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THE **LATIN AMERICAN ECONOMIES** IN 2016

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A Glimmer of Hope in 2016... But Stiff Challenges Remain

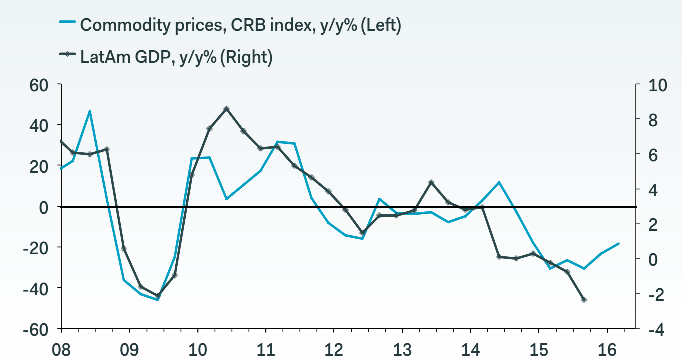
* We expect growth in Latin America to improve in 2016, especially during the second half of the year, when an accelerating U.S. economy and stabilization in China will be helpful. The economic upturn, though, will be modest, as many central banks will be forced to extend their tightening cycles to tame worrisome inflation, boosted by the El Niño and the lagged effects of FX depreciation. **We look for a regional GDP contraction of only 0.1% in 2016 as a whole, less bad than the 0.5% drop in 2015.** This relatively benign scenario assumes that commodity prices, especially oil and copper, don't fall further. Currencies will continue to be under pressure, as the U.S. keeps tightening, but FX depreciation will be much more modest than in 2015.

* **The outlook is still uneven across the region, with Mexico, Colombia, Peru and Chile in a relatively benign position.** At the other extreme, Venezuela will have another grim year, and inflation will run rampant again. The opposition's landslide victory in the legislative election will not result in serious policy reforms. In the middle will stand Brazil, which will remain very fragile this year, due to the political and fiscal crisis, low consumer and business confidence, and high inflation and interest rates. But the recession will ease.

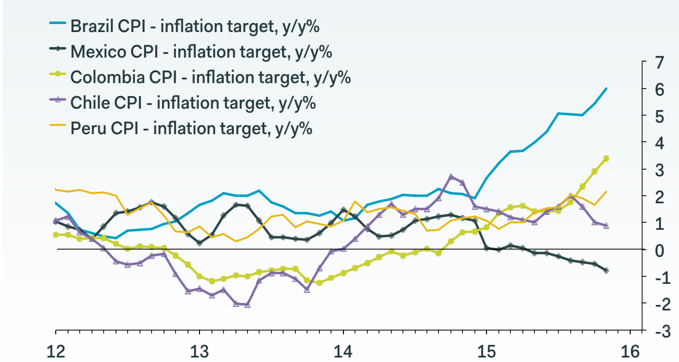
* We expect **Brazil's** 2016 GDP to contract by 2.0%, as the country battles structural and cyclical challenges. Monetary policy tightening, fiscal chaos and regulated price increases have damaged confidence, pushing the economy into the worst recession in decades. The economy will stabilize this year as the big drag from falling investment eases, but the country will only start growing in H2, at a very modest pace. Annual inflation will remain uncomfortably high, but should gradually subside to 7%. **We expect the Copom to increase rates by 25bp during the first quarter, and then remain on hold until late in the year.** In Q4 the central bank will be able to cut rates, by 50bp, in order to help the modest recovery of economic activity.

* Economic activity in **Mexico** is improving, but it will not accelerate this year. Rising exports to the U.S. and robust domestic demand, coupled with low inflation, will help to offset the hit from low oil prices, the lagged effect of the MXN's depreciation and a short monetary policy tightening cycle. The second half of the year will be better as the US economy gathers strength. We expect 2.8% GDP growth this year. **We look for Banxico to raise rates 25bp in both the March and June meetings, ending the year at 3.75%.**

ECONOMIC GROWTH WILL STABILIZE AT A SUBDUED PACE



INFLATION WILL REMAIN A WORRY DURING MOST OF 2016



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* **Argentina's** economic outlook has improved significantly thanks to the election of Mauricio Macri as president. The new government is starting to address an array of complex economic problems, including high inflation, and untrustworthy statistics, and will try to return the country to international markets. The recent 30% ARG devaluation will hit the economy during the first half, squeezing domestic demand and lifting inflation, but the country's prospects will gradually improve as investor and consumer confidence strengthens.

