

# EU-Latam relations

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September 14, 2023

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# EU-Latam relationship and their structural challenges

# Europe and Latam are key partners that would benefit from stronger ties

- Slow per-capita growth in EU & Latam. Need private investment to increase productivity growth
- Several “points of contact” EU-Latam that could increase the likelihood of these goals:

## TRADE

- Deficient **intra-regional trade** in Latam
- Europe is a **sizable market** and already a **key trade partner** for high-value-added exports, especially for South America.
- **Latam has resources to offer** to Europe, including for climate change. Strategic Autonomy
- **Is there really appetite for trade deals?**

## INVESTMENT

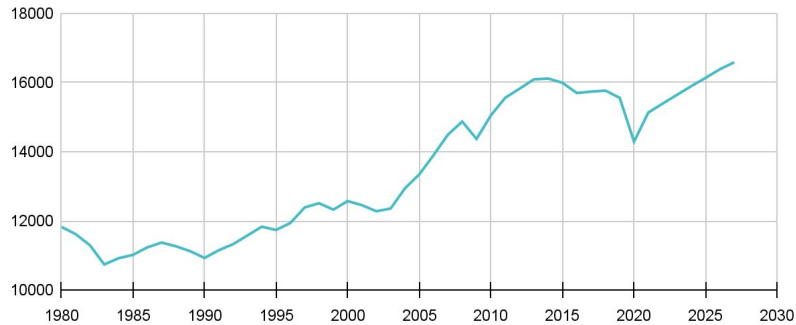
- **EU is the main investor.** Even more weight of Europe in FDI to Latam
- **FDI from Latam** starting to go to Europe

## PEOPLE

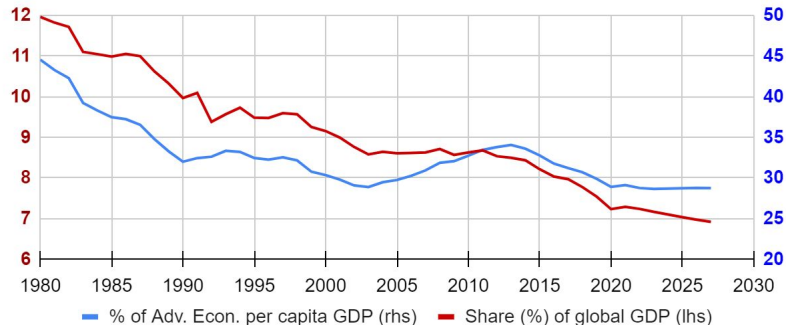
- **Strong migration to EU** (especially from South America)
- **Tourism** flows also greatly engage EU and Latam (especially South America)
- Latam needs **higher human capital.** Europe “exports” education that could fill positions with different skill sets (for which there is strong demand in Europe)

# Latam: dealing with the fourth negative shock in short succession

## LATAM GDP PER CAPITA - CONSTANT USD PPP



## LATAM GDP GAPS - IN PPP



Source: IMF and BBVA Research.

- Four Shocks to the region since 2014
  - End of commodity supercycle (2014).
  - COVID (2019).
  - War in Ukraine (2022-).
  - Tightening global financial conditions.
  - GDP per capita not likely to recover until 2025 (A missed decade? But not like the 80s!).
  
- Latam's share of Global GDP continues to decline.
  - This is not just the rise of Asia: the gap of GDP per capita between Latam and Advanced Economies remains at historical highs.
  
- Need to revamp productivity growth. How?

# Europe: evolving geopolitics, technology and climate change realities pose new challenges and call for new policies and shifts of economic models

## NEW AND OLD STRUCTURAL CHALLENGES IN EUROPE

## CAN LATAM HELP?

### ■ Geopolitics:

- Ukraine war and lack of confidence of Russia.
- Position in the face of increased US-China rivalry.
- Evolving role of international forums (G7, G20, WTO).



### ■ Trade:

- US increased protectionism: tariffs, IRA.
- Economic dependency on China vs geopolitical pressure.



### ■ Climate change:

- Increased awareness of climate challenges.
- Lack of some key metals and energy sources.



