The Vulnerability and Resiliency of Latam Countries to Global Shocks: The 2008-2009 Global Recession Case

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Note

In November 2009, Professor Morss taught a course at the University of Palermo Business School on the global recession. Students were required to write a paper on how an individual Latin American country had been affected by the Western banking collapse and the global recession. This paper summarizes the findings in those papers and goes further to analyze in more detail how the countries were affected by these two external shocks. Some results and data is not identical to the student's papers because we updated all the information.

We include the student's papers at the final of the background papers. Ecuador and Mexico cases were written by Diego H. Gauna and Elliott R. Morss.

Introduction

The global credit freeze and recession provide an excellent opportunity to test Latam countries for resiliency to external shocks. We selected eight Latam countries to study. They represent 92.3 % of the total GDP, 90.6 % of total Exports, 83.1 % of total population and 98.7 % of the Stock Market Capitalization of listed companies.

Country Background

As Table 1 shows, Brazil has by far the largest area, population, and GDP in Latin America. Mexico has the greatest population density and is also the largest exporter of the group.

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Table 1. – Data on Latin American Countries, 2008

Region	Population (in mil.)	Land Area (km^2)	Pop. Density	GDP (US$ bil.)
Brazil	191,971,506	8,514,877	23	1,333
Mexico	106,350,434	1,964,375	54	1,023
Colombia	44,534,000	1,141,748	39	208
Argentina	39,876,118	2,780,400	14	262
Peru	28,836,700	1,285,216	22	107
Venezuela	27,943,249	912,050	31	228
Chile	16,758,114	756,102	22	164
Ecuador	13,478,600	283,561	48	53

More information, including GDP growth rates, foreign direct investment, debt, global trust in government, sovereign interest spread, doing business rating, export dependency (on one or two commodities, on one or two primary importers), remittances, stock market importance, fiscal balance, trade balance) will be included in later sections where we attempt to explain differences in resiliency among countries.

Research Methodology

The global economy was recently subjected to two major shocks. The first was the Western banking collapse. This started in mid-2008 causing a global asset loss (stock market and real estate) in early 2009 of US$36 trillion. The resulting "wealth effect" led to a major reduction in global demand causing the second major shock – the global recession. In many part of the developed world, the recession continues, but there is evidence elsewhere that recoveries are underway.

The question to be addressed in this article is: what sort of impact did these two shocks have on the largest 8 Latam countries?

The timing of both shocks is known and data on their effects are available. The analytical model used is reflected in Table 2 where the major shocks and their effects are represented.

Table 2. – Shock Model

Event/Sector	Domestic Effects	Foreign Effects
Global Credit Freeze		
Financial Sector	No Asset Backed Securities Deposits Up	Letters of Credit Delayed
Government Policy	Interest Rates Down Reserves Increased	
Asset Loss		
Stock Market	Equities Sold	Equities Sold
Real Estate	New Investments Delayed	Capital Delayed
Wealth Effect/ Global Recession		
Government Policy	Consumption Down Investment Down Fiscal Stimulus	Exports Down Remittances Down
Overall Impact	GDP Trade Balances Government Deficit	Foreign Direct Investment
Recovery	Stock Market Real Estate Consumption Investment GDP Trade Balances Government Deficit	

1. Credit Freeze

a. Stock Market

Table 3 presents data on stock market losses for Latin American countries and the rest of the world. At one point, global markets had lost $36 trillion while Latam countries were

down $1.1 trillion. Latam countries have recovered far more rapidly than the rest of the world: Argentina,
Chile, Colombia and Mexico markets are now higher than they were at their peak before the credit freeze. In contrast, global markets are still down $17 trillion.

Table 3. – Stock Market Reaction

Index	Index High	Index Low	Hi-Low % Loss	Hi-Low $ Loss (US$ bil.)	Index April 2010	Hi-April 2010 % Gain. Loss (-)	Hi-April 2010 Gain, Loss (US$ bil.)
S&P Euro Index	1,858	728	-60.8%	-7,210	1,198	-35.50%	4,211
Nikkei 225 (Japan)	18,239	7,569	-58.5%	-2,590	11,339	-37.8%	1,675
S&P 500 (US)	1,558	683	-56.2%	-10,350	1,178	-24.4%	4,492
S&P Asia 200	6,749	3,145	-53.4%	-6,850	4,907	-27.3%	3,501
S&P Lat Am 40	59.51	21	-64.7%	-850	50	-16.6%	218
TSX (Canada)	14,984	7,591	-49.3%	-810	12,267	-18.1%	298
Argentina (Merval)	2,339	829	-64.6%	-22	2,450	4.7%	-2
Brazil (Bovespar)	73,516	29,435	-60.0%	-642	70,668	-3.9%	41
Chile (IPSA)	3,499	2,101	-39.9%	-149	3,835	9.6%	-36
Colombia (IGBC)	11,439	6,461	-43.5%	-62	12,198	-6.6%	-9
Mexico (Mexbol)	32,721	16,869	-48.4%	-227	33,600	-2.7%	-13
Peru (IGBVL)	23,790	6,054	-74.5%	-24	15,464	-35.0%	11
Venezuela (IBVC)	62,013	34,172	-44.9%	-4	58,361	-5.9%	1
Total 7 LA Countries				-1,130			-6
Total				-29,790			14,388
Total Adjusted*				-36,000			17,388

* Adjustment based on Bloomberg data.

