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# Capital Flows to Latin America

## First Quarter 2006



UNITED NATIONS



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## CAPITAL FLOWS TO LATIN AMERICA First Quarter 2006\*

Asset prices in emerging markets rallied to record highs in the first quarter of 2006, with bonds and equities posting strong performances on top of already remarkable 2005 gains. Spreads on dollar-denominated bonds issued by Latin American borrowers tightened by 68 basis points in the first quarter of the year, according to the Latin component of J.P. Morgan's EMBI+ index, while the Morgan Stanley Capital International (MSCI) for Latin America, an indicator of stocks' performance, increased by 15%.

Emerging and Latin American markets continued to be supported by active debt management in the first quarter of 2006, as countries continued to take advantage of the favorable external environment. Brazil, Colombia and Venezuela announced buybacks during the quarter, with up to US\$25 billion of bonds to be retired from the market. A large part of the buybacks concentrated on Brady bonds (US\$6.6 billion for Brazil and US\$3.9 billion for Venezuela).

In the first quarter of 2006, new Latin American debt issuance amounted to US\$15 billion, its highest level since the first quarter of 2000. Capital inflows remained strong during the quarter, and interest in local markets continued to grow. In the near future, Latin America's external debt should be supported by strong demand and by a diminishing supply of foreign currency-denominated bonds resulting from the region's low financing needs for the rest of the year, and its increasing focus on local currency issuance.

Investors' interest in emerging markets assets has been a result of their perception that emerging market countries' fundamentals are strong. Improvements in emerging markets' external positions in recent years, as well as solid fiscal and monetary policies, are credited to have increased resilience to shocks. However, improvement in fundamentals alone cannot fully explain why investor demand for emerging markets assets has been so intense. Risk appetite seems to be as important as fundamentals in explaining investors' enthusiasm, and it has helped to drive spreads to their current low levels. In the first quarter of 2006, global liquidity contributed not only to lower emerging market spreads, but also to lower high-yield spreads. While in the second half of 2005 the correlation between emerging and high-yield spreads turned negative, it turned positive again in early 2006 (0.8), as global conditions benefited both asset classes (Chart 1).

**Chart 1:  
High Yield vs EM Spreads  
January 2005 - March 2006**



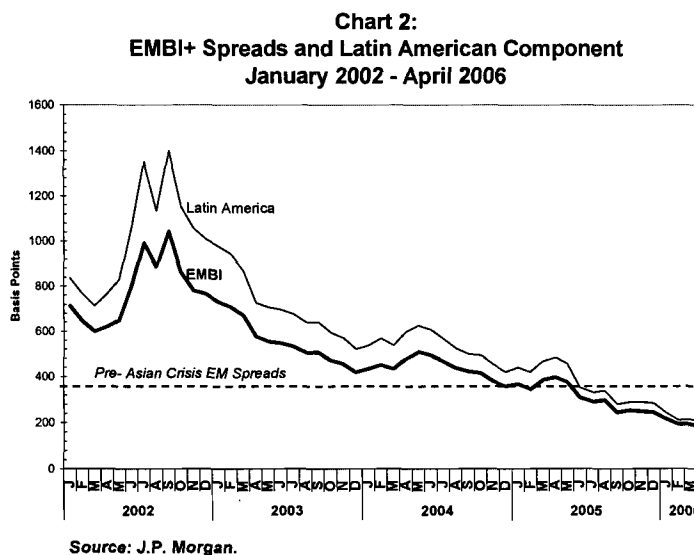
Source: ECLAC, on the basis of data from Merrill Lynch's U.S. High-Yield Master II Index (H0A0), and JP Morgan Chase's EMBI+.

\* This document has been prepared on the basis of market views and developments. All data and information are from market sources, unless otherwise noted.

This past May brought a hearty dose of volatility to financial markets. Uncertainty towards the global economic outlook amid rising interest rates prompted investors to abandon riskier markets around the world, and stocks in emerging markets plummeted as a result. The turbulence of the past few weeks was a wake-up call, showing that emerging markets could yet be derailed despite the improvements in local markets, the diversification of investment and the use of new instruments such as credit default swaps, which have helped to transfer and spread risk. Whether increased volatility may be an inflection point in emerging markets remains to be seen, however. It will be a test of the notion that things are different this time around for this traditionally volatile asset class.

## I. Bond Markets and Debt Management

The trend toward higher credit ratings of emerging market issuers in recent years has supported a significant compression in bond spreads since the latter part of 2002 (Chart 2). In the first quarter of 2006, emerging market bond spreads continued to drift near record low levels, as investors kept their enthusiasm about the asset class. Emerging market bond spreads, as measured by the J.P. Morgan EMBI+ index, tightened by 53 basis points in the first quarter of 2006, while the Latin American component narrowed by 68 basis points.



Part of the compression in emerging market spreads since 2002 is due to the interest from a broader class of investors, who are willing to commit to longer-term goals, making liability management programs more viable. Brazil, Colombia, Mexico and Venezuela announced debt buybacks in the first quarter. Brazil and Venezuela announced the retirement of all remaining Brady bonds totaling US\$6.6 and US\$ 3.9 billion, respectively. The buybacks are part of a more general trend of debt liability management in emerging markets aimed at reducing external vulnerabilities. Emerging market countries have also been paying down their debt to the international financial institutions (IFIs), as well as retiring Paris Club debt.

The buybacks of external debt and the payment of the debt to the IFIs have been contributing to a relative shortage of foreign currency-denominated emerging market bonds. Many Latin American countries have already reduced their ratio of public debt to GDP substantially, as well as the ratio of external debt to exports. In addition, increased remittances from overseas workers and higher commodity prices are contributing to make financing requirements more manageable for some Latin American countries.

The focus on buying back debt that has a shorter maturity, as well as the shift towards local market instruments, have reduced debt service, lengthened maturity and duration of external debt, reduced currency mismatches and increased liquidity in the local debt market, factors that have

helped to further improve fundamentals and creditworthiness. This is reflected on the continued trend towards better credit quality in the first quarter, with 11 positive and no negative actions taken by S&P and Moody's in Latin America, including rating upgrades for Venezuela, Brazil and Argentina, as well outlook upgrades for Uruguay, Ecuador, Colombia, and Paraguay (Box 1).

