

Argentina

Proposed Amendments to Regulation of Financial Entities

Investing in

Listed LatAm Infrastructure Companies

The Roubini Group

on LatAm

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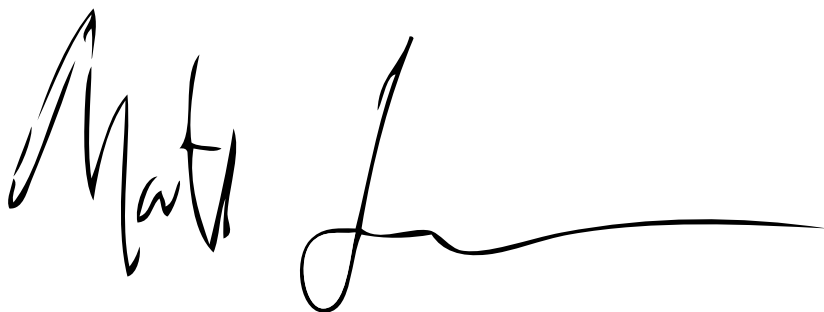
Letter from the Editor

As we approach the passing of another year with the world focused on the tedious process of recovery, Latin America is still enjoying their experience won-insulation from the most severe effects of the latest economic crisis. The region now looks within its own borders and to other emerging markets where previously only the US and Europe were potential investors. With China's growth predicted to remain stable, Latin America's anchor – Brazil – is estimated to have secure growth as ALI discussed with Latin American Economist of the Roubini Group, Bertrand Delgado. Elections have been a focal point in the region, however Brazil's administration change will most likely cause no significant ripples. The passing of Nestor Kirchner, on the other hand adds some measure of uncertainty to the future of Argentine politics, whether Mrs. Fernandez will falter without the counsel of her husband, as well as the duration of the voting public's sympathy.

I look forward to the coming year with great hope and curiosity for how the economic and political landscape will change as the 'developed' world struggles with sub-standard growth compared to the impressive numbers of this region.

In addition I would like to thank our growing readership for their support over the past year and promise that Alternative Latin Investor will continue to provide comprehensive coverage of the stories, sectors, regions and investments which fall through the cracks of main stream media.

On behalf of the ALI team and myself we wish you very happy holidays and a prosperous new year.



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INVESTING

in Listed Shares of Latin American Infrastructure Companies

■ Patricio Abal

Acquiring exposure to the Latin American infrastructure sector is becoming increasingly accessible for investors. Although the infrastructure sectors and capital markets in the region still have a long way to go to match, in many aspects, those of United States, Canada, Europe or Australia, there are a number of investment strategies that can be executed around the three clusters that make up this sector (utilities, transportation and energy) covering, in this way, a broad spectrum of risk - return profiles.

These investment strategies result from the combination of (i) the investment vehicle; (ii) the business underlying or, the investments performed by, said vehicle; and (iii) the sub-sector chosen.

There are several investment vehicles used to acquire exposure to the infrastructure sector: private and publicly traded equity funds, debt instruments issued by infrastructure builders or operators, direct investments and listed shares of companies.

The investment vehicles can have different underlying businesses or perform different types of investments. Surely the risk - return profile of the investor allocating money into a private equity fund whose mandate is to acquire stakes during the early stages of greenfield projects in Colombia or Brazil will be different to that of an investor acquiring "infrastructure bonds" issued by a Chilean concessionaire holding the rights to operate a toll road between two major cities.

The exposure to certain sub-sectors can also be the answer to the need for higher or lower risk - return. Investments in bridges, tunnels, toll roads, pipelines, energy transmission and distribution grids and water and sewage systems have a lower risk - return profile than similar investments in airports, rapid rail transit or seaports. These latter have, at the same time, a lower risk - return profile than similar investments in merchant power generation or satellite networks.

Back in 2008, Standard & Poor's estimated that the total market capitalization of global listed infrastructure assets that were members of the "S&P/Citigroup Broad Market Index" was of around \$2.8 trillion dollars.

This number will grow in the coming years and Latin America will certainly contribute to this growth. On the supply side, governments, as owners of most infrastructure assets, will keep going to the market aware of the benefits of the several ways of privatizing these assets. On the demand side, the private sector will keep competing and bidding for these assets because of some of the characteristics that shall be explained later on.

Governments from emerging economies find it hard to self-finance the construction of quality infrastructure because of a limited tax base and are often understandably concerned with the possible consequences of printing money or issuing too much debt.

Furthermore, these governments understand that not only is it important to develop high quality infrastructure, but that it is also critical to maintain high operating standards. It is often the case that private sector corporations are the only economic actors that have the resources (technological, human and financial) to meet those standards.

Moreover, as public liabilities increase (pension, health care, foreign debt, among others) and budgets stretch out, governments, this time not only from emerging economies but from developed economies as well, will continue to transfer rights

over existing infrastructure assets to the private sector in exchange for monetary compensation.

From a demand point of view, marketable infrastructure assets generally offer consistent returns. The reasons are that infrastructure companies usually have solid fundamentals, hold concession rights or licenses that restrict competition and protect them against inflation, and are usually relatively immune to the economic cycle.

Listed infrastructure shares are seen by investors as an attractive option because of intrinsic characteristics of both the underlying business and the investment vehicle.

The first reason is that recent volatility has increased the demand for assets that deliver consistent returns. Listed shares of several infrastructure companies in Latin America have shown precisely that: stability and growth. They have, over this past year, outperformed their benchmarks: the "S&P Global Infrastructure Index Fund", the "Macquarie Global Infrastructure 100 ETF" and the "S&P Emerging Markets Infrastructure Index Fund" (See graphs for this past year's performance of certain Brazilian, Chilean, Colombian, Peruvian stocks and for the benchmarks.)

It is interesting to note that, despite the evidence in the graphs, Latin American companies still have a nominal weight in the global funds. The S&P Global Infrastructure Index Fund has holdings in Brazilian, Chilean and Mexican companies but if we consider the market value of the holdings as a percentage of the fund's net assets these are 2% (Brazil), 0.77% (Chile) and 0.75% (Mexico). As for the Macquarie Global Infrastructure 100, it only has holdings in Brazilian companies and the country's weight is of 0.88%.

A second reason is that, despite certain exceptions, both oversight agencies and concession or offtake contracts allow companies providing public services to hike the rates charged to cover raising costs derived from an inflationary process. The reason is simple, a rate freeze can lead to a halt in the execution of investment plans, a decrease in the investments needed to maintain and/or expand operations, divestiture and eventually, if the government does not step in, to the company's bankruptcy. This whole process of interrupted and inefficient operations would necessarily cause an overall decline in the quality of the service provided.

Moreover, these companies benefit from relatively stable cash flows because of the nature of the service provided or because of long term contracts such as offtake arrangements. It is also because of the nature of the service provided that companies in the infrastructure sector are usually relatively immune to economic cycles particularly those that provide essential services such as those in the water and sewage sub-sector.

The need to diversify portfolio risk is another reason for investors to seek infrastructure stocks. It is precisely because infrastructure companies are protected from inflation and are

somewhat immune to business cycles added to the highly local nature of their assets that these shares have low correlations with other stocks and bonds.

Dr. Andrew Bogan, Managing Member of Bogan Associates, LLC, adds some more advantages to investing in listed shares of infrastructure companies: (i) efficiency of asset prices set in an open market; (ii) clarity of dividend yields; (iii) liquidity; and (iv) higher standards of transparency and reporting.

Needless to say, these investments are not risk free. There are a number of reasons that can make the value of an infrastructure company's stock to decline temporarily or to plummet for good.

Companies in the infrastructure sector often provide critical services to the population therefore governments zealously regulate and oversee their operations and maintenance, financial and commercial transactions, rates, customer service, etcetera. The danger that Dr. Bogan mentions of governments capping prices and squeezing profitability in an effort to benefit consumers is always present and has occasionally materialized in the region.

Certain governments in the region have also chosen, sometimes making it state policy, to nationalize infrastructure assets because of ideology and/or the cash flow.

There is also a systemic risk associated with investing in a large market that cannot be avoided. Yet, it is important to distinguish the short-term risk from the long-term risk. The latter depends on the company's fundamentals and, in general, companies in the infrastructure sector offer solid ones.

To conclude, it is clear that as Latin America consolidates its economic growth the infrastructure sector will have to keep up with the rest of the sectors. Fortunately, most governments in the region have adopted policies that foster the involvement of the private sector in the development of infrastructure. The results of these policies will not only benefit the general population but also a wide range of investors.

As we have seen, some private sector corporations are listed in the domestic and, in some cases, international stock exchanges, and can boast attractive results. As more infrastructure companies go public, it will be interesting to follow the creation of more funds with a mandate to invest in their stocks and also to study the regulatory impact, if any, of this increased exposure to market volatility.

Patricio Abal is Alternative Latin Investor's Infrastructure Editor. He holds a J.D. from the Universidad Católica Argentina and is a Master in Project Evaluation Candidate at UCEMA & ITBA in Buenos Aires, Argentina. He is an Associate at DFG Abogados.

DISCLAIMER: The contents in this article are not intended to serve as any type of recommendation, reference, advice, suggestion, and/or proposal for the design and/or execution of any and all types of financial products and/or investment strategies and/or commercial transactions.

Benchmarks



EMIF: iShares S&P Emerging Markets
Infrastructure Index Fund

GII: SPDR FTSE/Macquarie
Global Infrastructure 100 ETF

IGF: iShares S&P Global
Infrastructure Index Fund

Source: Google Finance

Brazil



CIG: Companhia Energetica de Minas Gerais (ADR)

SBS: SABESP (ADR)

CPL: CPFL Energia (ADR)

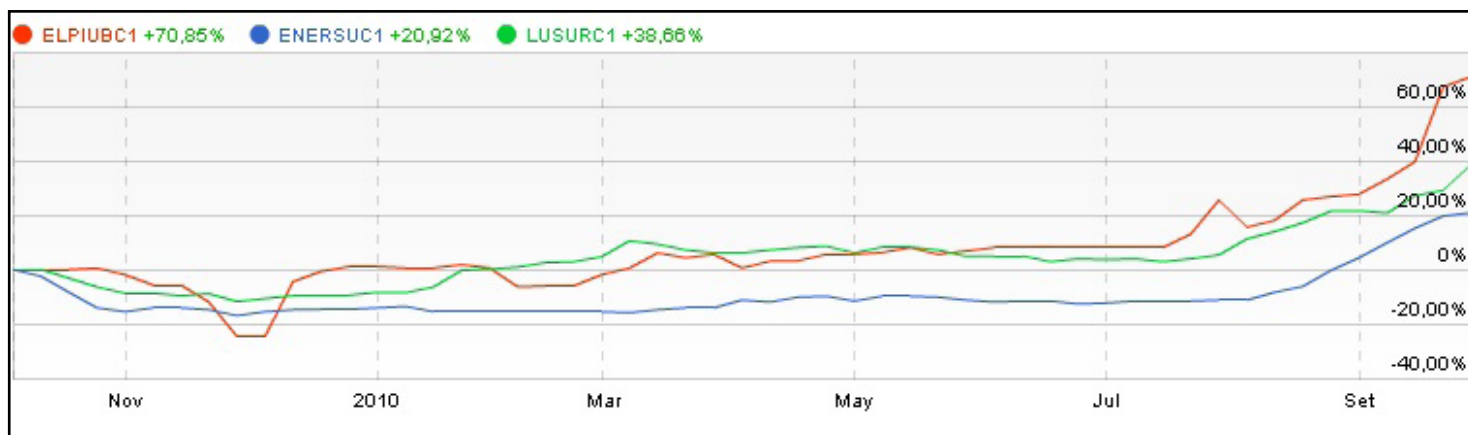
Electric Energy: generation, transmission, distribution, and commercialization

Water and sewage services

Electric Energy: generation, distribution, and commercialization

Source: Google Finance

Peru



ELPIUBC1: Empresa Eléctrica de Piura S.A.

ENERSUC1: EnerSur S.A.

LUSURC1: Luz del Sur S.A.A.

Electric energy: generation and distribution

Electric energy: generation

Electric energy: distribution

Source: Lima Stock Exchange ("Bolsa de Valores de Lima")

Colombia



GASNATURAL: Gas Natural S.A. E.S.P.

Gas: storage, commercialization and distribution

EEB: Empresa de Energía de Bogotá S.A. E.S.P.

Electric energy: transmission

ISAGEN: ISAGEN S.A. E.S.P.

Electric energy: generation and commercialization

Source: Colombian Stock Exchange
("Bolsa de Valores de Colombia")

Chile



ENI: Enersis S.A. (ADR)

EOC: ENDESA - Empresa Nacional de Electricidad S.A. (ADR)

Electric Energy: generation, transmission, and distribution

Electric energy: generation and commercialization

Source: Google Finance

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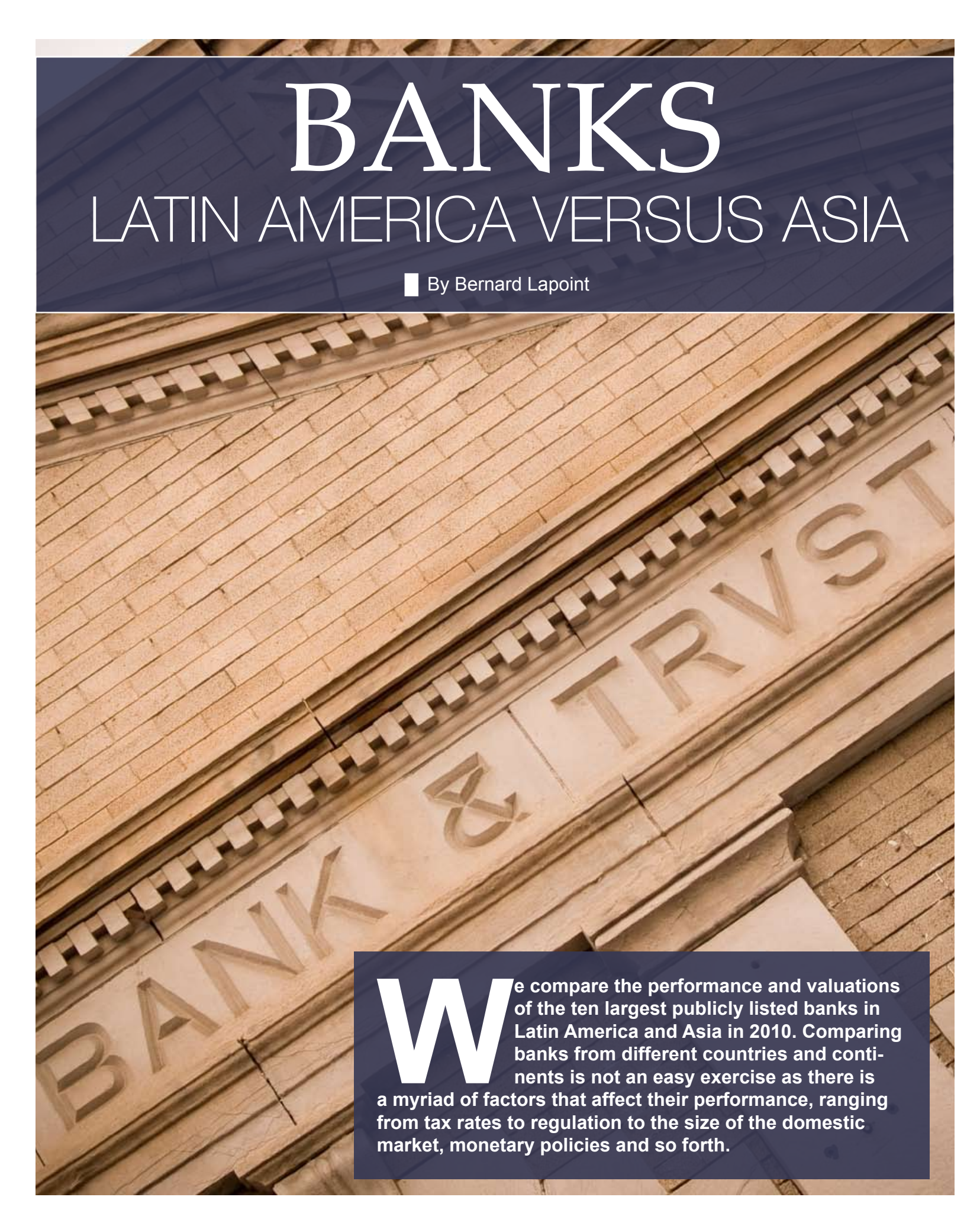
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BANKS

LATIN AMERICA VERSUS ASIA

■ By Bernard Lapoint

We compare the performance and valuations of the ten largest publicly listed banks in Latin America and Asia in 2010. Comparing banks from different countries and continents is not an easy exercise as there is a myriad of factors that affect their performance, ranging from tax rates to regulation to the size of the domestic market, monetary policies and so forth.