For Latin American countries, did these asset losses have a significant wealth effect and cause consumption and investment to fall? That depends on who bore the losses. Table 4 provides one useful indication – the total stock market value as a percent of GDP.

Table 4. Stock Market Importance

Region	Stock Mkt. Cap % of GDP
Chile	130%
Brazil	103%
Peru	99%
Colombia	49%
Mexico	39%

Argentina	33%
Ecuador	9%
Venezuela	?

Source: World Bank

Taken at face value, the table suggests that any stock market fluctuation would have a greater impact in Chile than in Ecuador. However, this is not conclusive because it does not allow for foreign holdings of stock. For example, if a large portion of a country's equities are held by foreigners, stock market losses should not have a significant wealth effect domestically.

According to World Bank data, the net portfolio inflows to Latin America and the Caribbean totaled about US$53 billion in the 2005-2007 period. According to the World Federation of Exchanges, the total capitalization of the Latam stock markets we are examining was US$2.2 trillion at the end of 2007, falling to US$1.1 trillion a year later. This suggests that foreign holdings were quite insignificant as a per cent of the total.

b. Real Estate

The credit freeze, and resulting stock market losses in Western nations, resulted in large part from a sharp downturn in the real estate. It does not appear a similar downturn occurred in Latin America. Real estate data on prime office space is presented in Table 4.

Table 5. – Real Estate in Major Latam Cities

	Vacancy		**Lease Price Change**	**Sales Price Change**
City	**End 2008**	**end 2009**	**End 08 - 09**	**End 08 - 09**
Buenos Aires	6.4%	9.0%	-20.0%	no change
Caracas	1.0%	3.5%	6.0%	20.0%
Lima	1.9%	8.4%	no change	no change
Mexico City	4.0%	7.8%	-23.0%	no data
Rio de Janeiro	3.1%	3.7%	9.0%	no data
Santiago	1.0%	3.4%	no change	no change

Source: CB Richard Ellis (cbre.com)

Vacancy rates in all cities increased somewhat in 2009, but that was mostly the result of new space becoming available. Lease prices have fallen significantly in Both Buenos Aires and Mexico City, but even in those cities, there is considerable optimism. In short, Latin American countries are not suffering the massive real estate collapse that took place in Western nations.

c. Banking

Despite the Western banking collapse, there was no panic and little stress in the banking sectors of our countries. High international reserves and almost no exposure to Asset Backed Securities kept the crisis from spreading into our countries. Deposits increased as a result of the crisis with clients liquidating investments for cash.

2. Global Recession Effects - Overall Impact

In order to assess the effects of the global recession, we developed three indices for our countries:

- Vulnerability – how much did each GDP fall immediately as a result of the two external shocks;
- Resiliency – how much has the growth rate of each country recovered since the recession, and
- Volatility – taken together, how much did the growth rate fall and how much has it come back.

These indices are defined more precisely and provided for our countries in the following paragraphs.

Vulnerability

It is useful to have an overall measure of the external effects of global recession on our Latam countries. For this, we have developed a vulnerability index – how much did the recession cause the GDP growth rate to fall at first. More specifically, we define our Vulnerability Index (VulI) as the percent change in GDP due to the changes in exports, remittances and foreign direct investment caused by the global recession.

Exports

A significant portion of the shock effect was translated to Latam countries via a reduction in export demand. The effects of this reduction on Latam economies depended on the importance of exports in their economies. Data on this are presented in Table 6.

Table 6. – Export Reduction Effects of the Shocks in Real Terms

		Exports		GDP Effects	
Country	**Exports/GDP**	**2009**	**2010 est.**	**2009**	**2010**
Mexico	30%	-15.19%	9.6%	-4.58%	2.89%
Venezuela	18%	-12.88%	4.2%	-2.29%	0.75%
Ecuador	38%	-5.90%	4.8%	-2.26%	1.84%
Chile	40%	-5.60%	9.5%	-2.22%	3.76%
Colombia	19%	-8.16%	4.8%	-1.51%	0.89%
Brazil	14%	-10.28%	7.3%	-1.42%	1.01%
Argentina	13%	-6.41%	8.9%	-0.85%	1.18%
Peru	28%	-2.48%	4.7%	-0.68%	1.30%
World	29%	-14.4%	4.3%	-4.18%	1.25%

Source: Central Banks for each country and Prospects for the Global

Economy 2010, World Bank.

In the table, countries are ranked by the size of the negative impact on GDP in 2009. It is not surprising that the countries in which exports are most important were at the top of the list. In the cases of Venezuela and Chile, it is also noteworthy that a single commodity (Venezuela – oil, Chile – copper) dominated exports. There was a sharp reduction in Brazil's exports, but because exports are not important in Brazil relative to other Latam countries, the GDP effect was less.

It is also notable that most Latam countries were less affected by the shocks than the world overall. Only Mexico's exports fell more than the world overall. And the estimated export recovery in 2010 is better in all countries except Venezuela than for the world.

Besides size, it is important to analyze the export composition because a high dependence on single or limited number of commodities, such as oil and copper, increase the degree of vulnerability to the global recession. The following table shows the Export Concentration Index[3] for the year 2008:

Table 7. – Export Concentration Index

Country	2008
Brazil	9.02%
Argentina	14.54%
Mexico	15.34%
Colombia	20.07%
Peru	25.60%
Chile	39.10%
Ecuador	52.57%
Venezuela	85.73%

Source: UNCTAD.