BOX 1: Credit Rating Actions in Latin America - Q1 2006	
<p>In the first quarter of 2006, there were no negative credit rating actions in Latin America. There were 7 positive credit rating actions by Standard &amp; Poor's and 3 by Moody's.</p>	
<p><b>January:</b></p> <ul style="list-style-type: none"> <li><b>Uruguay:</b> on January 9, S&amp;P raised the sovereign's credit outlook to positive, from stable, citing strong growth and a firmer currency—the latter easing debt repayment obligations. S&amp;P rate the sovereign as 'B'—two notches below investment grade, and suggest that further reductions in fiscal and external debt burdens will support improved creditworthiness.</li> <li><b>Jamaica:</b> on January 18, S&amp;P affirmed B rating, with a stable outlook.</li> <li><b>Ecuador:</b> on January 30, Moody's raised sovereign's credit outlook to positive, in light of the country's improved liquidity position and declining debt ratios. Its rating on foreign currency debt was reaffirmed at Caa1.</li> </ul>	
<p><b>February:</b></p> <ul style="list-style-type: none"> <li><b>Venezuela:</b> on February 3, S&amp;P raised the sovereign's credit rating to BB- from B+, citing the continuing sharp improvements in the nation's external and debt indicators. The upgrade leaves the rating three notches below investment grade.</li> <li><b>Colombia:</b> on February 22, S&amp;P revised its outlook on Colombia's long-term foreign and local currency sovereign debt to positive from stable on the strength of better economic prospects and improvements in the country's external indicators.</li> <li><b>Paraguay:</b> on February 27, S&amp;P affirmed Paraguay's rating and revised its outlook to positive, citing not only the country's improved economic and fiscal profile but also the leadership of President Nicanor Duarte Frutos in office since 2003, who has pushed through several economic reforms.</li> <li><b>Brazil:</b> on February 28, S&amp;P raised its long-term sovereign credit rating of Brazil to BB- from BB-. The outlook is stable. According to the press release, the upgrades based on the continued and marked improvement in Brazil's external debt indicators and active management of existing debt to reduce currency exposure. Brazil's net public sector external debt burden has moved much closer to that of other BB- peer credits and the upgrade places the country's sovereign debt two notches below investment grade, and is the highest that S&amp;P has ever assigned to the country.</li> </ul>	
<p><b>March:</b></p> <ul style="list-style-type: none"> <li><b>Colombia:</b> on March 9, Moody's raised the outlook on Colombia's sovereign external debt rating from negative to stable, noting the improvement in the country's external finances and the government's stability management operations, which have reduced the vulnerability to external shocks.</li> <li><b>Chile:</b> on March 21, Moody's placed Chile's external debt rating under review for a possible upgrade, citing that revenue from copper allows the country to reduce its debt.</li> <li><b>Argentina:</b> on March 23, S&amp;P raised the sovereign's debt rating to B- from B-, with a stable outlook. The agency said the upgrade reflects improved fiscal and external flexibility, an improved debt position and restructuring.</li> </ul>	

Emerging markets and Latin American new debt issuance were remarkably vigorous in the first quarter of 2006, amounting to US\$45.9 billion (compared with US\$31.4 billion in the first quarter of 2005) and US\$ 14.7 billion (compared to US\$11.2 in the first quarter of 2005), respectively, according to ECLAC's estimates on the basis of J.P. Morgan and Merrill Lynch data.

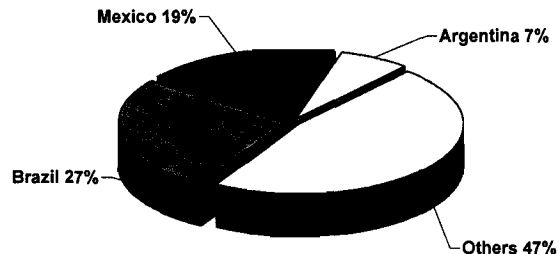
The volume of trade in emerging market debt instruments also hit a record in the first quarter of 2006, reaching US\$1.631 trillion and up 15% from a year ago according to the Emerging Markets Traders Association (EMTA), the highest level of turnover since EMTA started publishing quarterly surveys in 1997. This number represents an 18% jump in volume compared with US\$1.377 trillion in the fourth quarter of 2005.

The most commonly traded instruments included bonds from Brazil, Mexico and Argentina, with 27%, 19% and 7% of total trading. Brazil's, Mexico's and Argentina's debt instruments were the first, second and third most frequently traded instruments in the first quarter of 2006 (Chart 3).

Eurobonds and local markets accounted for 48% of the Survey volume each. The most frequently traded local instruments were issued by Mexico (US\$250 billion in trading), and Brazil (US\$133 billion).

**Chart 3:**  
**Q1 2006 Emerging Markets Debt Trading Volume: Country Shares**

Trade Volume in Q1 2006: US\$ 1.631 trillion



Source: EMTA

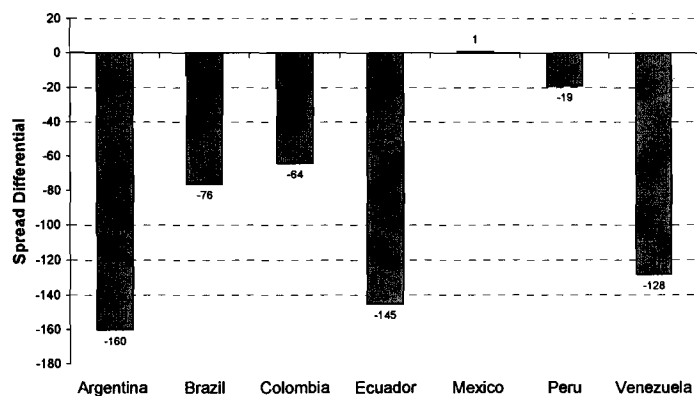
### A. Spreads

In the first quarter of 2006, the EMBI+ tightened by 53 basis points and its Latin American component by 68 basis points. Spreads tightened for all Latin American countries in our sample, with the exception of Mexico, where spreads remained roughly the same (Chart 4).<sup>1</sup>

On a monthly basis, Latin American spreads tightened in January and February, but widened in March for Brazil, Colombia, Mexico and Peru, due to country specific political factors, as well as increased volatility, led by rising core rates in the G-3 countries and crowded positions (Chart 5).

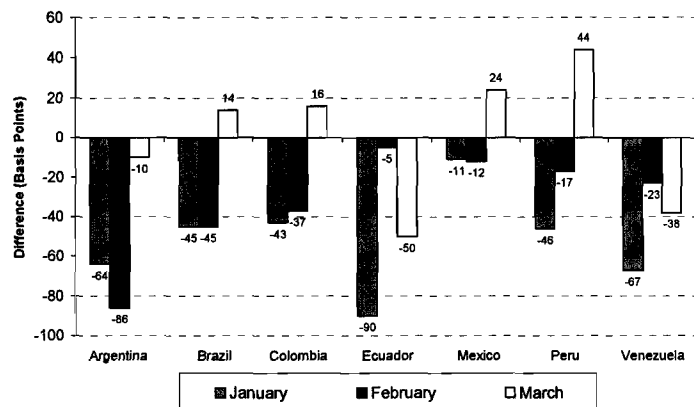
Argentina's spreads (according to the EMBI+) narrowed 160 bps in the first quarter of 2006, from 504 bps at the end of December 2005 to 344 bps at the end of March 2006. Spreads narrowed 30 bps more in April (Chart 6). After issuing US\$1.3 billion of Boden'12s to Venezuela earlier in the quarter, authorities initiated a process of diversifying the Treasury's refinancing away from the Boden'12, which was well received by the markets. In

**Chart 4:**  
**Spread Differentials Q1 2006**



Source: ECLAC, on the basis of data from JP Morgan.

