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FEATURED Q&A

How Will Carstens Handle Monetary Policy in Mexico?

Q Mexico's Senate on Tuesday confirmed Agustin Carstens to succeed Guillermo Ortiz as head of Mexico's central bank. What will the change mean for the bank's monetary policy? Will Carstens be able to fight inflation without choking off growth? How valid are concerns that Carstens is too close to Calderon?

A Alfredo Thorne, corporate general director at Grupo Financiero Banorte in Mexico City: "After President Calderon nominated Agustin Carstens to head Banxico, markets offered a sour welcome. The yield curve steepened—short rates went down and long ones up—anticipating that he will be more dovish and tolerant of inflation. However, markets may have overreacted. For one, Carstens is far from being a dove; he was the architect of Banxico's response to the 1994-95 peso devaluation, which brought inflation down from more than 50 percent in 1995 to the 4 percent where it stands now. When Carstens said in his Senate hearings that Banxico policy stance should remain unchanged at current levels he is not obviating inflation, but rather arguing that the tax-induced inflation shock starting in January should be treated as a once-and-for-all effect. A close inspection indicates that there are no reasons to believe that inflation will persist beyond the initial shock. For one, Mexico's output gap is highly negative and probably the largest within emerging economies. This

indicates that pricing power will remain low for some time. Second, Mexico's policy stance cannot risk deviating for too long from the U.S. Fed's stance, as this may risk an excessive appreciation of the currency and endangering the still-fragile recovery. Third, Banxico, unlike the Fed, did not overease. In fact, the real rate remained in positive territory and has less pressure to normalize. But this division between market perception and reality may well highlight the need for Banxico to continue making progress in making policymaking

Continued on page 3



Chavez Blasts Netherlands, Claims It Harbors 'Assassins'

Venezuelan President Hugo Chavez on Thursday blasted the Netherlands, claiming its self-governing islands in the Caribbean are harboring U.S. agents for an attack on Venezuela. See story on page 2.

Photo: Venezuelan Government.

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NEWS BRIEFS

Senator Drops Opposition to Brazil Ambassador Nominee

U.S. Sen. George LeMieux (R-Fla.) on Thursday dropped his block on the confirmation of Thomas Shannon as ambassador to Brazil. LeMieux for the past several weeks had held up the nomination of Shannon, who until last month was assistant secretary of state for Western Hemisphere affairs. In a statement, LeMieux said delaying the confirmation allowed him more time "to ask specific questions of Mr. Shannon and State Department officials." LeMieux said U.S. policy toward Cuba and Honduras must demonstrate "through action our insistence on democracy and respect for the rule of law."

Rights Group: 5,000 Mexican Migrants Have Died Since '94

Five thousand Mexican migrants have died trying to cross the border into the United States since 1994, Mexico's independent National Commission of Human Rights said Thursday. During 2007 and 2008, an average of three migrants died every two days in the deserts, rivers and mountains of the border region, the group said. The commission urged governments to help ensure migrants' human rights, noting that illicit activities like human smuggling prey on the migrants.

Number of Brazil Mobile Phone Users Top 169 Million

The number of mobile phone users in Brazil reached 169.8 million at the end of November, reflecting a penetration of 88.4 percent, Brazilian telecommunications agency Anatel said Thursday. The number of users added in the first 11 months of 2009 was 19.1 million, the second highest on record after 2008.

Political News**Chavez Accuses Netherlands of Harboring U.S. 'Assassins'**

Venezuelan President Hugo Chavez on Thursday blasted the Netherlands, accusing it of using its islands in the Caribbean to harbor U.S. soldiers and "assassins" for a planned attack on Venezuela, the Associated Press reported. Chavez, in Copenhagen for the U.N. Climate Change Conference, said the U.S. has sent war ships, intelligence agents and spy planes to Aruba, Bonaire and Curacao in advance of an attack on Venezuela. "They are three islands in Venezuela's territorial waters, but they are still under an imperial regime: the Netherlands," Chavez said. "Europe should know that the North American empire is filling these islands with weapons, assassins, American intelligence units, and spy planes and war ships." The United States for years has had a presence on the self-governing Dutch islands in the Caribbean for operations

“It's a threat to all the people of Latin America and the Caribbean.”

