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**REAL ESTATE CRISIS IN THE
UNITED STATES AND THE
LESSONS FOR LATIN
AMERICA**

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The current real estate crisis in the United States allows us to come to three conclusions: First, long periods of economic bonanza feed euphoria and speculation that lead to market bubbles and failures; second, that the economy doesn't move by easily predictable economic models and that interest rates are a double edged weapon; and lastly, in the absence of indicators and information concerning a specific event, regulators must move with diligence and decisiveness, letting themselves be led by the market for the single and exclusive purpose of making sure that the market doesn't lose confidence, and if it does, reestablish it.

“Fear is stronger than euphoria”

The financial crisis which started in the United States caused by high risk mortgages (subprime) has led to many investors and analysts striving to understand and evaluate this phenomenon based on previous experience, besides trying to explain its effects in the short and medium term. In this context, the former president of the Federal Reserve, Alan Greenspan, pointed out that “fear as a motor is much more powerful than euphoria.” In contrast, another group of analysts point out that this crisis has no precedent given the unusual

Confidence crisis

The current crisis is essentially a problem with liquidity, and a liquidity crisis always brings with it a crisis in confidence. The current turbulence experienced by the market has come from the banks' lack of confidence to continue lending money to each other because they are not sure of how solvent they really are, if they will be able to recover their money, and they are afraid of being exposed to the United State's high-risk mortgage problems. This particular situation can, by extension, harm other countries. And, confidence is something that depends on each and every one of us, which is why you can see how the regulators' intervention has served to soften the fall, which is no small feat, but it hasn't eliminated the investor's fear.

1987: A similar situation

Some analysts compare the current crisis to what happened during the last quarter of 1987, when the Dow Jones suffered its worse crisis during peace time: it fell 22%, in a crash that infected the European and Japanese stock exchanges. This stock exchange market crash, which revealed just how interconnected the different world markets are, occurred within the framework of an anticipated fear of a U.S. economic recession, since it had an enormous budget deficit with an inordinate increase in public spending. Just like now, the crisis happened in the middle of a period when the system was over indebted. In our opinion, both crises began at the microeconomic level.

1998: An isolated case

The second case we would like to present is the crisis of 1998, when a storm in the Asian financial markets provoked an unexpected default in payment of the Russian debt which eventually led to Long-Term Capital Management (LTCM) hedge fund to almost implode. The 1998 crisis was due to one specific hedge fund which was poorly managed. The current crisis is in response to a general product, the subprime, and a mortgage market niche that represents 13% of the U.S. real estate market. According to information released during a recent U.S. Senate meeting about aggressive loans, secondary loans, the category of greatest risk within aggressive loans, went from US\$150.0 billion in 2000 to US\$650.0 billion in 2005.

The perfect storm

The current crisis is called by some analysts as "the perfect storm," since three things have to happen for the secondary market to collapse: debtor revenues would have to drop, interest rates would have to increase, and housing prices would have to fall. It's obvious

that it's extremely strange for all three things happening at the same time.

Everything that goes up...

At *Ecoanalítica* we have observed that all three events (1987, 1998 and the current one), have one thing in common previous to the crisis, they all were in the middle of periods of economic bonanza, which naturally, led to investor euphoria and the relaxing of market control mechanisms. Another point they all had in common was that the epicenter of the event was in the United States and afterwards it quickly spread to other economies.

In 2007, things are different

According to available economic data, it can be pointed out that contrary to the previous crises, world economy is strong. The growth rates of developing and emergent countries are significant. What stands out with the current crisis is the existence of financial instruments and techniques, like securitization and credit derivatives, which didn't exist in the past. The second big difference with respect to the previous crises is in the reaction developed by the regulators which consisted in injecting liquidity into the system and lowering (in the case of the U.S.) or keeping (in the case of Europe) interest rates.

The priority is to minimize investor's fears

One of the effects of fear and the loss of investor confidence is that the economic agents are not willing to lend their money because they are scared that the capability to make payments will diminish. An essential characteristic of that fear is that it is uncontrollable, and one of its direct consequences is a wave of sales of financial assets, due to the fear that they may incur losses, and with it, spark a generalized fall in stock market prices. Experts point out that the loss of confidence in the financial markets can last from one to three months.

The IMF plays a key role

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An important aspect in order to contain the crisis is that world authorities, especially the IMF work in four environments: evaluate the necessary liquidity, risk management, exchange information concerning cross-border operations, and supervise rating agencies.