**Chart 5:**  
**Monthly Spread Differentials January to March 2006**

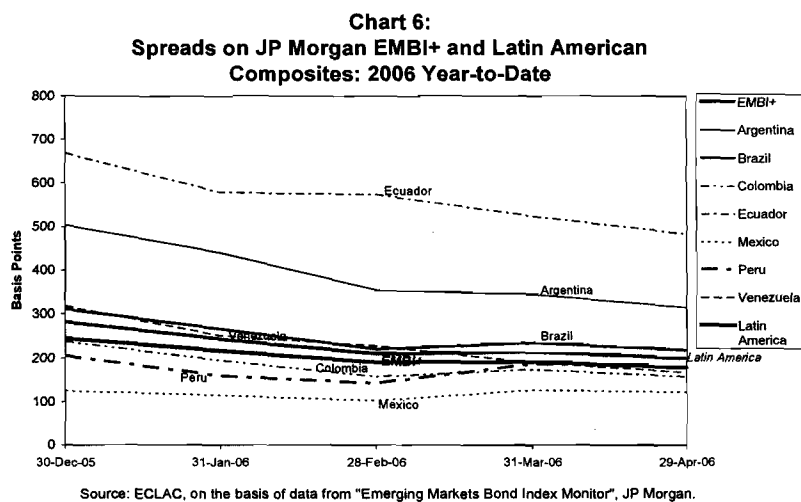


Source: ECLAC, on the basis of data from JP Morgan.

<sup>1</sup> See Appendix B, Table 3, for the evolution of the spreads of the EMBI Global Index, which also includes Chile and Uruguay in addition to the countries included in the EMBI+.

addition, inflation remained relatively stable during the quarter, supporting the trend toward lower spreads.

Brazilian spreads tightened 76 basis points in the first quarter, from 311 basis points at the end of December 2005 to 235 bps at the end of March 2006. A sudden change at the Finance Ministry led to increased volatility in March, but reassuring signals from the government indicating that low inflation and fiscal performance would remain a priority reaffirmed Brazil's benign macroeconomic outlook. Spreads tightened 17 bps in April as a result.



Colombian spreads fell from 238 basis points at the end of December 2005, to 174 bps at the end of March 2006, tightening 64 basis points. With President Uribe's poised to win reelection and a positive domestic backdrop, financial markets were calm. Spreads tightened an additional 17 bps in April.

Mexican spreads remained roughly the same in the first quarter of 2006, starting the quarter at 126 bps and ending it at 127 bps. Mexico's debt external outlook remained positive, and local markets improved. Political noise added to increased uncertainty in March. However, spreads tightened 5 bps in April, supported by strong fundamentals.

Spreads in Peru tightened 19 bps in the first quarter, from 206 basis points at the end of December 2006, to 187 basis points at the end of March 2006. Spreads widened in March as a result of election uncertainty, but fundamentals remained strong. Spreads tightened 6 basis points in April.

Finally, Venezuelan spreads narrowed by 128 basis points in the first quarter, from 318 bps at the end of December 2005, to 190 bps at the end of March 2006. Bond spreads were supported by high oil prices and abundant resources to cover Venezuela's financial needs and to reduce external debt. The government announced debt exchange operations during the quarter, and is set to improve its external debt profile. Spreads tightened further in April (23 bps), reflecting continuing improvement in Venezuela's external debt profile.

## B. Issuance

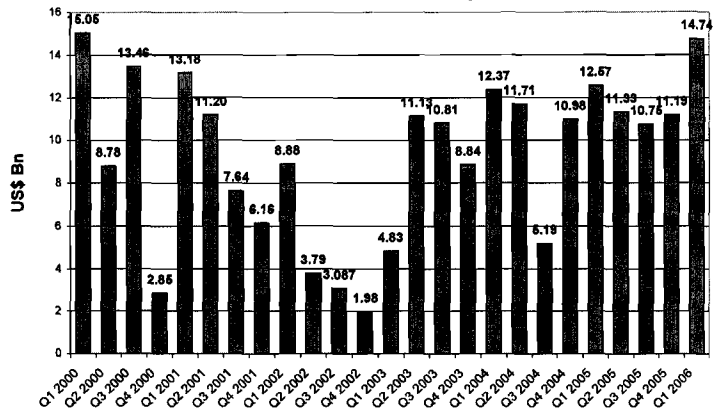
According to ECLAC's estimates based on J.P. Morgan data, emerging markets issuance in the first quarter of 2006 reached US\$45.9 billion. New issuance responded to favorable borrowing conditions and historically low yields, as well as to the improving quality of emerging markets credit. Latin American bond issuers placed a total of US\$14.7 billion in international capital markets in the first quarter, the highest level since the first quarter of 2000 (Chart 7).

The favorable borrowing conditions and improved debt structures in Latin American markets were reflected on the higher average maturity of the new debt issued during the quarter (Chart 8). Brazilian corporates issued three perpetual bonds in the first quarter, following the trend initiated in 2005. Perpetual bonds have no maturity date, thus are not redeemable, but pay a steady stream of interest forever. A perpetual bond offers a longer duration for investors seeking long-term investments.

Latin American issuance was the largest share of total emerging markets issuance (Chart 9). In January 2006, Uruguay closed its external financing gap after reopening its existing bond due in 2022, and Brazil's National Treasury released its Annual Financing Plan highlighting that about 85% of this year's external financing needs had already been met. The favorable global economic and financial environment has facilitated liability management operations on the part of key emerging market countries, including the refinancing of more expensive debt by less expensive money and the pre-financing of a large share of obligations due in 2006.

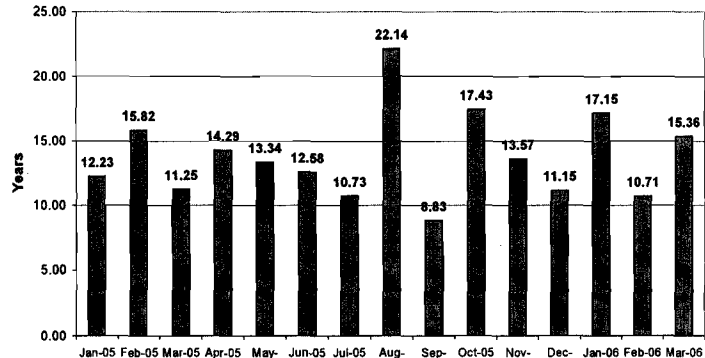
Latin American sovereigns issued significant amounts in the first quarter. Mexico issued US\$3 billion, Brazil US\$ 1.9 billion, Panama US\$1.4 billion, Uruguay US\$1 billion, Colombia US\$0.3 billion and Jamaica US\$0.25 billion (Appendix C). Sovereign issuance amounted to US\$8 billion or 54% of Latin American issuance in the first quarter, but corporate and bank issuance in Latin America was also strong, amounting to US\$7 billion, or 46% of total Latin American issuance in the quarter (Table 1).