### ■ AI and digital:

- Very much behind the US and China in some technologies (AI, chips, batteries).



### ■ Ageing and migration:

- Ageing and diminishing labour force.
- Diminishing pools of immigrants in the future.

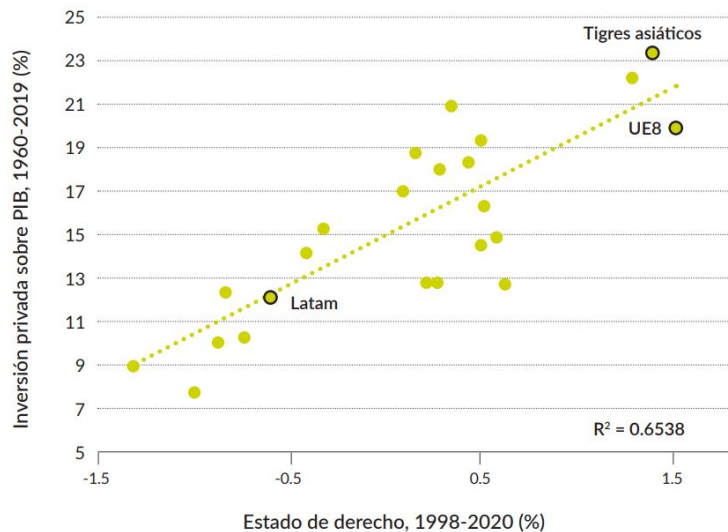


# 02

## Levers for productivity growth

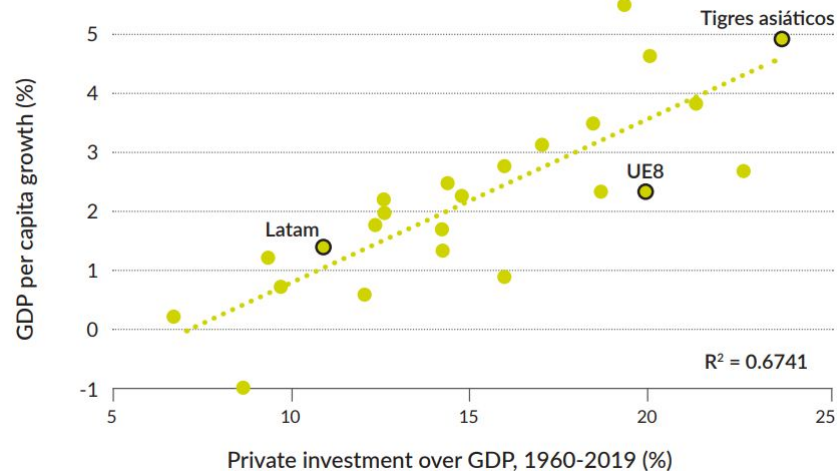
# Latam and Europe need to increase per-capita growth: the role of private investment and institutions is key

## PRIVATE INVESTMENT AND RULE OF LAW



Source: IMF, World Governance Indicators and BBVA Research.

## PRIVATE INVESTMENT AND GROWTH



Source: IMF, Penn World Tables and BBVA Research.

Countries with better institutions and better rule of law correlate with higher investment  
Higher private investment translates into higher per-capita growth and faster convergence.

## Lever 1: Trade. Increasing trade is a win-win for Latam and EU

### LATAM

- Difficult **intraregional trade**: deficient infrastructure, atomized trade deals.
- **Nearshoring**: an opportunity for Mexico. (South America is much farther away; never took advantage of rise of value chains).
- China: important destination for commodities, but not for high-value-added exports.
- US: Low appetite for new trade deals.

What is the EU's appetite to advance trade deals?