When the confidence returns to the markets, the bubble will deactivate. In any case, readjustment periods are good for the economy, since each bubble will have its own deactivation period. At ***Ecoanalítica*** we believe that real market bubbles are more dangerous and take longer to deactivate than bubbles like this one, relative of the financial markets. When the systems once again are capable of payments, then the bubble will deactivate.

A recession is not expected

At ***Ecoanalítica*** we don't believe in catastrophic visions concerning the future, because we don't have any economic evidence that leads us to think that we are in the presence of a global recession. Up to now, all data, reports, and forecasts point to the contrary. Logically, there will be a slight deceleration in the economy, especially in the United States. However, the fact of the matter is that a lack of confidence exists, and you can't generate confidence from one day to another. But in two or three months, the markets will back to business as usual. In fact, we believe the worst is over. In October, the U.S. financial businesses balance reports will be published and the extent of the damage will be revealed. If it doesn't look too bad, the market will probably immediately bounce back.

GDP Growth Rate

	2004	2005	2006
China	10,1	10,2	10,7
Venezuela	18,3	9,3	10,3
Argentina	9,0	9,2	8,0
Costa Rica	4,3	5,9	7,9
Corea	4,7	4,0	5,0
Colombia	4,9	5,3	4,8
Bolivia	3,6	4,6	4,1
México	4,2	3,0	4,0
Chile	6,0	5,7	4,0
España	3,2	3,5	3,8
Brasil	4,9	2,3	3,7
Estados Unidos	3,9	3,2	3,4
Canadá	3,3	2,9	3,1
Japón	2,3	2,6	2,7
Francia	2,3	1,2	2,2

Sources: ONU and Ecoanalítica

Not everything will happen now

Another reason to assume that the economy won't be significantly affected is that most homeowners with variable type mortgages won't reach the default or eviction stage. According to an economics research company First American Core Logic of California, around 1.1 million cases of evictions due to default payments will occur, but they all won't happen at the same time but over the next six or seven years, a period long enough so as not to affect the economy.

The Latin American position

Many people believe that the countries most affected by this situation will be Latin American ones. However, at **Ecoanalítica**, we don't share this opinion. First, Latin American countries are used to weathering tense moments, they are veterans of many economic crises. Second, according to the IMF and the World Bank, during the next few decades the Latin American markets are forecast to significant increases in economic growth rate and development. The reason behind this is that

Latin American economies are rich in natural resources and in raw materials, something that is increasingly precious in a world scarce in resources and in the middle of an ever increasing economic growth cycle.

In Venezuela the key is inside

We would like to mention that the dangers to the Venezuelan economy are found in the enormous domestic imbalances that exist and are being produced by the current economic policies. Independently of what's happening in the international markets, if these imbalances aren't corrected, we are condemned to failure which will translate in a loss of well-being for all Venezuelans.

Economic Tips

Bono del Sur III. The orders to acquire this instrument, which price was fixed at 108%, will be able to be processed until Friday, September 28. On Thursday, October 4, according to the Ministry of Finance schedule, the requests that were processed will be liquidated. At **Ecoanalítica** we believe that this will be an excellent investment opportunity with the implicit exchange rate between VEB3,600 and VEB3,900 per US-dollar.

No more. The Venezuelan Government doesn't expect to be issuing any more *Bonos del Sur* during the rest of the year, said Finance Minister, Rodrigo Cabeza, after announcing the Bono del Sur III issue.

Inflation goal intact. Armando León, director of the Central Bank of Venezuela (BCV) stated that the monetary policies that have been carried out up until now are going in the right direction. So that it is totally realistic to expect that by the close of 2007 the inflation level will be at around 12% using as a macroeconomic premise the national budget. At *Ecoanalítica* we estimate inflation to close the year at 18.4%.

Regulated goods will remain intact. No provisions have been made for an adjustment in the prices of regulated goods. With the pending monetary conversion about to come into effect, the prices expressed in *Bolívares Fuertes* (strong bolivar) will be published in the *Gaceta Oficial*.

New taxes. José Vielma, tax superintendent, informed that two Law proposals were submitted to the Vice-Presidency of the Republic to be reviewed and subsequently approved by the Minister's Council. The proposals are regarding the Selective Consumption Tax Law which will tax the consumption of certain products like alcoholic beverages and cigarettes; and the Financial Transactions Tax Law, aimed at taxing inter-bank operation for legal persons.