**Chart 7:**  
**Latin American Issuance by Quarter**



Source: ECLAC, on the basis of data from Merrill Lynch and J.P.Morgan.

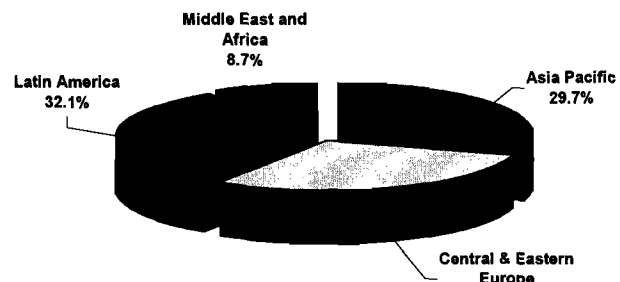
**Chart 8:**  
**New Latin American Debt Issuance: Average Maturity 2005 and 2006 YTD**



Source: ECLAC, on the basis of data from Merrill Lynch and J.P.Morgan.

Note: the May, June, July and September 2005, as well as January and February 2006 averages do not include the perpetual bonds issued by Brazilian entities.

**Chart 9:**  
**Emerging Markets Debt Issuance: Regional Breakdown 2006 Q1**



Note: Total emerging markets debt issuance for 2006 Q1 is US \$45.9 billion.

Source: ECLAC, on the basis of data from J.P.Morgan.



**Table 1**

Issuer Type Breakdown (% of Latin America's Total)	
Issuer Type	2006 Q1
Sovereign	54.3%
Corporate*	45.7%

\*Also includes bank issuance.

Source: ECLAC, with data from JP Morgan.

issued were denominated in dollars, 2.4% in euros, and 4.5% in Mexican and Colombian pesos (Table 2).

The share of local currency bonds in total Latin American debt in the first quarter was 4.5%. In the first quarter of 2006, 93% of the Latin American bonds

**Table 2**

Currency Breakdown (% of Latin America's Total)	
Currency	2006 Q1
Dollar	93.1%
Euro	2.4%
JPY	0.0%
Other*	4.5%

Source: ECLAC, with data from JP Morgan.

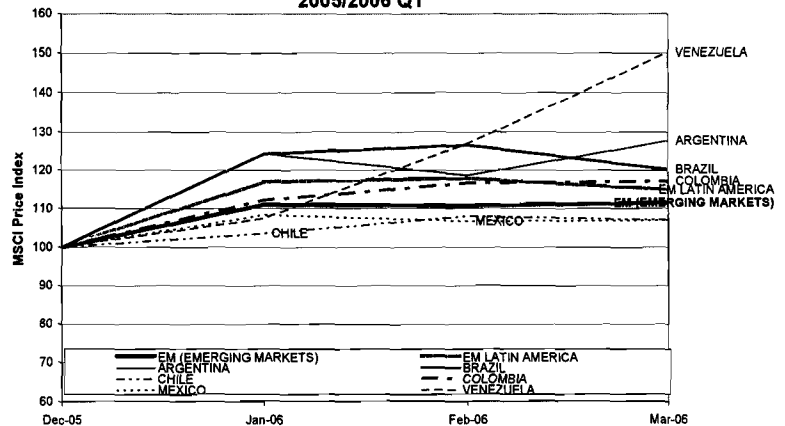
\* Issuance in Colombian and Mexican pesos.

Brazil and Mexico were among the top five issuers in emerging markets, ranking first and second, with amounts totaling US\$5.2 and US\$4.9 billion, respectively. The total amount issued by these two sovereigns represented 70% of the total Latin American issuance in the first quarter.

## II. Portfolio Equity Flows into Latin America

Latin American equity markets hit record highs in the first quarter of 2006 due to vigorous growth supported by a favorable external environment. According to the Morgan Stanley's MSCI (Morgan Stanley Capital International) Price Index, emerging market equity prices increased 11.5% in the first quarter. Latin American stock gained 14.9% in the quarter, compared to 1.8% a year ago and 2.7% in the previous quarter (Chart 10, Table 3). Venezuela showed the biggest gain in the quarter (50%), followed by Argentina (27.6%), Brazil (20.2%) and Colombia (17.1%).

**Chart 10:**  
MSCI Equity Price Index (USD)  
2005/2006 Q1



Source: MSCI Equity Indices, <http://www.msci.com/equity/index2.html>

**Table 3**

Stock Price Indexes 2005/2006 YTD											
	Price Index in US Dollars					Variation					
	31-Dec-04	31-Mar-05	30-Jun-05	30-Sep-05	30-Dec-05	31-Mar-06	Q1	Q2	Q3	Q4	Q1/06
Emerging markets	542.17	548.689	565.168	661.318	706.483	787.802	1.20%	3.00%	17.01%	6.83%	11.51%
Latin America	1,483.58	1,510.47	1,617.02	2,093.47	2,149.97	2,469.40	1.81%	7.05%	29.47%	2.70%	14.86%
Argentina	1,162.98	1,316.37	1,440.50	2,151.60	1,857.10	2,370.29	13.19%	9.43%	49.36%	-13.69%	27.63%
Brazil	1,046.55	1,090.51	1,145.92	1,560.62	1,569.44	1,886.23	4.20%	5.08%	36.19%	0.56%	20.18%
Chile	997.324	1,027.34	1,078.46	1,261.62	1,180.68	1,263.74	3.01%	4.98%	16.98%	-6.42%	7.03%
Colombia	245.007	236.54	277.572	349.72	495.667	580.398	-3.46%	17.35%	25.99%	41.73%	17.09%
Mexico	2,715.56	2,643.43	2,940.26	3,580.98	3,943.63	4,215.96	-2.66%	11.23%	21.79%	10.13%	6.91%
Peru	343.392	355.897	349.751	451.876	441.302	483.502	3.64%	-1.73%	29.20%	-2.34%	9.56%
Venezuela	151.033	127.631	121.717	107.636	107.377	161.066	-15.49%	-4.63%	-11.57%	-0.24%	50.00%

Source: MSCI Equity Indices, <http://www.msci.com/equity/index2.html>

MSCI Barra, which provides the benchmark MSCI Price Index, announced in April that the MSCI Venezuela Index would be removed from the MSCI Emerging Markets Index and reclassified as a stand-alone index. The announced changes became effective on May 31, 2006, in

the context of the May 2006 Annual Full Country Index Review. According to MSCI Barra, the removal of the MSCI Venezuela Index from the MSCI Emerging Markets Index was the result of continued presence of investability restrictions linked to the foreign exchange regime put in place in the country in February 2003, the lack of liquidity of most of its constituents and the continued weight decrease of the MSCI Venezuela Index in the MSCI Emerging Markets Index over the last several years.