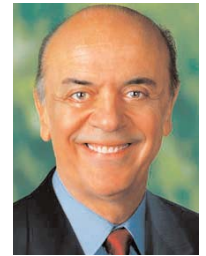
— Hugo Chavez

against drug traffickers and guerrillas in Colombia. In Washington, Ian Kelly, a State Department spokesman, said U.S. military personnel in the region are not there to prepare to attack Venezuela. "These allegations are baseless. These are routine exercises," Kelly said, according to the AP. "We seek cooperation with the region." Chavez said the U.S. military presence in the Caribbean is part of a plan to destabilize leftist governments in locations including Cuba, Ecuador, Bolivia and Nicaragua. "It's a threat to all the people of Latin America and the Caribbean," Chavez said. "Venezuela is being surrounded by military bases." Chavez has also repeatedly said that Venezuela is threatened by the recent U.S. agreement with Colombia that gives U.S. military

personnel greater access to Colombian military bases, which the United States says is needed for anti-drug operations.

Brazil's Serra Closer to Presidential Nomination as Rival Bows Out

Jose Serra, the governor of Brazil's Sao Paulo state, is all but certain to clinch the opposition Brazilian Social Democratic Party (PSDB) nomination for president after his main rival dropped out of the running Thursday, the Associated Press reported. Minas Gerais Governor Aécio Neves said he would not seek the PSDB nomination for president. Neves announced his decision during a news conference in Belo Horizonte. The decision strengthens the candidacy of Serra, who lost to President Luiz Inacio Lula da Silva in 2002. "There was a certain anxiety



Serra

File Photo: State of Sao Paulo.

due to the party's indecision," PSDB Sen. Alvaro Dias told the AP. "Now, the pressure's off." Neves' stepping aside from the race also puts an end to a possible looming split in the PSDB, which could have hurt its chances against Lula's Workers' Party (PT). "This way I will contribute so that the PSDB and its allies ... can build a path without tensions toward victory in 2010," said Neves. In the most recent opinion polls, Serra leads PT hopeful Dilma Rousseff, Lula's chief of staff and chosen successor, in advance of the Oct. 3 election.

Economic News**U.S. Offers Aid at Climate Talks as Leftist Leaders Blast Capitalism**

U.S. Secretary of State Hillary Clinton on Thursday said the United States would work with other developed economies to raise \$100 billion per year by 2020 in an effort to unblock negotiations over a global climate change agreement in Copenhagen, which have accentuated a rift between rich and poor nations.

Clinton's announcement, which a U.N. official said helped restart talks amid hopes that China is still open to reaching a deal, came a day after presidents Hugo Chavez of Venezuela and Evo Morales of Bolivia lashed out at capitalism as the primary cause of climate change, Dow Jones reported. "Capitalism, the destructive model of development, is ending lives, and it threatens to put an end to the human species," Chavez said. Morales called on developed countries to provide billions in reparations to the developing world in compensation for the harmful effects of global warming, and said countries should limit temperature increases to 1 degree Celsius over the next century, *The Guardian* reported. Obama addressed the conference today, saying the world will "be stronger and safer and more secure" with a global accord. In a telephone call earlier this week with Brazilian President Luiz Inacio Lula da Silva, Obama "noted the key role Brazil is playing, and explained both the steps that have been taken in the United States, and his commitment to an agreement in Copenhagen with emissions reductions, financing, and a transparent and internationally verifiable compliance regime," the White House said in a statement. On Thursday, Lula addressed fellow leaders in Copenhagen, calling on countries to reduce greenhouse gas emission by 50 percent by 2050, Reuters reported.

Company News

Petrobras to Lease and Operate Vessel From Holland's SBM

Holland-based oil services company **SBM Offshore** announced Thursday it had received a letter of intent from Brazilian national oil company **Petrobras** for a lease-and-operate contract worth \$1.7 billion for SBM's floating oil production and storage vessel *Espadarte*. The lease is for a period of 18 years on the Baleia Azul field off Brazil's coast. The vessel will be disconnected from its current location at the offshore *Espadarte* field and will be significantly modified and upgraded for the new project before being installed on the Baleia Azul field, the company said.

Featured Q&A

Continued from page 1

more transparent and effective. It is one of the few central banks that does not publish minutes, does not disclose the votes of its policy committee members and targets a very volatile component of inflation as is 'headline' inflation. I believe that Carstens assures that Banxico keeps making strides in policy reform."