Overall LatAm banks have performed better so far in 2010 with nine of the ten largest returning positive price performances with Credicorp (+61%) and Banco De Chile (+60%) leading the group- see Figure 1. In Asia returns are weaker with three banks showing negative returns. In fact only the two Indian banks in the sample, State Bank of India (+41%) and ICICI (+29%), have strong double digit returns. Agricultural Bank of China, up 18% since its initial public offering earlier this year, saves the year for China as results are fairly dismal otherwise- see Figure 2.

Figure 1. Ten largest Latin American banks by market capitalization

	Bank	Country	Market Cap US\$, mn	Price/ Book Value 2010, (x)	Stock Price Performance, Local Currency 2010, (%)
1	Itau Unibanco	Brazil	96,128	3.2	10
2	Bradesco	Brazil	67,925	2.9	-3
3	Santander Brasil	Brazil	46,255	1.5	3
4	Banco Do Brasil	Brazil	46,520	1.9	13
5	Santander Chile	Chile	14,547	4.2	42
6	Bancolombia	Colombia	11,102	3.3	47
7	Banco De Chile	Chile	10,367	3.9	60
8	Credicorp	Peru	9,159	3.9	61
9	Banorte	Mexico	7,473	2.0	5
10	Banco Macro	Argentina	2,935	2.6	56

Note: Data as of 21 Oct. 2010

Source: Bloomberg, Deutsche Bank, Credit Suisse

Figure 2. Ten largest Asian banks by market capitalization

	Bank	Country	Market Cap US\$, mn	Price/ Book Value 2010, (x)	Stock Price Performance, Local Currency 2010, (%)
1	ICBC	China	270,451	2.3	-2
2	Construction Bank	China	227,243	2.2	13
3	Agricultural Bank	China	151,070	1.8	18
4	Bank of China	China	150,082	1.6	9
5	Bank of Communications	China	62,019	1.8	4
6	Merchant Bank	China	58,347	2.9	12
7	State Bank of India	India	42,763	2.6	41
8	Citic Bank	China	30,916	1.4	-14
9	ICICI	India	26,350	2.4	29
10	Shanghai Pudong Bank	China	24,923	1.4	-32

Note: Excluding Japan, Hong Kong, Singapore. Data as of 21 Oct. 2010

Source: Bloomberg, Deutsche Bank, Credit Suisse

By total market capitalization the ten largest Asian banks dwarf LatAm banks by a ratio of over three to one. ICBC (Industrial and Commercial Bank of China) by itself has a market capitalization equal to that of the five largest LatAm banks combined!

The sample in Latin America is geographically diversified with six countries represented although Brazilian banks by far dominate in terms of size. In Asia, Chinese banks understandably trump all others with eight of the top ten by market cap. India manages to place two banks in the list. Absent are the Korean and Taiwanese banks.

What about valuations?

In terms of price to book value (P/BV), LatAm banks in the sample are slightly more expensive but have higher returns on capital (RoC) than their Asian counterparts. Historically the correlation between the two indicators is fairly high. LatAm banks' weighted P/BV and RoC is 2.7x and 18.6% versus 2.1x and 16.6%, respectively, in Asia. As figure 3 shows, however, Asian banks dispersion of P/BV and RoC is narrower than in Latin America. In the former, the median of P/BV and RoC is very close to the weighted average. LatAm banks are 'less similar', probably a result of a lack of economies of scale outside of Brazil. In fact, in the sample we note that banks from Chile and Peru, small domestic markets, have higher P/BV than Brazilian banks, which operate in a large market.

Figure 3. Valuations of ten largest banks

	Price/ Book Value		Return on Capital	
	Avg Weighted	Median	Avg Weighted	Median
Latin America	2.7x	3.1x	18.6%	19.4%
Asia	2.1x	2.0x	16.6%	16.7%

Note: Weighted by market capitalization

Source: Credit Suisse, author calculation

Interestingly revenue growth for Asia banks is forecasted to be stronger than in Latin America for 2010 and 2011.

Figure 4. Median Revenue Growth, year/year

	2010 F	2011 F
Latin America	7%	13%
Asia	25%	18%

Source: Bloomberg, author calculation

One further differentiable element between banks on both continents comes from foreign banks participation in the domestic banking system. In China and India foreign banks have a very small share of the loan/ deposit market and cater mostly to high-net worth individuals and corporations in large urban areas such as Beijing, Shanghai and Guangzhou. On the other hand in Mexico, foreign banks have close to 85% of total assets in the banking system. The number is lower in Brazil, 16%, but still higher than in China and India.

What can investors expect?

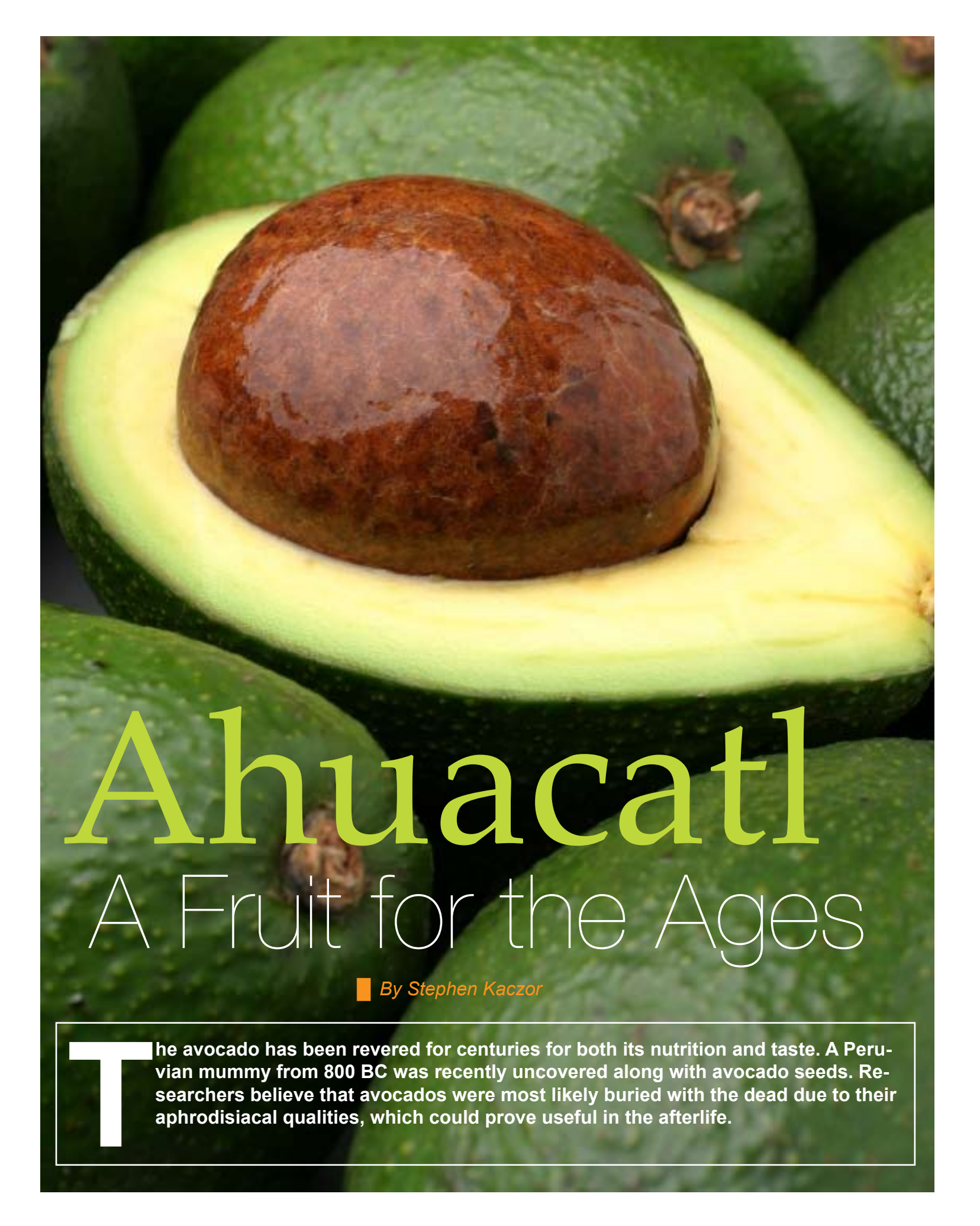
At the beginning of the year it was expected that Chinese banks would come to the market to raise funds and that some foreign shareholders – including some of the large western banks- would probably unload part of their holdings. It has happened and consequently this has put downward pressure on share prices. We believe that the bad news is in the price for Chinese banks and at current levels some interesting bargains are available for investors with a 12-18 month view, especially in Shanghai Pudong Bank.

In Latin America we think that stock returns and valuations are somewhat stretched except for Santander Brasil and Banorte and would probably lock in profits as the year-end approaches. Smaller banks, not covered here, could be interesting M&A targets from

the largest Brazilian players such as Banco Do Brasil, Latin America's largest bank by assets, or Itau Inibanco. It is no secret that Brazilian banks are looking to expand on the continent in order to compete with Spain's BBVA which has subsidiaries in five countries.

In conclusion, some of the largest Chinese banks offer better price appreciation prospects than most large Latin American comparables.

Mr. Lapointe is currently the managing director at ArgonautGlobal Capital, a capital advisory firm with a special focus on India and China. He spent ten years with Société d'Analyses Economiques et Financières, a French-based investment advisor, acting as global equities portfolio manager and co-chief of strategy. Prior to that he was with Bank of America (New York) as an Asian equity trader and Optimum Gestion (Montréal) as an international equities portfolio manager. Mr. Lapointe holds a Master's degree in Economics from the University of British Columbia. He speaks French and Mandarin.



Ahuacatl

A Fruit for the Ages

■ *By Stephen Kaczor*

The avocado has been revered for centuries for both its nutrition and taste. A Peruvian mummy from 800 BC was recently uncovered along with avocado seeds. Researchers believe that avocados were most likely buried with the dead due to their aphrodisiacal qualities, which could prove useful in the afterlife.

Avocados are high in valuable fats and appear to have a beneficial effect on blood serum levels. For a typical avocado:

- About 75% of an avocado's calories come from fat, most of which is monounsaturated.
- Avocados have 60% more potassium than bananas.
- They are rich in vitamins B, E, and K.
- Avocados have a high fiber content among fruits.
- High avocado intake has been shown to have a beneficial effect on cholesterol levels.

The avocado is a tree native to the Caribbean, Mexico, South America and Central America, classified in the flowering plant family Lauraceae along with cinnamon, camphor and bay laurel. Avocado or avocado pear also refers to the fruit (technically a large berry) that contains a large seed of the tree, which may be pear-shaped, egg-shaped or spherical. Avocados are a commercially valuable fruit and are cultivated in tropical climates throughout the world (and some temperate ones, such as California), producing a green-skinned, pear-shaped fruit that ripens after harvesting. Trees are partially self-pollinating and often are propagated through grafting to maintain a predictable quality and quantity of the fruit. The Aztec word for avocado is *Ahuacatl* meaning testicle tree due to the fact that the fruit of the tree hangs in pairs. Cortez conquered Mexico in 1519 to find avocados everywhere. Today, the Mexican state of Michoacán is the avocado capital of the Americas.

In Argentina, Bolivia, Chile, Peru, and Uruguay, the avocado is known as "palta", its Quecha name. The Nahuatl word for the fruit "ahuacatl" can be compounded with other words, as in *ahuacamolli*, meaning 'avocado soup or sauce', leading to "guacamole" in Mexico and the world.

Not until 1926 did Mr. Hass discover the avocado that bears his name. Today there are more than 40,000 acres of avocados in California, over 60% in San Diego County. Hass is the predominate cultivar; it tolerates cold far better than indigenous varieties. Avocado consumption has outpaced increases in production in the USA, so exports have trended downward. The USA is the world's largest avocado importer; it produces only half of what it consumes. The Hass Avocado Board has been a very successful generic commodity promotion board, credited for increasing the market for avocados to the point that few Superbowl parties lack guacamole.

Chile's avocados often have more oil than California's, making for a smoother texture. Chilean avocados are grown in the Central Valley, mainly between Petorca and Rancagua. But the transit distance to the U.S. is not easy on this delicate fruit. Yet Chile exports the majority of its avocado production, and the USA receives over 80% of its exports. Chile and the USA combined produce only 40% of Mexico's avocado yield.

Mexico is the leading producer of avocados worldwide, with over one million metric tons annually. Mexico's exports surpassed Chile's in 2005. P. Americana, or the avocado, originated

in Puebla, Mexico. The oldest evidence of avocado use was found in a cave located in Coxcatlán, Puebla, from 10,000 BC.

Colombia, Brazil, Peru, and the Dominican Republic have also been successful in commercializing avocados. Among consumers, France, Japan, and the Netherlands are the largest importers after the USA.

Avocado prices have fallen from over \$2,000/ton in 1990 to as little as \$1,200/ton in some years; they are highly variable due to production fluctuations. More predictable are demand increases, which have led to a stable and growing market in the USA and beyond. For a commodity and price profile, see aic.ucdavis.edu*/profiles/Avocados-2006.pdf

The avocado is climacteric, meaning a fruit that matures on the tree but ripens after picking or falling to the ground. The trees are only partially self pollinating and they do not bear fruit until year five. The premier research centers for avocado propagation are the Volcani Centre in Israel, the Instituto de Investigaciones Agropecuarias in Chile, and the University of California, Riverside.