Equity issuance is expected to accelerate in 2006. Seven initial public offerings (IPO) so far have already taken place in the region in the first three months of 2006. Latin American local markets are expected to attract an increasing number of investors, as corporate governance is improving and local markets are becoming more vibrant. In addition, U.S. listings have grown to be more difficult and costly after the Sarbanes-Oxley Act took effect in 2004. Companies are now weighing the benefits of issuing in New York more carefully as a result of the heightened regulation, which can translate into higher operating costs.

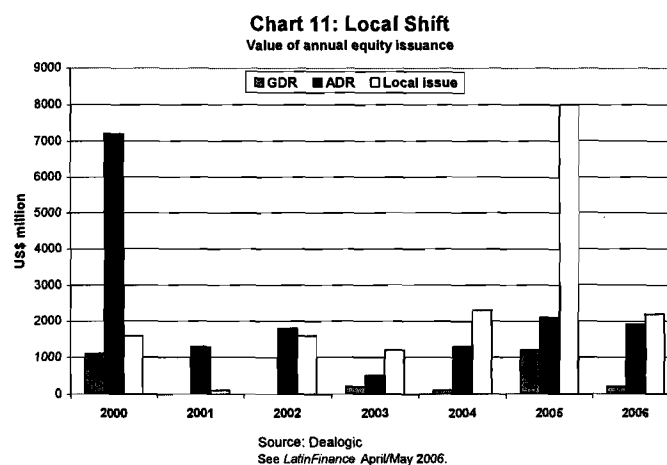
Companies can issue American Depositary Receipts (ADRs) in the New York Stock Exchange, Global Depositary Receipts (GDRs), which are identical to ADRs except they are exchanged globally, and local issues. The recent tendency in the region has been to issue locally, given the external backdrop of increased risk appetite and strong fundamentals in the region (Chart 11). Investing locally used to be difficult, but Brazil and Mexico, for example, have taken measures to increase transparency of their public listings and efficiency.

In the case of Brazil, it used to take between 60 and 100 days to set up a domestic account. Now setting up an account takes less than 24 hours and it can be done online. Mexico passed a stock market law in late-2005 to take effect in June 2006, with the goal of improving transparency of the country's 132 publicly listed companies.<sup>2</sup>

### III. Bank Lending

The latest data available on bank lending is for the final quarter of 2005. Latin America experienced a net inflow from commercial banks of US\$4.9 billion in the fourth quarter of 2005. For the year as a whole, the region experienced an outflow of US\$ 14.3 billion. Claims on the region increased by US\$14.1 billion in the fourth quarter, while deposits increased by US\$9.2 billion. For 2005 as a whole, claims on Latin America and the Caribbean increased by US\$8.0 billion, and deposits by US\$22.3 billion (Table 4).<sup>3</sup>

In the fourth quarter of 2005, Brazil and Mexico received a net lending of US\$9.4 and US\$6.9 billion, respectively. All the other countries in our sample experienced outflows of funds. For 2005 as a whole, Brazil and Colombia were the only countries receiving a net inflow of



<sup>2</sup> See "Escape from New York", *LatinFinance*, Number 176, April/May 2006, www.latinfinance.com.

<sup>3</sup> *BIS Quarterly Review*, March 2006 and *Provisional international banking statistics, fourth quarter 2006*, 25 April 2006.

funds, of US\$11.3 and US\$0.9 billion, respectively, with short-term credit inflows taking place for the first time in Brazil after more than five years.

Table 4

Cross-border bank flows to Latin America												
Exchange rate adjusted changes in amounts outstanding, in billions of US\$ dollars												
	Banks Position*	2004 Year	2005 Year	2005				Stocks at end-Dec 2004	Stocks at end-Sep 2005	Stocks at end-Dec 2005	Growth Q4	Growth 2005
				Q1	Q2	Q3	Q4					
Latin America	Claims	-14.7	8.0	2.7	-2.6	-6.2	14.1	257.3	248.4	260.9	5.0%	1.4%
	Liabilities	12.9	22.3	14.2	-6.9	5.9	9.2	289.8	297.8	304.3	2.2%	5.0%
Argentina	Claims	-5.3	-3.4	-1.3	-2.4	0.4	-0.2	18.9	15.2	14.8	-2.6%	-21.5%
	Liabilities	-0.3	-0.8	-0.1	0.6	-1.9	0.5	24.8	22.8	23.1	1.3%	-6.9%
Brazil	Claims	-7.4	9.3	2.9	1.4	0.8	4.1	77.4	81.5	85.0	4.3%	9.8%
	Liabilities	-4.8	-2.0	13.3	-9.4	-0.5	-5.3	53.7	55.4	49.2	-11.2%	-8.4%
Chile	Claims	-1.8	1.2	0.2	0.1	-0.3	1.2	20.9	20.6	21.6	4.9%	3.4%
	Liabilities	0.8	2.3	1.0	-0.6	0.6	1.3	15.4	16.1	17.3	7.5%	12.3%
Colombia	Claims	0.1	0.5	-0.4	-0.2	0.5	0.7	9.1	8.9	9.5	6.7%	4.4%
	Liabilities	1.8	-0.4	-0.3	-2.0	0.0	2.0	11.1	8.7	10.7	23.0%	-3.6%
Mexico	Claims	-0.9	-4.6	0.5	-3.2	7.6	5.7	65.3	54.8	60.4	10.2%	-7.5%
	Liabilities	-4.7	3.6	-1.5	2.1	4.2	-1.2	58.1	62.0	60.0	-3.2%	3.3%
Venezuela	Claims	-0.7	0.2	-0.4	-0.1	0.4	0.3	13.7	13.3	13.4	0.8%	-2.3%
	Liabilities	4.7	17.3	4.5	3.5	-0.2	9.4	33.7	41.1	50.5	22.9%	49.8%

Source: BIS Quarterly Review (Table 6A), 25 April 2006.

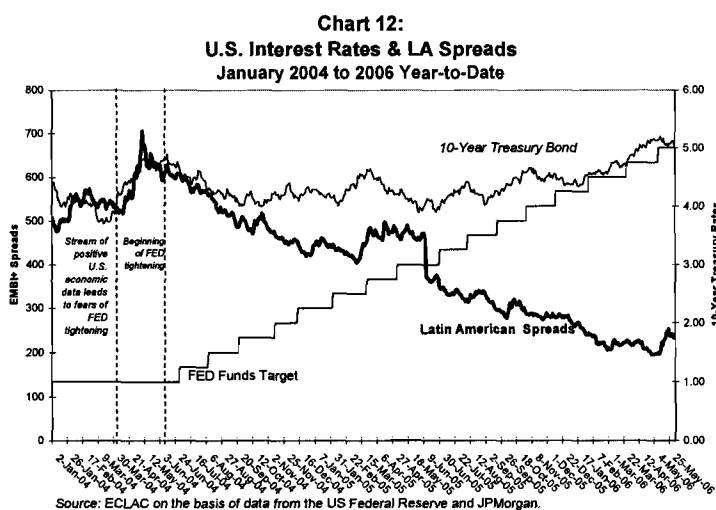
\* External on-balance sheet positions of banks in the BIS reporting area. Liabilities mainly comprise deposits. An increase in claims represents an inflow into Latin American economies; an increase in liabilities an outflow.

