



Latin America: Financial decoupling, real concerns

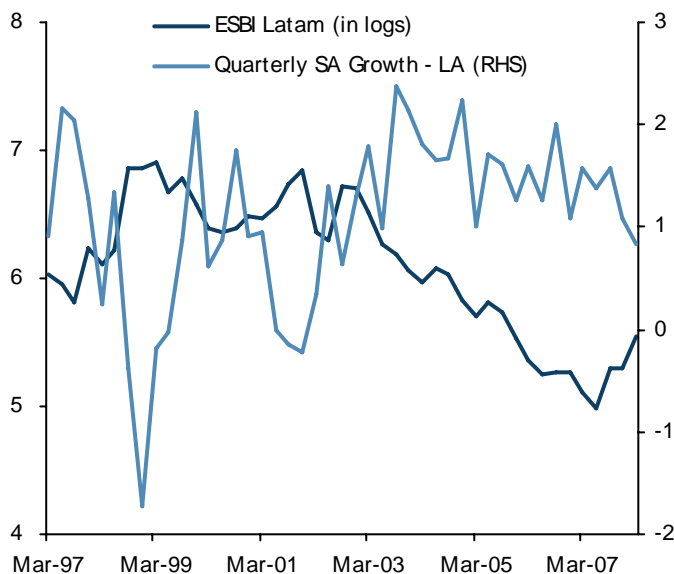
Eduardo Levy Yeyati

Latin American Research Team

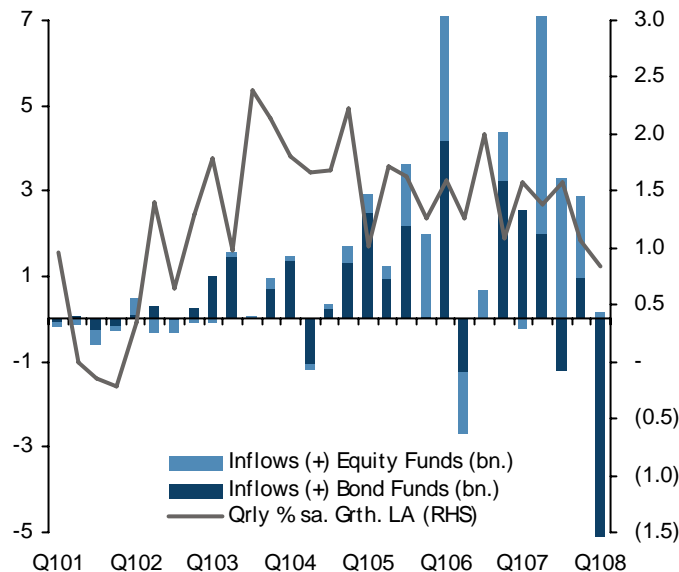
The real/financial channel: Decoupled...

- The decoupling of the real economy from financial shocks is a key structural change in EM in the 2000s...

Real channel: Not what it used to be...



