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FEATURED Q&A

Why Is Trade Conflict Between Brazil and Mexico on the Rise?

Q A strengthening Brazilian real has given Mexico an advantage in auto exports, leaving Brazil with a trade deficit of $1.6 billion in that sector in 2010. Although a Mexican delegation has been sent to Brazil to discuss the South American country's dissatisfaction with a decade-old automotive trade deal, Mexican officials said that they are not seeking to renegotiate the pact, Dow Jones reported. What does discord over the auto trade deal reveal about the two countries' trade relations with each other? Does it have other implications for businesses hoping to do more intra-regional trade? How significant are rising labor costs in Asia for improving the competitiveness of manufacturers within the Americas?

A Ruben Olmos, partner at Global Policy Strategies in Washington: "The trade dispute over Mexico's auto exports to Brazil does not bode well for trade relations between the two countries. As Bruno Ferrari, Mexico's secretary of the economy, has stated, the row could put in jeopardy negotiations toward a free trade agreement between the two countries—slated to begin anew this year. The FTA, years in negotiation, will not likely come to fruition in the near future. In 2011, Brazil barely saw its manufacturing industry expand. The year also saw Brazil engage in a trade spat with Argentina over auto trade. With a real that will likely stay costly due to low rates that look to be continuing in the country, Brazil will have to resort to the politics of trade to assuage its growing auto deficit. Though, as the global economy picks up, Mexico's peso will probably see a modest rise as foreign capital flows return and the country's presidential election occurs without problems. Although labor costs may be rising in China, they are still significantly cheaper than those in Latin America. Chinese workers make $300 to $400 a month—a fraction of the salary for a Mexican or

Continued on page 2

Nicaragua's Central Bank Chief Quits Amid Flap With Ortega

Nicaraguan Central Bank President Antenor Rosales has stepped down amid a disagreement with President Daniel Ortega over using central bank reserves to help fund a regional development bank created by the Venezuela-led ALBA bloc. See story on page 2.

File Photo: www.lavozdelsandinismo.com.

Inside This Issue

FEATURED Q&A: Why Is Trade Conflict Between Brazil and Mexico on the Rise?.....1

At Least 272 Killed as Fire Sweeps Through Honduran Prison.....2

Nicaragua's Central Bank President Quits Amid Flap With Ortega.....2

Venezuelan Court Orders Opposition Voter Lists Kept.....2

Banco do Brasil Reports Lower Profit, Beats Estimates.....3

The Dialogue Continues: Would Falling Commodity Prices Sink Latin Economies?.....3

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NEWS BRIEFS

Venezuelan Court Orders Opposition Voter Lists Kept

Venezuela's Supreme Court on Tuesday ordered electoral officials not to destroy lists of voters who participated in Sunday's opposition primary elections, the Associated Press reported. The court's ruling was condemned by opposition leaders who wish to keep voter identities secret, fearing the government of President Hugo Chávez could use the information to intimidate opposition supporters in next October's national elections. The court order was sought by a mayoral contender who lost in Sunday's primary and called for the voter lists to be reviewed, according to the AP.

Chilean Central Bank Leaves Interest Rate Unchanged at 5%

Chile's central bank decided Monday to leave their benchmark interest rate unchanged as the country is experiencing faster growth than expected, Bloomberg News reported. Policymakers, led for the third meeting by new bank chief Rodrigo Vergara, kept the overnight interest rate at 5 percent. Chile's economy is estimated to have grown 6.3 percent last year and the central bank is expecting growth of 3.75 percent to 4.75 percent this year.

India's Sterlite Ordered to Pay Grupo Mexico Unit $83 Million

U.S.-based **Asarco**, a unit of mining giant **Grupo Mexico**, on Tuesday won an $82.8 million lawsuit against Indian copper producer **Sterlite Industries**, Bloomberg News reported. The case, which yielded much less than the $2.28 billion Asarco was seeking, stems from a failed deal to buy Asarco out of bankruptcy. Grupo Mexico eventually acquired Asarco in 2009 after years of litigation and negotiations with Sterlite.