According to the Institute of International Finance (IIF), Latin America is likely to experience net outflows to commercial banks in 2006, which would be the sixth consecutive year of net repayments, with Brazil and Mexico accounting for most of the net repayments. Net outflows are projected to be less than US\$1 billion, however.<sup>4</sup>

#### IV. Prospects

Given the favorable global background for Latin American credit and equity markets, investors brought a great amount of money to the region's financial markets in the first quarter of 2006. Equity markets in Brazil and Mexico reached new records, local currencies strengthened and Latin American bond spreads continue to hover around record low levels. New debt and equity issuance were also strong during the quarter.

The major risks to Latin American markets in the near future are the fear of global inflation, the corresponding rise in global interest rates, and the uncertainty over monetary policy in the U.S., which can adversely affect global liquidity. Latin America is expected to be well cushioned for a tightening in global liquidity. However, the recent increase in volatility in May, with stocks tumbling as a result, showed the region still remains vulnerable to fluctuations in commodity prices and in the G-3 interest rates. Interest rates in the U.S. have been rising and Latin American spreads have been falling in recent years (Chart 12).



<sup>4</sup> "Update on Capital Flows to Emerging Market Economies", *Institute of International Finance, Inc.*, 30 March 2006.

In May, however, with the spike in volatility resulting from uncertainty towards the global economic outlook amid rising interest rates and inflation fears, the correlation between the Fed funds rate and the EMBI+, as well as its Latin component, turned positive.

Given the current uncertainty about the likelihood of further increases in the U.S. federal funds rate and how to price them, fluctuations in volatility may be a feature in global markets in the near future. Whether they will derail Latin America's and other emerging markets remains to be seen. The notion that emerging markets are now cushioned for a decline in global liquidity given their strong fundamentals, improved debt profile and current account surpluses, may be tested in future quarters if volatility returns to financial markets.

**APPENDIX**

- A. Credit Ratings in Latin America**
- B. Latin American Spreads**
- C. New Latin American Debt Issuance**

## A. Credit Ratings

**Table 1:**  
**Credit Ratings in Latin America**

	Moody's		S&P		Recent Moody's Action		Recent S&P Action	
	Rating	View	Rating	View	Action	Date	Action	Date
Argentina	B3		B		Upgrade, stable	29-Jun-05	Upgrade, stable	23-Mar-06
Barbados	Baa2		BBB+	(-)	Affirmed, stable	9-Jul-02	O/L changed to (-)	29-Jul-05
Bolivia	B3		B-	(-)	Affirmed, stable	16-Apr-03	O/L changed to (-)	7-Jun-05
Brazil	Ba3	(+)	BB		Upgrade, O/L (+)	12-Oct-05	Upgrade, stable	28-Feb-06
Chile	Baa1	(+)	A		Review for possible upgrade	21-Mar-06	Affirmed, stable	19-Dec-05
Colombia	Ba2		BB	(+)	Affirmed, O/L changed to stable	9-Mar-06	Affirmed, O/L changed to (+)	22-Feb-06
Costa Rica	Ba1	(-)	BB		Affirmed O/L (-)	16-Apr-03	O/L changed to stable	10-Jun-05
Cuba	Caa1		nr					
Dominican Republic	B3		B		O/L changed to stable	24-May-05	Upgrade, stable	29-Jun-05
Ecuador	Caa1	(+)	CCC+		O/L changed to positive	30-Jan-06	Affirmed, O/L changed to stable	4-Oct-05
El Salvador	Baa3		BB+		O/L changed to stable	18-Dec-03	Affirmed, stable	15-Sep-05
Guatemala	Ba2		BB-		Affirmed, stable	8-Jul-97	Affirmed, stable	5-Aug-05
Honduras	B2		nr		Affirmed, stable	29-Sep-98		
Jamaica	B1		B		Downgrade, stable	27-May-03	Affirmed, stable	16-Jan-06
Mexico	Baa1		BBB		Upgrade, stable	6-Jan-05	Affirmed, stable	27-Apr-06
Nicaragua	B2		nr		Affirmed, stable	30-Jun-03		
Panama	Ba1		BB		Affirmed, stable	7-May-03	O/L changed to stable	18-Feb-05
Paraguay	Caa1		B-	(+)	Downgrade, stable	28-Apr-03	Affirmed, O/L to (+)	27-Feb-06
Peru	Ba3		BB	(+)	Affirmed, stable	28-Oct-02	O/L changed to (+)	11-Jul-05
Trinidad & Tobago	Baa2		A-		Upgrade, stable	9-Aug-05	Upgrade, stable	21-Jul-05
Uruguay	B3		B	(+)	O/L changed to stable	10-Nov-04	Affirmed, O/L changed to (+)	9-Jan-06
Venezuela	B2		BB-		Upgrade, stable	7-Sep-04	Upgrade, stable	3-Feb-06

*Changes for the first quarter of 2006 are highlighted in yellow, for S&P actions, and in green, for Moody's actions.*

Note: Moody's ratings are qualified by outlooks and reviews while S&P ratings are qualified by outlooks and watches.

A review/watch is indicative of a likely short-term development.

An outlook suggests that a review/watch or long/intermediate-term movement is likely.

Source: JP Morgan, Emerging Markets Outlook, January 13, 2006.

Rating Scale					
	MOODY's	S&P	MOODY's	S&P	
Upper Investment Grade	Aaa	AAA	Lower Non-Investment Grade	B1	B+
	Aa1	AA+		B2	B
	Aa2	AA		B3	B-
	Aa3	AA-		Caa1	CCC+
	A1	A+		Caa2	CCC
	A2	A		Caa3	CCC-
	A3	A-		Co	CC
Lower Investment Grade	Baa1	BBB+	C	C	
	Baa2	BBB+	Default	SD	
	Baa3	BBB-		D	
Non-Investment Grade	Ba1	BB+			
	Ba2	BB			
	Ba3	BB-			