Remittances

As can be seen by Table 8 remittance income, mostly from the US, is quite important to several Latam countries.

Table 8 . – Remittance Income as a Percent of GDP

Region	Remittances/GDP	Remittances 2008-2009 Change	GDP Effect
Ecuador	6.10%	-11.60%	-0.71%
Colombia	2.40%	-18.00%	-0.43%

[3] Expressed as Herfindahl-Hirschmann indices derived from three-digit SITC product categories. The Herfindahl-Hirschmann index is defined as the sum of squares of the percentages of the shares of each commodity as a proportion of total exports. Results are normalized and range from 0 (atomistic market) to 1 (maximum concentration).

Mexico	2.60%	-15.80%	-0.41%
Peru	2.10%	-4.17%	-0.09%
Argentina	0.30%	-12.50%	-0.04%
Venezuela	0.10%	-8.60%	-0.01%
Brazil	0.40%	1.80%	0.01%
Chile	0.00%	n.a.	0.00 %

Source: Remittances Watch, World Bank and the central banks of each country.

The table shows that the drop in remittances was higher in Colombia, although its effect over GDP is higher in Ecuador because of the importance of remittance income for the Ecuadorian economy.

Foreign Direct Investment

The following table includes estimates from ECLAC on net foreign direct investments (FDI) to Latam countries for both 2008 and 2009. As can be seen, the global recession caused FDI to fall in all of our countries except Peru and Brazil, countries whose prospects for growth are most favorable.

Table 9 . – Foreign Direct Investment (as % GDP)

Region	FDI/GDP	FDI 2009	GDP Effect
Brazil	1.70%	-42.41%	-0.72%
Chile	5.84%	-16.33%	-0.95%
Peru	3.16%	-31.25%	-0.99%
Mexico	2.01%	-50.73%	-1.02%
Venezuela*	0.29%	n.a.	-1.09%
Colombia	3.44%	-31.96%	-1.10%
Argentina	2.28%	-49.67%	-1.13%
Ecuador	1.82%	-68.83%	-1.25%

* Venezuela has been experiencing a net outflow of FDI. Consequently, for this table, we used the absolute change in FDI for this table.
Source: Foreign Direct Investment in Latin American and Caribbean, ECLAC, May 2010.

Total External Impact

Table 10 provides summary data on the external impact of the shocks based on the sections above, being the sum of each impact our vulnerability index.

Table 10. – Total External Impact

Country	Exports	Remittances	FDI	Vulnerability Index (VulI)
Mexico	-4.58%	-0.71%	-1.25%	-6.54%
Ecuador	-2.26%	-0.41%	-1.02%	-3.69%
Venezuela	-2.29%	-0.01%	-1.09%	-3.39%
Chile	-2.22%	0.00%	-0.95%	-3.17%

Brazil	-1.42%	0.01%	-1.10%	-2.51%
Colombia	-1.51%	-0.09%	-0.72%	-2.32%
Peru	-0.68%	-0.43%	-0.99%	-2.10%
Argentina	-0.85%	-0.04%	-1.13%	-2.02%

It appears that are our countries fall into three groupings:

- Mexico was extremely vulnerable to the external shocks;
- Venezuela, Ecuador y Chile were somewhat less vulnerable, and
- Brazil, Argentina, Peru and Colombia were least impacted by the shocks.

Resiliency

In addition to a Vulnerability Index, we developed a Resiliency Index (RI). The RI measures the extent to which a countries GDP growth rate returned to where it was prior to the recession. More specifically, it is defined as the forecasted growth rate for the 2010-2011 period as a percent of pre-recession growth rate defined above such that an Index of 100 would mean complete recovery.

Table 11. – GDP Resiliency Index (RI)

Country	Before Recession	After Recession	Resiliency Index
Chile	4.63	5.36	116
Mexico	4.23	4.26	101
Brazil	4.82	4.8	100
Ecuador	3.19	2.38	75
Peru	8.3	6.15	74
Colombia	7.24	3.13	43
Argentina	8.56	3.25	38
Venezuela	9.01	-1.14	-13

Source: Data from ECLAC and Central Banks for each country
Forecasts are from WEO, IMF, April, 2010.

Finally, we constructed a Volatility Index (VolI). We define VolI as simply the sum of the downturn and upturn GDP growth changes as presented in the following table.