Political News

At Least 272 Killed as Fire Sweeps Through Honduran Prison

At least 272 inmates have been killed and dozens more were seriously burned after a fire swept through a Honduran prison Tuesday night, the Associated Press reported today, citing Lucy Marder, head of forensic medicine for the local prosecutor's office. The blaze happened in a prison holding nearly 800 inmates in Comayagua, 90 miles north of Tegucigalpa. Josue García, a spokesman for Comayagua's fire department, described the scene as "hellish," adding that victims were "burned to death or suffocated in their cells," the AP reported. Prisoners were trapped in their cells because the guard who had the key to them could not be found, said García. Several inmates may have escaped during the blaze, said Hector Iván Mejía, a government security secretariat spokesman. The cause of the fire is under investigation, but officials believe it started either after an electrical short-circuit or amid a prison riot.

Economic News

Nicaragua's Central Bank President Quits Amid Flap With Ortega

Nicaragua's central bank president, Antenor Rosales, has resigned amid a disagreement with President Daniel Ortega about using central bank reserves to provide funding to a regional development bank for the eight-nation ALBA bloc, which is led by Venezuela, Bloomberg News reported Tuesday. During a meeting in Caracas on Feb. 4, Ortega and other leaders of the bloc agreed to place 1 percent of their reserves with the new bank. In Nicaragua's case, the figure would be about $17 million. Two days later in Managua, Rosales told reporters that no other countries should be allowed to use

Featured Q&A

Continued from page 1

Brazilian worker. Latin America also lacks the demanding quality and emissions standards present in Europe and the United States, making it a fertile market for cheaper Chinese cars. Regionally, trade relations seem to be advancing. Last year, Mexico signed an FTA with Peru and the United States signed FTAs with Panama and Colombia. This year, even insular governments in the region, like Correa's in Ecuador, could see trade improve with a pick-up in the global economy."

A João Augusto de Castro Neves, Latin America analyst at the Eurasia Group: "Despite a laundry list of regional and sub-regional institutions, economic integration remains a tentative reality in Latin America. Brazil's recent decision to review its automotive trade deal with Mexico highlights the distance between an ambitious integrationist rhetoric and the harsher constraints that local industries face. High taxes and labor costs as well as infrastructure bottlenecks greatly reduce the competitiveness of Brazilian companies amid growing imports from Asia. The problem does not pertain only to Brazil and its relationship with Mexico. Seeking to uplift revenues while protecting its local industry, Argentina recently implemented a set of trade restrictions that will affect its trading partners, mainly Brazil. Trade agreements among three of the largest economies in the region, therefore, remain vulnerable to a multitude of competing interests and the unpredictable ebb and flow of international trade flows. From past experience, it is expected that diplomatic efforts will quell the furthering of tensions, avoid formal fragmentation of regional institutions and bring about a temporary solution to the problem. Considering that three protocols have been added to the

Continued on page 4

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Nicaragua's reserves. "The resignation of Rosales sends a bad message to the people of Nicaragua," opposition lawmaker Wilfredo Navarro said in a speech to the National Assembly, Bloomberg News reported, citing a local television station. "He was defending the legality of the country's central bank institution. Withdrawing funds for an unknown bank is a violation of the institution." Ortega has named Finance Minister Alberto Guevara as Rosales' replacement, according to ruling Sandinista Party lawmakers. Ortega's government has sent Guevara's appointment for approval to the National Assembly, said chief Sandinista legislator Edwin Castro. He did not say whether Guevara would continue as finance minister. Castro added that Rosales' stepping down was not a result of his disagreement with Ortega, but instead was "normal government procedure." The new development bank aims to back sustainable projects, fight poverty and support member nations' sovereignty and integration with a "just, dynamic, harmonic and equitable economic exchange," the bank says on its Web site. Venezuelan President Hugo Chávez said Feb. 4 that his country is willing to provide $300 million in funding to the new bank.

> "The resignation of Rosales sends a bad message to the people of Nicaragua."
>
> *— Opposition lawmaker Wilfredo Navarro*

The Dialogue Continues

Would Falling Commodity Prices Sink the Region's Economies?