According to Volcani's Amos Blumenfeld, "The avocado is unusual in that the timing of the male and female flower phases differs among cultivars." Another unique consideration is that certain cultivars, such as the Hass, have a tendency to bear well only in alternate years. After a cold season with low yield, the trees tend to produce abundantly the next season.

Stephen is a Panama-based writer, entrepreneur, and consultant. He is a partner at International Market Resources, a Latin American trade consultancy, and the founder of Changes In Latitude, a travel company. The focus of Stephen's consulting is strategic market development, research & management. In addition to consulting and writing, he is passionate about Latin American culture, travel, and sustainable agriculture.



Latin American Art Gains Momentum in Europe

■ By Stefanie Kogler

Art from Latin America has seen a steady rise in buyers over the past three decades or so. As reported in a previous issue of ALI, Christie's organized its first auction of Latin American Art in 1981 and now holds two auctions a year that specialize in art from this region. Names such as Frida Kahlo, Fernando Botero, Jesús Rafael Soto and Carlos Cruz Díez among many others have become household names and some of them sell artworks in excess of US \$2 million. Virgilio Garza, Head of Latin American Art at Christie's stated that the world record in art sold from Latin America reached a total of \$33 million made at auction in recent years.

There is not only great interest in Art from Latin America in the USA. As of lately, this interest has gained momentum in Europe. TATE Modern, one of the UK's biggest public collections of modern and contemporary international art inaugurated its collection of Latin American art and has since acquired 317 works of art from that region. In a recent press release, Nicholas Serota, the Director of TATE stated that '...[the] Collection has been significantly enriched over the past decade with an expanded geographical reach and an energetic focus on collecting work from areas outside Europe and North America, particularly in Latin America...'. TATE held retrospective exhibitions of both Hélio Oiticica and Cildo Meireles with considerable success. As mentioned in Alternative Latin Investor's last issue, PINTA the Modern and Contemporary Latin American Art Fair set up stall in the UK for the first time in June 2010.

It was hailed as a success by the organizers and galleries involved. PINTA not only brought a number of well-known and established artists to Europe, it also introduced new comers to the European art market. Numerous European collections and museums acquired artworks during the fair. Museo Nacional de Arte Reina Sofía in Madrid, Centre Pompidou in Paris and of course our own TATE Modern in London ensured that Latin American Art is here to stay.

It is in this vein that Austin/Desmond Fine Art decided to venture into this area and showed its first exhibition of Geometric Abstract Art from South America and Europe. 'Abstraction Creation Post-War Geometric Abstract Art from Europe and South America' is a survey of 29 artists that were especially active from the 1940's until the 1970's. This time is marked as one that enjoyed significant artistic advances in both South America and Europe. The list of artists is impressive and includes some notable and well-known names from both sides of the pond such as: Max Bill, Klaus Staudt, Raúl Lozza, Mira Schendel, Luis Sacilloto, José Pedro Costigliolo, Carlos Cruz Díez, Sergio

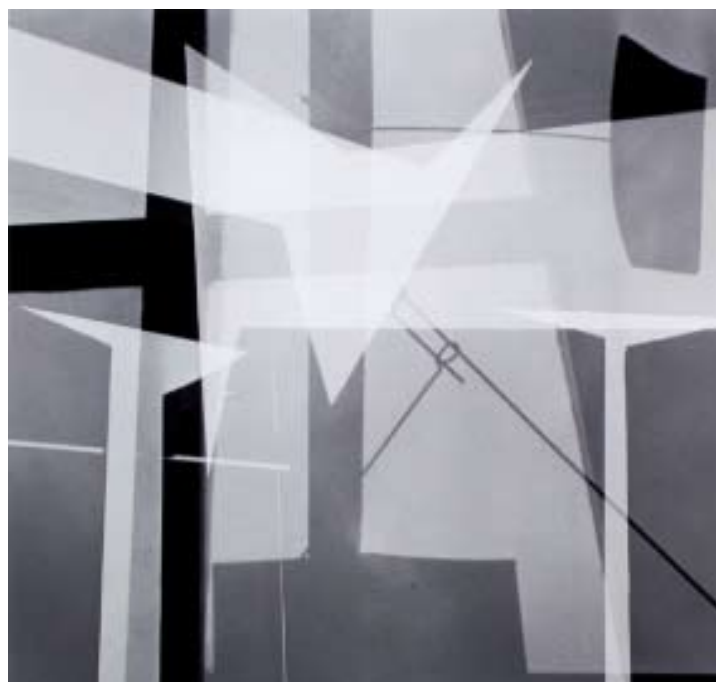


Figure 1: Geraldo de Barros, Pampulha (from the series Fotoforma), 1949

Camargo, Victor Vasarely, Anthony Hill, Heinz Mack, Mary Martin, Francois Morelet, Joseph Albers, Arturo Bonfanti, Jesús Rafael Soto, Carmelo Arden Quin, Antonio Calderara, Gianni Colombo, Aurélie Nemours, Antonio Llorens and Bridget Riley. Moreover, key artists from the concrete art movement in Brazil in the 1950's include Hélio Oiticica, Lygia Clark, Lygia Pape, Lothar Charoux, Geraldo de Barros and Hermelindo Fiaminghi. Their contribution to geometric abstract art is undeniably pertinent and this is successfully recognized in this exhibition. All artworks move away from figurative representation and seek to find true meaning in abstraction and geometric forms. Triangles, rectangles, circles, cubes, plains, colour, light, irregular



shaped frames are a recurring element in all works, which visually reminds the viewer of the strong conceptual beliefs behind the art production during those years. The use of material is diverse and the mediums include paintings, photography, collages and sculptures and journals. Walking through the gallery, the themes and ideas, despite being from different artists from opposite ends of the world, mirror a common drive away from the

figurative tradition and toward a fresh, exciting and conceptual way of creating and approaching art.

The importance of Brazil as producer, and at the same time, buyer of art is highlighted by John Austin, Director of Austin/ Desmond Fine Art: Brazil is a major world economy, Brazilian art collectors have always been very serious buyers but mainly nationalistic. Domestic Brazilian artists have been reaching enormous prices, for example, prices for Sergio Camargo works are now in excess of a million dollars. However Brazilian collectors are becoming more international, buying other Latin American artists such as Venezuelan artists Carlos Cruz-Díez and Jesús Raphael Soto. A country like Argentina, not a very rich country but has a great history of Concrete Art, these artists are also beginning to catch the eye of Brazilian collectors... Although it is Brazil that seriously collects and produces art, Europe is definitely beginning to catch up with the interest and perpetuates a steady increase in prices of artworks from all over Latin America. There seems to be no better time than now to become involved and invest.



Figure 2: Austin/ Desmond, from right to left: Victor Vasarely, Wombi - 2, 1956, Anthony Hill, Relief Construction, 1962, Sergio Camargo, untitled, 1973

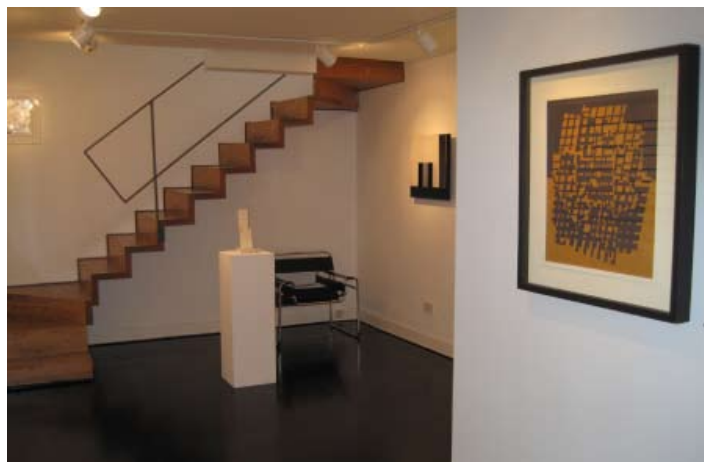
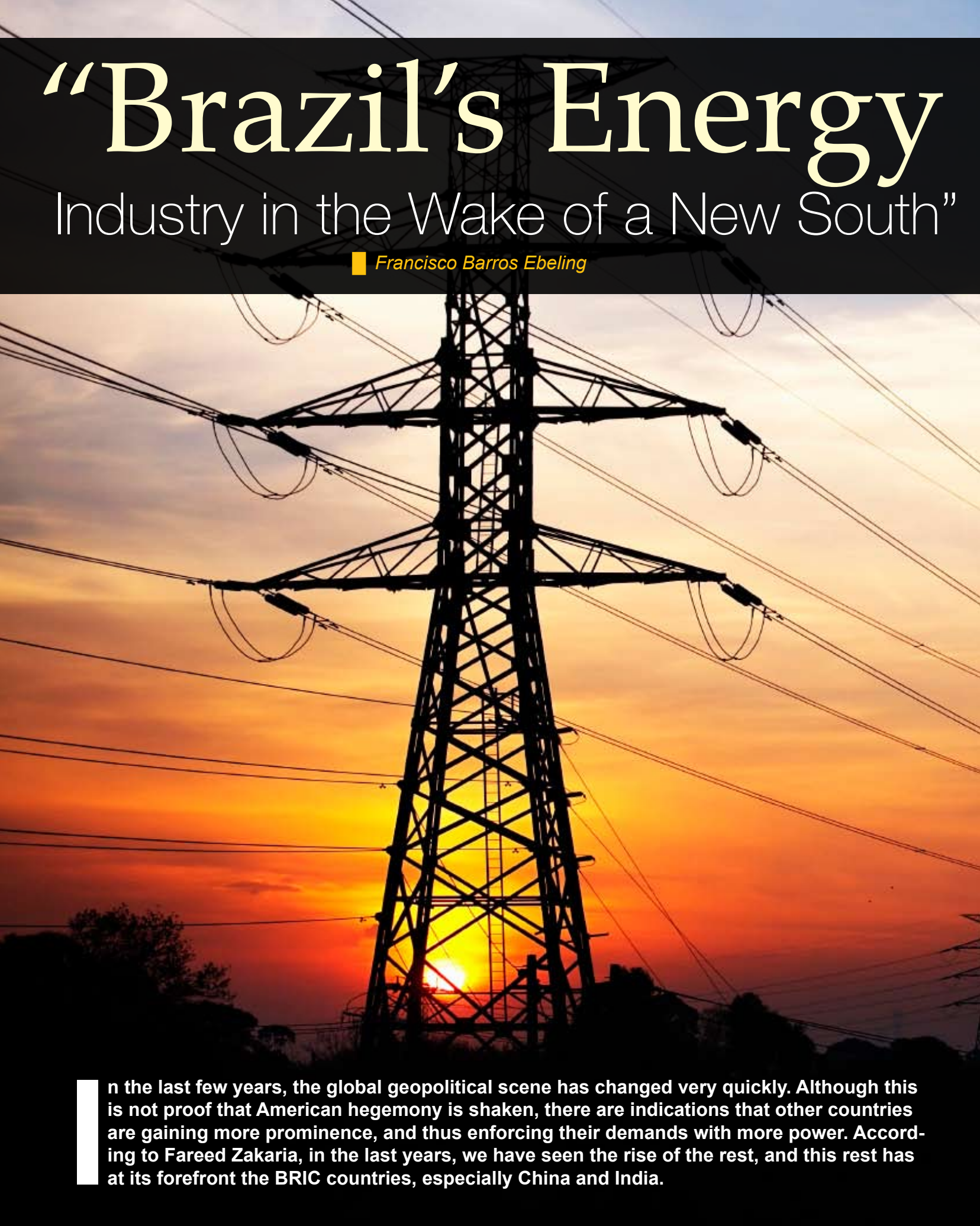


Figure 3: KLaus Staudt, Gleichmäßig Hell/Dunkel, 1972-1973



Stefanie Kogler is a Latin American Specialist focusing on Art in Latin America. She graduated at the University of Essex, UK and worked as Archive Assistant at the University of Essex Collection of Latin American Art (UECLAA) Europe's biggest public collection of Latin American Art. Stefanie continues to be involved with the Collection voluntarily. She has written an in depth undergraduate dissertation on censorship in Contemporary Colombian Art which achieved one of the highest marks in her year group. As part of her degree, Stefanie spent a year in South America studying and researching Art in Latin America. She will attend a Master in Curating Latin American Art at the University of Essex. Currently, she is involved with the research and execution of 'Abstraction- Creation- Post-War Geometric Abstract Art from Europe and South America' at Austin Desmond Fine Art, London, UK.



“Brazil’s Energy Industry in the Wake of a New South”

■ *Francisco Barros Ebeling*

In the last few years, the global geopolitical scene has changed very quickly. Although this is not proof that American hegemony is shaken, there are indications that other countries are gaining more prominence, and thus enforcing their demands with more power. According to Fareed Zakaria, in the last years, we have seen the rise of the rest, and this rest has at its forefront the BRIC countries, especially China and India.

Due to their quick economic growth and the potential that they have - both material and human - these countries have increasingly been bringing to the global agenda the issues that still hinder their full development, in particular the issues of energy and raw material supplies. In this sense, in the last years, multilateral relations that are entirely new and that will have the ability to shape new global geopolitics have emerged. Recently, when they want to commercialize their products or obtain their raw materials, these countries don't necessarily dialogue with the countries that they used to. In this context, relations between Brazil and China or between South American countries and India occur.

In the field of energy, this new tendency has taken on a special character in the last two or three years. In global geopolitics, it has long been speculated that Brazil would become a kind of "farm" for the world, since it would be one of the most fruitful, due to its arable land and natural resources such as water. The Brazilians, of course, refuse to accept this tendency, since specialization in primary-exporting activities has a side-effect, at least in the historical experience of other countries, a fast and cruel process of deindustrialization. There is evidence and theories proving that this Brazilian "manifest destiny" is not inexorable, or in other words it is possible to reconcile economic development with fairness in agriculture and mining. The key is to reinvest what has been generated in agriculture and in mineral extraction into the industrial dynamic sector, as has been well theorized by developmental structuralism authors. There is, however, a long way to go, but the current state of the nation has shown optimism about the possibilities that this dual development, based on a combination of industry and extractive activities, can transpire.

In the field of energy, Brazil has gained prominence in the last years due to two main developments. Since the beginning of the first decade of the third millennium, the world has seen Brazil as a big center for production of biofuels. In recent years, this interest has manifested itself in a stronger way as foreign capital has been invested in this business. One example has been the recent fusion of Cosan, the largest Brazilian sugar-alcohol company, with Shell, in which their business networks were merged. This has spurred an increase of industrial concentration in the sector, as the Brazilian players feel threatened in their positions, and therefore begin to buy their competitors. Someday we will probably see something like the "seven sisters of ethanol" coming out in Brazil as a kind of company oligopoly in the sector. On an international level, such configuration will be virtuous because it is going to improve the terms of exchange in the sector and it will enable it to attract the necessary financing to increase the biofuel production.