Table 12. – GDP Volatility Index

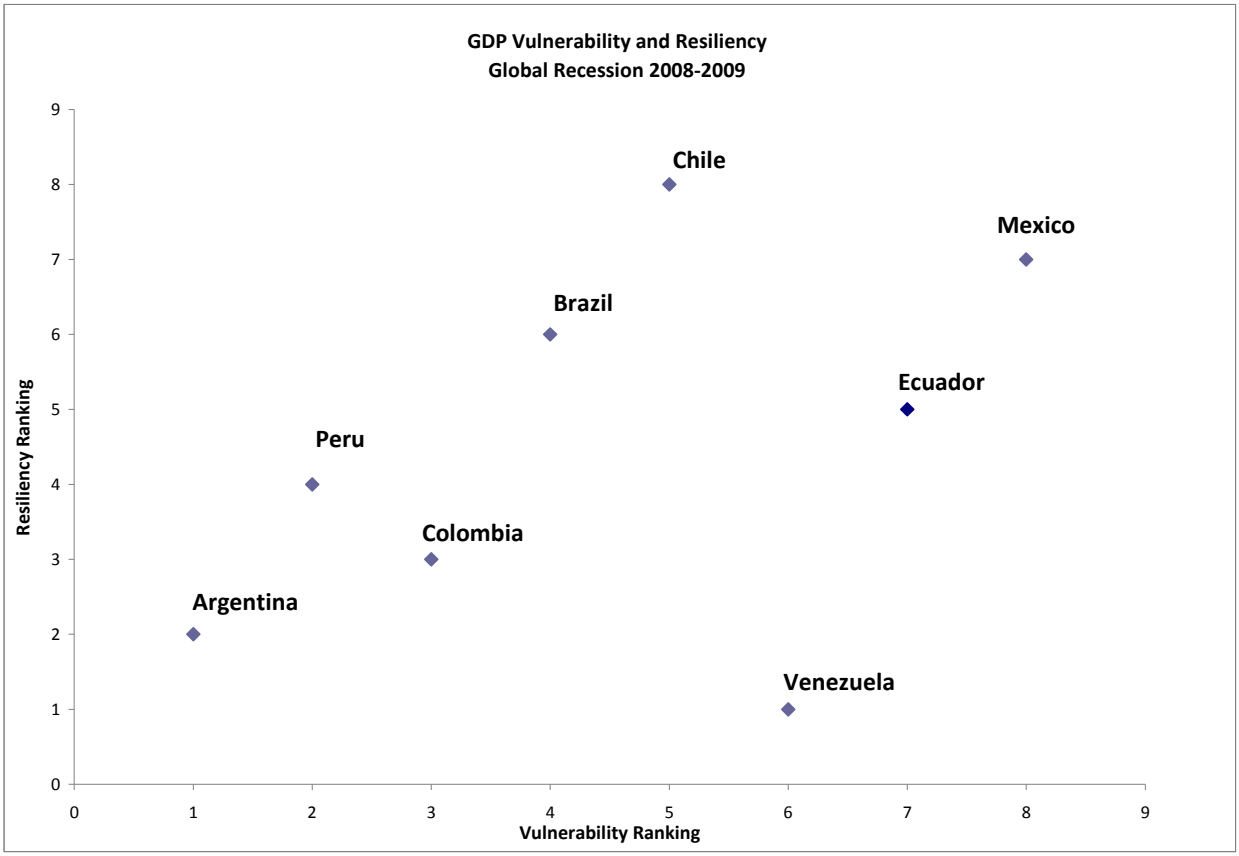
Country	Recession	Rebound	VolI
Ecuador	2.83	2.02	4.85
Colombia	6.88	2.77	9.65
Brazil	5.01	4.99	10.00
Argentina	7.66	2.35	10.01
Peru	7.44	5.29	12.73
Chile	6.13	6.86	12.99
Mexico	10.73	10.76	21.49
Venezuela	12.30	13.44	25.74

To analyze the relationship between vulnerability, resiliency and volatility, we ranked countries so that a "better" VulI, RI and VolI score would get a higher ranking, where better means low vulnerability, high resiliency, and low volatility. So, for example, Argentina gets an 8 ranking on VulI, Chile gets an 8 ranking on resiliency, and Ecuador gets an 8 ranking on volatility.

Table 13. – Rankings

Country	VulI	RI	VolI
Brazil	4	6	3
Colombia	3	3	2
Ecuador	7	5	1
Peru	2	4	5
Chile	5	8	6
Argentina	1	2	4
Mexico	8	7	7
Venezuela	6	1	8