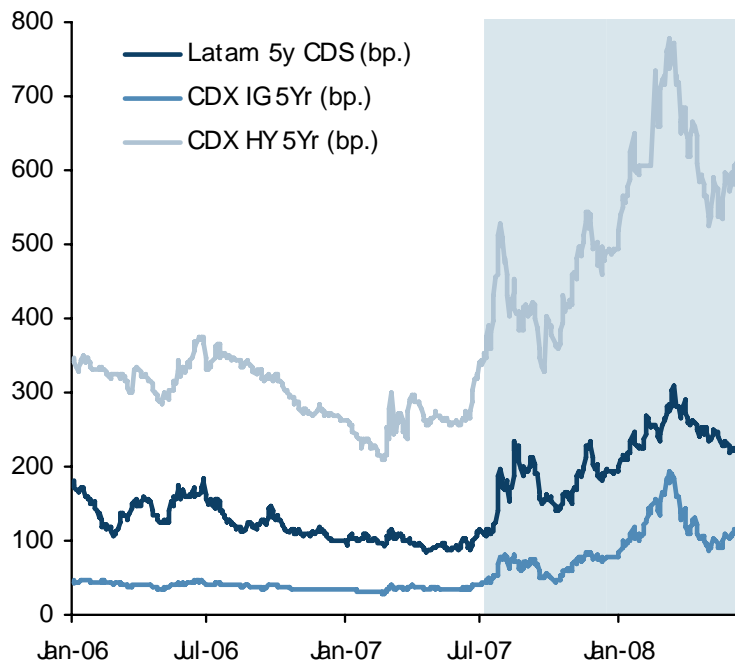
Growth less dependent on inflows



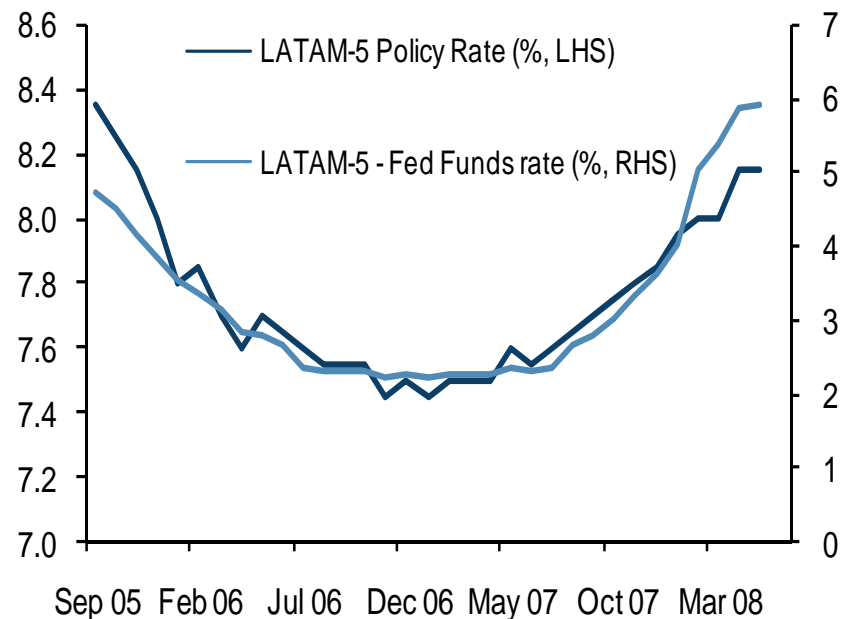
...and already permeating the financial channel

- ...that is already permeating into valuations.

EM Trying on investment grade shoes...



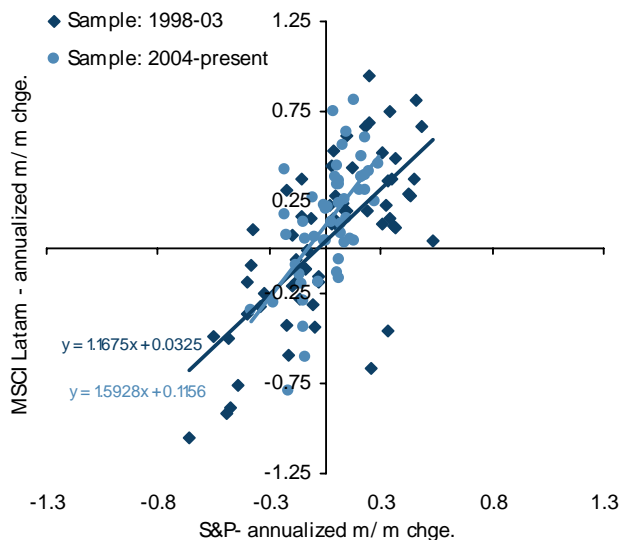
...and monetary autonomy



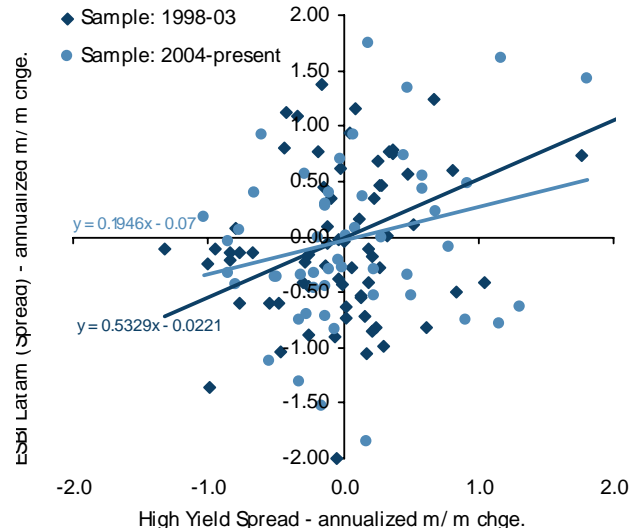
The financial channel: Still there?

