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Latin America Advisor

The Interactive Forum for the Region's Leaders Thursday, August 29, 2002

Today's Top News

Advisor ANALYSIS

Q **Foreign banks are angered by proposed legislation in Argentina's Congress that would force them to cover deposits in their local units, postpone inflation indexation on loans, and delay asset seizure on errant debtors. Will the legislation be approved in the face of the bankers' fierce opposition? What will the banks do if it is approved? Will the International Monetary Fund (IMF) delay an agreement with Argentina until the dispute is resolved?**

A **Guest Commentary: Gustavo Casir:** "The approval by Congress of the legislation as described is, on the one hand, unlikely, but on the other hand difficult to predict in a country where common sense is the less common of senses. However, legislation delaying the application of an inflation index on bank loans (already approved by Congress but not yet promulgated by the Executive, thus not technically a law) and/or permitting the auctioning of delinquent debtors' assets is more likely. In any event, if any of these measures are approved by Congress, pressure from the financial sector (domestic and foreign), including the IMF, may result in the Executive exercising its veto power over such legislation. With respect to the effect of the aforementioned legislation on the negotiations with the IMF (even when the government can only reasonably expect a rescheduling of short-term loans), it may indeed delay a possible agreement like a weather forecast indicating rain throughout September."

Guest Commentary: Steve Hanke: "Argentine banks finally have got their dander up over proposals by Argentina's Congress to rob them, yet again. That's fine and dandy. But where were the banks in November 2001, when then-Economy Minister Domingo Cavallo took them to the cleaners with debt swaps? And where were the banks in January, when the loony Pesification project took a whopping $12.6 billion -- an amount that exceeded the total capital in the banking system at the time -- out of their vaults? Talk about being asleep at the wheel! In Argentina, where the sanctity of contracts and property rights floats in the wind, nothing is certain. However, one thing is certain: bad ideas

> "The Argentine government has sent the message that the bad guys in this play are the banks."
>
> -- Ricardo Seeber

*see **Q&A**, page 2 ...*

*... **Q&A**, from page 1*

have a long shelf life in Argentina. Consequently, some form of these nutty legislative proposals will end up going through the front door, if not the back door. The IMF should (and probably will) delay an agreement until some of the most egregious abuses of the rule of law are removed or mitigated, however. Glenn Hubbard, the chairman of President George W. Bush's Council of Economic Advisors, recently wrote that 'the rule of law is an essential underpinning of growth.' And his remarks were pointedly aimed at Buenos Aires."

Guest Commentary: Ricardo Seeber: "The legislation will be approved. It is a direct consequence of the erratic economic policies adopted by the Administration of President Eduardo Duhalde. The only goal Duhalde had in mind when taking office was to 'terminate the model' by means of a devaluation. After that, not even the appointed economic teams have known how to handle the crisis. It seems that the Administration's absolutely naive expectation was that the IMF, the U.S. government, and the rest of the world would help Argentina by remitting fresh funds. The Argentine government has sent the message that the bad guys in this play are the banks and not the government, which devalued the Peso and declared the default. So far, this proposed legislation has not provoked any reaction, at least publicly, from the banks. It is important to consider that the banks' traditional activities -- to take deposits and then loan them to customers -- these days no longer exists. Although some money has been deposited into the banks, it is not in an amount that could lead me to conclude that confidence in the economy and in the banks has been restored. It appears that the IMF will delay an agreement with Argentina, not only because of this proposed legislation, but also because Argentina has not offered a reasonable and realistic economic plan. Today, the country is a real mess and the government does not contribute at all to creating confidence. It has no leadership and issues contradictory legislation. The only purpose is, apparently, not to fall into hyperinflation and to reach the presidential election scheduled for March 2003."

Gustavo Casir is Partner at Muñoz de Toro & Muñoz de Toro in Buenos Aires.

Steve Hanke is Professor of Applied Economics at The Johns Hopkins University.

Ricardo Seeber is Senior Partner on the Corporate Team at Estudio Beccar Varela in Buenos Aires.