Chart 1 – The Relationship Between Resiliency and Vulnerability



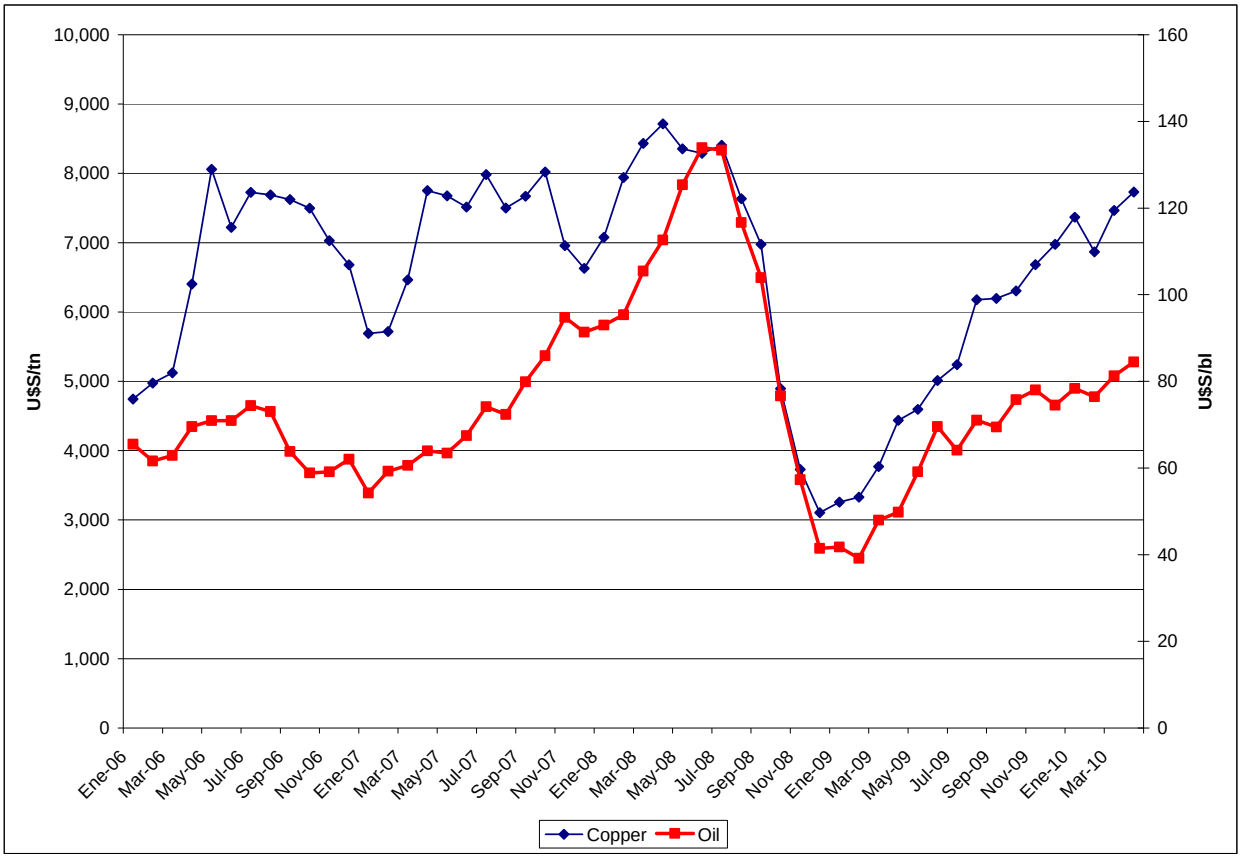
Venezuela is undoubtedly the country with the worst performance during the global recession. It has the sixth ranking in the Vulnerability Index and the lowest in the Resiliency Index.

There is no clear relationship between vulnerability and resiliency. However, one can see certain relationship between sub-groups:

- Peru, Colombia and Argentina as a group have low vulnerability and low resiliency;
- Ecuador and Mexico are relatively vulnerable with high resiliency;
- Venezuela is vulnerable with no resilience;
- Chile is highly vulnerable and the most resilient, and
- Brazil is in the middle in both rankings.

Ecuador, Mexico, and Chile depend strongly on commodity prices for exports. As a consequence, they were vulnerable because of the collapse in commodity prices at the onset of the global recession. Chile's rebound depended importantly on the quick recovery of the copper price. As Chart 2 illustrates, the copper price recovered more rapidly than the oil price. And that might explain why Chile has a higher resiliency score than Mexico or Ecuador.

Chart 2 – Oil and Copper Prices



Source: Chart based on IMF data.

Argentina, Peru and Colombia are not as dependent on exports and consequently had lower vulnerability and resiliency ratings.
In Brazil, there is an on-going domestic dynamic, just like there is in China. China's exports fell 34% in 2009. Exports are 37% of China's GDP which means the export decline should have caused a decline in china's GDP of 11.5% unless other dynamics were at work. In fact, China's GDP growth rate only fell from 9% in 2008 to 8.7% in 2009. The same probably holds for Brazil – that is, there is a powerful internal economic dynamic that keeps the country growing.

Government Policy Reactions to Shocks

The external shocks influenced the domestic economies of our countries in ways described above. But what did the governments of the countries do to mitigate these effects? In what follows, we describe what they did using exchange rate, monetary, and fiscal policies.

Prior to the external shocks, most of our countries were growing rapidly, and government policy was focused on containing excess aggregate demand and inflation.

Table 14. – Latam Countries' GDP Growth and Inflation

	GDP Growth		Inflation	
Country	2006	2007	2006	2007
Argentina	8.5	8.7	9.8	8.5
Brazil	4.0	6.1	3.1	4.5
Chile	4.6	4.6	2.6	7.8
Colombia	6.9	7.5	4.5	5.7
Ecuador	4.7	2.0	2.9	3.3
Mexico	4.9	3.3	4.1	3.8
Peru	7.7	8.9	1.1	3.9
Venezuela	9.9	8.2	17	22.5

Source: IMF, "Western Hemisphere Regional Outlook", May 2010

Governments were also concerned about the relationship between exchange rates and inflation, not wanting to put their exporters at a competitive disadvantage in capital markets.

a. Monetary Policy

The Western banking collapse and credit freeze changed everything. Most central banks immediately considered what they could do to insure that their banks did not fail. They relaxed restrictions on banks and offered them more liquidity. Whereas a number of central banks had been buying US dollars with their currency before the collapse, they reversed course and started selling dollars to help satisfy the dollar demand that panicked customers believed US dollars offered. Several countries arranged loans with the IMF. Colombia borrowed US$10.5 billion and Mexico US$47 billion from the IMF. Mexico already had in place a US$30 billion currency swap facility in place with the US government.

It is important to note that in Latin America that countries have different monetary policy approaches:

a. Brazil, Colombia, Chile, Peru and Mexico follow explicit inflation-targeting regimes, in line with most of the developed countries.
b. Argentina and Venezuela have central banks with weak autonomy, leaving the room for uncontrolled expansion in monetary aggregates. They do not have inflation targets.
c. Ecuador uses the US dollar as its currency, so there is no room for monetary policy.