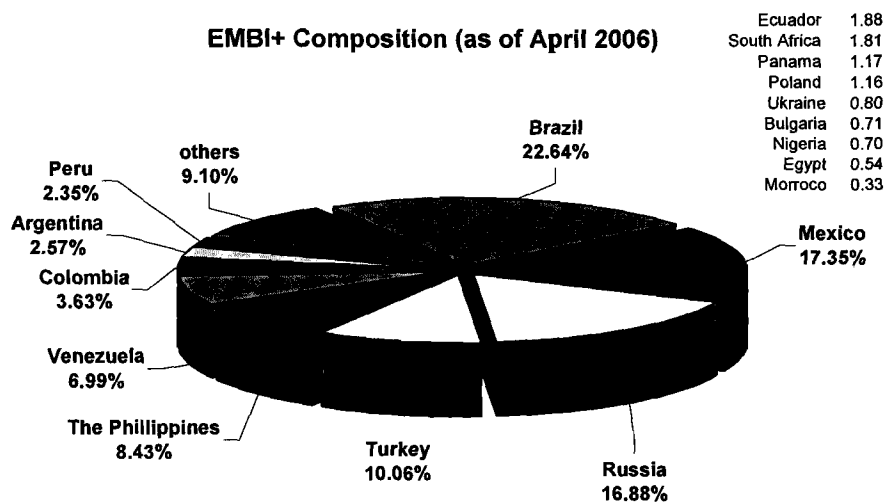
## B. Latin American Spreads

Table 2:

Sovereign Spreads on JP Morgan EMBI+ and Latin American Composites									
	EMBI+	Argentina	Brazil	Colombia*	Ecuador	Mexico	Peru	Venezuela	Latin America
30-Jan-04	432	5764	493	430	714	204	343	641	536
27-Feb-04	449	5815	579	426	762	189	356	733	568
31-Mar-04	432	4873	559	379	701	183	343	667	536
30-Apr-04	478	4628	663	443	925	201	393	692	598
28-May-04	508	4964	701	523	909	208	473	666	626
30-Jun-04	493	5188	650	486	952	215	439	647	607
30-Jul-04	466	5036	593	437	852	200	411	581	566
31-Aug-04	436	5258	521	408	813	183	357	550	524
30-Sep-04	421	5440	469	408	778	188	323	490	498
30-Oct-04	413	5440	473	400	745	183	318	462	493
30-Nov-04	377	5194	414	338	696	172	274	407	451
31-Dec-04	356	4703	382	332	690	166	220	411	420
31-Jan-05	366	5129	418	365	644	162	239	461	439
28-Feb-05	343	4980	393	344	632	153	211	437	419
31-Mar-05	384	5393	458	396	660	180	239	459	466
29-Apr-05	395	6298	457	407	810	188	234	492	482
31-May-05	372	6498	420	354	875	164	206	498	455
30-Jun-05	307	462	414	332	808	168	206	466	350
29-Jul-05	290	413	402	317	735	152	173	434	331
31-Aug-05	296	439	413	309	727	152	169	425	337
30-Sep-05	244	349	345	236	634	136	138	309	280
31-Oct-05	253	371	357	258	660	132	176	302	288
30-Nov-05	248	495	340	239	642	117	158	323	288
30-Dec-05	245	504	311	238	669	126	206	318	283
31-Jan-06	217	440	266	195	579	115	160	251	243
28-Feb-06	191	354	221	158	574	103	143	228	210
31-Mar-06	192	344	235	174	524	127	187	190	215
29-Apr-06	178	314	218	157	483	122	181	167	199

Source: "Emerging Markets Bond Index Monitors"; JP Morgan

EMBI+ composition by market sector (end-Apr. 2006): Brady, 17.23%; Benchmark Eurobonds 82.44%; Loans, 0.33%.  
 by country: Brazil and Mexico account for 39.99% of the total weighting.  
 by region: Latin: 59.40%; Non-Latin: 40.60%.



**Table 3:**

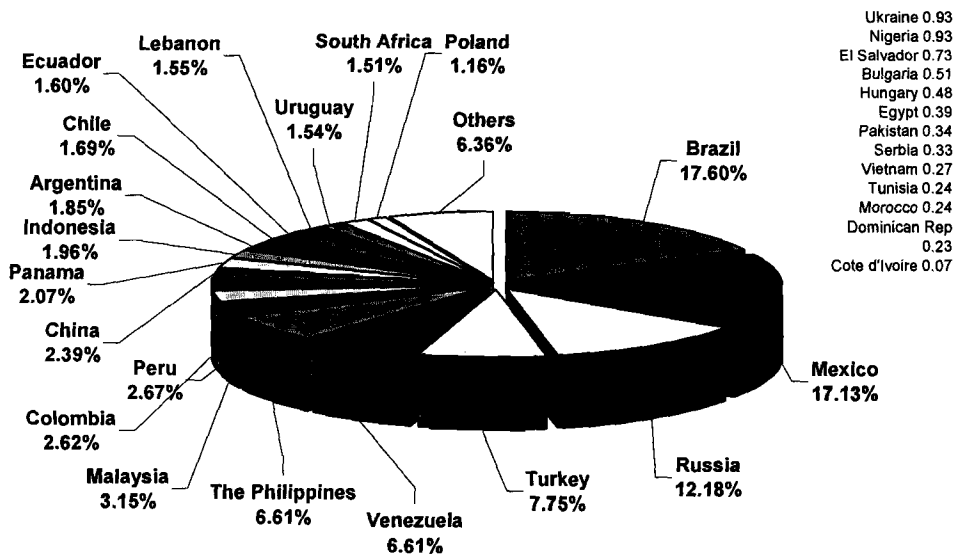
**Sovereign Spreads on JP Morgan EMBI Global and Latin American Composites**

	EMBI Global	Argentina	Brazil	Chile	Colombia	Ecuador	Mexico	Peru	Uruguay	Venezuela	Latin America
30-Jan-04	414	5619	489	94	425	714	205	357	585	633	531
27-Feb-04	431	5622	575	88	424	762	191	371	638	720	563
31-Mar-04	414	4840	554	91	379	701	184	355	576	647	531
30-Apr-04	468	4534	660	92	443	925	204	406	658	684	588
28-May-04	494	4838	696	92	521	909	210	483	682	659	614
30-Jun-04	482	5087	646	83	483	952	218	450	710	643	600
30-Jul-04	453	4994	590	80	435	852	201	424	601	584	556
31-Aug-04	425	5237	518	70	406	813	184	372	598	550	518
30-Sep-04	409	5389	466	78	407	778	189	340	497	490	492
30-Oct-04	399	5269	470	81	401	745	185	337	507	459	481
30-Nov-04	363	4987	410	73	340	696	181	293	414	400	433
31-Dec-04	347	4527	376	64	332	690	174	239	388	403	415
31-Jan-05	356	5022	412	60	364	644	172	267	402	452	434
28-Feb-05	333	4827	388	59	343	632	161	247	344	427	413
31-Mar-05	373	5105	455	71	393	660	188	277	427	455	459
29-Apr-05	384	5757	452	72	406	810	198	279	470	491	473
31-May-05	364	5956	415	68	353	875	176	251	446	494	448
30-Jun-05	297	462	409	60	331	808	181	252	406	460	337
29-Jul-05	276	413	397	56	316	735	165	218	366	430	316
31-Aug-05	281	439	409	55	307	727	165	223	376	419	320
30-Sep-05	235	349	341	55	240	634	82	183	310	303	267
31-Oct-05	242	371	353	74	261	660	146	213	327	298	274
30-Nov-05	237	495	337	74	243	642	133	199	320	318	274
30-Dec-05	237	504	308	80	244	661	143	257	298	313	272
31-Jan-06	210	440	264	73	200	565	132	203	247	248	233
28-Feb-06	187	354	218	68	156	551	122	185	231	223	204
31-Mar-06	191	344	232	73	263	503	140	226	223	190	208
29-Apr-06	179	314	215	78	157	461	135	205	224	167	194