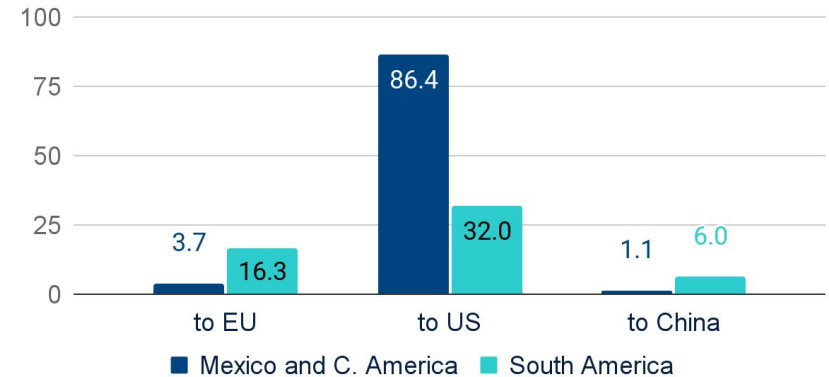
Agreements with Latam in the pipeline:

Mercosur (ratification);  
Chile (modernization);  
Mexico (modernization)

### EU

- Open up new markets.
- Access to commodities and key resources for climate-friendly growth and new industries (commodities, rare earths).
- Strategic autonomy with requires stronger links and investment.

### EXPORTS OF MEDIUM- AND HIGH-TECHNOLOGY % OF TOTAL EXPORTS OF ITS KIND





## Lever 2: Keep up and increase FDI from Europe in key sectors (in a world where the US and China are trying to catch up)

### DI STOCK IN LATAM, 2021

(% OF SUM EU+US+CHINA)



### CUMULATIVE FDI FLOWS TO LATAM, 2010-20

(% OF SUM EU+US+CHINA)



### A big win for Latam

- Key component of transfer of know-how.
- Institutional anchor.
- EU and US still dominant in Latam
  - Stock of EU+US FDI is 20 times bigger than China's;
  - 5 times bigger flows than China during 2010-2020

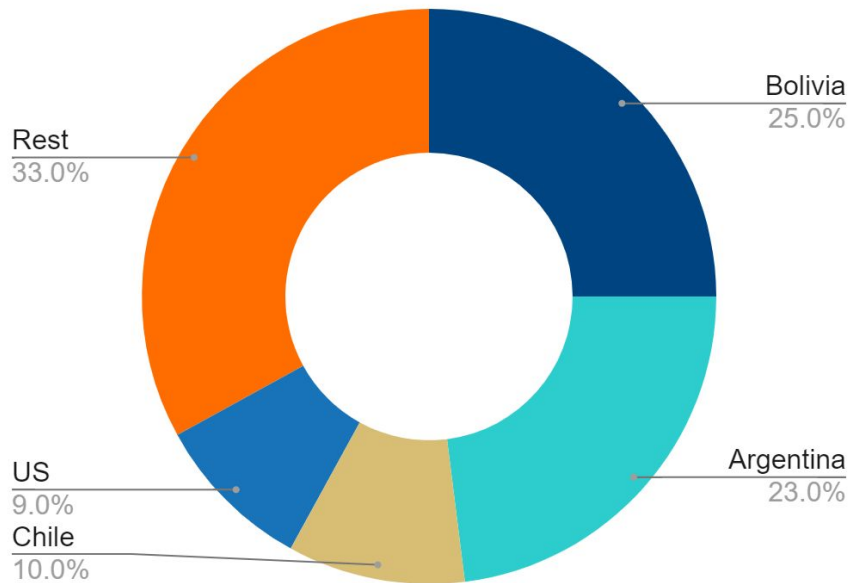
### A big win for Latam

- Access to key resources.
- Access to local markets.
- Export platforms (eg USMCA).

## Lever 3: EU-Latam and the scope for cooperation on climate change

### LITHIUM RESERVES

(% OF GLOBAL)



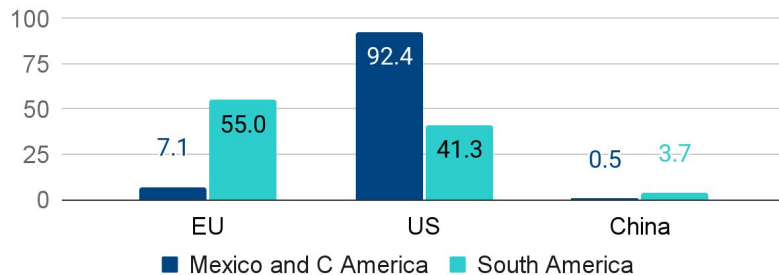
Source: IADB and BBVA Research.