- EM Equity remains very responsive to S&P sell offs (high betas), but credit and FX have been less responsive to core markets than in the 1990's (low betas)

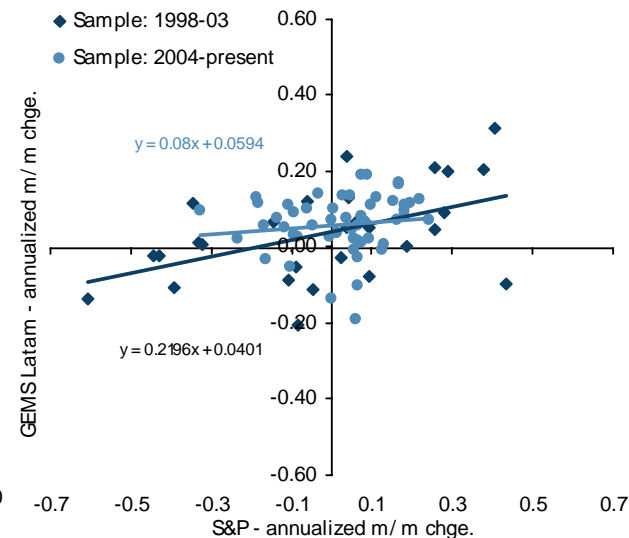
Financial channel: still strong in equities...



...less so in credit...



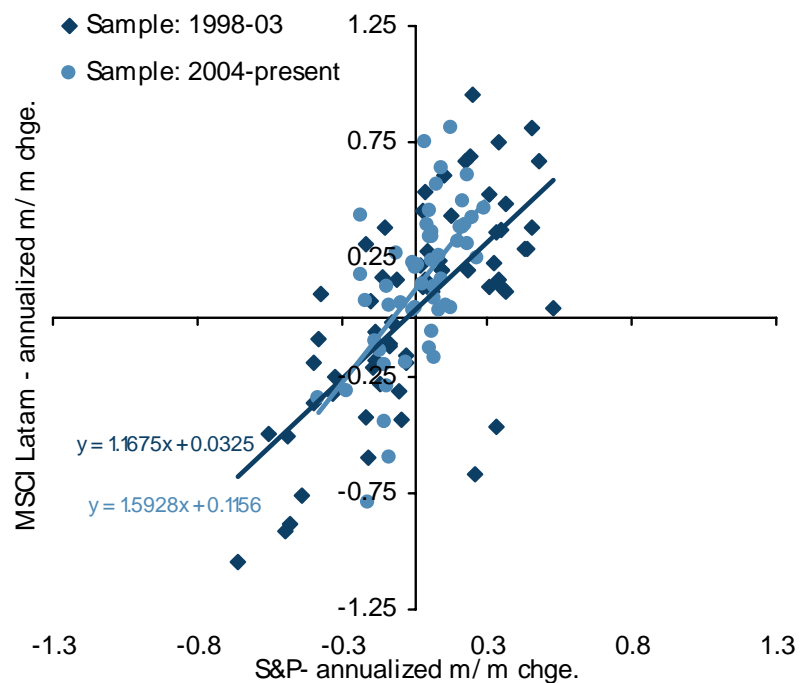
...and FX.



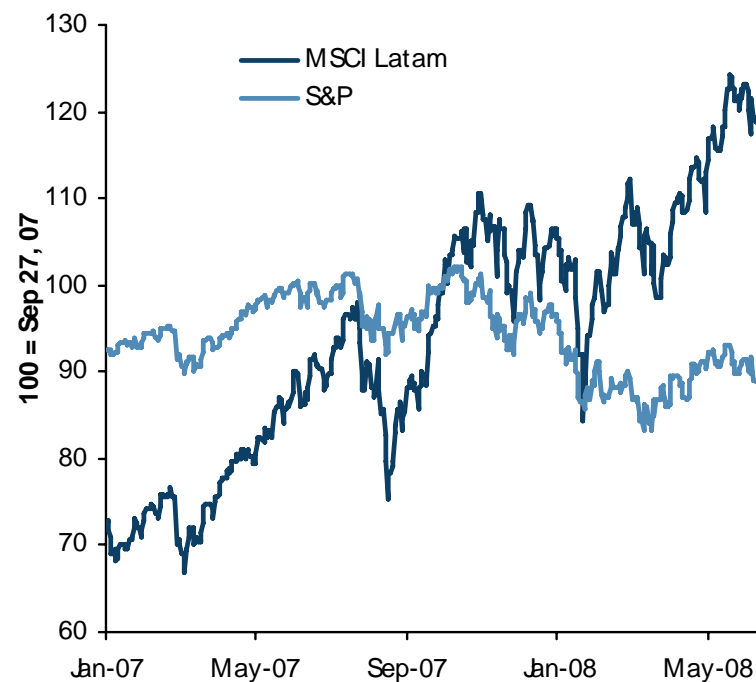
Still there? LatAm's slow divergence

- What do talk about when we talk about betas?