The second focus area is on the pre-salt oil, which nowadays is nothing new. This prospective area will concentrate, in the coming years, on massive economic resources, both technological and human, to allow a production that is believed to reach as much as five million barrels a day by 2020 - by adding the pre-salt to the so-called post-salt production, which are the fields where oil was previously exploited in Brazil. As Brazil is a peaceful country with regards to global diplomatic relations - there are no significant disputes with neighbors or even internal rivalries - the international partners, who seek supply sources of energy such as ethanol or oil, naturally see with great interest the possibilities of doing business involving energy in Brazil.



That's where the emerging BRIC countries come in - especially China and India. In basic terms, the first is hailed to be the world manufacturing center and the second is the leading provider of human resources. They are not specialized in energy but have an open and honest channel of communication with Brazil. In the ideological spectrum, the three are emerging countries of the "south of the world." Thus, business relationships involving these agents tend to work.

Three recent examples stand out. In the last year, the Chinese have been looking eagerly for Brazilian pre-salt. This is reflected by investments in Petrobras that are planned to happen in the next years, as well as by autonomous investments from Chinese state oil companies in other prospecting areas other than pre-salt and, more recently, by the desire of these firms to have greater participation in companies that are operating here already. Just over one month ago, Sinopec bought 40% of Repsol's assets. The transaction was US \$4.1 billion dollars. Sinopec and CNOOC have also indicated the possibility of buying part of the assets of OGX – an oil company owned by the billionaire Eike Batista, ranked seventh richest billionaire by Forbes magazine. This business deal has not materialized yet.

The Indians, on the other hand, have been interested in ethanol. According to a report published by "Valor Economico" last month India wants to import Brazilian ethanol because they have raised the levels of ethanol in their gasoline to 5%, which could represent an annual consumption estimated at 1.05 billion liters per year. If it turns into a business, the Brazilian market will find an excellent business partner with a dynamic market which can, above all, be long-lasting. This could ensure the sales of large parts of Brazilian ethanol, which would free the Brazilian ethanol companies from market fluctuations that are much less safe, such as in the case of the American market, a potential competitor. All of this is due to good relations - bilateral and ideological - that guarantee convergence of commercial interests.

The most resourceful example, however, is the possibility of exporting Brazilian technology rather than the product itself, in

order to produce biofuels in Africa. Africa is a continent where Chinese capital has had a leading role in many countries for more than a decade, which provides subsequent returns to China. If this model gets consolidated, we will have a commercial relationship between these countries in terms of energy, which will be completely unique and beneficial to all parties. While Brazil could improve as a future holder and supplier of technological solutions and products, the African countries could be able to generate jobs and foreign exchange. In addition, the Chinese would have a guaranteed supply of energy (its biggest concern) that would be clean, unlike coal, a fuel used on a large scale in Asia. It is, in short, a genuine win-win situation, where all nations prosper in a partial reconfiguration of international relations guided by "the rise of the South."

In conclusion, there are new elements being formed that will change, at least on a small scale, the geopolitical world's energy scene, which has as its backdrop the improved relationships of such culturally diverse but economically and socially similar countries as China, India and Brazil. The change will not be very abrupt because the cooperation involving energy with developed countries such as the United States will still be much stronger and managed by very powerful agents.

Unlike former geo-economical tendencies and cycle geo-economics which clearly took the form of a center and a periphery - thus involving a relationship of uneven exploitation - this new relationship which has been set up will form a new foundation not necessarily based on a clear hegemonic center.

On the other hand, cooperation is now a key element, although the economic and political power of these new partners is not necessarily equal. Therefore we cannot discard power asymmetries, but these are not a focus in this primary phase. For business, this is an excellent prospect, as some markets that simply did not exist previously will be developed. It is an entirely new niche and it will be extremely beneficial for the Brazilian economy, and also for the future of South America, because there is a tendency for other countries in the continent to embrace new relationships that are being formed.

About the Author

Francisco Ebeling Barros is an economist, currently serving on the board of Management of Economy and Energy Policy of the IBP - Brazilian Institute of Oil, Gas and Biofuels. He studied at the Institute of Economics of UFRJ, has completed specialization courses in Energy Economics and has worked as a research assistant in the Group for Energy Economics from UFRJ. He is the editor of the monthly PPI Monitor (www.ibp.org.br) and is one of the editors of the literary Beehive (www.revistacolmeia.com.br). He is also a member of AB3E (Brazilian Association for Studies in Economics of Energy) and IAEE (International Association of Energy Economics).





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Global Economy:

Leveraging the power of technology to improve lives

“ I see Latin America and Asia and the Middle East in similar positions in that both regions are witnessing impressive economic growth yet in many places failing to lessen the gap between rich and poor. The digital divide plays a large role in this gap in these regions and therefore our organization can play a similar role of helping to bridge this divide ”

- Moustafa Mourad, Interim President, One Economy

One Economy is a global non-profit organization whose mission is to ensure that every person, regardless of income and location, can maximize the power of technology to improve the quality of his or her life and enter the economic mainstream. Their initiatives help to bring broadband internet into the homes of low-income individuals, employ youth to train their community members to use technology effectively, and provide public-purpose media properties that offer a wealth of information on education, jobs, health care and other vital issues.

Reports show a direct correlation between broadband penetration and employment growth. One Economy's media properties training and tools offer solutions that can lead to inclusive economic growth globally. Most countries in the region have seen a boom in Internet service offerings in recent years, and it is now critical to have both skills and appreciation for technology to find a good job. Unfortunately, many of Latin America's poorer areas and citizens lack these important skills and they risk falling even farther behind socioeconomically if nothing is done about it.

One Economy uses a participatory approach in bringing 21st century technology to communities. They work directly with community leaders, NGOs and elected officials to ensure they are providing information and resources that are relevant to each region. Their commitment to fully engaging the communities enables them to offer a unique value proposition in Latin America. According to Global One's Interim President Moustafa Mourad "Our programs can be a part of a productive solution for bridging both the technological and socioeconomic divide that plagues low-income Latin Americans, so that they may find opportunities to improve their lives and communities."

One Economy has considerable experience working with the Latin American populations in the US and has training programs and Internet web content that have been specifically designed for this population - such as the Spanish version of the their online resource forum - US Beehive, and our special section "La Buena Vida". These assets were a great basis for their expansion into Latin America.

In an interview with Interim President, Moustafa Mourad, Alternative Latin Investor inquired as to which regions of Latin America he felt have the most sincere need for One Economy's program initiatives. Mr. Mourad responded, "There are many areas in Latin America where low-income communities do not have affordable access to the Internet and online resources.





Potato farmer from Rwanda

Our vision is that every person has that access and we will be bringing initiatives to every underserved Latin America community. Even in countries with strong economies, there are residents and communities that lag far behind. One Economy will work wherever the technological divide threatens equitable prosperity.”

Currently One Economy has been joined by community and corporate leaders, residents and elected officials, Cisco and E-Mexico for a special premiere of www.InfoFacil.mx, a website that will connect low-income residents of Mexico to online interactive tools to improve their lives and enter the economic mainstream. InfoFacil.mx, which is One Economy and Cisco's first joint initiative in Latin America, will provide information on jobs, money management, health care, education, civil rights, and other issues pertinent to Mexico.

Moustafa Mourad (Interim President of One Economy) and Eloisa Talavera (director of e-Mexico) In addition to bringing important resources to low-income residents, InfoFacil.mx also supports the Mexico government's National Development Plan, which includes increasing technology advancements in order to improve Mexico's economic outcomes. One Economy also plans to partner with E-Mexico to operate 8,000 technology centers in poorer areas of Mexico.

Currently One Economy is seeking funding to launch a youth technology and leadership program in Latin America. After completing the curriculum, the youth would become technology ambassadors in their communities, helping residents and family members use technology more effectively.

Finally, they are developing mobile phone-based solutions that interact with relevant online content, which will allow them

to bring invaluable resources to the growing population that is more likely to receive information via mobile devices than computers.

From an investment perspective, now is the time to invest in organizations such as One Economy whose focus is the spread of technology. If Latin America is going to reach the levels of a fully developed economy it must have societies where more citizens have a chance at entering the economic mainstream. Widespread technology adoption is absolutely critical in this process. Access to high-quality information, online tools, and training can enable low-income people to lead their own development. This can enable more people to find sustainable opportunities for growth for themselves and their communities, offering more economic growth for society.

One Economy has created a successful model for leveraging 21st century technology globally and facilitates each step to digital empowerment. One Economy executes and implements its initiatives through strong public-private partnerships and engages local stakeholders, including local community organizations and other non-profits to create a comprehensive and sustainable digital network.

“I and numerous members of my community are extremely grateful and thankful. We hope that One Economy continues to help this community as there is high unemployment rate and this center allows the youth and the unemployed access to jobs.”

As one example of a community that has made a successful turn around do to the attention of One Economy is Jordan Beehive - a community website which receives 90,000 visitors a month, on average, for its content in Arabic. During their stakeholder engagement session in Amman residents informed One Economy of the immense need for information on pregnancy for women in Jordan. There was very little written on this topic in Arabic and pregnancy is still not a comfortable topic for many people in a public setting. The Arabic content on pregnancy available on this website now receives thousands of visitors each week from countries across the Middle East and North Africa and users of the site have

sent One Economy significant feedback telling them how the site has helped them have healthier and more informed pregnancies.

Another example is not a community but a person whose life was greatly impacted by having access to the Internet and relevant online information.

Rita, a struggling mother of two daughters enrolled in computer classes at One Economy's Community Knowledge Center, funded by Cisco, in Durban. Though she had no knowledge of computers or the means to purchase one, by the end of the course she had created a business plan and today is a successful entrepreneur.

She continues to use the center for day-to-day operation of her business including online networking with other business people. "I and numerous members of my community are extremely grateful and thankful and hope that One Economy continues to help this community as there is high unemployment rate and this center allows the youth and the unemployed access to jobs."

One Economy is predominantly funded by private firms with a strong sense of corporate social responsibility. One of their biggest funders for their global work is Cisco. They also work with Citigroup and Symantec. These organizations are supportive of One Economy's mission and offer not only funding but products, services and time in helping them to expand their work. The majority of donors are indeed private technology companies who understand not only One Economy's philanthropic value but also how they can help grow their customer base in crucial emerging markets.



In line with standard practice in the nonprofit industry, One Economy's projects have a maximum of 12% overhead costs. Of the total amount of each grant, 88% must be used directly in program implementation.

One Economy receives grants for launches of technology projects which are available to anyone with access to the internet

well beyond the time of the grant period, and One Economy continues to devote resources and staff to operate projects beyond the time of initial funding. Therefore, it would be fair to say that, over time, 100% of the funding reaches the poor directly. According to Mr. Mourad, "When One Economy was founded ten years ago, the vision of using technology to improve the lives of low-income people was a hard one to sell. Today, One Economy

has turned that vision into a reality and a successful model that is capturing investors' time, support and funding. We have done that with an entrepreneurial spirit and a participatory approach. We listened to the people that we served and it is that simple but unique approach that has been the cornerstone of our mission."

At no other time in history is One Economy more uniquely positioned to significantly expand its work globally. Leaders worldwide recognize the importance of broadband and technology in strengthening economies and many governments; including the United States have developed national plans for leveraging technology.

One Economy's plan is to have broadband and technology programs on every continent in the world over the next five years. "This is a vision, like the one we had ten years ago, that we are confident will be a reality."

For more information visit: <http://www.one-economy.com/>

Moustafa Mourad – Interim President, One Economy

Moustafa Mourad is the Interim President of One Economy Corporation. As such, he oversees all of One Economy's operations and will run the Program and Community Impact Departments. He will continue to work closely with Chairman of the Board Rey Ramsey on all matters of strategic importance. Mr. Mourad has been with One Economy since 2005. Before becoming interim president, Moustafa was the President of One Global Economy, One Economy's international division. Under Mr. Mourad's leadership, One Global Economy helped provide broadband internet access and relevant content in 11 countries in Africa, the Middle East, and Europe.

Previously, he was the principal of Mourad, Warnke & Associates, an international community development consulting firm with projects in Oman, South Africa and Honduras among others. Mr. Mourad was also the Director of Planning, Design, and Development at the Enterprise Foundation, the second largest national community development intermediary in the United States. He also created the foundation's "Asset-Building Taskforce", a multi-disciplinary team whose members' experiences range from community organizing to micro-enterprise development and housing construction. Prior to his tenure at Enterprise, Mr. Mourad held positions as Senior Planner with the City of Boston, and City Planner for the City of Cambridge, Massachusetts. He also consulted for USAID, the Ford Foundation as well as the governments of Egypt, Sri Lanka and the Sudan on a number of development issues ranging from affordable housing policies to economic development and employment.



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8-9 DECEMBER 2010 ■ HILTON SAO PAULO MORUMBI, SAO PAULO, BRAZIL

The Latin American Investment Forum will bring together Institutional Investors, Family Office and Foundations, as well as Asset Managers and Consultants to explore investment opportunities and strategies in Latin America and abroad.

This two day event will take place in the booming city of Sao Paulo, Brazil from December 8th to the 9th.

SELECT TOPICS OF DISCUSSION AT THE FORUM INCLUDE:

- Navigating the Latin American Investment Environment
- Dynamic Commodity Strategies
- Latin American Infrastructure
- Comparing Global and Regional Real Estate Investment Opportunities
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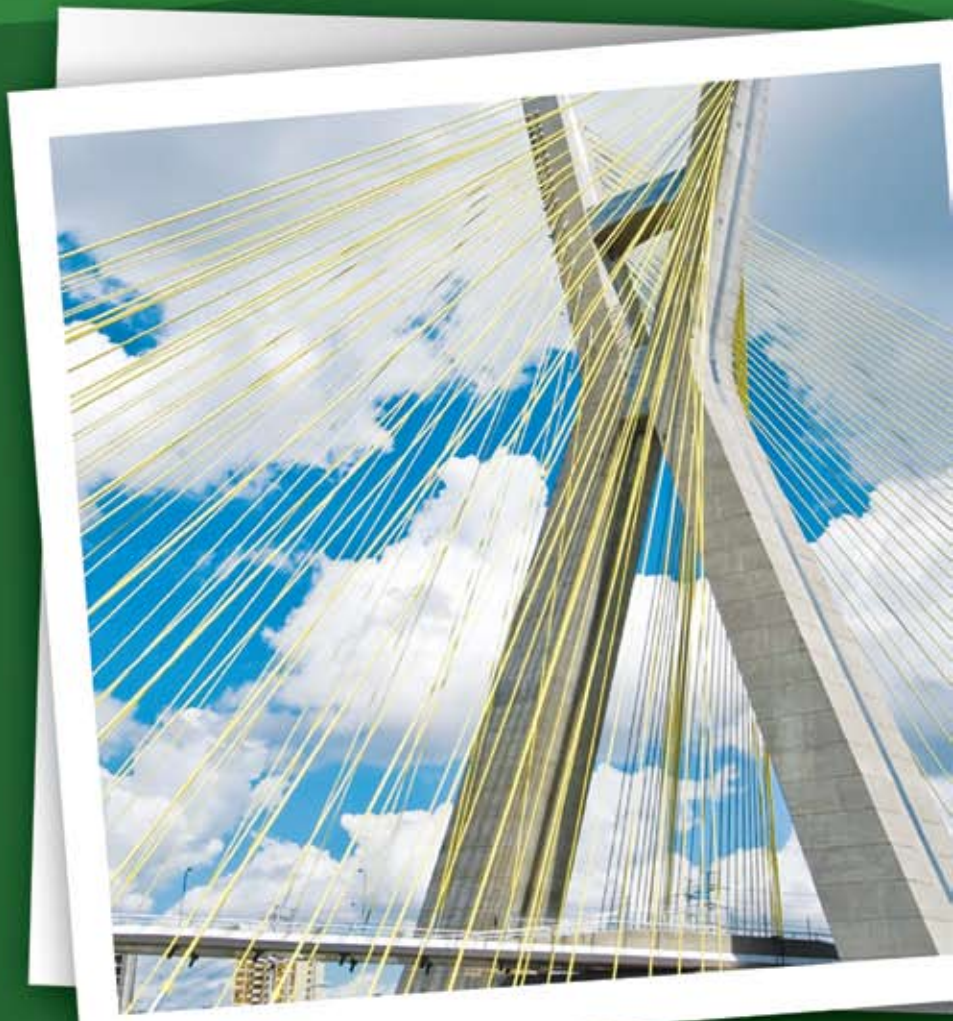
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ALI Speaks with Bertrand Delgado

Senior Analyst for Emerging Markets and Latin America at Roubini Global Economics.