- **Latam: leveraging Climate action for growth?**
  - Latam has a larger share of **key resources** (copper, lithium) than its share of global GDP
  - Latam is also prone for **clean energy export** (hydrogen) to EU or receive **energy-intensive industries**, part of GVCs.
  - LatAm also needs to unlock the **potential of natural capital**, to combat the loss of biodiversity
  - But it needs the right investment and regulatory framework as **private investment is key**
- **EU: securing green transformation**
  - Secure supply chains for climate action, including clean energy.
- **EU investment in clean Value Chains in Latam?**
  - Work toward EU emissions goals.
  - Part of the value added to remain in Latam.
  - Help improve Latam environmental standards.

## Lever 4: Developing EU-Latam human ties

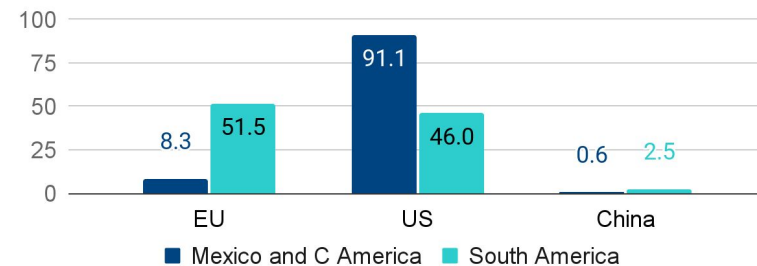
### ORIGIN OF TOURISTS TO LATAM, 2019

(% OF SUM EUROPE+US+CHINA)



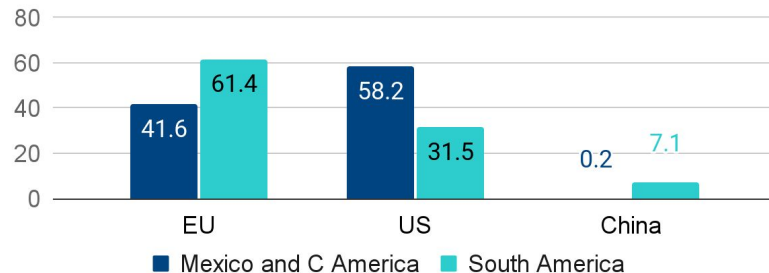
### DESTINATION OF LATAM TOURISTS, 2019

(% OF SUM EUROPE+US+CHINA)



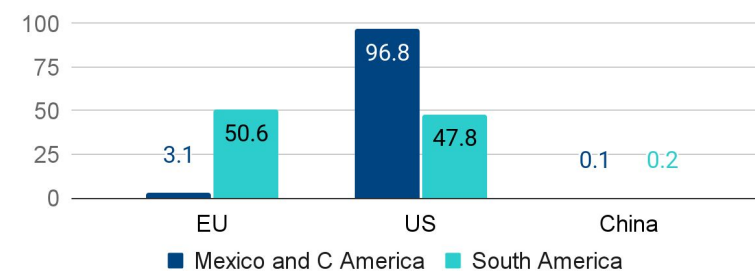
### DESTINATION OF LATAM STUDENTS, 2019

(% OF SUM EUROPE+US+CHINA)