High-frequency correlation...



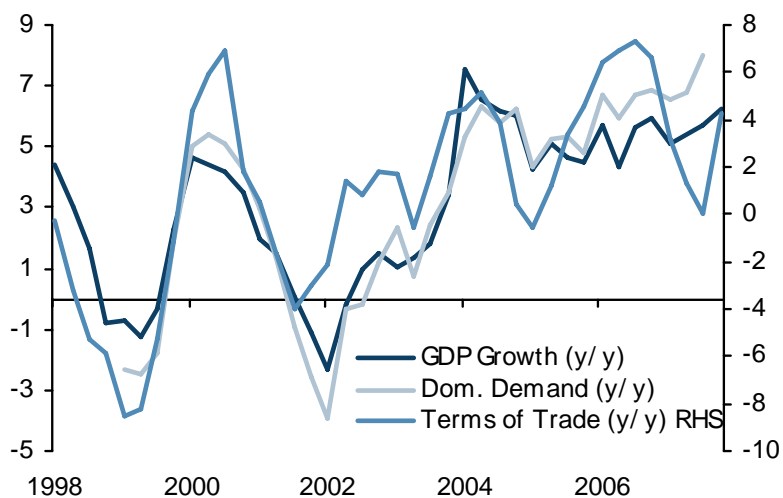
...low-frequency divergence



The real channel: Buying external slack...

- ...which could be wiped out by an (unlikely) decline in commodity prices

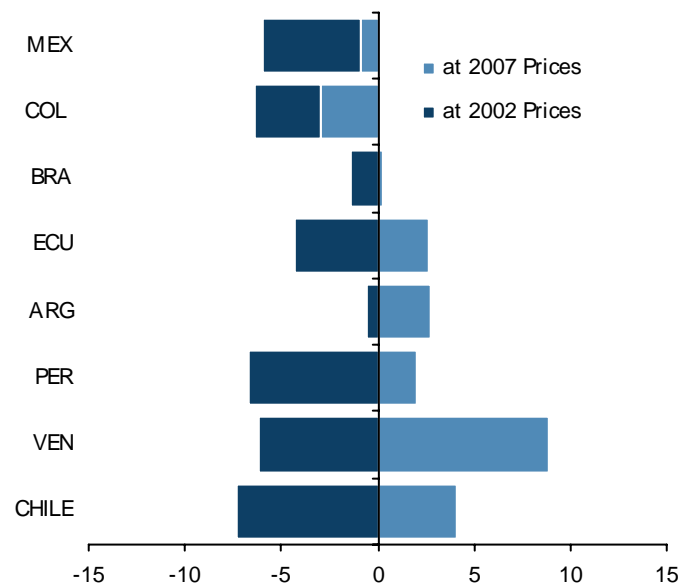
Growth and Terms of Trade



Note: PPP weighted.

Source: Haver Analytics, Barclays Capital

The Impact of Terms of Trade on the Current Account



Source: Barclays Capital



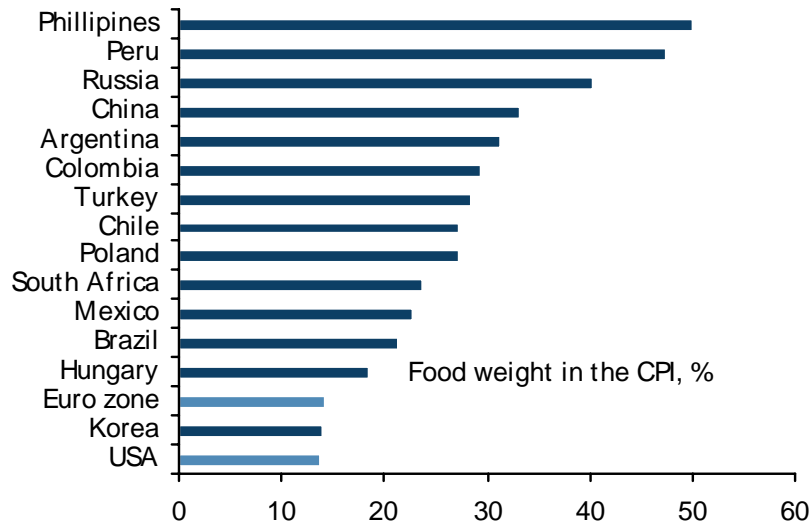
The curse of inflation targeters

Please read carefully the important disclosures at the end of this publication.