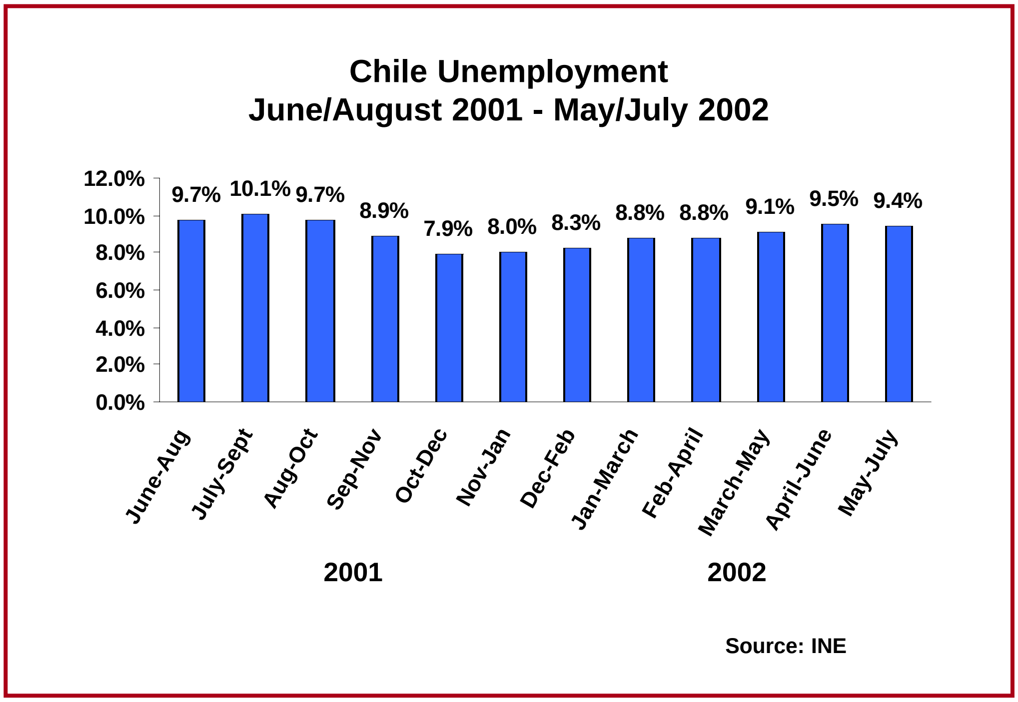
Economic News

Brazil's Central Bank Adjusts 2002-2003 Inflation Forecasts Due to Weaker Real

Brazil's Central Bank on Wednesday said it adjusted inflation projections for this year and 2003 given the depreciation of the Brazil Real since the last meeting of its monetary policy committee (COPOM) in July. The Bank forecasts inflation of over 6 percent in 2002 compared to the target of 5.5 percent it established last month, according to the minutes of COPOM's August 20-21 monthly meeting. However, projected inflation for 2003 should fall below the Bank's 4 percent target, as most of the impact of the currency's depreciation on inflation will take place this year. The Real has lost approximately 26 percent of its value against the Dollar since January. Last week, the Central Bank unanimously voted to keep Brazil's benchmark interest rate at 18.5 percent to stem inflationary pressures. However, the Bank changed its bias from 'neutral' to 'downward,' meaning it can lower rates before COPOM's next monthly meeting September 17-18. COPOM attributed weak economic activity in the first half and start of the second half of this year to deteriorating expectations given an unfavorable external environment and an increase in uncertainty over Brazil's October 6 presidential election. In other Brazil news, a CNT/Sensus poll published yesterday confirmed a decline in support for opposition candidate Ciro Gomes of the Labor Front coalition. According to the poll, taken August 24-26, voter support for the second-place Gomes fell to 25.5 percent from 28.6 percent in the previous poll. A poll released Tuesday by Vox Populi showed Gomes' support slipping 7 points to 25 percent, while Ibope had Gomes falling from five points to 21 percent. All three polls also recorded gains by government candidate José Serra, who remains in third place. Opposition Workers' Party candidate Luiz Inácio "Lula" da Silva is the frontrunner in all polls with over 30 percent support.

Chilean Government Surprised by May-July 9.4 Percent Jobless Rate

Unemployment in Chile reached 9.4 percent in the three months to July, down 0.1 percent from the April-June period, and up 0.5 percent from the same period last year, the government's national statistics institute (INE) said Wednesday. The improvement in Chile's jobless rate during the country's winter months surprised the government, prompting Finance Minister Nicolás Eyzaguirre to say that the prospect for double-digit unemployment in the upcoming months appears more distant. The number of unemployed reached 551,690, in the May-July period, a 3.2 percent decline from a year ago. Year-on-year, employment grew the most in the service, electricity, and gas sector (15.7 percent), followed by transport, food storage, and communications (5.3 percent). Employment declined in mining and quarrying (-2.7 percent) and in the social and community services sector (-1.8 percent). In other economic news, industrial manufacturing rose 8.6 percent year-on-year in July, in part due to two more working days in July of this year versus the same month in 2001.



