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## PORTFOLIO INVESTMENT STRATEGY

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## The Latin American Risk Review

- Argentina: Menem pulling strings from afar? Unlikely!
- Brazil: Some positive numbers give Lula something to sing about on the road.
- Mexico: The political parties start to return to their old constituencies
- Venezuela: Oil surge lifts growth prospects (and inflation)
- Peru: Scandals sink Toledo to new lows, if such was possible!

### ARGENTINA

These reports have constantly warned about the explosive social situation in Argentina irrespective of the impressive rebound in the economy. The so-called "piqueteros", unemployed and fellow travelers roaming the streets and roads with demonstrations, blockages and occupations, have increased their pressure exponentially in recent weeks. The authorities are trying to imply that former president Carlos Menem is behind the unrest with a view of destabilizing the Kirchner presidency and come back as the providential savior. Although one cannot rule out anything from the wily Levantine (who has created a new movement within Peronism from his legal exile in Chile), it is unlikely that such a scheme would succeed if there was no fertile ground for it. Unemployment is officially 14.4% but this is after deducting 5% of the work force which is on state-funded emergency programs. GDP grew by 9.8 % in the first 4 months, but the April figure, at 6.3%, was the first drop in the rate for nearly 2 years, and many expect it to fall further to no more than 3% by the second semester. The authorities are expecting 6% growth for the full year.

There is criticism against Kirchner for not having used the upswing for any reforms, though it is not clear what he could realistically have done in the circumstances. He stood up well to pressure by the Duhalde faction to share more revenue with the provinces, but the security situation continues to be a major headache and an end to the recovery will definitely not help. There is also little likelihood of a further review of the debt offer, beyond the odd detail, even though bondholders were lukewarm, to say the least. The statement by the IMF that it was "standing aside" in the matter, should be interpreted as an indication that it considers the country's offer as sufficient,

### BRAZIL

President Lula da Silva led a team of nine ministers on a US visit last week, during which they had, not only praise heaped over their country's situation and prospects by the likes of the IMF and the

Secretary of the Treasury, but could also show (very conveniently) improved figures. Not only does trade continue to do well (5 months' surplus up 40% at US\$ 11.24 bn), but May unemployment fell to 12.2% and was 0.6 points below the year-ago level. Last month's fiscal results, though not as miraculous as March and April, were still encouraging. The 5-month primary surplus was up a modest 3.5 % at some US\$ 12 bn, but a 20.5 % lower interest bill (US\$ 16.5 bn) meant that it could be covered at 73.6% rather than the previous 50% to 55%. After an initial Senate setback, the administration also managed to pass a lower increase in the minimum wage (to US\$ 83 per month) than many populist representatives wanted.

"The worst is over" said Lula to New York investors. A dangerous sentence, previously used by a (still) famous Wall St. analyst about Argentina a few weeks before the place collapsed. Though Brazil may not be about to collapse, and the statistics are encouraging, there is still enough to be very cautious about. The improvement in overall fiscal accounts is due to previous falls in interest rates, which are unlikely to continue, and if reversed, could be crippling. Despite the fall, the interest bill is still running at US\$ 40 bn a year. The devaluation of the Real has added 2 % to the public debt (totaling US\$ 300 bn) in May alone. That month, no less than US\$ 13 bn of securitised debt matured, but the authorities could only roll over 2.8 bn. No less than US\$ 100 bn (ponder that figure!) of Brazil's public debt matures in the next 12 months. On the growth front, despite the overall statistics, incomes were down in May for the 15th month running. The average interest rate for consumers was still running at 142%. How long can you continue to buy on credit at such a cost if your income is actually falling? The president was booed at the wake of the late Lionel Brizola, a stalwart historical leader of Brazil's left who passed away recently, and his positive approval rate is down to 29.4% from the 56.6% of 18 months ago.

It will take more than a few employment and fiscal swallows to remove the risks and uncertainties still associated with Brazil. Lula is no fool, as he hedged his bets by also declaring that his administration "could not correct in 4 years the mistakes of 500 years".

## CHILE

Whereas the debate is barely starting on whether there is high-level corruption in Chile (there is, but the culprits are as good as hiding their tracks as the pirates of old in the Caribbean hid their treasures on deserted islands), a new front has opened. The genuinely low-level of micro-corruption in the public service seems to be increasing exponentially. The past few weeks alone have seen the revelation of misdeeds by the office issuing identity cards, the judicial system, the uniformed police, prison guards and hospital services. Of course, you will not read about any of this in the international press, who are too busy interviewing the same mantra-reciting Chicago boys, robber-baron businessmen and blinkered Wall St. analysts, all of whom continue to take their cue on the subject from the ratings of the infamous Transparency International.