Source: "Emerging Markets Bond Index Monitors"; JP Morgan

EMBI Global composition by market sector (end-Apr 2006): Brady, 13.48%; Benchmark Eurobonds 85.86%; Loans, 0.66%.  
 by country: Brazil and Mexico account for 34.73% of the total weighting.  
 by region: Latin: 56.36%; Non-Latin: 43.64%.

**EMBI Global Composition (as of Abril 2006)**





C. New Latin American Debt Issuance

C1. January 2006

Table 4:

New Latin American Debt Issuance					
Jan-06					
Country	Issuer	Issue date	Amount (million)	Amount US\$ (mm)	Maturity
Brazil	CVRD	5-Jan-06	USD1000	1000	11-Jan-16
Brazil	Rebuplic of Brazil	10-Jan-06	USD1000	1000	20-Jan-37
Brazil	Banco do Brasil	13-Jan-06	USD500	500	Perpetual
Trinidad y Tobago	National Gas Company	17-Jan-06	USD400	400	15-Jan-36
Panama	Republic of Panama	18-Jan-06	USD1363	1363	16-Jan-36
Argentina	Banco Hipotecario	23-Jan-06	USD150	150	16-Nov-10
Brazil	Cosan	24-Jan-06	USD300	300	Perpetual
Uruguay	Republic of Uruguay	24-Jan-06	USD500	500	18-Nov-22
Mexico	Telemex	25-Jan-06	MXN4500	429	31-Jan-16
Brazil	Vicunha	26-Jan-06	USD450	450	Perpetual
Trinidad y Tobago	Mirant Trinidad	26-Jan-06	USD100	100	1-Feb-16
Brazil	Friboi	26-Jan-06	USD200	200	7-Feb-11
Mexico	Permex Master Trust	26-Jan-06	USD750	750	15-Dec-15
Mexico	Permex Master Trust	26-Jan-06	USD750	750	15-Jun-35
Brazil	Rebuplic of Brazil	30-Jan-06	EUR300	351	3-Feb-15
Brazil	Banco Fibra	30-Jan-06	USD50	50	10-Feb-09
<b>Total</b>				<b>8,293</b>	

Source: ECLAC, on the basis of data from J.P.Morgan, *Emerging Markets Outlook and Strategy*.

*January average maturity: 17.15 years.*

**Currency Breakdown**

(% of Latin America's Total)

Currency	Jan-06
Dollar	90.6%
Euro	4.2%
JPY	0.0%
Other*	5.2%

Source: ECLAC, with data from JP Morgan.

\* Issuance in Mexican Pesos.

**Issuer Type Breakdown**

(% of Latin America's Total)

Issuer Type	Jan-06
Sovereign	38.8%
Corporate*	61.2%

\*Also includes bank issuance.

Source: ECLAC, with data from JP Morgan

C2. February 2006

Table 5:

New Latin American Debt Issuance					
Feb-06					
Country	Issuer	Issue date	Amount (million)	Amount US\$ (mm)	Maturity
El Salvador	AES El Salvador	7-Feb-06	USD300	300	1-Feb-16
Colombia	Fondo Latinoamericano Flar	8-Feb-06	USD250	250	15-fev-11
Brazil	Friboi	8-Feb-06	USD75	75	7-Feb-11
Brazil	Centrais Eletricas	10-Feb-06	USD100	100	14-Feb-12
Brazil	Cosan	10-Feb-06	USD150	150	Perpetual
Brazil	Banco Panamericano	21-Feb-06	USD50	50	24-Feb-09
Jamaica	Jamaica	21-Feb-06	USD250	250	28-Feb-36
Brazil	CESP	22-Feb-06	USD300	300	2-Mar-11
Chile	Autopista del Nordeste	22-Feb-06	USD162	162	15-Jan-26
Brazil	Banco Industrial Comercial S/A	24-Feb-06	USD120	120	3-Mar-16
<b>Total</b>				<b>1,757</b>	

Source: ECLAC, on the basis of data from J.P.Morgan, *Emerging Markets Outlook and Strategy*.

*February average maturity: 10.71 years.*

**Currency Breakdown**  
(% of Latin America's Total)

Currency	Feb-06
Dollar	100.0%
Euro	0.0%
JPY	0.0%
Other*	0.0%

Source: ECLAC, with data from JP Morgan.

**Issuer Type Breakdown**  
(% of Latin America's Total)

Issuer Type	Feb-06
Sovereign	14.2%
Corporate*	85.8%

\*Also includes bank issuance.

Source: ECLAC, with data from JP Morgan.

C3. March 2006

Table 6:

New Latin American Debt Issuance					
Mar-06					
Country	Issuer	Issue date	Amount (million)	Amount US\$ (mm)	Maturity
Mexico	United Mexican States	3-Mar-06	USD3000	3,000	15-Jan-17
Argentina	Loma Negra	3-Mar-06	USD100	100	15-Mar-13
Colombia	Republic of Colombia	6-Mar-06	COP537billion	237	22-Oct-15
Dominican Republic	Dominican Republic	13-Mar-06	USD300	300	20-Apr-27
Brazil	Republic of Brazil	16-Mar-06	USD500	500	20-Jan-37
Uruguay	Republic of Uruguay	16-Mar-06	USD500	500	21-Mar-36
Brazil	Banco Cruzeiro	21-Mar-06	USD41	41	19-Mar-08
Brazil	Banco Panamericano	24-Mar-06	USD100	10	24-Feb-09
<b>Total</b>				<b>4,688</b>	

Source: ECLAC, on the basis of data from J.P.Morgan, *Emerging Markets Outlook and Strategy*.

*March average maturity: 15.36 years.*

**Currency Breakdown**  
(% of Latin America's Total)

Currency	Mar-06
Dollar	94.9%
Euro	0.0%
JPY	0.0%
Other*	5.1%

Source: ECLAC, with data from JP Morgan.

\* Issuance in Colombian Pesos.

**Issuer Type Breakdown**  
(% of Latin America's Total)

Issuer Type	Mar-06
Sovereign	96.8%
Corporate*	3.2%

\*Also includes bank issuance.

Source: ECLAC, with data from JP Morgan.