Inflation-targeting involves setting a target inflation rate and having the monetary authority focus its policies on not allowing inflation to exceed or fall much below the target rate.

Table 15 shows the evolution of the monetary policy in our countries:

Table 15. – Interest Rates for Monetary Policy

Country	Interest Reference Pre-Recession*	Last Interest Reference Rate (May 2010)	Change in Policy Rate
Chile	8.25%	0.50%	-7.70%
Colombia	9.50%	3.00%	-6.50%
Peru	6.50%	1.25%	-5.25%
Brazil	13.75%	9.50%	-4.25%
Mexico	8.25%	4.50%	-3.75%

Source: Central Banks for each country. * At the end of 2008.

It is clear from the table that our countries used interest rate policy aggressively to counter the global recession. The difference in policy between these 5 countries as compared with Argentina and Venezuela is notable. These 5 countries relaxed monetary policy and it had no effect on the inflation rate. On the other hand, Argentina and Venezuela have inflation rates above 20 %, mainly because of the uncontrolled increase in monetary aggregates. While neither country uses interest rates as a monetary policy instrument, rates also dropped in these countries following the onset of the recession. In Argentina, the overnight interest rate fell from more than 11% at the end of 2008 to 9% in May 2009. Venezuela has almost no operations in the interbank system, but there is some evidence to suggest a fall in rates as well.

Table 16. – Inflation Targets in Latam Countries

Country	Inflation Target	Target Range	Actual Inflation 2008	Actual Inflation 2009
Brazil	4.5 %	2.5-6.5 %	5.9 %	4.3 %
Chile	3.0 %	2-4 %	8.7 %	1.5 %
Colombia	3.0 %	2-4 %	7.0 %	4.2 %
Peru	2.0 %	1-3 %	6.7 %	0.2 %
Mexico	3.0%	2-4%	6.5%	3.6%
Argentina*	None	None	7.2 %	6.5 %
Venezuela	None	None	31.9 %	28.9 %

Source: Central Banks for each country and ECLAC.
* Inflation Statistics in Argentina are questioned by outside observers. Some estimate inflation above 20 % in 2008 and 2009.

b. Fiscal Policy

As the world moved from a banking crisis into a global recession and the external effects described above started to be felt, governments initiated a wide variety of programs to stimulate their economies. It is very difficult to quantify the effects of these policies, but a rough approximation can be gained by examining data from various sources.

It would be valuable to have some idea of the quantitative impact of the government stimulus packages. However, such estimates are difficult to make because of the wide variety of elements included in the packages.

However, the International Labor Organization did a study of stimulus packages and included 4 of our countries: Argentina, Brazil, Chile, and Mexico. Also, LatinFocus reported that Peru's stimulus package amounted to 3.2% of GDP. These packages will impact the economies over the 2009-2010 period. It does not appear that either Colombia or Venezuela has developed a stimulus package, and Ecuador is limited in what it can do because it uses the US dollar as its currency.

Table. 17 - Stimulus Packages as Percent GDP

Mexico	4.7%
Argentina	3.9%
Peru	3.2%
Chile	2.3%
Brazil	0.2%

Source: ILO http://www.ilo.org/public/english/bureau/inst/publications/discussion/dp19609.pdf and LatinFocus

It is unknown how good the these estimates of stimulus packages actually are, so it is worth looking at changes in overall government budgets for another indicator of fiscal efforts to mitigate the global depression. In Table 18, the primary balance of the public sector of our countries is presented.

Table 18. – Primary Sector Balances

	Public Sector Primary Balance (% GDP)					**Balance Change**
Country	**2006**	**2007**	**2008**	**2009**	**2010 (est.)**	**2008-2009**
Chile	8.5	9.5	5.8	-3.9	-1.4	9.7
Peru	4.1	4.9	3.7	-0.7	-0.2	4.4
Venezuela	0.5	-1.2	-1.2	-4.4	3.0	3.2
Ecuador	5.8	4.1	0.4	-2.8	-2.9	3.2
Mexico	1.8	1.3	1.1	-2.0	-0.8	3.1
Colombia	2.9	3.2	3.2	0.6	-0.1	2.6

Argentina	4.0	2.4	2.7	0.2	-0.8	2.5
Brazil	3.2	3.4	4.0	2.1	3.3	1.9

Source: IMF, "Western Hemisphere Regional Outlook", May 2010

The final column represents the change in the balance between 2008 to 2009. This column provides another estimate of the net stimulus impact of our governments. Unfortunately, these changes include revenue drops that probably had little or no stimulatory impact. Consider Chile as an example. Much of its 9.7% change results from a drop in copper revenues, and it is highly unlikely that these reductions had the same stimulatory impact that a reduction in individual income tax rates would have had. In light of these problems on the revenue side, we examine changes in government expenditures only below.