How have emerging markets fared since October 2008, compared to the rest of the world?

We know now that regions within the emerging markets differ from one another. Asia and Latin America are stronger compared to emerging Europe for example. The reason why this dynamic evolved is because most of these countries performed structural reforms. They built up solid buffers against external vulnerability, they cleaned up their balance sheets and they improved their financial system regulation and they were not too involved in all of the toxic asset meltdown mostly due to strict regulation in their financial systems. Most of these companies are involved in sound macroeconomic policies. There are differentiations within these regions and not everyone should be looked at under the same scope, within Latin America we have solid credits like Brazil, Peru and Chile to a lesser extent Colombia and Mexico – Mexico mostly because of their ties to the US. The third tier is Argentina where things are not neces-

sarily the best outlook unless something changes as to how the country is being run.

What would you say is the global perception of Latin America specifically?

It is very positive we are seeing more and more interest in the region on all levels. This has to do with all of the reforms and structural changes that have taken place starting with Chile and most recently Peru. I think that overall the perception is that these countries have a positive outlook but then again depreciation needs to be taken into consideration. Solid domestic demand driven growth is what is going to make the distinction moving forward. In that sense again the three countries that I mentioned comply with these characteristics, while we've seen that Mexico and Colombia domestic demand drivers were not as strong as expected. In Argentina there has been a robust investment cycle and consumption is mostly driven by very loose macroeconomic policies. I don't think you will see Argentina growing at 9 or 10% over the next few years, especially with the inflation dynamics. The projection is positive; however of course there are risks per country that need to be taken into consideration. From a general perspective I think the risk now is an access liquidity coming from abroad, in terms of quantitative easing in the US and other countries falling into currency wars and interventions – all of those things are putting a cloud of uncertainty over the region – there are still differentiations that need to be done.

In your opinion would you say that Latin America might suffer from a sort of PR crisis of some sort as they are showing good numbers – however with the crisis in Argentina, Cartels in Mexico, the situation in Colombia – would you say that investor confidence is not fully bolstered by economic performance but also by the media coverage?

I would look at the actual numbers – the data. We have discussed this with analysts and it is true there is some sort of media and PR affect – of course Mexico's going through tough times in terms of security issues and it might get worse before it



gets better that's been known to cycle as we have seen in other countries. Hopefully they'll be able to solve it within the next few years rather than the next few decades so that's a question mark that needs to be addressed sooner than later. Venezuela is again a country that is most likely going to deteriorate farther before we see some sort of positive change although the position has been gaining some momentum. In Argentina there are two sides of the story, one that I think has been sponsored by the government is that the country has solid credit and some people are giving the government the benefit of the doubt and investing heavily, while the other crowd is suspecting more profound changes in the way the country is being run. There are a lot of fiscal policies, monetary policies – so they will await more structural change before they consider it to be a country of great potential.

Would you say China's growth is sustainable enough to maintain its position in Brazil?

I think that there's a little bit of high collation – however Brazil has its own dynamics. Our view here is that China will continue to grow with great potential but not necessarily at the same level of growth that we have witnessed over the last decade. Mostly because the economy will not be growing as strongly as before therefore the export growth that China has taken as a model is currently being tested and most likely being changed to one that is more focused on consumption. That balance and that shift is delicate and even if China is successful in moving towards a more domestic demand driven economy – because the population is relatively poor – as this mass of population moves towards higher income the first thing they do is eat better which will increase demand. As the population moves from rural to the city – they will need to import food. How will this play in an environment where the economy continues to grow in a relatively sluggish way and in the case of the Real – there is a very delicate equilibrium because in the long term if the commodity export continues to grow and they are now trying to create a second buy on appreciation of the currency on relative terms more money will go into that sector. Meanwhile, the non commodity export sector is the one that will suffer and will tend to be relatively losing competitiveness and all of the issues that come with currency inflation – that is likely to take place in the medium term if the real continues to be weak. Over the next couple of years – Brazil is still the star; there is a lot of investment going on in the country, massive infrastructure developments. On top of that you have the petrobras projects to be funded and so far domestic demands remain quite solid.

Would you say that Brazil is overexposed, for example there are 400 hedge funds in Latin America and 290 are in Brazil, without the proper fiscal policy can Brazil put the policies in place and sustain the money that's coming in?

Definitely not. That is a problem not only in Brazil, however all emerging market economies. How are you going to be able to live with a strong currency? One of the keys to understand as to whether or not a country can live with a strong currency are their

gains in productivity. Although in Brazil the productivity has been improving it's still a long ways to go. Increasing productivity is not something that can be achieved quickly. It takes time and furthermore it takes human capital and fixed capital. On the fixed capital side you can buy more technology but the human capital takes time to develop and since Brazil in particular and Latin America education in general is still poor compared to other regions in the world, that's a disadvantage. For decades Latin American education was left behind because it was believed to be better to have cheap labor then educated labor. Now we are paying the consequences of that – now that the money is coming our way.

In the long-term what would you say Brazil needs to do to make the transition from exporting raw materials and grow quickly to the industrialization?

Human capital – invest in human capital so that your investment keeps growing and then you can sustain large capital inflows so although your currency continues to appreciate in real terms the productivity of your labor force can comply with that and still make you competitive globally. It's a gap – that is the risk, they will have the money and commodities but not the people. In order to industrialize you will need to target industrial products domestically but also to your external demand and you cannot do that while you have a very strong currency and your level of productivity is not growing faster than that. I think the incoming government is in it for the long haul and they know what they need to do. Lula has made education a focus and reduced the technology gap.

Would you say there is a growth in inter-emerging market investment and trade, say between China and Brazil for example and how is that affecting the global economy?

Yes it is positive. We have seen that the Latin American region is the third largest importer of Chinese goods. So definitely that is something that helped to insulate massive imbalances from the advanced economies affecting emerging markets. That is one of the reasons why we didn't see too much of a credit here, because these interregional (within Latin America) and extra regional (between Latin American and Asia) those ties have been improving and evolving thanks to free trade agreements and concessions. You have to understand that the Chinese investing in Latin America are targeted towards commodities and logistics so they secure the supply of commodities even if there are changes in government. It would be hard for a dictatorship or socialism to break the supply chain if you are invested in the logistics. You can nationalize everything but the supply chain needs to be taken care of – so it's a safe bet.

As the Latin American markets grow would you say there is a growth in intermarket trade between emerging markets – the movement of similar commodities between the Latin American markets?

I think this trade between countries in South America has played to the benefit of Latin America and has avoided a much deeper decline in input and output such as Mexico experienced.

From an averaging point of view – you discussed a bit about Colombia and Peru but how would you rate Latin America, taking Brazil out of the equation?

Chile is definitely a solid player, Peru is moving in that direction – hopefully the next presidential election will not derail that. Colombia is also something to take into consideration; Mexico of course is a solid player – however unfortunately it is tied to the US, which is the “sick guy” at this point in time.

What is your perception of alternative investments within Latin America, hedge funds, and private equity funds?

I think that Latin America is a region that is going to keep growing robustly and hopefully policy makers will maintain a sound macro environment and that's ground for financial institutions including hedge funds to keep profiting from. It's growing and expanding so in the next few years there is a positive outlook for the region. Again you have to be careful how you maneuver through each country and how all of this unstable equilibrium will play out in the next few years – but Latin America is still a safe bet.

If you look at many of the LatAm hedge funds they have a lot of national institutional participation, what do you think the perception of US institutions are towards Latin America?

I think that the perception that emerging markets should be a higher percentage of your portfolio is an ongoing issue. Of

course that implies a strong kind of loss theory for appreciating currency, it seems to me that the portfolio minds would like to have a larger piece of Latin America.

If you compare Latin America to Asia – what do people think when comparing the two in terms of investing in an emerging market?

Both are looked at obviously – Asia has a larger or more diversified market and has a larger potential for growth than Latin America and that is still the way investors see it – more opportunities in Asia. Then again that depends on how close you are to a particular region and that would be based on each investor's situation.

What is the Roubini groups' outlook for Latin America for 2011, positive?

Yes – my forecast is that the region will grow well above potential this year and at potential in 2011.

What are your thoughts on Cuba, do you see it having a successful future in the post Castro ages?

I think it has a bright future depending on which investors move there and because of the 50 years of distortion it will take time, but it has potential.

Bertrand Delgado is a senior analyst for emerging markets and Latin America at Roubini Global Economics. Bertrand's areas of expertise are monetary and fiscal policy, international economics, inflation, currencies, and politics. Bertrand holds a master's degree in international affairs with a specialization in international finance and economics from Columbia University's School of International and Public Affairs, and a bachelor's degree in economics with a specialization in mathematics from the University of Wisconsin-Madison.

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Finding an Entrance into Mexico's Affordable Housing Construction Finance Market

■ By Lawrence McDaniel

Construction lending opportunities in Mexico's affordable housing sector continue to look attractive to us; buttressed by strong fundamental demand for new units, readily available takeout finance provided by Mexico's two state-sponsored mortgage banks Infonavit and Fovissste, and a structurally constrained supply of construction finance. Existing unmet demand for affordable homes hovers at around 5 million units or so depending on which source you quote, and new family formation increases this amount by around a million new units annually. However, Mexico's home builders are expected to only meet 60% of this in 2010, not due to any shortage of land or construction capacity but solely due to an ongoing lack of construction finance.



Why Is There a Persistent Shortage of Construction Finance in Mexico?

Post-crisis loan underwriting standards have indeed tightened in this market, resulting in project sponsors now contributing around 50% more equity capital to each project. However, homebuilders have been surprisingly quick to adapt to the new risk paradigm. Faced with little or no ability to raise additional equity to bridge the gap, the industry has adapted in part by improving per-project turnover time: they simply focus the same resources on a shorter list of simultaneously managed projects. But some have gone even further by incorporating sophisticated preferred equity structures into their financing strategy, thereby providing a new form of market participation for total return investors, but more importantly, enabling the home builder to avert production declines entirely. We therefore are inclined to discount post-crisis underwriting standards as a meaningful contributor to the growing backlog of demand.

Mexico's largest homebuilders in fact are healthy and quite busy. Mexico's 12 largest homebuilders represent around 30% of total market share and are capable of maintaining continuous construction pipelines of at least US\$10mn. As such, they continue to be well served by the traditional banking industry; that is at least, those of them who have successfully adapted to banks' stricter post-crisis underwriting guidelines. The problems begin to surface with the other 900 or so homebuilders in the industry. Until 2008, 2nd tier regionally focused homebuilders – the other 70% of market share – primarily relied on SOFOLES, lightly regulated non-deposit-taking mortgage banks, for both project construction loans as well as at least a portion of homebuyer mortgage take-out finance. Even though the SOFOL industry was a relative late arrival to the global credit crisis, as an industry it was disproportionately affected by a 3-way tsunami of vanishing warehouse lines, a closed mortgage securitization market, and ultimately, severe performance deterioration in their whole-loan mortgage portfolios. SHF, the Mexican government's administrator of the SOFOL industry, deserves praise for rapidly expanding its mandate to fill the warehouse funding void that was created by an exodus of foreign owned banks and hedge funds during the darkest days of the crisis. On the other hand, they should be scorned for having subsequently overseen the wholesale destruction of nearly all institutions under their supervision. How? SOFOLES needs to recapitalize, and meanwhile SHF – rightfully – will not provide new wholesale funding for origination of new loans. However, SHF continues to insist on holding most of its warehouse lines at par, and unsurprisingly, in nearly two years' time no equity in-

vestor has shown a willingness to own equity in a SOFOL who's liabilities exceed the true market value of its' assets. In an industry that depends on loan origination fees, the ongoing freeze on originations has caused each SOFOL to cannibalize the little remaining equity capital it has until it finally becomes insolvent. The SOFOL industry has subsequently shrunk from 27 institutions at the onset of the crisis to 15 institutions at present; with all remaining institutions surviving solely on the basis of a non-economic "extend and pretend" program with their sole lender, SHF. Barring any surprise change in posture from SHF, there is no reason to expect anything over the mid-term but more of the same. So, the other 70% of the home building industry that is understandably too small to be served by commercial banks, has no means of financing its projects.

But this doesn't wholly answer the question. CNBV regulated Mexican banks are healthy if not some of the most profitable banks worldwide. They have superior deposit-based funding sources, and construction finance is not only a market that

they know and understand but also an area where they would like to expand. An inspection of today's SOFOL industry quickly answers the question of why the one does not acquire the other. If you eliminate the SOFOLES who are already bank-owned, the industry has only US\$12bn-equivalent in portfolio assets, which is approximately on par with the assets of a single medium-sized US regional bank. If you also eliminate Su Casita and Metro Financiera (as each is an unmitigated mortgage banking catastrophe) then the industry is further reduced to 12 problem-laden institutions

The SOFOL industry has subsequently shrunk from 27 institutions at the onset of the crisis to 15 institutions at present; with all remaining institutions surviving solely on the basis of a non-economic "extend and pretend" program with their sole lender, SHF.

totaling just below US\$7bn-equivalent in portfolio assets. So at US\$350mn in average portfolio assets, there simply are no individual institutions large enough to merit the effort required to acquire and integrate them; even before considering the uphill battle of trying to get SHF to see the light of day about releasing its liens on market terms.