Public debt now in the Stock Exchange. Luis Dávila, director of the National Office of Public Credit, announced that in a period of about a month or a month and a half, the public debt instruments known as covered interest and capital titles (TICC) will begin to be offered through the Caracas Stock Exchange.

On the eve of the monetary conversion. Starting in October, business must begin to show the prices of their products in both currencies. With respect to accounting, all fiscal registers must continue to work with bolívares until December 31 of this year. After January 1, businesses will have up to 10 days to adjust their machines to the new currency.

Supermarkets as bolívar exchange centers. The Central Bank of Venezuela (BCV) is in communication with the National Association of Supermarkets and Related Businesses (ANSA) in order to increase the number of exchange centers for bills and coins, including the local ANSA affiliates.

CADIVI published its first list of offenders. The Commission for the Administration of Foreign Currency (CADIVI) published its first list of approximately 1000 names of people who must appear at the headquarters of the organization located in Los

Chaguaramos, Caracas, in order to justify the correct use of the foreign currency they were authorized.

Banco del Alba. The Ministry of Finance is currently defining the construction of the *Banco del Alba* which will count on the participation of Nicaragua, Bolivia, Cuba and Venezuela. The Minister of Finance, Rodrigo Cabeza, announced that the amount each country will contribute to the bank's capital is still being discussed, though he admitted that Venezuela will be contributing the largest amount.

Banco del Sur operations to begin by the end of 2008. The *Banco del Sur*, sponsored by President Chávez, in which Paraguay, Brazil, Uruguay, Bolivia and Ecuador will also participate, expects to begin operations by the end of next year. The aim of this bank is to convert the resources of the member countries into raw materials for development, so said a number of the bank's promoters.

Public entities ask for more The Ministries and public entities had until the end of August to submit their budget proposals so that they could be considered in the 2008 Budget law. However, the budget requests must be re-adjusted since the budget amounts proposed would make the National Budget reach VEB200 trillion, and the desired final budget figure for next year is not to exceed VEB160 trillion.

Crude oil price scenarios for 2008 are going from US\$30 to US\$50 per barrel. The planning and finance ministries are developing the different scenarios in order to be able to define the 2008 Budget. In the evaluations that they are carrying out six oil scenarios are contemplated. The first scenario forecasts the price for a barrel of oil at US\$30, and the other scenarios follow calculating the price at US\$33, US\$35, US\$40, US\$45 and US\$50. This time around, the technicians present scenarios all considering high prices, something that hasn't been done in previous forecasting sessions. However, official sources say that the tendency will continue to be to set a conservative price as has been done for previous budgets.

National Collection Plan a success. The SENIAT carried out a notification and collection operative which allowed them, through emails to taxpayers, to collect more than VEB216 million in 20 working days.

Workday to be reduced to 6 hours starting in 2010. Rafael Chacón, Vice-Minister of Labor announced that when the constitutional reforms begin to be implemented, the shortening of the workday will begin starting on May 1, 2010, just like President Chávez said a few days ago.

Unemployment drops steadily. National Statistics Institute (INE) figures show that unemployment continued to drop during the month of August settling at 8.6% of the economically active population. This figure is 1.9% less than was registered in August last year.

BCV with a positive balance. The financial balance of the BCV for the month of August reflects earnings of VEB80.80 billion. Fiscal contributions total VEB47.00 billion for the month of June.

OIL TIPS

Keeps going up. The Venezuelan crude oil basket has been increasing at a sustained rate for four weeks now. This week it increased by US\$1.95 with respects to the previous week settling at US\$73.11 per barrel.

Portuguese company makes a pact with PDVSA. The Portuguese company Galp Energía is studying an agreement with PDVSA to carryout joint exploitation and gas and oil production projects. Galp Energía is looking for Venezuela to become one of Portugal's main importers of oil.

OPEC adjusts to clarify Venezuelan oil extraction quota. OPEC's restructuring of production quotas reduced Venezuela's production ceiling by 753 thousand barrels per day (23.3%) starting in November this year. Venezuela has never had an extraction quota for crude oil less than 2.49 million barrels a day since 1997, because the evolution of the quota allotments allowed the country has always tended to increase since the production control system was established in 1982.

