PANTHEON™ MACROECONOMICS

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THE **LATIN AMERICAN ECONOMIES** IN 2015

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Challenges Ahead as the Fed Hikes; Domestic Economies Improving?

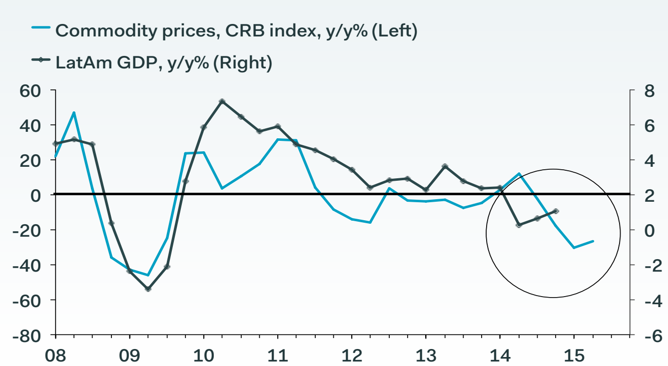
* We expect growth in Latin America to improve in the second half of the year, thanks in part to an accelerating U.S. economic recovery and stabilization in China's growth, but the upturn will be modest. *We look for regional GDP of only 0.6% in 2015 as a whole.* Next year should be better, assuming the Fed's monetary policy normalization—which we expect to start by September—does not trigger sustained FX weakness in LatAm, and provided commodity prices, especially oil, don't fall further.

* The outlook is uneven, with the Pacific Alliance countries—Mexico, Colombia, Peru and Chile—enjoying faster growth in the second half. At the other extreme, Venezuela and Argentina have very weak macroeconomic fundamentals, and inflation will continue at dangerous levels, especially in Venezuela, where the economy is chaotic and political instability is a real risk. Between these poles, Brazil, the biggest economy in Latin America, will remain fragile this year, with weak economic activity and high inflation.

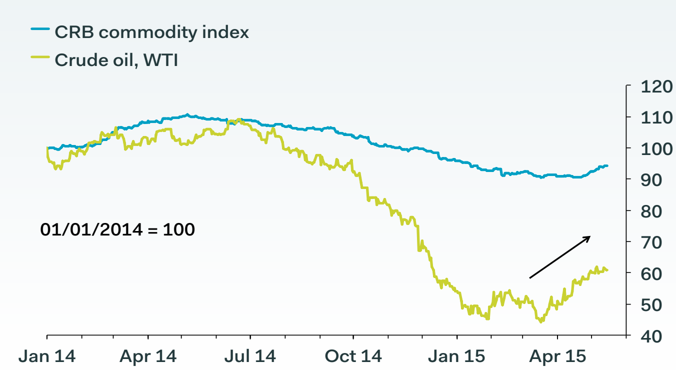
* We expect GDP to contract by 1.2% in **Brazil** this year. Fiscal and monetary policy tightening and structural adjustments have damaged business and consumer confidence, pushing the economy to the verge of a recession. The economy will improve next year, as benefits of political and economic reforms kick in. Still, we look for 2016 growth of only 1%. Annual inflation will remain just above 8% this year, before gradually subsiding to 6% next year.

* Economic activity in **Mexico** is recovering, thanks in part to rising exports to the U.S. and robust domestic demand, reflecting accommodative policy, coupled with low inflation. But growth will continue to be constrained by low oil prices, and the lagged effect of the MXN's depreciation—about 4.5% year-to-date—pushing import prices up, preventing a real improvement in confidence. Next year will be better as the US economy gathers momentum. We expect 2.8% GDP growth this year and close to 3.5% in 2016.

THE OUTLOOK IN THE REGION REMAINS GLOOMY...



...BUT THERE ARE SOME SIGNS OF STABILIZATION AND HOPE



* Economic activity in **Colombia** has slowed in the recent months, due mostly to lower oil prices, which have pushed up both the current account and budget deficits. But domestic demand is partially offsetting the oil hit and will continue to do so in coming quarters, though at a slower pace. BanRep will remain on hold this year, worried about inflation and the current account. Inflation is high, but it will decline through the second half, reflecting the slowdown in economic activity. GDP should rise 3.3% this year, and 3.7% in 2016.

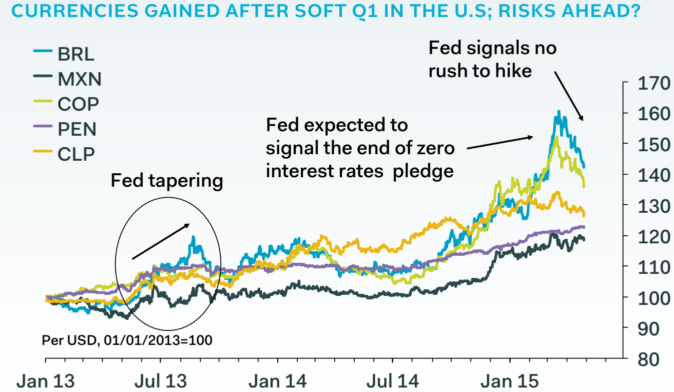
* **Chile** is rebounding slowly from the downshift in growth over the past year. Low copper prices, labor-friendly reforms in 2014 and recent political scandals have severely damaged business confidence and private investment. But the economy is recovering, at last, thanks to the lagged effect of the substantial easing of monetary policy last year, and higher public spending. GDP growth should reach 2.6% this year and 3.5% in 2016. That's weak compared to the previous cycle, but Chile will have to adjust to a new, slower trend unless commodity prices rebound substantially.

* **Peru's** economy is starting to pick up after a weak year, due mostly to low metal prices. But the government boosting to the economy with stimulus packages, and additional measures for the mining sector. Mining activity is stabilizing and should begin to expand over the coming quarters. GDP should grow 3.5% this year and 4.3% next. But note that the El Niño weather pattern, which was predicted in 2014 but failed to materialise, is a major risk as it can seriously hurt crops and fisheries. Inflation is high but will start gradually converging to the 2% target over the coming quarters.

* In **Argentina**, confidence and real activity is improving at a very moderate pace, as October's presidential election get closer. The three main candidates seem willing to address complex economic problems, such as high inflation, untrustworthy statistics and returning the country to international capital markets. Looking ahead, we expect an improving but still weak economic activity and high volatility prior to the election. We expect GDP to contract by 1.1% in 2015 and about 0.5% next year.

* Finally, **Venezuela** is still a mess. The economy is contracting and will shrink again next year, due to FX rationing and irresponsible economic policies. Low commodity prices are not making life any easier for the country, and international reserves have hit a new 12-year low. The central bank has not published official GDP figures since last year, so putting numbers on a forecast is difficult. Social and political instability will remain, due to the severe macroeconomic imbalances and government intervention. CPI Inflation will continue running above 70% year-over-year.

CURRENCIES GAINED AFTER SOFT Q1 IN THE U.S; RISKS AHEAD?



INFLATION WILL SLOW DUE TO SUBDUED ACTIVITY