INDEPENDENT • INCISIVE • ILLUMINATING

LATIN AMERICA IN 2015

ANDRES ABADIA, SENIOR ECONOMIST

A Positive 2015, but Still Fragile And Dependent on External Factors

* Most Latin American economies should improve in 2015, but **we expect the region as a whole to expand by only 2%, following a growth of just 1.2% last year.** The second half of the year should be better than the first, assuming the Fed's monetary policy intentions become clear. An accelerating U.S. economic recovery will be positive for the region, with Mexico benefiting most. The biggest downside risks come from lower commodity prices, especially oil, and the slowdown in China, though our base case is that Chinese growth will soon stabilize close to its current rate.

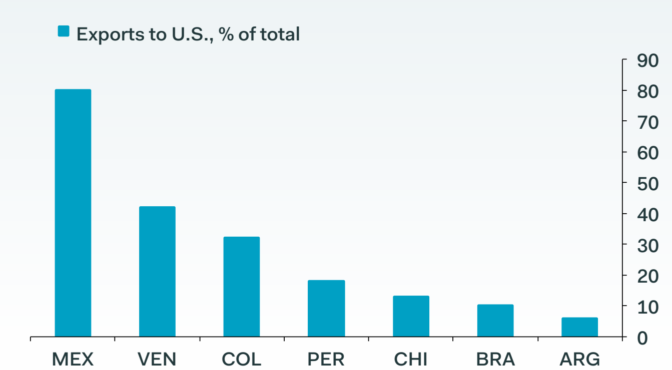
* The economic picture in the region for 2015 is mixed. **The Pacific Alliance countries—Chile, Colombia, Mexico and Peru—will record the highest growth rates, with inflation under control.** At the other extreme, Venezuela and Argentina have very weak macroeconomic fundamentals, and inflation will remain at dangerous levels. Finally, the Brazilian economy, the biggest in Latin America, is an intermediate case. It will remain fragile, but we expect the new economic team in the re-elected Rousseff administration government to implement significant policy and structural reforms, boosting confidence.

* **Brazil** has already shown incipient signs of recovery over the last few months. But the economy is still very weak and we look for growth of only 0.7% year-over-year growth in 2015, after 0.3% last year. We expect the BCB to seek to dampen inflation pressures by **increasing the Selic policy rate to 12.5%** by the end of 2015.

* **Mexico** is beginning to enjoy a cyclical recovery, but growth will be constrained by low oil prices, and **political and social problems will prevent a real improvement in confidence.** The second half of this year, when the impact of economic reforms will be fully translated into the economy, will be better. We expect 3.5% GDP growth, after 2.2% in 2014, thanks mostly to stronger consumption and investment. Banxico will begin to normalize monetary policy by the end of 2015, before an accelerated economic growth is in place.

LATAM GROWTH SHOULD STABILIZE AFTER 2014 WEAKNESS

THE IMPACT OF STRONGER U.S. DEMAND VARIES ACROSS LATAM



THE **LATIN AMERICAN ECONOMIES** IN 2015

* Economic activity in **Colombia** has slowed in recent months, due to lower oil prices and the recent Banrep tightening. But **the strength of domestic demand has helped partially to offset the impact of these factors,** and will continue to do so in coming quarters. GDP should grow 4.2% in 2015 after 5.0% last year. We expect Banrep to remain on hold in 2015, due to the drop in oil prices.

* **Chile** is rebounding at a moderate pace from the slowdown in economic activity over recent quarters; low copper prices have severely damaged private investment. But we remain positive for the economy as the **substantial easing of monetary policy over the past year, together with higher public spending, will support growth.** GDP growth should reach 2.6% in 2015, up from 1.7% last year. We believe the BCCh will leave the policy rate on hold, at least until the third quarter of 2015.

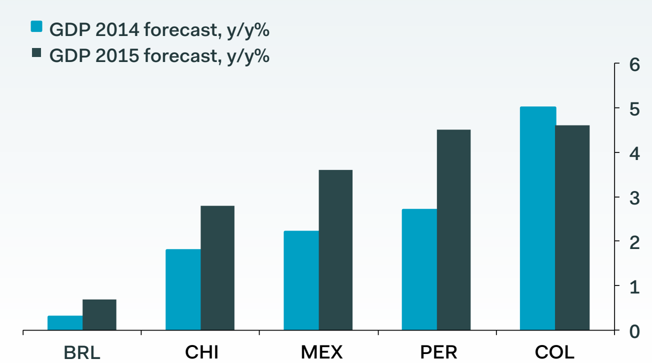
* **Peru's** economy is starting to pick up, after a weak 2014, due mostly to low metals prices. But the government is planning to boost the economy with further stimulus packages, including tax reductions, and additional support for the mining sector. **Mining already is showing some signs of stabilisation** and we are confident the improving trend will be maintained over the coming quarters. GDP should grow 4.1% in 2015 from 2.7% last year. We expect the BCRP to stay on hold, at least until the second quarter of the year.

* Argentina and Venezuela are still a mess, and low commodity prices in the months ahead are not going to make life any easier for these countries. We expect both to be in recession for the next few quarters. **They will continue to flirt with hyperinflation** for the foreseeable future.

* In **Argentina**, confidence and real activity have been severely damaged by painful import and exchange controls. The recession, despite the picture portrayed by the scarce official figures, deepened in 2014. A fiscal deterioration, monetization of public debts, and ongoing problems with holdout creditors will continue to damage the economy. **Looking ahead, we expect more of the same,** with GDP contracting 1.6% in 2015 after a 1.8% drop last year.

* Finally, **Venezuela's** economy is contracting and will shrink again this year. The central bank has not published official GDP figures since 2013, so putting numbers on a forecast is difficult. **Social and political instability will continue, reflecting the dire economic situation.** CPI Inflation will continue running above 60% year-over-year.

2015 IS SET TO BE BRIGHTER FOR THE PACIFIC ALLIANCE BLOC



SHARP DECLINES IN COMMODITIES (01/01/2013=100)