Commercialization margin increases. The Ministry of Energy and Petroleum announced that starting on October 1 the increase in commercialization margins will be in effect for gas stations. This margin is what determines the station's profits, which allows it to face minimum wage increases. The commercialization margins that will apply to diesel and 91 and 95 octane gasoline will have an average adjustment of VEB2.89 per liter. Payment will be retroactive to September 1, 2006.

PDVSA offered oil workers an increase of VEB9,000. PDVSA offered union representatives that are discussing the collective bargaining agreement for oil workers a salary increase of VEB7,000 for this year, VEB1,000 for 2008, and VEB1,000 more for the next year, in all totaling VEB9,000. It also proposed that the collective bargaining agreement last for three years instead of two, as it has been doing so far.

Furthermore, the company's representatives suggested that the rest of the clauses that affected economic issues stay the same.

PDVSA becomes alarmed by protests. PDVSA activated a contingency plan in order to avoid company production operations to be impacted by labor disputes. Anzoátegui workers yesterday held an assembly in order to announce future protests that will be carried out due to the low economic offer that PDVSA has made them and they also insure that none of these actions will affect oil production.

Central America is worried. Guillermo Zúñiga, president of the Council of Ministers of Finance and Property of Central America, referred to the hardships that the high crude oil prices cause in these countries. He continued to say that the only solution is to buy oil from Venezuela, taking advantage of the preferential conditions offered by the PETROCARIBE agreement.

BUSINESS SECTOR TIPS

Loan portfolio increased by 80.3% over the last year. The bank loan portfolio increased by VEB38.7 trillion in a year compared to the same period last year.

Public banks don't intermediate. According to figures reported by SUDEBAN, 55.7% of the total assets of public banks correspond to investments in debt papers. All public banks accrue together an amount of investment in public and private papers that totals VEB6.3 trillion. It stands out that the public loan portfolio, which up until now amounts to VEB3.0 trillion, registered in August a 155.5% increase in delinquent credits in comparison with the same month last year.

Private banks unify services. Since last Monday the 24th of this month, Confederado, Banpro and Bolívar Banco clients can all carry out their operations in anyone of the 194 agencies belonging to these banks nationwide.

Iranian bank operating in Venezuela. The SUDEBAN authorized, through a resolution published in the *Gaceta Oficial*, the operation in the country of the Banco Internacional de Desarrollo, a universal entity which belongs 100% to the Iranian State. According to the resolution, the new financial institution has 90 days to start operations, with a capital of VEB40.0 billion.

CANTV extends labor conditions to affiliates. Starting from next year, CANTV, Movilnet, Caveguías and Cantv.net workers will all benefit from the same labor package in terms of economic aid, family well-being plans, and health programs. This information was released by Socorro Hernández, President of the company.

Ministry of Housing and Habitat continue supervision. Private and Public companies are being supervised for the purpose of verifying if they are contributing to the Obligatory Savings Fund. Through a statement it was announced that this Ministry will be carrying out a resource recovery process in order to maintain the objective of granting credits to those that are making payments to the housing plan.

Vargas state depending too much of Caracas. It was expected that with the construction of the new Caracas-La Guaira viaduct, Vargas state would begin to reflect some development with its inhabitants. However, the people from Vargas seem to prefer to do their shopping in the capital, since the coastal sector hasn't come alive as expected.

Corn production lower than expected. The Minister of Agriculture and Land informed that corn production would reach the expected level of 2.5 million tons due to the drought that lasted longer than expected and the rains that have affected the harvest.

Companies won't import wheat. Companies producing pastas have requested a 58% increase in the controlled price in order to be able to cover the cost of importing wheat that has a very volatile international market price. The Venezuelan Association of Pasta Manufacturers (Avepastas), informed that if this increase was not approved, a number of the pasta producing companies will have to stop importing the raw material during the last quarter of the year.

Powdered milk imports drop. Teresa López, executive director of the Venezuelan Chamber of Importers, Manufacturers, and Distributors of Dairy Products (Cavelácteos) announced that the increase in price of powdered milk on the international market has caused imports of these products to slow down considerably since the commercial activities of these companies have been considerably reduced.

No pork roast for Christmas. For the third year in a row, supermarkets will not offer pork roasts in December due to the marked difference between the product purchase and sale price.

Shortage of eggs too. The shortage of eggs in the market is due to the fact that wholesalers are selling the product over the regulated price. Therefore, merchants are

simply not buying them. The controlled price is VEB8,300 per carton. However, the *buhoneros* (street vendors) are charging up to VEB7,000 over the regulated price.