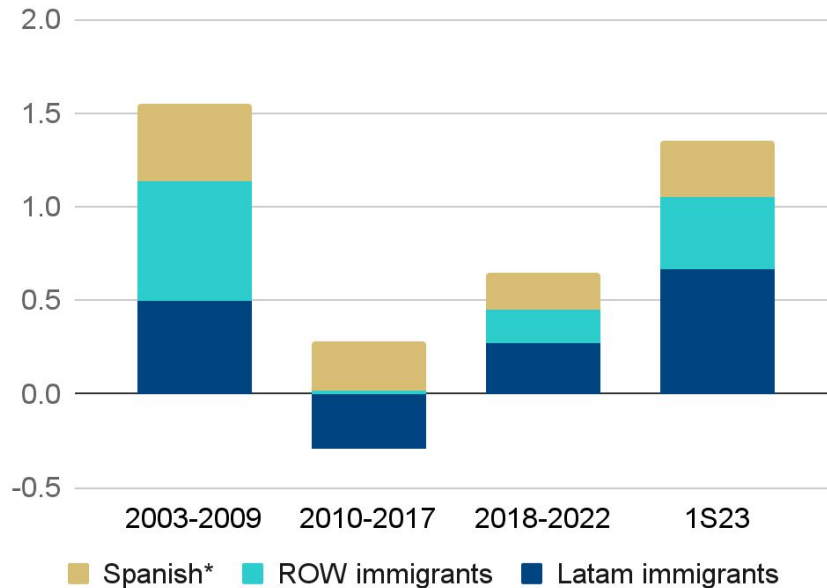
### DESTINATION OF LATAM MIGRANTS, 2019

(% OF SUM EUROPE+US+CHINA)



## Lever 4: EU-Latam: Taking advantage of demographic trends and strong human ties in migration and education

### SPAIN: CONTRIBUTION TO Y-O-Y GROWTH OF THE WORKING-AGE POPULATION (PERCENTAGE POINTS)



- **Ageing and diminishing labour force in EU**
  - Diminishing pools of immigrants in the future.
  - Scope for more organized migration from Latam. Qualified immigration.
  
- **Opportunities for EU-Latam cooperation on education**
  - Further attraction of Latam university graduates for further higher education.
  - Brain gain in Latam from higher education opportunities in Europe.
  
- **Baldwin's (2020) third great unbundling and opportunities for trade in services EU-Latam**
  - Latam: Massive increase in tertiary education cannot always find jobs locally.
  - Demand for services (personal and professional) is on the rise in advanced economies.

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# Takeaways

## Concluding remarks

- Cyclical slowdown in Latam, but structural challenges as well: need private investment for growth.
- Europe also needs to increase per-capita growth: investment, deregulation, innovation.
- Several points of contact EU-Latam towards these goals:
  - Trade agreements: not the panacea, but significant benefits.
    - For both: new markets; increase productivity and GDP per capita.
    - For EU: secure supply chains, including key resources for climate action.
    - For Latam: institutional anchoring.
  - Investment
    - For both: increase productivity; investment-for-climate-action.
    - For EU: investment opportunities; access to key resources, to local markets; export platforms
    - For Latam: know-how, technology transfer; institutional anchor.
  - Human dimension: migration; service exports; higher education opportunities for Latam in Europe.
- Keeping Latam in the “western” camp and supporting democratic values, avoid authoritarianism that hinders investment.

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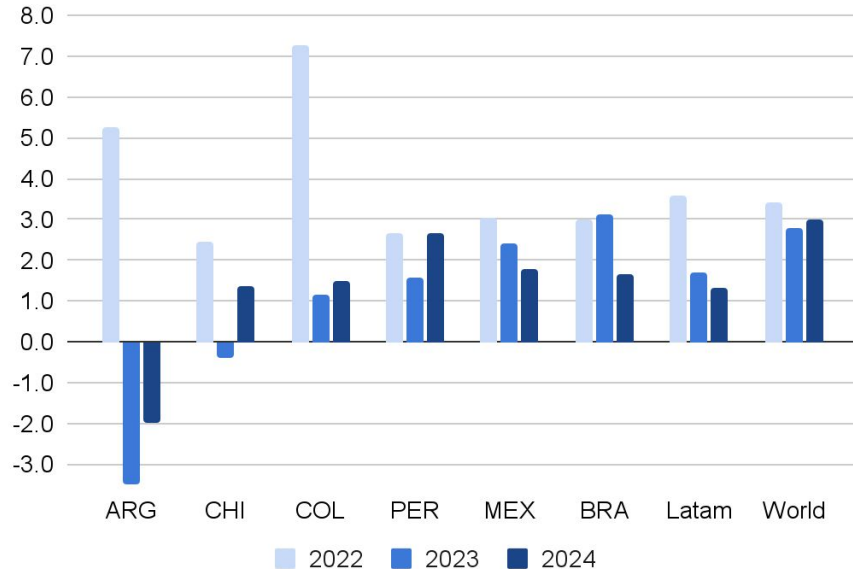
Annex