A Clear Case for Consolidation

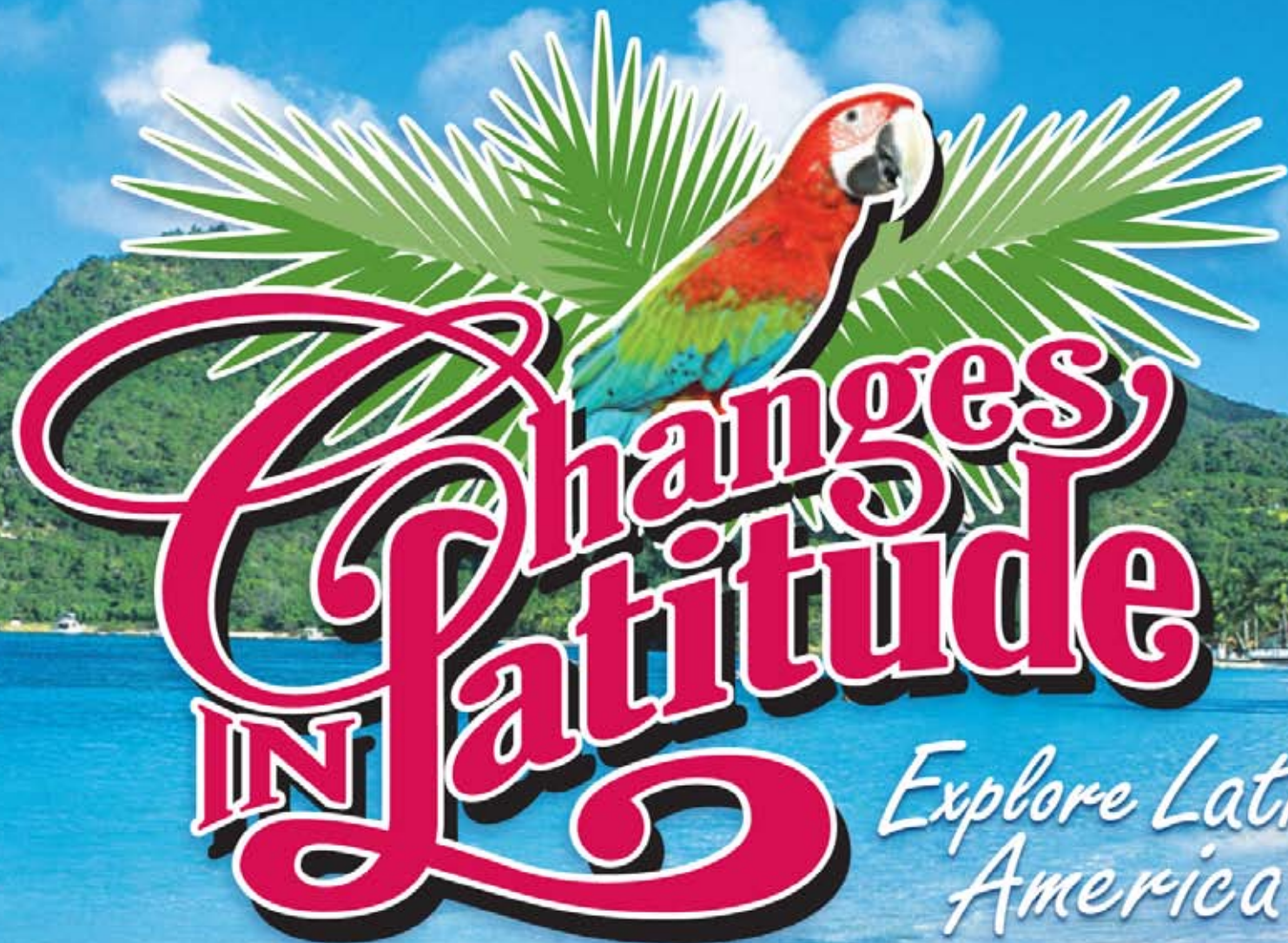
The SOFOL concept, in hind sight at least, is inherently flawed because of its dual reliance on external asset funding sources and asset-backed secondary market exit strategy; both of which proved to be far less resilient than anyone ever imagined. SHF's vision for solving both weaknesses is to architect the transformation of the institutions under its supervision into deposit-taking niche banks. While we appreciate the allure of this idea to SHF – if it works then they'll continue to be relevant over the long term – we think it's about as practical as a beachcomber stumbling upon an anchor and then deciding to

build a ship. Instead, we think that CNBV already does a good job of overseeing deposit-taking institutions, and, the banks under CNBV supervision already know lots about growing their deposit bases. While we completely agree that the solution to the affordable housing industry's construction finance problems lies in replacing warehouse lines and securitizations with bank deposits, we think it is more prudent (and easier) to find ways to tap into what the established deposit-taking banking industry has already created. That is, consolidate the remaining "healthy" bits of the SOFOL industry into a single, well-run institution that a CNBV-supervised bank would desire to own. We furthermore believe that an industry consolidation of this nature should be limited to construction lending since banks are already quite good at originating and servicing mortgages. Interestingly, the least damaged institutions are also the smallest, where the most value creation potential lies via platform consolidation. The ten smallest industry participants combined represent 1/3 of the industry if bank-owned SOFOLES are ignored. They have US\$3.5bn-equivalent in combined portfolio assets, which

incidentally is about the same size as Su Casita with whom SHF is nearing an agreement to restructure existing warehouse lines to somewhere between 35% - 50% of UPB. That makes us wonder if SHF might be willing to take a similar but orchestrated approach to the smallest institutions. Among these combined institutions we see around 60,000 performing whole-loan mortgages, and around 45,000 delinquent mortgages; quantities that are sufficient to enable sophisticated outsourcing schemes to the larger and more capable loan servicers affiliated with Info-navit, and in turn, facilitating a wholesale orderly wind-down of the mortgage origination and servicing cost centers. We also see around 600 construction loans of varying quality, which we believe represent enough critical mass upon which to rebuild and eventually create a construction lending institution that owns the market share that banks ultimately value and would make strategic sense to acquire into. Not that this strategy depends on an eventual bank-led exit however, as current margins on construction lending will drive strong earnings for quite some time and meanwhile, competition is nowhere to be seen.

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Increased Threat of Currency 'Wars' to Ignite Fourth Quarter FX Activity?

■ By Kevin Sollitt



As we publish, the scene is set for a potentially dynamic G-20 meeting of finance ministers and central bankers hosted by South Korea. The now customary purpose of this meeting will be to try and ensure ongoing global economic recovery in a framework for strong, sustainable & balanced growth.

In addition the G-20 will discuss strengthening the international financial regulatory system and the prospect of modernizing those associated institutions.

Reading between the lines, what does not appear in the official program of events, yet could quite understandably dominate the proceedings, will likely be some heated discussions on one of the hottest global topics right now, namely the wild card of Foreign Exchange currency fluctuations.

With the benefit of hindsight (and perhaps it's not just coincidence) a somewhat interesting trend over the past several months has become evident among certain nations, such as the EU, the UK, the US, Mexico and South Korea. They have seemingly stood aside and simply observed, while their home

currencies have depreciated and lost external buying power against the improving value in currencies of less established or competitor nations.

Some observers will say fluctuations such as the Euro plunging from \$1.50 to \$1.19, the Yen gaining from 90 to 80 or Aussie shooting up from 80 cents to 1:1 parity in short time frames are quite normal, yet these movements are certainly getting some media attention and market commentators are now digging a little deeper to determine both individual and collective perspectives.

The current focus may be due to a variety of recent publicity relevant to the industry: regulation in the US by the NFA and CFTC, the subsequent threat of exodus by financial corporations if regulatory measures become too draconian in the UK,

upbeat statistics from the BIS triennial foreign exchange survey indicating a huge rise in daily FX turnover since 2007 from \$3.3 trillion per day to \$4 trillion per day in 2010, anecdotal evidence of how cheap it was to go to Europe this summer or even the emergence of certain entities incurring Forex losses through inefficient hedging. There seems to be something for everyone to discuss, hence the 'hot topic' categorization.

As far as markets go, although it's fair to say the financial world has changed drastically since the Lehman Brothers collapse two years ago, it is still a little strange to grasp the popular concept of what some might call 'willful blindness' to currency depreciation. Especially given Western nations' inherent and traditional predisposition towards inflation, in part caused by concerns over money supply & perhaps a little ironic considering the inordinate amounts of cash being printed by said authorities.

With major economic powers seemingly and perhaps counter intuitively at ease with declining values of their respective national currencies, we would still suggest that the jury is out on the subject of whether or not nations are truly engaged in deliberate undervaluation policies, particularly given the nature of currency markets to take values to extreme levels before returning to realistic levels over time, e.g., the British pound soaring from \$1.4 to \$2.1 in 6 years from 2002 to 2008, settling now at around its ten year average of \$1.60.

That said, as recently as last month Japan announced that it did conduct official intervention to weaken the Yen (JPY), causing the unit to decline 4 or 5 percent in a couple of days against most major currencies, although as we go to press the market forces seem to have ignored the efforts by Japanese officials with Yen strength resuming, currently \$1 gets ¥81.25, a far cry from the ¥100 level seen not so long ago.

This approach was not entirely unexpected given official jawboning at the line in the sand at 80, yet seemed to trigger the debate that we suspect may now take place in Korea and could pave the way for something more significant out of the G-20.

In the earlier part of 2010 we questioned the (then) elevated status of the USD vs. Latin American currencies, in particular against the Brazilian Real. (ALI issue 1, 2010), where the \$ was worth 1.84 BRL against the current 1.67.

Against popular opinion at that time, our projections called for BRL to approach the low 1.60s by the end of the year and with

these levels being touched recently, a decisive break from previously conciliatory rhetoric on the subject of currencies occurred when Brazil's finance minister Guido Mantega evidently suggested that 'an international currency war' had broken out, alluding to the extremely low interest rates of the United States being mostly to blame for BRL strength amid a deliberate policy by the Americans to weaken the Dollar through ultra-loose monetary policy. This would naturally (as we suggested in previous issues of ALI) weaken the USD and strengthen the BRL on capital inflows to Brazil.

Whether Mr. Mantega's assertions are entirely accurate remains to be seen, let's not forget the huge fundamentals that con-

tinue to favor Brazil over so many of its competitors on the global stage. In any event, one undeniable truth is the actual appreciation of BRL during the course of 2010, the unit has risen from just under \$2 to the low 1.60s this year, the move accelerating in recent weeks with the combination of low US interest rates, high BRL interest rates and optimism over the new Brazilian government and a pessimistic political view of the US as it approaches mid-term elections.

As we head into the meeting and according to Mr. Mantega, US Treasury Secretary Timothy

Geithner has apparently "Guaranteed that US policy is not to weaken the dollar, on the contrary, it is to strengthen the dollar." Mantega told reporters, "Geithner said the impact of the Fed policy was being overestimated."

If this statement is true, Mr. Geithner is most likely referring to the market's reaction to the Fed's proposed second bout of quantitative easing (QE2), which may begin as early as next month and has nevertheless been responsible for some recent and heavy USD losses.

The Dollar has fallen some 5 percent in the last month or so against most currencies due to what can be described as market presumption of a likely 'shock-and-awe' approach to QE2, not seen in the dark days of 2008/09 where asset purchases were thought to be close to \$1 trillion at a time.

We do not think such an extreme tactic is likely and therefore suggest that the USD is at a short-term base, perhaps Mr. Geithner's reported thoughts may turn out to be correct after all. As far as Fed policy, a more likely outcome than throwing huge amounts of money at the system again (based on continued steady, non-declining economic performance) would see the next bout of asset purchases taking place in smaller tranches,

With major economic powers seemingly and perhaps counter intuitively at ease with declining values of their respective national currencies, we would still suggest that the jury is out on the subject of whether or not nations are truly engaged in deliberate undervaluation policies...

with a pause in between meetings in order to judge the effects. No need to panic just yet.

In fact this approach was suggested in a theory from Federal Reserve Bank of St. Louis President Bullard, such a gradual approach being akin to incremental adjustments in the Fed Funds rate, policies that have worked well for the Fed previously. In such instances the central bank could buy \$100 billion in long-term Treasuries next month and decide what, if any, subsequent future purchases to make on the merits of the actual course of economic recovery, rather than fear the worst from the beginning. Bullard's remarks were reported at a conference in late October hosted by the district bank.

Given all the above, there is definitely a range of implications for the USD and its trade partners, especially when one considers how Brazil is already turning up the heat through both dialog and monetary tools. Aside from vocal salvos, Brazilian officials have been extremely involved in the fight over currency intervention, criticizing the monetary policy of advanced economies while taking aggressive measures at home to weaken the Real.

Consequently, the BRL (having hit our initial and optimistic projections) may now undergo a bout of profit-taking as the new administration shuts out the speculators. Over the past month alone foreign investment into local bonds saw taxes raised from 2% to 6% and a series of loopholes have been closed to make that tax more pronounced, discouraging foreign ownership of bonds and therefore reducing appetite for the Real.

The central bank has also continuously purchased USD in the spot market to weaken the Real, the world's most overvalued major currency according to the 'Big Mac' index in "The Economist" newspaper. The most undervalued exchange rate is the Chinese Yuan, no surprise there to regular readers and anyone that has been tracking this developing and potentially explosive situation.

As far as an outlook for the rest of the year, we are cautious Dollar bulls. QE2 may not be as extensive or as necessarily lengthy as current market sentiment is allowing for, suggesting a move back to the low 1.30s in EUR/USD from the present 1.40. With the apparent presence of a lurking BoJ we expect a similar move in the Yen towards 90 from the current 81.25.

Before looking ahead much further into 2011 and beyond, we'll see what the outcome of this G-20 brings to the FX markets over the near term.

Mervyn King, the Bank of England Governor, has called for a "Grand Bargain" in order to avert the potential currency war that everyone seems to be talking about. This would be something not really seen since the famous "Plaza Accord" in 1985, where the G-5 agreed to limit the rise of the Dollar against the Yen and Deutschmark. The Dollar fell about 50% in the following two years.

It may be worth considering the potential for the Dollar to fall again once this next rally is over, only this time perhaps more so against the Chinese Yuan, whose valuation seems to be growing increasingly crucial and equally controversial to the global currency and debt market infrastructure.

We'll talk more about this in our next issue once the dust has settled on the South Korean outcome.

We remain constant and independent advocates for success of market participants and also for transparency in the FX industry and believe that as a whole we are only scratching the surface when it comes to realizing the potential benefits through disbursement of greater knowledge and understanding of the market.

We welcome discussion of related FX issues (see contact details) and our forecasts are also published on Bloomberg. For further discussion or related information please feel free to contact the author directly: kevinsollitt@pfxonline.com

Kevin Sollitt gained international FX trading experience in various financial centers including London, New York, Los Angeles, Sydney, Hong Kong & Tokyo. Kevin's career began in London during the 1980s, later transferring to Sydney. In the mid 1990s he returned to London under the challenging financial conditions of that era, experience that equipped him to successfully deal with more recent turbulent market conditions. In 1998, Kevin teamed with former colleagues at a super-regional bank in the U.S.A. and through strategic alliances, development of professional relationships & continuous positive trading results, became Head of Foreign Exchange Trading in 2006.



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ARGENTINA'S ENERGY FRAMEWORK:

Preparing for an Onslaught of Renewable Energy Investment

■ By Carlos St. James

Argentina recently began a massive new energy investment program with a goal of reaching 8% of its energy matrix from clean energy sources such as wind, solar, and biomass by 2016. This article is a brief primer explaining the basics of Argentina's energy policy and legal framework for those looking to participate in one of the most exciting energy investment opportunities in the region that will attract US \$5 billion dollars in the next few years.