Food inflation: The talk of the town

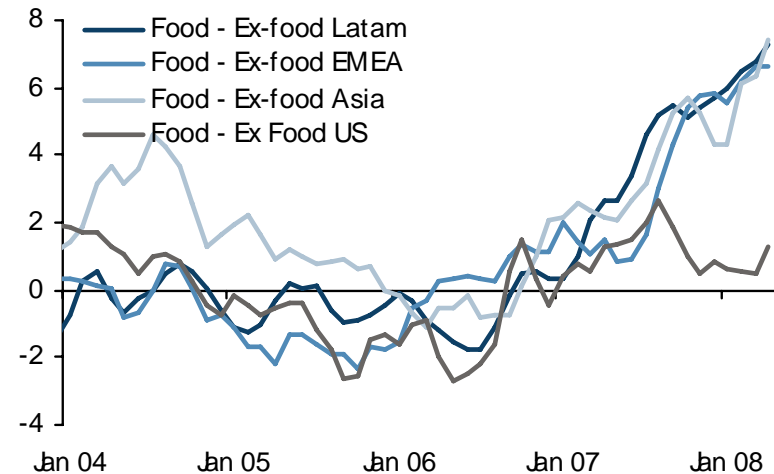
- The surge agricultural commodity prices affected EM disproportionately.
- Food has a higher weight in EM CPIs, and food prices increased relatively more in EM.

Food Is More Important for EM ...