Table 19.- Changes in Government Expenditures

	Public Sector Primary Expenditure (% GDP)					**Expenditure Change**
Country	**2006**	**2007**	**2008**	**2009**	**2010 (est.)**	**2008-2009**
Chile	19.2	19.9	22.6	26.0	25.5	3.4
Colombia	24.3	24.1	23.0	26.4	24.8	3.4
Argentina	25.9	29.1	30.6	33.8	34.6	3.2
Mexico	19.6	20.1	21.8	24.4	22.5	2.6
Brazil	32.8	32.3	32.5	34.2	33.3	1.7
Peru	21.3	20.9	22.9	24.4	24.4	1.5
Ecuador	21.6	24.8	33.0	32.8	34.2	-0.2
Venezuela	36.9	34.2	31.9	30.3	33.6	-1.6

Source: IMF, "Western Hemisphere Regional Outlook", May 2010

We conclude that these figures provide a good approximation of the fiscal stimulus packages developed by the governments of our countries. Ecuador, because it uses the US$ as its currency, could not afford a stimulus package, while the Venezuelan government did not launch a stimulus package. It is notable that although the Colombian government did not announce a stimulus package, its expenditure increase effectively provides as significant a stimulus as in any of our countries.

In Table 20, we present a comparison of the total external impact with the government stimulus from the table above.

Table 20. – External Shocks and Government Stimulus

Country	**External Impact**	**Government Stimulus**	**Net**
Mexico	-6.54%	2.60%	-3.94%
Ecuador	-3.69%	0.20%	-3.49%
Venezuela	-3.39%	1.60%	-1.79%
Brazil	-2.51%	1.70%	-0.81%
Peru	-2.10%	1.50%	-0.60%
Chile	-3.17%	3.40%	0.23%
Colombia	-2.32%	3.40%	1.08%
Argentina	-2.02%	3.20%	1.18%

It should be noted that a lower Net should not necessarily be taken as a measure of the appropriateness of the government's policy. The Mexican government probably anticipated a rebound in commodity prices and consequently did not want to provide an excessive stimulus. Ecuador could not afford a larger stimulus. The government of Venezuela appeared oblivious to the global recession. The governments of Brazil, Peru, and Chile provided stimulus packages close to what was needed. In both Argentina and Chile, important elections were being held which might have contributed to the large stimulus efforts.

c. Exchange Rate Policy

Exchange rates are extremely important in Latin America, and as Table 20 shows, most Latam currencies increased in value relative to the US dollar in years preceding the global recession. In fact, during this period, most Latam currencies had gained so much value relative to the US dollar that central banks were buying US dollars to mitigate the effect of their stronger currencies on the competitive position of their exporters.

In the panic that immediately followed the credit freeze, everyone wanted US dollars, and so all Latam currencies fell in value from the end of 2007 to the end of 2008, with the currencies of Brazil and Chile losing the most. To counter these declines, the governments of several of our countries started buying their own currencies with dollars. During 2009, the currencies of all countries with flexible exchange rates strengthened with the exception of Argentina. Peru's currency is now worth more than it was before the credit freeze. In early 2010, Venezuela devalued its currency by 100% relative to the US dollar. The Argentine and Venezuelan currencies are the only ones that continue to lose value, although, due to the high-inflation environment in both countries (above 20 % annually), it is probable that their currencies are appreciating in real terms.

Table 21. – Latam Exchange Rates vs. US$ (end of period)

	Percent Change		
Country	**2005-2007**	**2007-2008**	**2008-2009**
Brazil	24.4%	-32.2%	25.6%
Chile	3.5%	-26.8%	19.6%
Colombia	11.8%	-11.4%	8.8%
Peru	10.2%	-4.7%	8.0%
Mexico	-2.7%	-26.6%	5.4%
Ecuador*	0.0%	0.0%	0.0%
Venezuela**	-53.6%	4.5%	-14.0%
Argentina	-4.0%	-9.5%	-10.1%

Source: LatinFocus. *Ecuador uses the US$ as its currency.
** Market Estimation of Black Market Exchange Rate from www.controldecambios.com .

The official exchange rate for the Venezuelan currency was fixed at 2.15 Bolivars per US dollar in the 2005 – 2008 period. In March 2010, the official rate was devalued to 4.30 Bolivars per dollar. The actual market value of the Bolivar is much lower. For example,

today's estimate is 8.10 Bolivars per US dollar. In Table 21, we use an estimate of the black market rate.

A significant portion of the changing currency values reflects foreign confidence or lack of confidence in a country's policies. One indicator of confidence is the interest spread between the interest rate at which a country can borrow in international markets relative to the US Treasury borrowing rate.

Table 22 provides this data for our countries as of March 2010.

Table 22. – Interest Spreads for Latam Countries, February 2010

Country	Spread (bps)
Chile	132
Peru	179
Mexico	196
Colombia	211
Brazil	212
Argentina	806
Ecuador*	822
Venezuela	989

LatinFocus, March 2010

External Shocks, Government Policy Reactions, and Overall Country Growth

In Table 23, countries are ranked in accordance with how the economies actually performed relative to the external shock and the government's policy response. A negative number in the final column means actual performance was worse than what had been predicted by the shock and policy response. A positive difference would mean the internal dynamic of overall economy was more powerful than the combined effect of the recession and the government's counterpolicy.