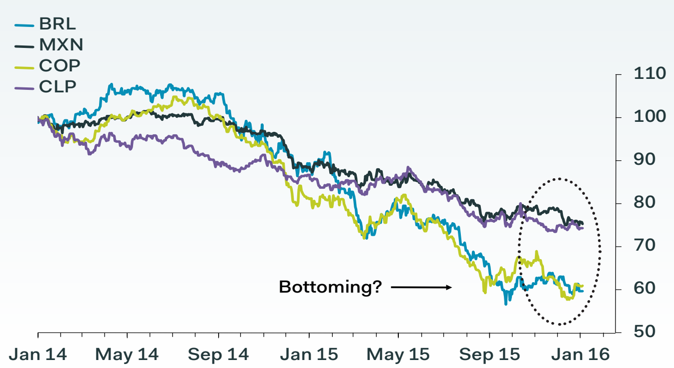
* Economic activity in **Colombia** will slow over the coming months, due mostly to the ongoing hit from low oil prices, the tightening of monetary and fiscal policy, and the lagged effect of the COP's depreciation on import prices. These factors will be partially offset by the execution of the 4G infrastructure program and the effect of the re-opening of the Cartagena oil refinery. Confidence will likely be boosted after the implementation of a peace agreement with the FARC. Inflation will remain high in H1, but it will decline during H2, reflecting the slowdown in economic activity. GDP should rise 2.5% this year. **We expect BanRep to end the tightening cycle at 6.0% in Q1.**

* **Chile's** economy will improve, but only marginally. The recovery will be driven by higher public spending, and stabilizing private investment, after significant declines in the past two years. Low copper prices, China's slowdown, and domestic business and private confidence will limit any significant acceleration over the near term. GDP growth should reach 2.5%; still weak compared to the previous cycle, but Chile is adjusting to a new, slower trend unless commodity prices rebound substantially. We don't expect that to happen soon. Inflation will slow, especially during H2, but will remain above the BCCh's target. **We believe the central bank will increase interest rates by 25bp to 3.75% in the first quarter.**

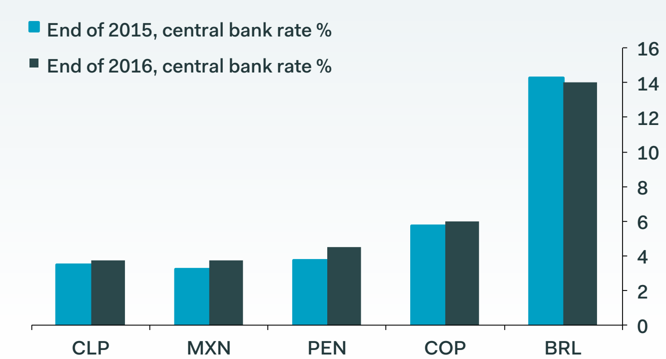
* **Peru's** economy will gather momentum this year, thanks mainly to a recovery in the mining industry, higher public spending, and the stabilization of private investment. This positive trend will be hampered, though, by the lagged effect of the PEN's depreciation—which has increased private debt—and El Niño, which could continue seriously to hurt crops and fisheries. GDP should grow 3.4% this year, and inflation will remain high, above the 2% target, over the coming quarters. **Monetary policy is likely to be tightened further this year.** Our forecast is for interest rates to rise by 75bp to 4.25%. Presidential elections will take place on April, and we expect a market-friendly result, with Keiko Fujimori, of the conservative Fuerza Popular party, winning.

* Finally, **Venezuela's** short term outlook is still a mess despite the opposition having claimed an historic victory in the legislative election on December. **President Maduro is still at the helm and the economy will still contract, due to FX rationing and irresponsible economic policies.** Low oil prices are not making life any easier, and international reserves are still plunging. 2016 will be less bad, especially the second half, provided oil prices stabilize. But social instability will remain a serious problem, due to the severe economic imbalances and government meddling. CPI Inflation will continue running above 100%.

LATAM CURRENCIES ARE BOTTOMING



MODEST FURTHER INCREASES IN INTEREST RATES AHEAD



THE **LATIN AMERICAN ECONOMIES** IN 2016

GDP (year-over-year, %)

	2013	2014	2015	2016	2017
Argentina	2.9	0.5	0.5	0.1	1.0
Brazil	2.8	0.2	-3.0	-2.0	0.8
Chile	4.3	1.9	2.2	2.5	3.2
Colombia	4.9	4.6	3.0	2.5	3.0
Mexico	1.4	2.1	2.5	2.8	3.4
Peru	5.8	2.4	2.8	3.4	3.6
Venezuela	0.9	-4.0	-8.5	-1.8	0.8
Latin America	*3.0*	*0.7*	*-0.5*	*-0.1*	*1.7*

Prices, CPI (year-over-year, %, average)

	2013	2014	2015	2016	2017
Argentina	10.6	25	22	25	10
Brazil	6.2	6.3	9.0	6.8	5.0
Chile	1.8	4.4	4.4	4.0	3.5
Colombia	2.0	2.9	4.9	4.0	3.2
Mexico	3.8	4.0	2.8	3.2	3.0
Peru	2.8	3.3	3.5	2.9	3.0
Venezuela	38	63	120	160	120
Latin America ex-Venezuela and Argentina	*3.7*	*4.1*	*5.4*	*4.4*	*3.3*

Central Bank Rate (end of year)

	2013	2014	2015	2016	2017
Argentina	14.50	29.50	--	--	--
Brazil	10.00	11.00	14.25	14.00	12.00
Chile	4.50	3.00	3.50	3.75	4.25
Colombia	3.25	4.50	5.75	6.00	5.50
Mexico	3.50	3.00	3.25	3.75	4.00
Peru	4.00	3.50	3.75	4.50	4.50
Venezuela	15.66	18.73	--	--	--
Latin America	*5.80*	*6.60*	*8.00*	*7.90*	*7.10*