Source: National authorities, CEIC, Barclays Capital

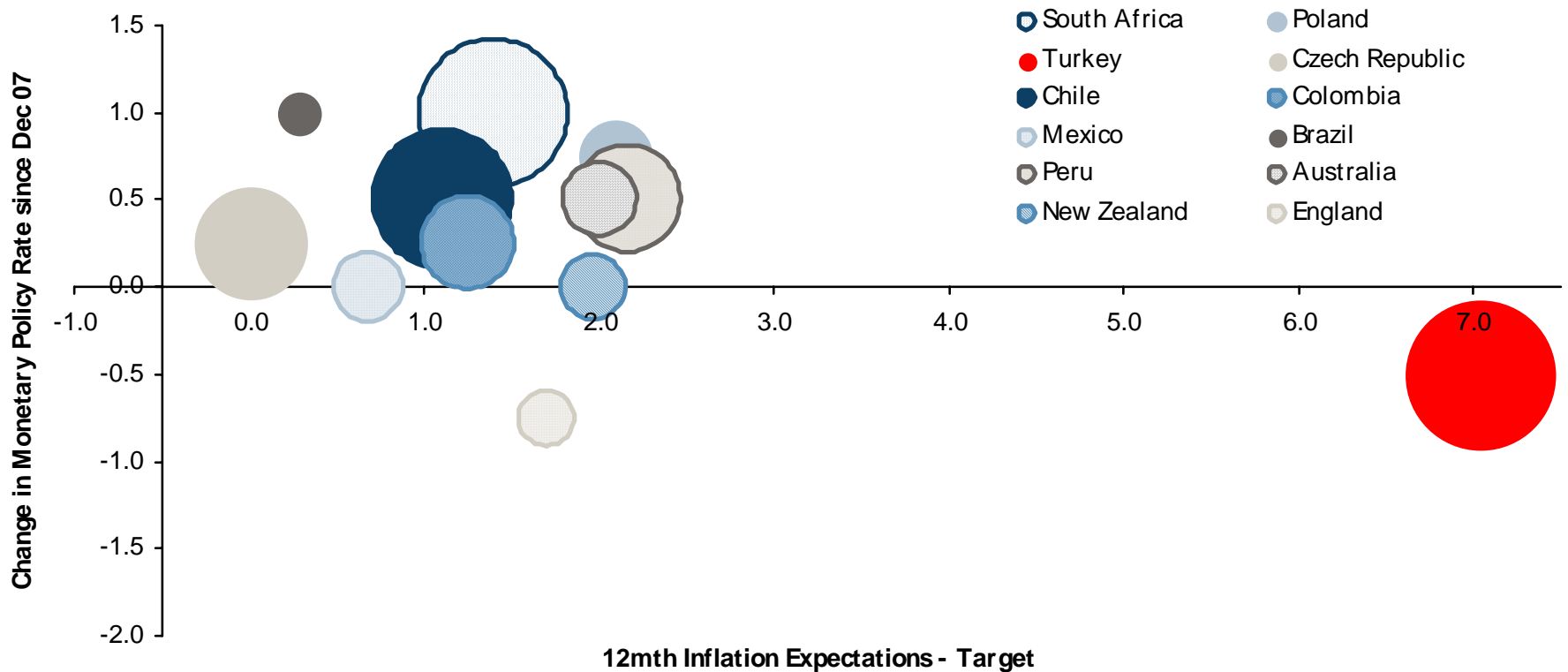
... and Increased Proportionately More



Source: Haver Analytics, Barclays Capital

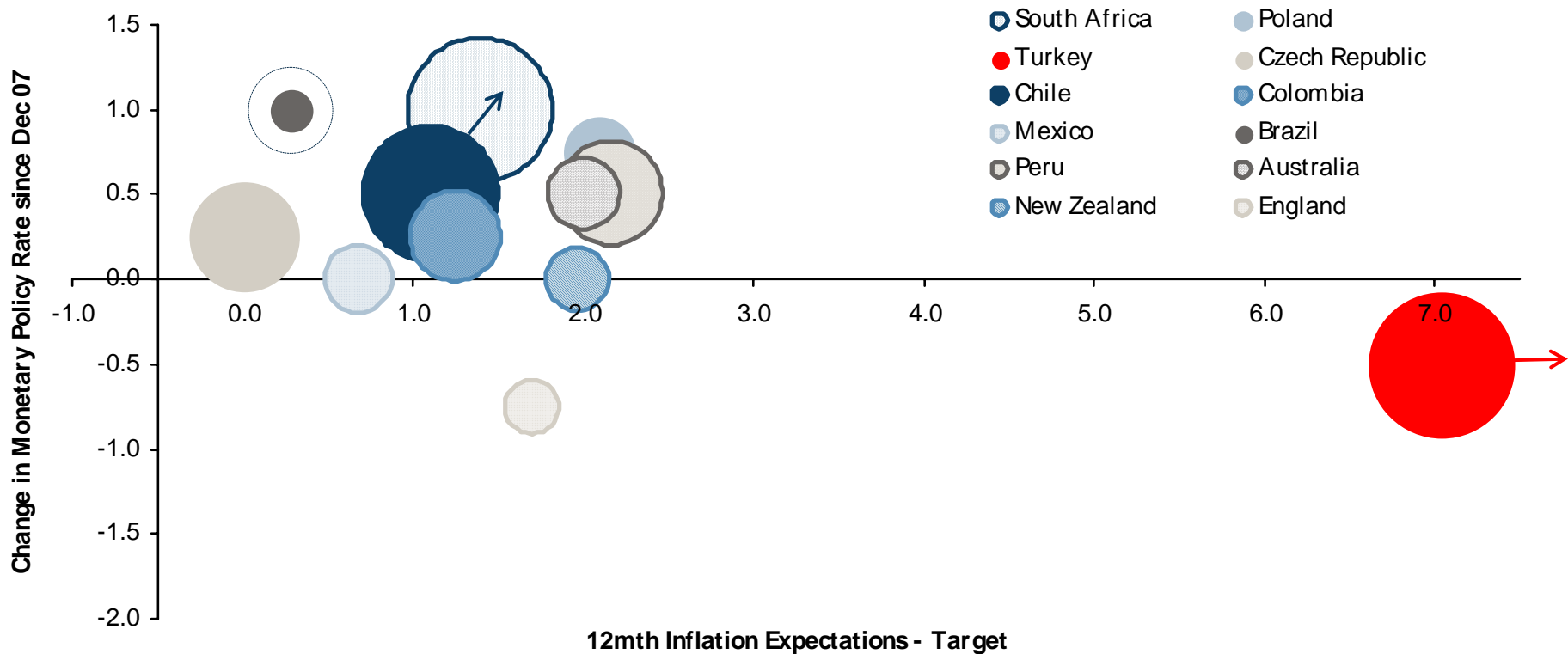
Hawks, Doves & Turkeys

- Central banks have responded to the problem in different ways (December 07 through June 5, 2008)...



