



# Inter-American Dialogue

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## Featured Q&A With Our Board of Advisors

**Q** Some analysts are predicting the price of oil could reach \$100 per barrel as early as next year amid unrelenting demand and constraints on supply. Do you see oil prices hitting such levels? What is the good and bad news for Latin America of higher oil prices?

**A** Guest Comment: Roger Tissot: "Despite media reports regarding an expected \$100 per barrel, it is not yet certain such a price increase will indeed occur. However, if that were to happen for a sustained period, one could expect four impacts in Latin America. First, oil-producing countries would continue to benefit from record-high export revenues. Venezuela, and to a lesser extent other resource nationalist administrations, would have less pressure to pursue investments in E&P, preferring to divert revenues to social and industrialization schemes. Countries with still-attractive fiscal terms would continue to attract the interest of the industry despite higher geological risks. Second, oil-importing countries such as Central America and the Caribbean would continue to struggle to pay their energy bills and would seek alternative options. Some would endorse Venezuela's petroleum diplomacy generosity while also seeking the development of alternative sources, such as biofuels. Third, a massive inflow of revenues would continue to pressure local currencies up, eroding

the competitiveness of non-oil exports. The risk of a 'Dutch disease' would increase, and the region would become more dependent on revenues from energy commodities. Fourth, subsidies for oil products would continue to eat the wind-falls from exports, requiring governments to address the need for investments in new or expanded refineries and the revision of domestic price policies. Energy-rich countries should use the current price boom to strengthen oil stabilization funds aimed at providing a financial cushion during lower price periods and as an inter-generational transfer of wealth. However, revenues should also help to solve the massive social

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### PHOTO OF THE DAY



Argentine President Nestor Kirchner (L) and his wife, presidential front-runner Cristina Fernandez de Kirchner, arrived in Mexico yesterday for meetings with counterpart Felipe Calderon. See related [story](#) on page 2.

*Photo: Mexican government.*

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## NEWS BRIEFS

**Latin American Bourses Rally After Worst Week in Five Years**

Stocks in Latin America rallied yesterday, as investors bought into companies in the region once again after last week's global sell-off. Brazil's **Bovespa** stock index jumped 3.1 percent, recovering nearly half of last week's loss, Bloomberg News reported. Mexico's **Bolsa** index, the second-largest in the region, rallied 2.2 percent. It was the biggest gain in Brazil since March 6 and in Mexico since July 3.

**Devon Energy's Polvo Oil Field Begins Production**

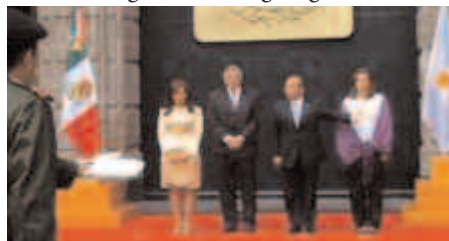
Oklahoma-based **Devon Energy** said Monday its Polvo oil field in Brazil began production. Polvo was discovered in 2004 and is located in the Campos Basin offshore Rio de Janeiro in approximately 300 feet of water. Gross production is expected to peak by the end of 2008 at approximately 50,000 barrels of oil per day. First sales are expected to begin in October. Polvo has estimated resource potential in excess of 50 million barrels.

**Ghezzi Joins Barclays, Ortiz Goes to Bear Stearns in New York**

**Barclays Capital** on Monday named Piero Ghezzi its head of emerging markets research, Reuters reported. Ghezzi will serve as a managing director in New York. He previously worked at **Deutsche Bank** as head of Latin America research. In related news, Wilfredo Ortiz will join **Bear Stearns** in August as a managing director to oversee Latin American metals and mining companies. He will be based in New York and report to Rowe Michels, director of global emerging markets research, Dow Jones reported.

**Political News****Mexico, Argentina Pledge New Strategic Relationship**

Argentine President Nestor Kirchner and his wife, senator and presidential candidate Cristina Fernandez de Kirchner, yesterday arrived in Mexico City for a three-day state visit. Calling for a closer relationship, Kirchner and counterpart Felipe Calderon signed a strategic agreement that



Upon arriving in Mexico City yesterday, Kirchner told Calderon "it's essential" that Mexico join Mercosur.