And medicines too. Representatives of the Venezuelan Pharmaceutical Federation (Fefarven) have pointed out severe shortages in medicine supplies. Shortages are observed in different products, but an outstanding fact is that a large part of these medicines do not have generic products that can replace them.

Request to control vehicle imports. Yesterday afternoon a delegation of workers from Toyota de Venezuela requested the Ministry of Light Industries and Commerce to regulate the flow of vehicle imports due to the explosive increase that has been registered especially over the last two months.

Dealers for Hummers. Hummers will be sold in Venezuela directly by its manufacturer. Therefore, by taking importers out of the commercialization chain, the prices of these vehicles will go down to between VEB98 million and VEB165 million. Ronaldo Znidarsis, GM CEO in Venezuela, explained that at the beginning only six car dealers will sell the vehicles in Caracas, Maracaibo, Puerto La Cruz, Valencia, and Puerto Ordaz, generating approximately one thousand new jobs. The company budgeted VEB55 billion for launching, marketing, and advertising.

Electricidad de Caracas (EDC) in the Energy Mission. Electricidad de Caracas is now part of the Energy Mission, which goal is to take measures to render energy use more efficient. Up to now, this mission's task has been restricted to replacing ordinary light bulbs with energy-saving bulbs, which, according to Wilfredo Olivares, member of the EDC energy planning and managing department has resulted in 30% saving in electric power bills.

Problems with the electric power supply in Ciudad Bolívar. Union leaders of the region have admitted that they are unable to solve the power supply problems being experienced there, because they have only one truck to respond to and try to solve the existing irregularities.

70% of the cooperatives belong to the service sector. Juan Carlos Alemán, National Cooperative Superintendent, explained that the fact that 70% of the existing cooperatives belong to the service sector is mainly due to the lack of training oriented to the production sector of the economy. However, the Superintendent has assured that the country's cooperative network contributes 14% of GDP and employs 18% of Venezuela's labor force. But, according to the National Statistics Institute (INE), personnel working in cooperatives would only represent 2% of labor force and BCV has reported that the whole informal sector represent around 15% of GDP.

Breweries regulate themselves. To fit beer advertising to the national legal framework, the breweries Cervecería Regional, Cervecería Polar, and AmBev Venezuela, signed a self-regulation code for commercial communications related to the brewery sector.

Political Tips

Private schools, the next target. President Hugo Chávez announced at the inauguration of the 2007-2008 school year that all schools, both public and private, must abide by the rules set forth in the Constitution and by the Bolivarian national educational system, otherwise “they will have to close their schools.” Government representatives will supervise schools and in the event that any director doesn’t allow officials to enter the school premises, that “school will have to be intervened,” according to Adán Chávez.

Bishops demand that Government guarantees a free education. “Every man has the right to know. Venezuelans must know History and dogmas that have existed or have been proposed. Knowledge isn’t the problem; the problem appears when it comes to indoctrination,” pointed out the Caracas assistant Bishop, Monsignor Nicolás Bermúdez.

“Casa por casa” (door to door) operative to inform about the constitutional reform proposal. Near Plaza Bolívar in Ciudad Bolívar, once the special National Assembly session to discuss the constitutional reform proposal was adjourned, the president of the AN, Cilia Flores, announced that the “Casa por Casa” operative will be launched to proceed with the consultation period about the reform proposal.

Campaign for Socialism. A group of Bolivarian students launched the National Campaign of Young Students for Socialism, with the aim of unifying the student movement that follows the Bolivarian Revolution. The event took place at the CANTV headquarters in Los Cortijos.

Separate vote in the Referendum. Julio Borges, coordinator of the party Primero Justicia, submitted a request to the TSJ asking to allow reform proposals to be voted separately, so that electors can approve or disapprove those articles they consider convenient.

25 or 30 other articles could be touched by the reform. More than 60 articles of the current Constitution will be modified by the reform proposal presented by President Chávez. The representative and member of the advisory committee for the constitutional reform, Carlos Escarrá, explained that although the proposal includes only 33 articles, if its spiral of influence is considered, this could impact between 25 and 30 other articles, only in form, not in substance.

Two out of every three Venezuelans disapprove indefinite re-election. The vice-president of Consultores 21 pollster, Saúl Cabrera, pointed out that, according to their polls, around two out of every three Venezuelans are against the indefinite presidential re-election. He also said that the real support that President Chávez has among the population ranges between 30% and 35%.