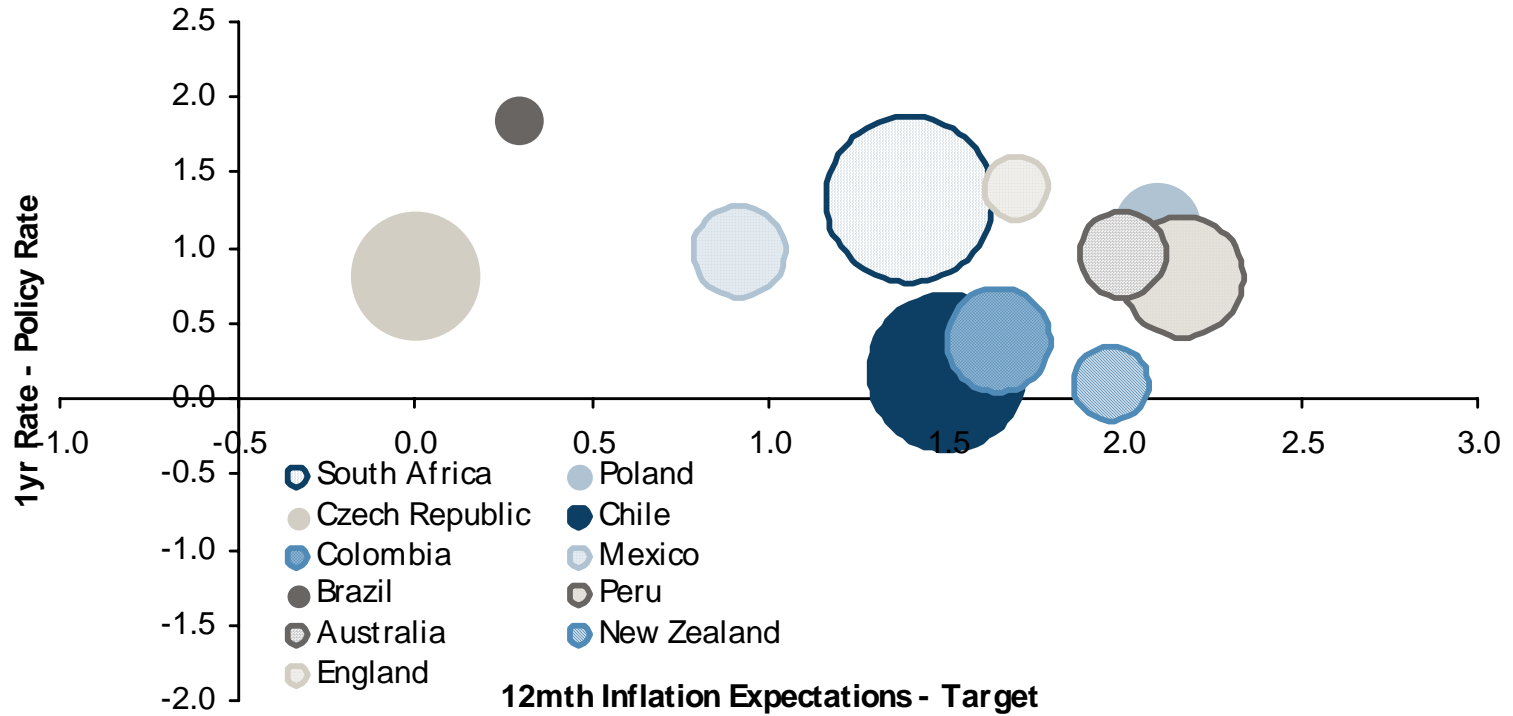
Hawks, Doves & Turkeys

- Central banks have responded to the problem in different ways (December 07 through June 10, 2008)...



Hawks, Doves & Turkeys

- ...and are perceived accordingly by the market (June 5, 2008)



Summing up

- Short-term challenge:
 - ▶ Monetary policy confronting food inflation again (in some countries, together with cyclical expansions), with risks of de-anchoring. Further tightening expected in Brazil, Chile, Mexico, and Peru, and (until recently) in Colombia.
 - ▶ IT prospects in an inflating world: Americanization (benign neglect); fiscalization (Chile) or outright overkill?
- Medium-term challenge: A dollar rebound and its effects on EM ToT and FX...