*Photo: Argentine government.*

pledged to increase trade and investment, and also promote joint cooperation for economic development, scientific cooperation and cultural exchange, according to a press release from Calderon's office. Kirchner focused the first day of the visit on trade integration, telling Calderon upon arriving that "it's essential" that Mexico join the Mercosur trade bloc, according to media reports. "We should hold the discussions step by step in order to have a balanced integration that will strengthen the Mercosur bloc and all its countries," said Kirchner in a news conference with Calderon. Kirchner said that the member countries of Mercosur were in favor of Mexico's inclusion and that Argentina supported the improvement of relations between Mexico and Venezuela since it wished to see all the countries in the region united, according to a statement from the Mexican government. In related news, presidential candidate Fernandez de Kirchner continues to enjoy high popularity ahead of October's national elections. A poll cited last week-end in the local *Clarín* newspaper found the number of voters who would elect the senator has neared the 45 percent needed to avoid a runoff, well ahead of the 18 percent support her nearest rival garnered.

**Economic News****South America Lifts Global Car Sales to Record High, Scotiabank Says**

Global car sales advanced by 3 percent in the first half of 2007, a stronger-than-expected result as South America has overtaken Asia as the world's fastest-growing regional vehicle market, according to a report released today by **Scotiabank**. Brazil is the largest auto market in Latin America, but Peru is the fastest-growing market. Sales in Peru surged by 41 percent in 2006 and have posted a further 38 percent jump through May this year, as economic activity continues to expand in excess of 7 percent year-over-year. "Peru is one of the fastest-growing economies in the Americas, but it has one of the lowest vehicle ownership rates," said Carlos Gomes, Scotiabank's auto industry specialist. "There are only 24 vehicles for every 1,000 people in Peru, less than China and only one-fifth the average across all of Latin America and the Caribbean." In Brazil, ongoing reductions in interest rates have lifted car sales by 27 percent in the first half, roughly double the 13 percent

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— Carlos Gomes

gain posted in 2006. Purchases are on target to exceed 1.9 million units in 2007. "Strength in auto production is, and will continue to be, a key driver of industrial activity in Brazil," said Gomes.

**Company News****HSBC's Latin America Profits Up 16 Percent in First Half of 2007**

UK-based bank **HSBC** announced yesterday its profit before tax in the first half of

the year in Latin America grew by 16 percent. Latin American operations now account for 8 percent of HSBC's profit, the company said in a Web site release. Improved credit performance in Brazil, coupled with strong asset growth, contributed to pre-tax profit growth of 43 percent, the company said. Revenue growth in Mexico "remained strong" at 23 percent on market share gains. "We have built a highly successful business in the last five years, which has already returned profits in excess of our total investment," said Stephen Green, HSBC's group chairman. HSBC in Mexico posted strong market share with credit cards, Tu Cuenta packaged accounts, and premier accounts, all growing by over 45 percent compared with the previous year, the company said. In Argentina, the integration of **Banca Nazionale del Lavoro**, an acquisition in May 2006, contributed to a 14 per cent rise in pre-tax profits to \$95 million, Green said.

### Telefonica Raises 2007 Latin American Growth Forecast

Spanish phone giant **Telefonica** raised its 2007 growth forecast on Monday after reporting strong revenue gains in the first half of the year, driven primarily by its broadband and mobile markets. In a press release, Telefonica said it saw first-half net profit rise to 3.83 billion euros (\$US 5.22 billion), a 66.4 percent jump over the same period a year ago. The company's Latin America unit, which contributed 34.6 percent of consolidated revenues, also recorded solid revenue of 9.63 billion euros, up 10.6 percent from the year-earlier period, thanks to strong mobile phone growth driven by the company's Mother's Day campaign in Latin America. Telefonica Latinoamerica upped its 2007 revenue forecast to 13-16 percent growth, compared to a previously announced 11-14 percent range. The unit's client base increased to 121.8 million access points, up 13.9 percent year-on-year.



Cesar Alierta,  
Executive  
Chairman.

Photo: Telefonica.

er period, thanks to strong mobile phone growth driven by the company's Mother's Day campaign in Latin America. Telefonica Latinoamerica upped its 2007 revenue forecast to 13-16 percent growth, compared to a previously announced 11-14 percent range. The unit's client base increased to 121.8 million access points, up 13.9 percent year-on-year.

### Featured Q&A

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gap as well as the infrastructure deficit, which drags the region's global competitiveness. The challenge is achieving these goals without falling into the traditional traps of the 'oil curse,' inflation, crowding out the private sector with public investments, and corruption resulting in construction of 'white elephants.' Latin America has had a long history of boom and bust cycles. Fortunately, the region has learned from past mistakes, but some countries are still pursuing non-viable

“ [OPEC] continues to lay the blame for the dramatic run-up in oil prices on geopolitical concerns and refinery bottlenecks, but the reality is that there is a crude shortage. ”

— Luis Giusti

models, which can only survive with an unsustainable model of constantly increasing oil prices.”