Judicial System Committee restructured. The TSJ published in the *Gaceta Oficial* the decision according to which the Committee for the Restructuring and Functioning of the Judicial System is being restructured. The decision established that Damián Adolfo Nieto Carrillo will be appointed chairman of the Committee which would include Alicia García de Nicholls among other members.

Other Tips

Colombia grows 6.9% in the second quarter. According to information disclosed by the Departamento Administrativo Nacional de Estadísticas (DANE), GDP for the second quarter, including illegal crops, grew 6.9% in comparison to the same period last year. If illegal crops are not included, growth is reported at 7.0%. Including illegal crops, the most dynamic sector for the quarter was: the financial businesses, insurance, real state and businesses services, 15.7%, followed by manufacturing industry and transportation, storage, and communications, both with 12.1%. Furthermore, commerce, service, repair, restaurant and hotel sector gained 10.8%. Construction, although it's still growing dynamically, registered a growth rate slower than the first quarter, 6.2%. With this last figure, GDP growth rate for the first quarter was at 7.5%, including illegal crops, since this growth reached 8.0% for the first quarter. Growth for the first half of the year totalled 7.6 if illegal crops are not included.

Inflation will be measured in Anzoátegui starting in November this year. Market patterns in Anzoátegui state will start to be considered, as of this coming November, in the calculation of the Consumer Price Indices that the BCV carries out every month.

This state was selected by the Administration to be included in the study that is currently being conducted for Zulia state and the Federal District.

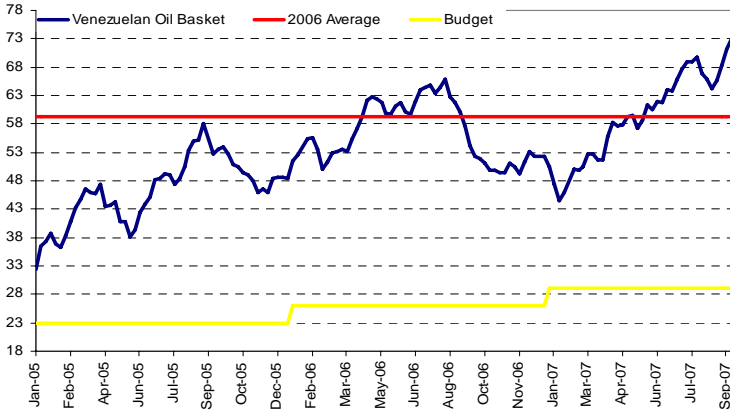
New time zone delayed. The vice-minister of planning of the Ministry of the People's Power for Science and Technology, Luis Marcano González, announced that the change in the time zone for Venezuela will take place in about two to three weeks since a few aspects have to be resolved first that have to do "with international notifications and engineering." President Chávez will officially announce the moment from which the clocks will have to be turned back one half hour.

Postnatal leave for fathers. According to the Law for the Protection of Families, Maternity, and Paternity, now the father will be able to request a 14 day paid leave for the date of his baby's birth. The period may be extended due to multiple births or health complications in the mother or child. The parents also benefits from not being able to be fired from their jobs until after at least one year from the child's birth.

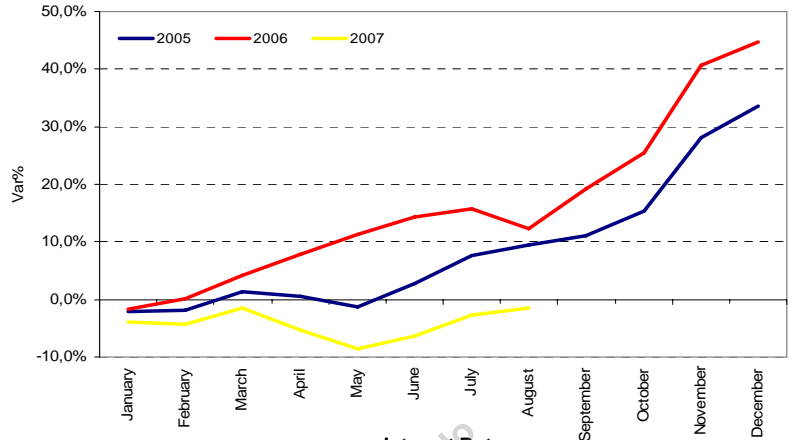
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ECONOMIC OVERVIEW