Q According to ECLAC, a decade of economic growth, on average, has helped lift 56 million Latin Americans into the middle class since 1999. However, some economists worry that a decline in demand for commodities, which have risen from 27 percent to 39 percent of exports over the past decade, could reverse these gains. What effect would a decrease in commodities prices have on the region? Will the newly emergent middle class slide back into poverty, or are the gains sustainable? Has deindustrialization become an urgent policy concern for some Latin American countries?

A Claudio Loser, senior fellow at the Inter-American Dialogue and former head of the Western Hemisphere department at the IMF: "A decline in terms of trade will have an adverse effect on the welfare of most Latin American countries, and will result at a minimum in a lower rate of growth for the region. In this sense, everybody will be affected by the decline in commodity prices, as has been observed in 2011. However the decline, about 10 percent from April to December, should be seen in the right perspective. On average, commodity prices in 2011 were higher than in any of the last 10 years except for a period in 2008, when commodities were subject to a speculative bubble. It is true that commodity prices may decline further, and probably will do so. However, this should not jeopardize the long-term well being of the region. Adjustments will need to be made, and problems will arise in public finances, but in the presence of very reasonable macroeconomic policies, it is unlikely that the region will be faced with a Greece-like situation. Moreover, most countries in the region are under a flexible exchange rate regime, and this will facilitate any possible required adjustment. Import prices will increase in real terms, but exports will become more competitive, thus reducing the impact of deteriorating terms of trade on economic performance. Under those conditions, domestic activity, including in manufacturing will be able to compete more effectively. In sum, some countries may find themselves in difficulty, but the region may be able to adjust well to the more realistic new economic conditions of the world."

Editor's note: the above is a continuation of a Q&A published in the Feb. 3 issue of the Advisor.

Company News

Banco do Brasil Reports Lower Profit, Beats Estimates

Banco do Brasil on Tuesday reported a lower fourth-quarter profit as compared to the year before, but beat analysts' estimates after gaining market share and trimming expenses, Bloomberg News reported. Adjusted net income for Brasília-based Banco do Brasil, the region's largest bank by assets, declined to 3.03 billion reais ($1.77 billion), as compared to 3.7 billion reais for the same period a year earlier. The average estimate in a Bloomberg survey of 11 analysts was for adjusted net income of 2.6 billion reais. The bank's stock rose on the news. The bank's loans increased 20 percent, a quicker pace than the industry's average, and higher funding from demand deposits helped improve net interest margin, **Itaú BBA Securities** said Monday in a report. Banco do Brasil's increasing income also helped to offset a 656 million real loss from the bank's **Banco Votorantim** unit, which primarily handles vehicle loans. Banco Votorantim's average delinquency rate increased in December to 5.8 percent. CEO Aldemir Bendine said he expects Banco do Brasil's default rate to remain stable this year. The default rate at the end of December stood at 2.1 percent.

Bendine

File Photo: Brazilian Government.

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Featured Q&A

Continued from page 2

Brazil-Mexico auto deal since it was signed in 2002, a renegotiation seems likely. A most durable resolution, however, is nowhere in sight. Without broad economic reforms to increase competitiveness and constant political coordination among countries, economic integration in the region will remain limited."

Luis de la Calle, managing director at De la Calle, Madrazo, Mancera, S.C. and former undersecretary for international trade negotiations in Mexico's Economy Ministry: "Mexico's superior competitiveness on manufacturing vis-à-vis Brazil has become ever more apparent with the appreciation of the real. Manufacturing has been transformed by almost 20 years of trade opening under NAFTA and operations in Mexico are now as competitive as any in the world. Brazil has chosen a different path to protect its domestic production. With rising commodity prices, its economy experienced a virtuous cycle that may be coming to an end: GDP growth has now stalled, while inflation is apparent. Dilma Rousseff faces a significant challenge in light of the difficulties of implementing countercyclical measures in the presence of inflationary expectations and indexation of wages. Adhering (or backtracking) to international obligations under the agreement with Mexico for the auto sector will be an indication as to whether Rousseff and her cabinet are more like Fernando Henrique Cardoso or Cristina Kirchner."

> "Operations in Mexico are now as competitive as any in the world."
>
> — *Luis de la Calle*

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

WHAT'S KEEPING YOU UP AT NIGHT?

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