...a topic for a future talk



Gracias



Latin America Outlook

June 2008

Eduardo Levy Yeyati

Emerging Market Research, Latin America

Please read carefully the important disclosures at the end of this publication.

Disclaimer

The persons named as the authors of this report hereby certify that: (i) all of the views expressed in the research report accurately reflect the personal views of the authors about the subject securities and issuers; and (ii) no part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in the research report.

For disclosures on issuers in this report see: <https://ecommerce.barcap.com/research/cgi-bin/public/disclosuresSearch.pl>

Any reference to Barclays Capital includes its affiliates.

Barclays Capital does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that Barclays Capital may have a conflict of interest that could affect the objectivity of this report.

IRS Circular 230 Prepared Materials Disclaimer: Barclays Capital and its affiliates do not provide tax advice and nothing contained herein should be construed to be tax advice. Please be advised that any discussion of U.S. tax matters contained herein (including any attachments) (i) is not intended or written to be used, and cannot be used, by you for the purpose of avoiding U.S. tax-related penalties; and (ii) was written to support the promotion or marketing of the transactions or other matters addressed herein. Accordingly, you should seek advice based on your particular circumstances from an independent tax advisor.

This publication has been prepared by Barclays Capital, Inc., a US registered broker/dealer and member of the FINRA. This publication is provided to you for information purposes only. Prices shown in this publication are indicative and Barclays Capital is not offering to buy or sell or soliciting offers to buy or sell any financial instrument. Other than disclosures relating to Barclays Capital, the information contained in this publication has been obtained from sources that Barclays Capital knows to be reliable, but we do not represent or warrant that it is accurate or complete. The views in this publication are those of Barclays Capital and are subject to change, and Barclays Capital has no obligation to update its opinions or the information in this publication. Barclays Capital and its affiliates and their respective officers, directors, partners and employees, including persons involved in the preparation or issuance of this document, may from time to time act as manager, co-manager or underwriter of a public offering or otherwise, in the capacity of principal or agent, deal in, hold or act as market-makers or advisors, brokers or commercial and/or investment bankers in relation to the securities or related derivatives which are the subject of this publication.

Neither Barclays Capital, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this publication or its contents. The securities discussed in this publication may not be suitable for all investors. Barclays Capital recommends that investors independently evaluate each issuer, security or instrument discussed in this publication, and consult any independent advisors they believe necessary. The value of and income from any investment may fluctuate from day to day as a result of changes in relevant economic markets (including changes in market liquidity). The information in this publication is not intended to predict actual results, which may differ substantially from those reflected.

This communication is being made available in the UK and Europe to persons who are investment professionals as that term is defined in Article 19 of the Financial Services and Markets Act 2000 (Financial Promotion Order) 2005. It is directed at persons who have professional experience in matters relating to investments. The investments to which it relates are available only to such persons and will be entered into only with such persons. Barclays Capital - the investment banking division of Barclays Bank PLC, authorised and regulated by the Financial Services Authority ('FSA') and member of the London Stock Exchange.

Subject to the conditions of this publication as set out above, **ABSA CAPITAL**, the Investment Banking Division of ABSA Bank Limited, an authorised financial services provider (Registration No.: 1986/004794/06), is distributing this material in South Africa. Any South African person or entity wishing to effect a transaction in any security discussed herein should do so only by contacting a representative of ABSA Capital in South Africa, **ABSA TOWERS NORTH, 180 COMMISSIONER STREET, JOHANNESBURG, 2001. ABSA CAPITAL IS AN AFFILIATE OF BARCLAYS CAPITAL.**

Non-U.S. persons should contact and execute transactions through a Barclays Bank PLC branch or affiliate in their home jurisdiction unless local regulations permit otherwise.

Barclays Bank PLC Frankfurt Branch is distributing this material in Germany under the supervision of Bundesanstalt fuer Finanzdienstleistungsaufsicht.

ã Copyright Barclays Bank PLC (2008). All rights reserved. No part of this publication may be reproduced in any manner without the prior written permission of Barclays Capital or any of its affiliates. Barclays Bank PLC is registered in England No. 1026167. Registered office 1 Churchill Place, London, E14 5HP.

Additional information regarding this publication will be furnished upon request. [080129USD]

US10016

Latin America: Financial decoupling, real concerns

Eduardo Levy Yeyati

Latin American Research Team