A Pamela K. Starr, associate professor at the University of Southern California's Center on Public Diplomacy: "The recently announced succession at the Bank of Mexico was not unexpected, and not merely because of the bad blood between Guillermo Ortiz and President Calderon. Agustin Carstens has long coveted the post, leading to rumors back in 2006 when he accepted the job as finance minister only after some arm twisting that this would be his reward. Carstens is highly qualified for the central bank post and is unlikely to implement significant monetary policy changes. As a senior

“ Calderon's choice of
Ernesto Cordero to replace
Carstens at the Finance Ministry
... is cause for concern. ”

— Pamela K. Starr

economist at Goldman Sachs quoted in *The New York Times* put it, 'A great bank president leaves. A great bank president arrives.' Calderon's choice of Ernesto Cordero to replace Carstens at the Finance Ministry, however, is cause for concern. The issue is not Cordero's talent and promise, but his lack of experience and an international profile. His selection seems imprudent given that both Fitch and Standard & Poor's identified a deteriorating fiscal position as the reason

for their recent decisions to downgrade Mexico. These concerns are only deepened by Cordero's deep partisan loyalties to the president. Agustin Carstens is a technocrat with roots in the PRI (as well as a skilled negotiator) and thus well-positioned to negotiate with PRI legislators on the budget. Ernesto Cordero is a PAN partisan and Calderon loyalist whose elevation to the Finance Ministry inevitably places his name on the short list of possible PAN presidential candidates for 2012. The PRI is unlikely to see him as an honest broker and will be motivated to deny him budget victories that could enhance his standing as a candidate."

A Andrés Rozental, member of the Advisorboard, president of Rozental & Asociados in Mexico City and member of the Inter-American Dialogue: "I don't believe there will be any fundamental change in the central bank's monetary policy as a result of Carstens' appointment and ratification by Congress. He is an old Banco de Mexico hand with many years of experience in the financial sector. Doubts about his independence from President Calderon are misplaced since he is well aware of the bank's constitutionally mandated objective to maintain the peso's value and defend the economy against inflation and loss of jobs. In addition, the man he is replacing, Guillermo Ortiz, was also appointed by a president (Zedillo) in whose cabinet he served just like Carstens in the current administration. Calderon's appointment of Ernesto Cordero as Carstens' replacement in the Finance Ministry hasn't been as well received by the country's private sector and in international banking circles. Cordero is relatively unknown in the financial world, having only served for less than a year in the ministry as an under secretary. His close relationship to the president and the fact that he is considered a political rather than a technical appointment breaks with a long tradition in Mexico. Time will tell whether

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Featured Q&A*Continued from page 3*

Cordero will be able to gain the confidence of both the domestic and international financial world."

A Sergio Martin, head of research and chief economist for Mexico at HSBC Mexico:

"We see no amendment or bias in monetary policy under Carstens' mandate. Some press reports question Carstens' nearness to the president and will to operate independently, inducing some doubts into the autonomous conduct of monetary policy. Our opinion is that his credentials and reputation are above all doubts and he will contribute to the conduct of monetary policy in line with sound research and analysis. We believe it would have been quite hard to find someone better qualified for the job than Carstens. Financial markets and media had already anticipated the Carstens' nomination as the central bank governor because of his professional trajectory that started precisely at this institution and ended with him being the bank's chief economist for many years. His experience in the Finance Ministry as deputy secretary (2000-2002) and later as deputy managing director at the International Monetary Fund (2003-2006) gives him relevant credentials and a highly positive reputation as a conservative economist. We believe that the board of governors will keep conducting monetary policy in the same autonomous fashion as in the past. In particular, Agustin

Carstens stated explicitly to the press that it is not his intention to change the central bank's mandate to include promotion of economic growth. This public position establishes clearly Carstens' view about the priority of price stabilization for the Bank of Mexico. He has also stat-

“It would have been quite hard to find someone better qualified for the job than Carstens.”

— Sergio Martin

ed that while price stabilization is the priority in the central bank's mandate, the balance of risks, where economic growth is a key ingredient, must also be considered. To strike the right balance will not be easy for him, as it has not been for Ortiz, but we are confident that the board of governors will keep doing a relatively good job."

The Advisor welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.

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