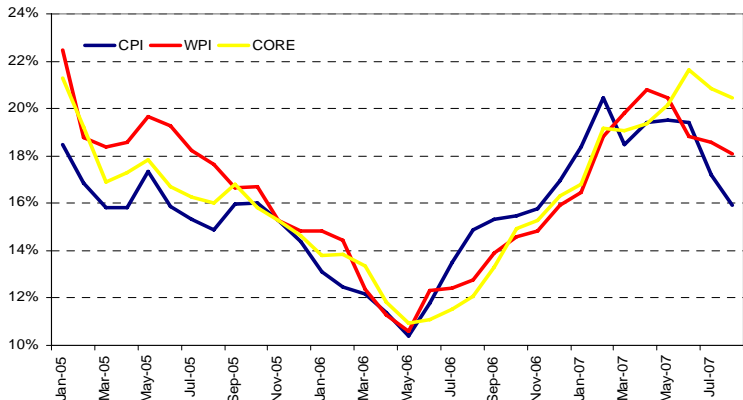
Oil Price
(Venezuelan Basket US\$/pb)



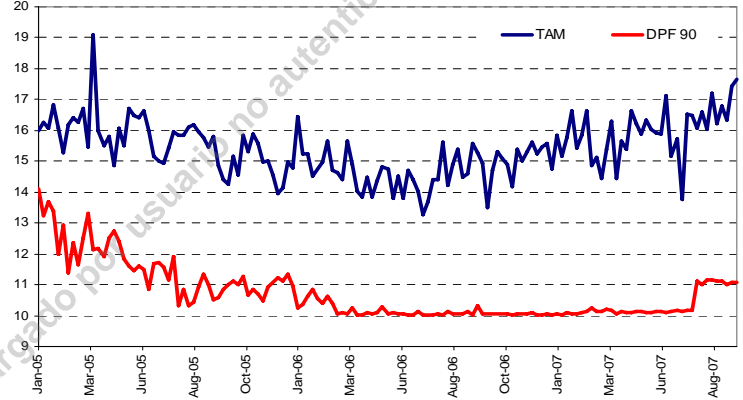
Real Expansion (M2)



Inflation
(Last 12 Months)



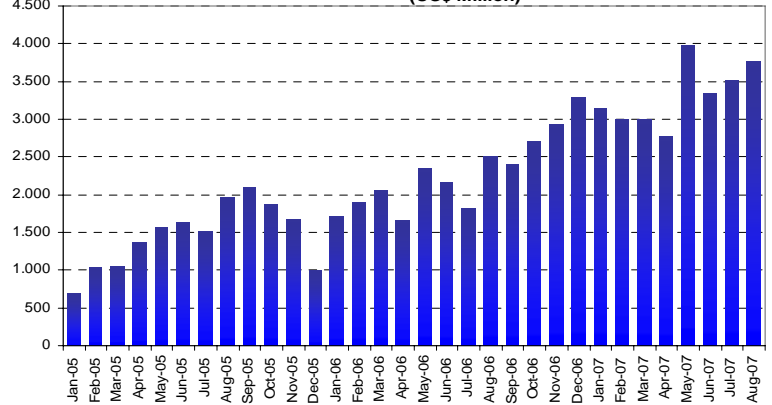
Interest Rate
(Six Principal Banks)



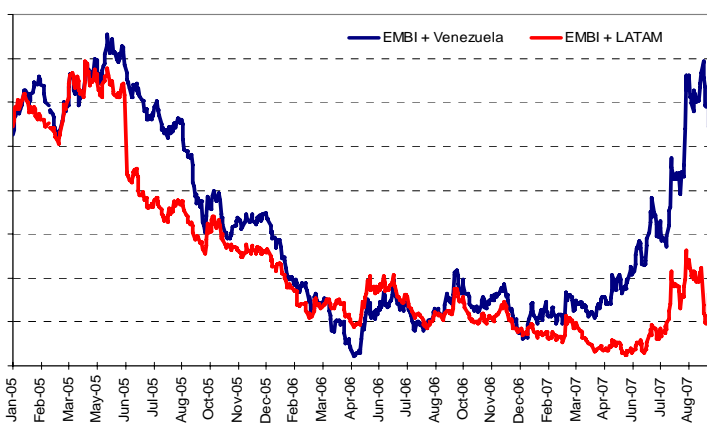
Fx Reserves - BCV
(US\$ Million)



Disbursement
(US\$ Million)



EMBI



Central Government
(VEB Billion)

