Latin America: an uneven recovery

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Financial markets in Latin American have continued to enjoy significant gains over the last few months, largely due to the reduced level of concern over US economic policies and a perception that any increase in interest rates by the Fed will be implemented gradually. While the international outlook is favourable, a number of regional confidence indicators remain pessimistic, despite the significant recovery being experienced in Brazil and, more recently, in Mexico.

Given this environment, we stand by our prediction that Latin America will return to its previous level of growth after a four-year period of slowdown. To be precise, we predict a growth rate of 1.1% this year and 1.8% for 2018, after the negative growth of -1.4% in 2016.

The good news will be concentrated in the three largest countries in the region. The recovery in Argentina, which has already shown signs of growth, will begin to firm up, while Brazil seems to be coming out of its period of adjustment and returning to growth this year. For its part, Mexico's economy is now beginning to show chinks of light, as it is now anticipated that the trade measures taken by the United States will be less aggressive than earlier feared. On the other hand, the prospects for growth look less optimistic in Peru and Colombia due to the weak economic data recorded over the last few months, pessimism in the private sector, delays in infrastructural projects and, in the case of Peru, the negative effects of the heavy rain brought by the phenomenon known as "El Niño".

Inflation will continue on its downward path in South America due to weakness in domestic demand and the relative strength of local currencies. In this context, we expect new cuts in interest rates (which are likely to be more aggressive in Brazil), while at the same time the rate of inflation will continue along the path favoured by the central banks, a process that has shown a little more resistance to change than expected in Argentina. In sharp contrast, inflation continues to increase in Mexico, although the recent recovery in the exchange rate has moderated inflationary pressures to some extent. This prospect of less unfavourable inflationary conditions will also tend to reduce the intensity of the monetary tightening cycle that was predicted for Mexico at the beginning of this year.

The risks to which the region is exposed are continuing to follow a downward trend. On the external side of the equation, the shorter-term tensions associated with China and US trade policies appear to be easing, though in the former case the medium-term risks are increasing as the Chinese authorities are putting off measures to deal with the country's structural imbalances. Within the region there remain a number of risks connected with the overall political panorama and the delays affecting infrastructure construction work going on in a number of countries. Within this scenario of slow regional growth it will be essential to keep a close eye on the very crowded electoral calendar in Latin America during the course of this year and the next.