Company News

Telecom Italia Set to Clear Hurdle to Offer Mobile Service in Brazil

Italian telecommunications giant **Telecom Italia** said Wednesday it had reached an agreement to reduce its indirect stake in Brazilian fixed-line operator **Brasil Telecom**, allowing Telecom Italia to begin offering mobile services across Brazil. Telecom Italia said it would lower its 37.29 percent stake in **Solpart Participações**, which indirectly controls Brasil Telecom, to 19 percent, according to a company statement. Telecom Italia plans to sell the 18.29 percent stake to **Timepart Participações** and **Techold Participações** for $47,000, a price which one source cited by Reuters described as "symbolic." The source said Telecom Italia would raise its stake in Brasil Telecom again later. With Telecom Italia's stake in Brasil Telecom under 20 percent, the threshold established by telecom regulators, the company's mobile unit **Telecom Italia Mobile** could offer service across Brazil once it meets mandatory service targets. Telecom Italia said it would hold onto its 38 percent stake in Solpart's privileged shares. Last year the Italian company spent over $1 billion on three regional mobile licenses in an effort to become Brazil's first nationwide wireless operator.

Mexico's Unefon Seeking to Restructure $350 Million Debt

Mexican mobile company **Unefon** said Wednesday it is seeking to restructure a $350 million debt with Canada's **Nortel Networks**, according to Reuters. Unefon says it can pay the debt in full, but wants to restructure to capture lower interest rates. The news follows an announcement Monday by Mexico's number two broadcaster, **TV Azteca**, that its board had approved spinning off Unefon and walking away from its $250 million investment. "After an extensive market survey to study initiatives to maximize value from our Unefon investment, the board concluded that a distribution of Unefon shares is a superior option for a spin-off of the company," CEO Pedro Padilla said in a statement. TV Azteca said its shareholders will receive a distribution of about 0.37 Unefon shares for every TV Azteca CPO, its locally-traded stock, or about 5.88 Unefon shares for each American Depositary Receipt, before the end of the year. Unefon shareholders will vote on the spin-off in September. **Azteca**

Holdings, which owns the majority of TV Azteca voting stock, has said it favors the move. The broadcaster said that payment of the proposed distribution would cut its assets and shareholders' equity by $176 million and that it would be subject to a $80 million financing support agreement granted to Unefon in July 2001. TV Azteca will also remain subject to a $35 million commitment to support Unefon through 2002.

AES Colombian Unit Granted Extension on Debt Repayment

Colombian hydroelectric generation company **Chivor**, a unit of U.S. power giant **AES Corp.**, said it was granted an extension until December 2006 to pay off a $330 million loan as it undertakes a bankruptcy restructuring, according to a statement it submitted to Colombia's securities superintendency, Bloomberg News reported. Chivor defaulted in December on a final payment of a $400 million syndicated loan obtained in 1996 to finance the company's purchase by Chile's **Gener**. AES acquired Gener last year. Chivor listed $588.6 million in assets and $349.3 million in liabilities in its bankruptcy filing. Earlier this week, Brazil's **Eletropaulo Metropolitana**, also controlled by AES, paid part of a $225 million syndicated loan owed to **JP Morgan Chase** and other banks and extended the payment on the rest of the debt.

Political News

Paraguay Most Corrupt Latin American Country - Report

Paraguay ranked as the most corrupt Latin American nation, according to a report published Wednesday by **Transparency International** (TI). The Berlin, Germany-based group's "Corruption Perceptions Index 2002," covering 102 countries, placed Chile as the 17th least corrupt, one notch above the U.S. Argentina ranked 70th, while Brazil and Peru placed 45th and Mexico and Colombia tied for 57th place. "In parts of South America, the graft and misrule of political elites have drained confidence in the democratic structures that emerged after the end of military rule," said TI Chairman Peter Eigen. The report draws on 15 surveys from nine independent institutions. [Editors note: the full text of the report is available via http://www.transparency.org.]

Correction

A chart on Brazil in yesterday's issue of the *Latin America Advisor* mistakenly labeled current account figures as a percentage of GDP. In fact, the figures represented Brazil's current account in absolute terms, in $US billions. The *Advisor* regrets the error.

Latin America Advisor
is published daily by the
Inter-American Dialogue,
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Inter-American Dialogue
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