■ Key Players

Argentina's energy planning is the domain of the Ministry of Federal Planning, Public Investment and Service, under which the Secretariat of Energy executes. The country's electricity distribution system, known as SADI (Sistema Argentina de Interconexion) is administered by another government entity, the Compañía Administradora del Mercado Mayorista Eléctrico SA, aka CAMMESA.

In 2004 the government also established Energía Argentina SA, aka ENARSA, which is currently owned by the government but has plans to sell shares in the open market at some point. ENARSA is taking the lead in renewable energy projects. The company's mandate is broad and includes pursuing the exploration, extraction and production of hydrocarbons. It also conducts business in the field of generation, transportation, distribution, and electric power trade, and is entitled to trade all types of energy assets. These activities are undertaken by ENARSA itself, or by means of agreements with third parties, or associated to other parties, domestic and foreign.

All of these above entities typically work with the private sector through the Argentine Renewable Energies Chamber (CADER), an industry trade association established formally in 2008, for matters pertaining to clean energy solutions.

In Argentina, all roads lead to Buenos Aires -- and so do the power lines. The country's electricity grid is set up to lead into

the mass demand markets in and around Buenos Aires. As a matter of fact, fully two-thirds of the country's energy demand lies in the corridor between the cities of La Plata and Buenos Aires on the banks of the Rio de la Plata, and up along the Paraná River to the city of Rosario, in Santa Fe province. However, this area generates 43% of the country's total energy, thus having to bring in power from the rest of the country -- and at times from neighboring Brazil. This existing grid spanning the country has the ability to take on new energy generation projects before significant new power lines need to be added.

■ Legal Framework

Law 25.190 dating to 1998 and known as the National Wind and Solar Energy Law, established the initial framework for clean energy providers. It states that these two are "of national interest" and creates fifteen-year investment incentives for the private sector: deferment of payment of the Value Added Tax (currently as high as 21%) on capital equipment, or accelerated depreciation of these assets. It also demands the creation of a Renewable Energy Trust Fund that will fund the higher cost of these energy sources, funded by a new energy tax.

This was followed by Law 26.190 in 2006, known as the Renewable Energy for Electricity Law. This law was significant in that it established a goal of 8% of the country's primary energy matrix be derived from renewable sources within ten years; it is currently still well below 1%. Given a current installed capac-

ity of some 28 gigawatts in Argentina, this represents a new market for no less than 2.2 gigawatts (2,200 MW) of new clean energy by year 2016.

The specifics of this law needed to be regulated by the Executive branch of government through the Ministry of Federal Planning, but this did not occur until mid-2009 under Decree 562 and thus investment languished. Decree 562/2009 provides greater detail on the incentives offered for investment in renewable energy projects. The subsidies available from the Renewable Energy Trust Fund were increased to ranges from 1.5 centavos/KWh for wind, geothermal, and other sources, to 9 centavos/KWh for solar PV projects. This new law and its decree, coupled with the establishment of ENARSA in 2006 and the trade association in 2008 gave the industry the push it needed.

ENARSA has very successfully received numerous proposals under its Renewable Energy Generation Tenders (aka GENREN), to date approving 32 new private sector investment projects representing 895 MW of wind, solar, thermal-biodiesel and mini-hydro technologies which require in excess of US \$2 billion in investment. If all of these are completed, over 3% of the country's energy matrix will be comprised of clean sources and sufficient inertia will be established to reach the 8% goal by 2016.

Another mechanism commonly used to add power to the system – be it fossil fuel, natural gas or clean energy -- is through Resolution 220 that dates to 2007. It allows for the execution of electricity supply contracts between a new producer and CAMMESA on ten-year terms, and must include the participation, in any form, of a government agency such as ENARSA. Some cleantech investors are opting to enter the Argentine energy market via Resolution 220 rather than the fifteen-year GENREN tenders.

As is often said in the media, Argentina is poised to become the Saudi Arabia of renewable energy in the 21st century. Inves-

tors, vendors, technology providers and lenders are increasingly gathering in the country to take part in what is becoming one of the largest shifts in energy supply ever seen in Latin America.

Carlos St. James is the Managing Director of Santiago & Sinclair, LLC, an advisory firm focusing on the clean tech sector in Latin America. He is also the founder and President of the Argentine Renewable Energies Chamber and Vice Chairman of the Global Renewable Fuels Alliance. In 2008 he was voted "Biofuels Personality of the Year" by readers of Biofuels Digest, and will soon appear in Esquire magazine's annual "Best and the Brightest" issue for his work towards developing renewable energies in Latin America. He holds a masters degree in international relations from The Fletcher School at Tufts University. www.SantiagoSinclair.com.



The Winds of Change

■ By Mark McHugh

In the renewable energy auctions held in Brazil on August 25th and 26th market forces yielded a significant reduction in wind energy prices. Wind energy contracts were awarded totaling more than 2 GW, at an average tariff of R\$130.86 (US\$ 75) per MWh. Prices bid for wind energy were lower than biomass and comparable with small hydro. The authorities are declaring a major breakthrough, placing wind energy firmly in the mainstream. It is perceived to be an important step towards achieving or possibly exceeding the government target of 15GW from alternative energy sources by 2035. However, as the dust settles, industry insiders believe that project returns are now approaching the cost of capital, creating controversy as to how much of the contracted capacity will actually get built.

As one of the BRICs, quick to rebound from the global recession, the Brazilian economy continues to advance at a fast pace with projected GDP growth rates for this year approaching 8%. Government plans are targeting rapid expansion in green energy, as part of a major push on infrastructure investment. March saw the launch of the second four-year growth acceleration program (PAC 2), which envisages R\$11 billion (US\$7 billion) in renewable energy investment. Brazil already occupies the high ground with the best energy matrix of any of the major economies—48% of total energy usage is from renewable sources.

At the same time, Brazil is playing catch-up on the world stage, as one of the fastest growing wind energy markets. Capacity grew at 75% in 2009. The present aim is to achieve 5GW of installed wind capacity by 2014. In their recent report IHS Emerging Energy Research—“Latin America Wind Power Markets and Strategies: 2010 – 2025,” concluded that Brazil will lead the region with 31.6 GW installed by 2025. This is considered an optimistic view. However, longer-term, the overall prospects for wind energy along Brazil’s 9,600 km wind-swept coastline are not in doubt. The estimated potential is a massive 144 GW and could be doubled with higher towers over 100 meters.

The first tentative steps towards creating today’s burgeoning wind energy industry were taken in 2002. The original PROINFA program provided government incentives for alternative energies through feed-in tariffs and twenty year contracts with guaranteed demand. A number of government tax incentives and discounts on transmission tariffs have further encouraged development. Perceptions at the beginning were that wind energy would always be expensive and would be unable to fulfill

a significant part of projected energy demand. Nonetheless, efforts were focused on wind and biomass. Energy planners were particularly keen on wind energy, because of the complimentary nature between wind and hydro. Hydro schemes still represent 75% of total installed capacity and 90% of electricity production in Brazil. When hydro-flows are at their best from January to June, there are lower winds and vice versa. Effectively by holding water in the reservoirs, hydro can act as a virtual storage system for wind energy.

Early entrants in the Brazilian wind energy market enjoyed comfortable returns based upon the highly attractive feed-in tariffs ranging from R\$ 258 to 294 (US\$ 150 to 170) per MWh. By the end of 2009, fifty four wind farms were contracted under PROINFA, with a total 1,423MW capacity—thirty-five of which are now in operation. Despite the relatively high prices paid, most observers agree that government stimulus was essential to nurture the embryonic wind sector. The PROINFA program has been an important step toward establishing a longer term healthy industry.

The next stage in the process came in December 2009 with the first national wind energy auction sponsored by Brazil’s National Electricity Regulatory Agency (ANEEL). It moved away from the feed-in tariff system, which depends on monthly production and produces an unstable income pattern. Bids were based upon a quantity of MWh annually divided by twelve to smooth monthly income. The auction contracted 1,806 MW capacity over a twenty year period, at an average price of R\$ 148.39 (US\$87) per MWh, with the lowest bids at R\$ 131.00 (US\$75) per MWh. The substantial fall in prices began to raise fears about the long-term viability of the wind industry. This was especially true

	Projects Registered	Total MW Registered	Contracted Projects	Total MW Contracted	Price R\$/MWh
Small Hydro	18	168	7	132	130.73
Biomass	61	2375	12	713	134.47
Wind	399	8202	70	2048	130.86
Total	478	10745	89	2892	131.74

at the bottom end of the scale, where yields were perceived to be approaching the cost of capital.

With turbine manufacturers and international developers facing increasing competitive pressure in their traditional markets of Europe and North America; Brazil with its stable economy, high projected growth rates and hereto attractive profitability has invited increasing attention from the global industry.

There are now many major international players from the wind turbine industry present in Brazil—Alstom, Enercon, Gamesa, GE, IMPSA, Siemens, Suzlon, and Vestas. These companies have, or are in the process of establishing manufacturing facilities to meet local content targets. Also knocking on the door are the Chinese, including Asia's largest wind turbine manufacturer—Sinovel. They are very competitively priced and hoping to establish a bridgehead through offering financing from Chinese banks. Spurred by this intense competition, costs per MW of installed capacity today have fallen by more than 30% compared to PROINFA.

The developers market can be segmented into four main categories—large international developers such as Spain's Ibedrola/Gestamp and Acciona Energia; Brazilian utilities like CHESF and CPFL; mid-size Brazilian developers including, Renova, Brennand and Eolica; and a number of smaller Brazilian entrepreneurs who are looking to sell licensed projects with PPA. In general international developers have been slow to capitalize on the boom in the Brazilian wind energy market and leverage their procurement muscle and international expertise in project execution. Less experienced Brazilian developers have been more successful in winning bids, which is arguably why projects are slow to get going. Red tape also appears to be holding up the process. None of the seventy-one projects awarded at the end of 2009 have commenced construction. The first projects are expected to start building in the first quarter of

2011 and all must be completed before the end of 2012 to meet the conditions of the auction.

The latest round of auctions on August 25th and 26th has produced even more intense competition. The average price achieved for wind energy was R\$130.86 (US\$75) per MWh, a 12% reduction from Dec 2009. Wind tariffs are now lower than biomass and comparable with small hydro.

The inexorable pressure on project financial returns is further bringing into question the economic feasibility of many of these projects. There is growing concern that some players in their desire to establish a strategic position in the Brazilian wind energy market and to “place a flag on the map” are aggressively pricing and undermining the long-term profitability of the market. Time will tell—there is a three-year grace period in which owners must complete construction and projects become operational or there is the risk of forfeiting their bid bond.

Nonetheless, from the perspective of the regulator, the auction was a resounding success. According to Nelson Hübner, Director of ANEEL:

“The results of the energy auction represent a new paradigm in power generation in Brazil because they confirm it is possible to produce wind energy at a price that is competitive with those of thermal plants, which are more polluting.”

As the tariffs are falling it is anticipated that there will be a trend for developers to move away from the regulated market and seek PPAs in the open market, where better prices are achievable. The regulated market with tariffs set by government auction represents 70% of the Brazilian electricity market. The remaining private market consists of special consumers, traders and self-generation. Individual or groups of consumers with a demand of 3MW qualify as special consumers and are free to negotiate and enter into bilateral contracts with generators.



The majority of bank financing in the renewable energy sector to date has been through the national development bank, BNDES and government owned banks—Banco do Nordeste and Caixa Federal. All seventy-one projects from the 2009 auction are using some form of government funding. Bank debt has a maturity of sixteen to twenty years, with interest rates in the range of 7 to 9%. For a developer, bank debt typically represents 70% of total funding, with private capital providing the remaining 30%. To date, there are few international banks involved in project financing—principally Banco Santander and Standard Bank. Citibank, Black River Asset Management and Liberty Mutual are participating through their equity in SIIF Energias do Brasil, one of the key participants in the PROINFA program. What is more, as investment levels ramp up, there is a growing opportunity for international investment in conjunction with local financing.

Declining profitability has a number of potential consequences. It is expected to impact the type of investors willing to participate in the Brazilian wind energy sector favoring: utilities, IPPs, green funds and pension funds, which are able to take a longer-term view. Private equity investors, typically aspiring to higher rates of

return and a three to five year exit, will find it increasingly more difficult to meet their investment objectives. In the same way, it will be harder for the smaller entrepreneurial and less experienced developers to compete against the scale and negotiating

power of the larger players. This scenario will likely result in a shake-out over the next couple of years, as developers reassess their project portfolios. It is anticipated that a wave of M&A activity could result before construction deadlines expire.

Given the pressure on profitability, there is no longer any margin for error for developers. Projects need to be financially optimized to be successful or may simply never get funded. Brazilian developers must seek ways to increase their negotiating power and expertise to

maximize value. Specialist advice on project financing can add significant value. It is more and more important to present projects to international investors in a language they understand, to ensure projects are 'bankable'. Financial leverage and effective risk management are two of the most important drivers of profitability for the potential investor. Expert financial structuring, as applied in Europe and North America, incorporating such alternatives such as vendor finance, will undoubtedly become a critical success factor as the industry matures.



Mark McHugh is Managing Partner, Brazil of Bauhaus Capital Partners, a boutique M&A and investment advisory firm focused on the renewable energy sector. The firm brings to bear substantial expertise with debt and equity raising and structured finance gained in Europe and North America and applies it to the emerging renewables market in Brazil. Mark was until recently, Vice President of Marketing Americas for Shell based in the US. His extensive know-how of the energy business was developed during a thirty-year international career in marketing, sales, strategy consulting, and general management. He is skilled in investment strategy, leading new business development initiatives, M&A, and managing new business start-ups. He has developed a close "on the ground" understanding of clean-tech and the alternative energy market in Brazil.



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New Bills Proposed

to Amend the Law on Financial Entities in Argentina

■ By Javier Canosa

The Argentine National Congress is currently analyzing three amendments to law No. 21,526 that regulates the activities and functioning of Financial Entities since 1977 (the “Law on Financial Entities”). Three bills are being discussed by the Financial Committee of the House of Representatives in order to modify the Law on Financial Entities. The bills were introduced by the following deputies:

1. Carlos Heller, member of the political party Encuentro Popular, closer to the current administration;
2. Gerardo Milman, member of Generación Encuentro Nacional (GEN); and
3. Federico Pinedo, member of Propuesta Republicana (PRO).

We will analyze the main characteristics of the three bills:

a. Bill introduced by Carlos Heller, from Encuentro Popular:

The bill introduced by Deputy Carlos Heller proposes to replace the Law on Financial Entities by a so-called “Law of Financial Services for Economic and Social Development,” which would be conceived from the point of view of the needs of consumers, hence regulating financial services as a public service aimed to favor the “transactional” needs of savings and credit “for all citizens of the nation.”

The proposed bill aims at regulating the activity of banks in an exhaustive manner, providing a **restricted list of authorized operations** for commercial banks (*numerus clausus*) in opposition to the previous criteria of admitting all operations that were not specifically forbidden, a move towards a specialized banking model.