**Guest Comment: Roger Stark:** "Since 9/11, uncertainties regarding supply and demand have caused oil prices to reflect an unusually volatile 'risk premium.' A combination of 'peak oil' concerns (positing an irreversible decline in reserves) and political risks associated with terrorism, resource nationalism, and the war in Iraq create significant uncertainty in forward production estimates. Demand is skewing upwards because of burgeoning economies in China and India, among others. However, higher oil prices spur innovation: new technologies increase energy efficiency and enhance the economics of non-petroleum substitutes (e.g., renewable resources and nuclear energy) which, in turn, moderate demand. Greenhouse gas initiatives and carbon

regulation will further moderate hydrocarbon consumption. Because the resulting environment is one of supply-side risks that are largely reflected in current oil prices, and of increased opportunities for mitigating growth in energy demand, oil prices should stabilize below the \$100/barrel level unless a major event changes the production risk profile."

**Guest Comment: Luis Giusti:** "During the past six months, OPEC has been very successful in putting a floor under oil prices. In the meantime, it continues to lay the blame for the dramatic run-up in oil prices on geopolitical concerns and refinery bottlenecks, but the reality is that there is a crude shortage. Geopolitical concerns about Iran and Iraq have eased off, with Nigeria remaining the hotspot—750,000 barrels per day (bpd) of shut-in production—while refinery bottlenecks have a relative influence on the price of oil. OPEC seems to fear a repeat of last year's second-half price slide of \$28 per barrel, which truly reflects the fragility of the current levels. However, at the London-based Centre for Global Energy Studies we believe that OPEC's forecast of 51 million bpd of non-OPEC oil in the fourth quarter of this year is one million bpd too high. If OPEC does not raise production sufficiently over the coming months, prices will remain on an upward trend until they are pushed so high as to trigger a collapse in demand, as occurred in the mid-1980s. Already, a sustained damping effect on demand growth has been observed. If OPEC's stance remains unchanged, prices would reach the lower 80s by the end of this year, and a price of \$100 per barrel by the fourth quarter of 2008 is conceivable. Nevertheless, we believe that OPEC would open up production well before that would happen, especially considering that it has an implicit target of \$60 per barrel for its basket. The negative consequences of such extremely high prices for both producers and consumers leads one to believe that a more likely scenario is that

*Q&A continued on page 4*

**Featured Q&A***Continued from page 3*

prices will hover in the high 70s for the remainder of this year and ease to the mid 70s on average for next year."

**A** **Guest Comment: Jose Valera:** "If the price of oil were to reach \$100 as early as next year, my view is that, on balance, it would be bad news for Latin America. The plus side would be small. The oil-exporting countries in the region, notably Mexico and Venezuela, would see a relatively minor benefit. Mexico exports crude oil to then import refined products in large quantities. The net flow from this trade would continue shrinking, as crude export volumes decrease (in line with the present trend) and the price

“Higher international oil prices would be very detrimental to Bolivia.”

— *Jose Valera*

of refined products increases. Venezuela would see its net go up, but it all goes to the government, not to the private sector that invests it and creates jobs. The Venezuelan government tends to be a heavy spender. The minus side would be big. Especially vulnerable are countries that depend significantly on imports for transportation, power generation, and industry, and don't have economies that can absorb the extra cost. All the Central American countries fall in this camp. Argentina, Ecuador, and Bolivia would also hurt because local oil production in those countries is not keeping up with demand. In Argentina, as imports of refined products and gas increase, the government is going to run out of options to keep domestic gas and electricity prices artificially low. Sooner or later, the consumer is going to see tariffs going up, and the costs of raw materials will also increase. Ecuador is incapable of putting forth a framework and policies that will actually encourage additional oil exploration and production, and in

the meantime it has to import the majority of its refined products requirements. The government is not passing the true cost of the imported fuel to state power company customers. This huge deficit would only get worse and significantly handicap the Ecuadorean treasury. Bolivia already has shortages of jet fuel, gasoline, and diesel. Its local oil production and output of refined products has no prospect of increasing in the short term. Higher international oil prices would be very detrimental to Bolivia. Brazil, Colombia, and Peru would see a lesser adverse impact. Brazil's oil production is nicely supplemented by ethanol. But Brazil's weak point is gas, which it is going to import in increasingly higher volumes. Peru is helped by low domestic prices of Camisea gas, industrialization of gas, substantial exports of Camisea gas liquids, and plans to increase refinery capacity. This offsets the higher costs of imported light crude. Colombia is still a net oil exporter and is increasing its refinery capacity. Chile relies almost exclusively on imports for its oil and gas requirements. However, the Chilean economy can more comfortably offset these increased costs through productivity, additional mineral export revenue, and subsidies targeted at the low-income population with available government resources."

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