# Latam: after COVID growth rebound, slowdown is expected in 2023-24, on external and domestic headwinds

## GDP GROWTH

(%)

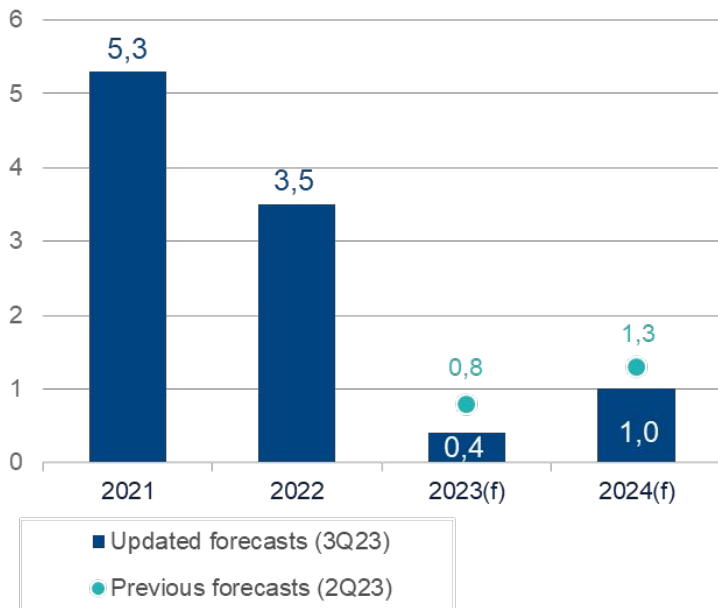


- Growth will slow down significantly in 2023-24, to around 1.5%
- Inflation in Latam has moderated significantly due to early and fast monetary tightening
- First rate cuts are starting in some countries. They will spread before year-end. But the road to neutral monetary policy is long.
- Fiscal policy in Latam is broadly neutral but it could probably help more to reduce price pressures going forward.

## EU: After the sharp exit from Covid, GDP growth has been affected by the Ukraine war, higher interest rates and, more recently, China's sub-par growth

### EUROZONE: GDP GROWTH PRELIMINARY FORECASTS

(%)



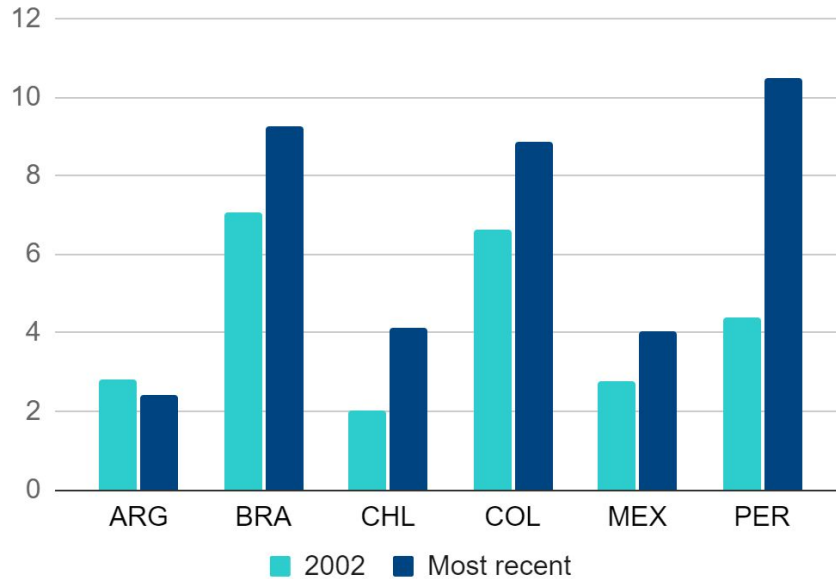
- **Growth:** Bias to lower growth, mostly due to lower than expected performance in China and
- **Fiscal policy is still supportive**, but will likely become more targeted and less expansionary onwards. It is pending on an agreement on fiscal rules to be applied in 2024
- **Inflation remains relatively high.** It has started to flex down thanks to lower commodity prices, base effects and higher rates, but remains far from target
- **ECB:** Very close to maximum rates expect another hike this year and no rate cuts for a long period of time
- **Risks** include the war, higher energy prices (negative competitiveness shock), China's deceleration, more persistent inflation, collapse of the current growth model, especially in Germany (and impact of China US industrial policies)