The minimum wage has been increased by 3.8% to the monthly equivalent of US\$ 190. The increase is nearly three times the rate of inflation, and makes the Chilean wage arguably the highest in the region. This should continue to fuel the consumer boom, though there is a limit to how much you can afford to borrow, even at low interest rates (May retail sales were up just 3% on a year earlier, but bank consumer loans 18% higher over the same period. Case proven). Higher VAT and copper revenues are likely to produce the first fiscal surplus since 1998. On the election front, preparations are accelerating for the October municipal polls, and a strong outsider as ruling coalition candidate, former president Eduardo Frei, may be out of the 2005 presidential race for health reasons. Defense minister Michele Bachelet is still leading a field of eight official hopefuls, and consequently her portfolio is getting the full blast of the efforts by sole Rightist candidate Joaquin Lavín.

## COLOMBIA

President Uribe's bid at having the principle of (his) reelection voted by Congress appears to have succeeded, and he has become cockier recently. The murder of 34 coca-leaf growers by the FARC guerrillas attracted his ire about "do-gooders who only criticized paramilitary violence but not that of the Left". Facing him will be, among others, former Bogota Mayor Antanas Mockus, who has already had one bid at the presidency, and is mainly known for his eccentricity (he once bared his bottom at protesting students when he was university dean, and got married on top of an elephant with a rabbi and a priest jointly officiating). Though the economy may end 2004 with growth slightly below 4 %, that level is the official long-term target for the 2005-2014 decade. The fiscal deficit is running at 2.5 % of GDP with little prospect of significant improvement next year.

## MEXICO

There are a number of important regional and local elections in coming weeks, which are generally expected to further boost the PRI's standing at the cost of a wilting ruling party and lame-duck administration. The events of recent months have pushed both the PAN and the leftist PRD closer to their traditional power bases, after earlier moves to occupy the center. The latter has now opened up for its traditional PRI occupier again. Mexico City's PRD mayor now has to cope with a new grass-root movement against insecurity, which has taken a leaf from its Argentine equivalent (though the problem in Mexico is neither new, and in fact worse than Argentina's, and nor confined to the capital). The economy continues to tick over at a better rate (official GDP forecasts for 2004 are now for 4%, with April activity at 4.2%), but the impact on jobs has yet to be seen. PEMEX continues to pump oil at a high rate, which many think could end up damaging some wells and shortening their productive life spans. The foreign ministry claims that there are negotiations with China towards directing up to 30 million Chinese tourists to Mexico by 2010 (total visitors from everywhere now number 20 million), as a way of compensating the increasing competition on the industrial front.

## PERU

With his administration crumbling around him, president Toledo announced he was going to Israel soon. This gave a field day to the campaign against his Belgian-Jewish wife, which had been gathering strength not least due to her own peculiarities. The whole thing has strong anti-Semitic overtones, with a leading paper publishing a list of Toledo's "Jewish circle" (a number of people of that faith close to him, in both the public and private sectors). There was also comic relief with the resignation of the agriculture minister whose son was found to be running a brothel where under-age girls were working. The economy grew by a slower 3.3% in April, but May unemployment in Lima was at its lowest level of the year, and trade figures continue stupendous. The Finance Minister maintained a full-year growth forecast of 4.5 to 5%. Even fiscal results, which have been worrying some, are on the mend with an overall surplus in May for the Central Government. Sendero Luminoso has been flexing its muscles again, and the US\$ 12 million reportedly being paid to a US "image" firm to boost the president's (domestic) popularity may be urgently needed.

## VENEZUELA

The betting is wide open on whether the recall referendum will actually take place on the new date of August 15 and if so, what would the consequences be. A four-day delay would prevent new elections with Chavez's own appointed vice-president stepping into his nominal shoes. If he is defeated, the opposition has neither candidate nor policy behind which to unite, and subject to a constitutional interpretation, Chavez may be able to stand again, and even win. If he wins outright, his ego and boasting will most likely be insufferable. He has been stacking cards in his favor by registering illegal Colombian immigrants on the electoral roll, and allowing the military, generally sympathetic to him, the right to vote. Fuelled by the high price of oil, the economy is officially estimated to have grown by up

to 15% in the second quarter, with the full year outcome ending at between 10-12% according to the Central Bank. This should put the country at the top of the regional league, though it unfortunately holds the same post for inflation too.

#### SMALLER COUNTRIES

In **Bolivia**, with the referendum questions far from attracting enthusiasm, there is now a wrangle over whether its results will be binding. Three ministers have resigned in **Ecuador**, though president Gutierrez has bought himself a reprieve by moving closer to the Right. **Paraguay's** troublesome plotter general Lino Oviedo has vowed to return soon and face the music, whilst suggesting that the population resort to direct action to ascertain their rights. **Uruguay** went through candidate-selection primaries on June 27 with a low turnout from the electorate.

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