The Central Bank will be in charge of watching over the limitations established by the proposed regulation.

Additionally, the bill includes a restricted list of types of financial entities, in accordance with the specialized banking model.

The main points of the bill are:

- More restrictive criteria for the activities of foreign banks in Argentina, defined as those entities with more than 30% of their capital being of foreign origin.
- Maximum interest rates for loans to micro and small-sized business. The rates may not surpass in a proportion of five percent (5%) the weighted average rate of the financial system for that segment. Simultaneously, a maximum rate for personal loans for less than one hundred thousand pesos (approximately US\$ 25,000).
- Financial entities will have to assign, directly or indirectly, not less than thirty eight percent (38%) of their total financ-



ings in the private sector to micro, small, and medium-sized businesses, and two percent (2%) to small undertakings.

- No financial entity will be able to hold participations in the whole financial system superior to eight percent (8%), both in the total of the deposits of the private sector, and in the total of loans granted to the private sector.
- A geographical criterion will be laid down in order to allow the opening of new branches of financial entities.

The alleged purpose of this bill is to promote the universal access to financial services (it's referred to as democratization of the financial system.)

b. Bill introduced by Gerardo Milman, of GEN:

The project introduced by Deputy Gerardo Milman proposes to replace the Law on Financial Entities by the "Law on Financial Relations and Guarantees to the User of Credits and Deposits", which promotes public saving and the spread of banking entities throughout the national territory.

The bill establishes a saving system for individuals under legal age, by means of granting special accounts without administrative charges, willing to revitalize an old scheme and to improve the relation of people with the banks in the long term.

Additionally, the bill includes micro-credit banks as a type of financial entity, with the aim to "give a possibility of development to all citizens and give assistance to those activities that in the past did not qualify for any type of financing because of their size or the situation of the citizens."

This proposal is inspired by the microfinance system of the Grameen Bank that succeeded all around the world. Finally, the bill includes several regulations on the publicity made by financial entities, establishing that only authorized financial entities will be able to use the denomination provided for them by the law in order to protect users, thus prohibiting any type of publicity or action tending to gain clients by non-authorized entities.

c. Bill introduced by Federico Pinedo, of PRO:

The bill introduced by Deputy Federico Pinedo defines the banking activity as of public interest, as opposed to its characterization as public service made by the bill introduced by Deputy Carlos Heller.

The bill establishes that the financial activity cannot be considered as a public service, or as a simple activity, given the magnitude of the activities involved and their effects. In such context, the characterization as a public interest will assure the supervision of the State over the authorization given to the private sector that renders the financial services.

The promoters of the bill say that it "Seeks the protection of savers, to guarantee that those who access credit do so in reasonable conditions in order to finance their activities, considered as the only way of generating genuine employment".

The main points of this proposal are the following:

- Creation of a free unique universal account;
- Development of a system for the opening of bank branches;
- Implementation of a system of mandatory guarantee on banking deposits, in order to restore the responsibility of transactions to financial entities and to guarantee to depositors the full and effective reimbursement of their funds in the case of liquidation of a financial entity;
- Protection of users and consumers by means of the creation of the figure of the Ombudsman of Users and the Administrative Court on financial matters;
- Prevention of practices of money laundering and financing of terrorism, with emphasis in preventive policies over repressive policies;
- Creation of an Advisory Committee of Monetary and Credit Policy to coordinate the policies between the Central Bank and the Ministry of Economy, among others; and
- Creation of a Debtors Central in order to facilitate access to credit for individuals, and a Financial Statements Central for companies, in order to promote competition between financial entities for gaining those clients who have good financial behavior.

In connection with the types of entities, the bill adds exchange entities to the financial entities regime, and additionally, although the bill includes a detailed list of the types of entities subject to the financial entities regime, it also provides that the Central Bank may include any other financial entity based on the volume of its activities or for monetary and credit policies reasons.

Additionally, the bill proposes to eliminate the distinction between Argentine and foreign financial entities with absolute equality of treatment between foreign and national entities, considering that this will not obstruct but promote the development and insertion of Argentine work in other countries, opening channels of opportunities and inexpensive financing for local capital.

Notwithstanding the abovementioned, foreign financial entities will have to disclose to their clients and make vast diffusion of the reach of the guarantee and support given by their parent entities or parent companies to the local entities' operations in Argentina.

Among other things, the bill proposes to establish an organic method of relation between the monetary authority and the political power, without detriment to the autonomy of the first one or the legitimacy that the popular representative concedes to the second one.

The authors of the bill said, "The purpose of the bill is to generate a long term structural change willing to obtain a productive economy, plenty of saving, seriousness and credit".

Conclusions:

The most important difference between the bills is the character of public service that the bill of Encuentro Popular tries to attribute to the financial activity.

In opposition, the bill introduced by GEN refers to the financial activity not as a public service but as a public interest.

This distinction is crucial in terms of the role of the State in the financial activity, considering that the characterization as public service involves a concession (which might be revocable) and in the case of a public interest, it is a matter of an authorization given by the State.

Thus, the bill introduced by the GEN party authorizes commercial banks to conduct all the operations that are not prohibited, in contrast, and in a stricter sense, the bill introduced by Encuentro Popular explicitly details the activities that commercial banks can do jointly with the creation of a Code of Conduct of the organizations entrusted to the Central Bank.

The adoption of either concept is preferable to the adoption of a single system combining elements of both, which would turn the financial system into a hybrid.

However, both bills have convergent points in relation to the protection of users of the financial system, as a response to the past financial crisis, a topic which is also being considered in the banking reform under discussion in the United States at the moment.

On the other hand, the bill introduced by PRO does not put the accent in these questions but in public saving and prevention of money laundering.

This bill assures that the banking system and the financial activity should not be considered as public services, since that would lead to greater intervention of the State in the banking and financial activity.

We can conclude that the three bills agree in impelling the protection of the consumer and the extension of banking accessibility to all sectors of society, and to micro, small and medium-sized businesses.

The question is if any of these bills are sincerely aimed to reform the financial system in a permanent way or will they result just in another temporary amendment.

Bill For Amending the Organizational Law of the Central Bank:

Apart from the bills introduced for modifying the Law on Financial Entities, the deputy and legal advisor to the General Confederation of Work (the CGT) Héctor Recalde, introduced a bill in the National Congress which had been previously proposed by the current president of the Central Bank, Mercedes Marcó del Pont, in order to modify the Organizational Law of the Central Bank.

The initiative proposes to modify section 3 of the Organizational Law of the Central Bank, which determines the purposes of the monetary authority. "It is the primary and fundamental mission of the Central Bank to preserve the value of the currency," the current version says.

The bill proposes to extend the purpose of the Central Bank and to include that the Central Bank should support economy and full employment.

Additionally, the bill states that it constitutes primary mission of the Central Bank to preserve the value of the currency, in consistence with policies oriented to maintain a high level of activity and full employment, in a context of sustainable expansion of economy and to guarantee the stability of the financial system. The bill aims to differentiate the mission of the Central Bank today from the one of the 90s, when there was a fixed exchange rate.

The new version of the Organizational Law emphasizes the functions of cooperation between the entity and the objectives of the national government.

The proposed text for section 3 reads: "In the formulation of monetary, credit, financial and exchange policies, **the Central Bank will coordinate its work with the National Executive Power**, without being subject to orders, indications or instructions of the latter on the management of the means of its competence".

The new proposed text comes to respond to the close relation that has existed between the Central Bank and the Executive Power in the last period, which caused the removal of the previous president of the banking organization.

Javier Canosa is the managing partner of Canosa Abogados. Javier helps foreign entities and funds setting up and developing their business in Latin America.

He has vast experience in mergers and acquisition and the negotiation of commercial agreements. Javier has represented and advised several companies, including financial institutions, in corporate M&A, business development and real estate undertakings. In addition he teaches International Business Law at the Universidad de Buenos Aires since 2003 and he has published numerous articles in local and foreign publications. Javier can be reached at jc@canosa.com.ar



How Will Nestor's Passing Affect Argentina: ALI asks its readers

■ Best Case Scenario:

- The business environment remains stable, as President Fernández de Kirchner does not seek reelection and works towards “keeping the house in order” until October 2011.
- Post 2011 presidential elections, the power vacuum is filled by a more pro-business administration, which performs a drastic change in the role of the State in the economy and seeks to integrate the country's economy with the international markets.
- The politicians will shelve their differences and focus on the best interests of the country, which include embracing free market capitalism, strengthening institutions, and attracting foreign investment.
- Nestor Kirchner is dead and so is “Kirchnerismo”. Argentina moves quickly to the center and regains common sense by embracing economic policies such as those of Chile, Peru or Colombia, which limit government spending, welcome foreign direct investment (much needed in infrastructure), intend to reduce inflation, and focus on 2020 not on the 1970's.



■ Worst Case Scenario:

- President Fernández de Kirchner seeks and finds a strong supporter for reelection in the leader of the unions, Hugo Moyano, which deepens the anti-business policy that has tainted the Argentine economy for the last decade. The Governor of the Province of Buenos Aires, Daniel Scioli, said to be now the de-facto head of the peronist party decides to run for President as well. Political and economic instability occurs due to clashes between these two forces.
- President Fernández wins reelection and stays the course of the Kirchner's proprietary interventionist economic policy marked by strong union power, monetary devaluation, arbitrary laws and regulations, and high levels of subsidies, import taxes and corruption.
- Cristina further organizes the left (through empty bribes), pushes Scioli's candidacy for the Presidency and together they continue down the path towards solidifying Argentina's role as an irrelevant banana republic.
- President Cristina Fernández - Daniel Scioli - Hugo Moyano clinch to power for one more turn and limit Argentina's full potential for one more decade.



ALTERNATIVE LATIN INVESTOR SPEAKS WITH ELEMENT-360 FOUNDER, CHAD MARTIN

How did you get become an expert in second home real estate located in emerging markets?

Over the last decade my business partner, Lisa Sharpe, and I have done research and marketing work for a number of developers including the largest international second home developer in the world. Our track record is built upon providing comprehensive services representing \$10 billion in resort development revenue across the Western hemisphere. We identified an opportunity to improve the development process and in response, created Element-360, a research based, real estate services company providing insight, leadership and results to a wide range of clients. In concurrence with the United States economic downturn, E360 recognized a demand for research based services in the emerging markets of Latin America and the Caribbean. Our projects initiated in Mexico and quickly expanded into Panama, Costa Rica, Honduras and the Caribbean resulting in a \$210 million portfolio of affordable second home projects.

What kind of companies are you working with?

E360 is currently working with financial institutions, private land owners and real estate developers of ranging sizes. Our current client list includes one of the largest investment banks in Costa Rica, large land owners in Mexico and the Caribbean as well as developers in Panama. We have supported independent projects and boutique brands as well as the internationally recognized branded real estate offerings including Starwood, Four Seasons and Rosewood.

What has been driving demand for your business to date?

In the past, E360 has seen significant demand for market research that is now transitioning into the execution of sales and marketing. Clients requested our research services in an effort to secure financing and validate product, pricing, phasing and target markets. Currently, we have seen an increased demand in marketing strategies and execution. What separates our business practice from other real estate companies is that every recommendation is market driven based on facts. We put a strong emphasis on understanding what product is moving at what price and to whom before we ever spend a marketing dollar. We achieve this by surveying the competitive landscape and running statistical demand analysis.

What trends are you seeing in second home markets?

E360 recently completed one of the largest existing second home owner surveys. In that survey, we discovered the priority of attributes and amenities owners prefer. One trend that was identified is the high value on views. The quality of real estate with a view ranked more important than health and wellness facilities or capital heavy amenities. Another trend, which isn't surprising, is affordability. Given market conditions and the availability of a strong value proposition, buyers know they can expect an affordable option. Repeatedly developers get focused on the price per square foot value ratios in an effort to better understand profit margins, however the consumer may have an absolute price point and more flexible on the square footage.

Who is the second home consumer of today's economy?

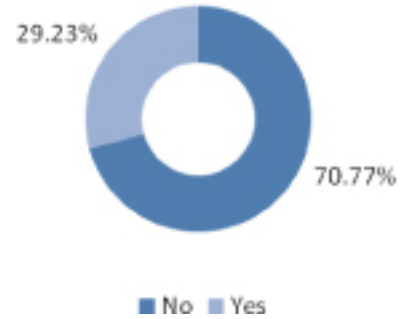
Consumers searching for second homes are educating themselves on the comparable projects, price points and amenities. They research on the internet for long periods of time prior to connecting over the phone. We have identified the same amount of Generation X buyers as Baby Boomers which is consistent with what other industry insiders have reported also. Within this generational profile, there niche market segments that should be considered depending on the lifestyle offering of the project.

You mentioned your latest second home survey report, what findings surprised you the most?

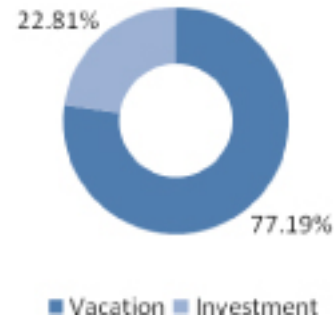
We were very surprised by the number of existing U.S. second home owners who are sitting on the sideline waiting to see a strong indication of market recovery. These existing second home owners are the ones who have been buying low and selling high for decades. They bought at the bottom of the market and sold at the top. Our survey results indicated 57% of existing second home owners are either likely or very likely to buy in Latin America over the next two years. To the right are some of the key findings from the survey. Please visit our website dashboard for more research at www.element-360.com or contact Chad at chad@element-360.com.



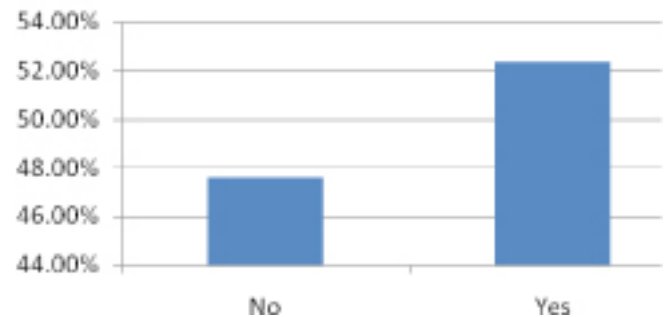
Would you use mortgage financing to purchase a second home?



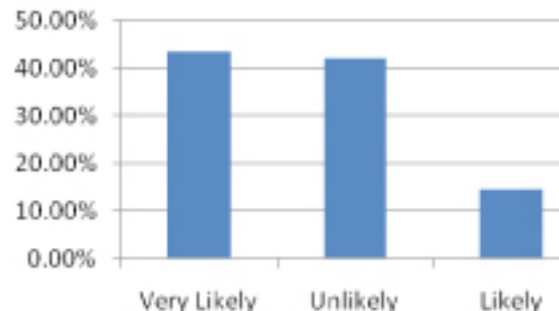
What would be the reason for you to purchase a second home?



Is now a good time to purchase a second home?



What is the likelihood of you buying a second home in the next two years?



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