## What does Europe need to increase per-capita growth?

- **Increase labour force (immigration) and labour use** (higher participation of older and female workers).
- **More investment**, especially in sectors that address new needs (clean energy, EVs).
- **More trade openness** to third countries.
- **Focus on effective innovation** (AI and digital, clean energies), less regulatory burden.
- **Autonomous payment systems** (which may benefit third countries) that do not depend on the US.

# What does Latam need to increase per capita growth? More investment. What prevents it?: Lack of political consensus for micro reforms

## NUMBER OF EFFECTIVE\* PARTIES IN CONGRESS



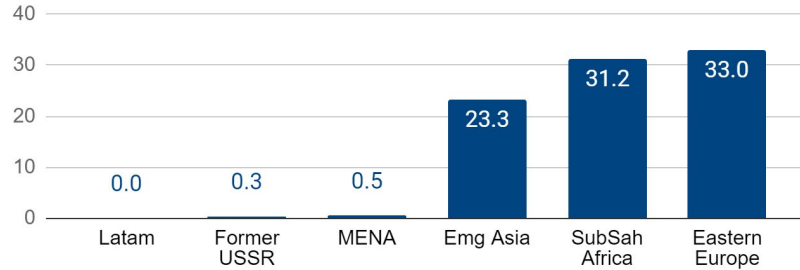
party seats in Congress.  
Source: National Congresses and BBVA Research.

- 2022-24 is the latest election cycle in Latam (CRC, COL, BRA, ARG, PRY, GTM, MEX, ELS, VEN, URU)
- Pink Wave (PER, COL, BRA, CHI) cannot be generalized: see ARG, ECU, CRC.
- Since 2018, opposition has won 76% of elections in Latam. No ruling party has won the presidency.
- “Punishment vote” started around 2015, with the growth slowdown. “Punishment vote” reduces the length of mandates, relative to long mandates in the high-growth decade (2003-13)
- Winning coalitions since 2015 usually united in protest.
- Polarization and fragmentation have become the norm. Elected Presidents on average got 37% of vote in first-round in 2018-22 (48% in 2009-13).
- Difficult governability. Difficult to pass reforms.

# Environment: Geostrategic US-China rivalry and the Latam-EU relationship

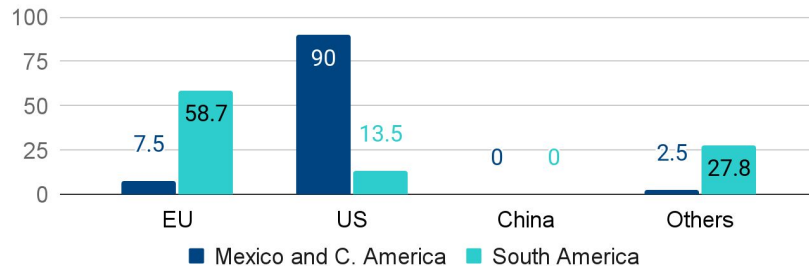
## WEAPONS IMPORTS FROM CHINA 2021-22

(% OF WEAPONS IMPORTS OF EACH REGION)



## ORIGIN OF WEAPONS IMPORTS IN LATAM 2021-22

(% OF TOTAL WEAPONS IMPORTS)



- It does not seem that the US and EU have abandoned Latam to China when looking at
  1. Destination of high-technology exports from Latam (mostly US and EU);
  2. FDI stocks and flows;
  3. Financial flows;
  4. Human links (tourism, students, migration)
  5. Military links with the US (see graph)
  
- But the EU and US need to rekindle a closer relationship held in the past. And dealing with countries that demand a stronger voice (their own voice) in foreign affairs. Europe could be the first to understand it and build on that

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