince them of its advantages."

Carlos Janada is Senior Economist at the *Institute of International Finance*.

Dennis Jett is a former US ambassador to Peru and Partner at the law firm *Tew Cardenas* in Washington.

C. Mateo Paz-Soldan is Partner at *Schmeltzer, Aptaker & Shepard, PC*.

Liliana Ruiz de Alonso is President of *ALTERNA Consulting* and Peru's negotiator for the FTA.

Latin America Advisor

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

Erik Brand,
General Manager, Publishing

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Vice President, Social Policy

Viron Vaky,
Senior Fellow

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

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