Table 23. – Exogenous Shocks and Actual GDP Change

Country	External Impact	Government Stimulus	Net	Actual GDP Change	Difference
Mexico	-6.54%	2.60%	-3.94%	-6.50%	-2.56%
Chile	-3.17%	3.40%	0.23%	-1.50%	-1.73%
Venezuela	-3.39%	1.60%	-1.79%	-3.29%	-1.50%
Colombia	-2.32%	3.40%	1.08%	0.36%	-0.72%
Argentina	-2.02%	3.20%	1.18%	0.90%	-0.28%
Brazil	-2.51%	1.70%	-0.81%	-0.19%	0.62%
Peru	-2.10%	1.50%	-0.60%	0.86%	1.46%

Ecuador	-3.69%	0.20%	-3.49%	0.36%	3.13%

For five of our countries, this was not the case: GDP growth was actually less than we predicted. What can explain the differences? Several things:

- The total external impact/policy responses are in Keynesian terms, the "first round impacts"; actual changes in GDP will include effects from "later rounds".
- For our bigger countries, like Brazil, there is an on-going domestic dynamic, just like there is in China. China's exports fell 17% in 2009; exports are 37% of china's GDP which means the export decline should have caused a decline in China's GDP of 6.3%. In fact, China's GDP growth rate only fell from 9% in 2008 to 8.7% in 2009! The same probably holds for Brazil – that is, there is a powerful internal economic dynamic that keeps the country growing.
- The magnitude of the domestic market and the management of the exchange rate policy also need to be emphasized. With a large internal market, the economy can substitute local production for imports if the local currency weakens. With a negative shock and a flexible exchange rate, the local currency will lose value, thereby stimulating exports and reducing imports, adjusting the current account. But with a fixed exchange rate, all the adjustment has to be done via a reserve decrease or with a sharp adjustment in the local economy.

The Ecuador case is quite surprising. It has a small internal market and uses the US dollar as its currency. Here, the external impact should be greater. The dollar increased in value during the crisis which means imports became cheaper from neighboring countries while at the same time its exports became more expensive to neighbors.

Conclusions

Our major conclusions from this exercise are presented below.

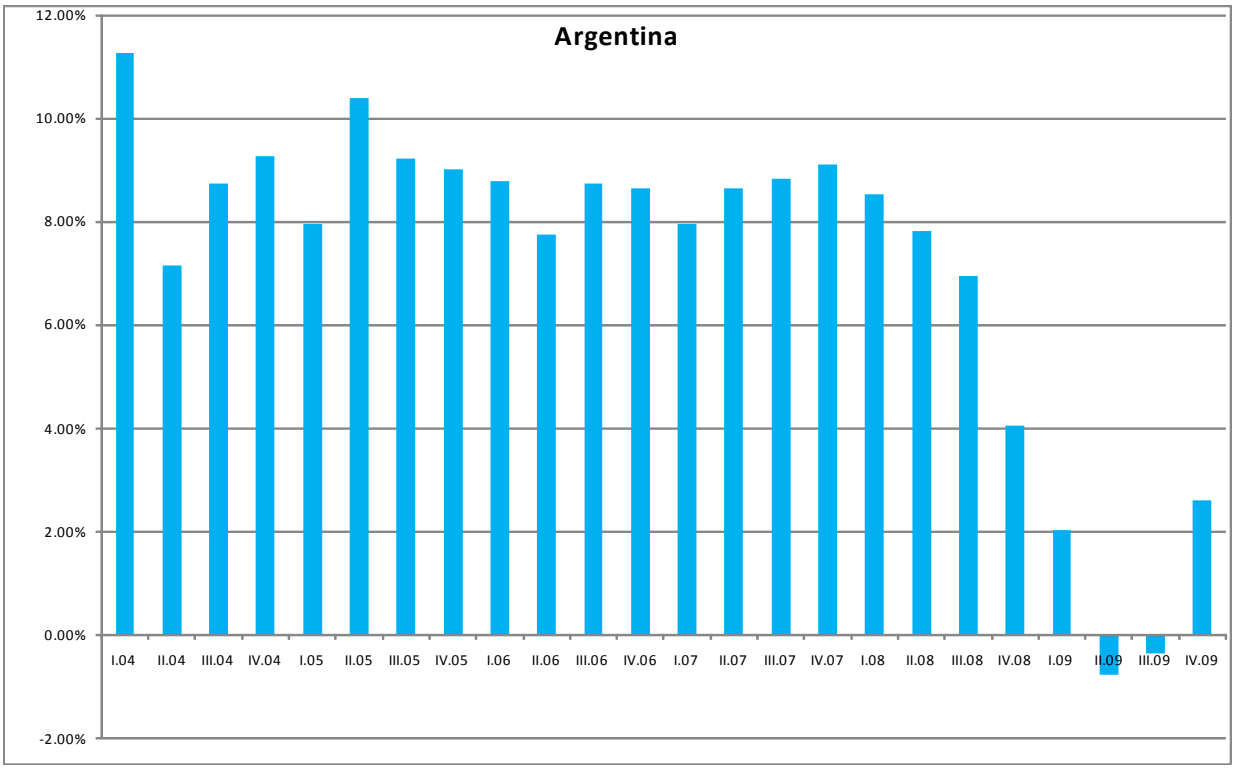
- The stock markets of Latam countries sold off as sharply as Western markets at the outset of the crisis. However, in most cases, they have recovered far more rapidly than is true for other regions.
- The real estate markets in Latin America have shown very little weakness following the real estate collapse in Western nations. This could be due to the role of "safe investment" that families in Latam countries assign to real estate and the low percentage of families that have debt mortgages.
- Despite urgings from Western banks and academics[4] to increase leverage and risk, the Latam banks have pursued more conservative courses and have shown little stress during the financial crisis. The banks did not hold or trade a significant amount asset backed securities (ABS).

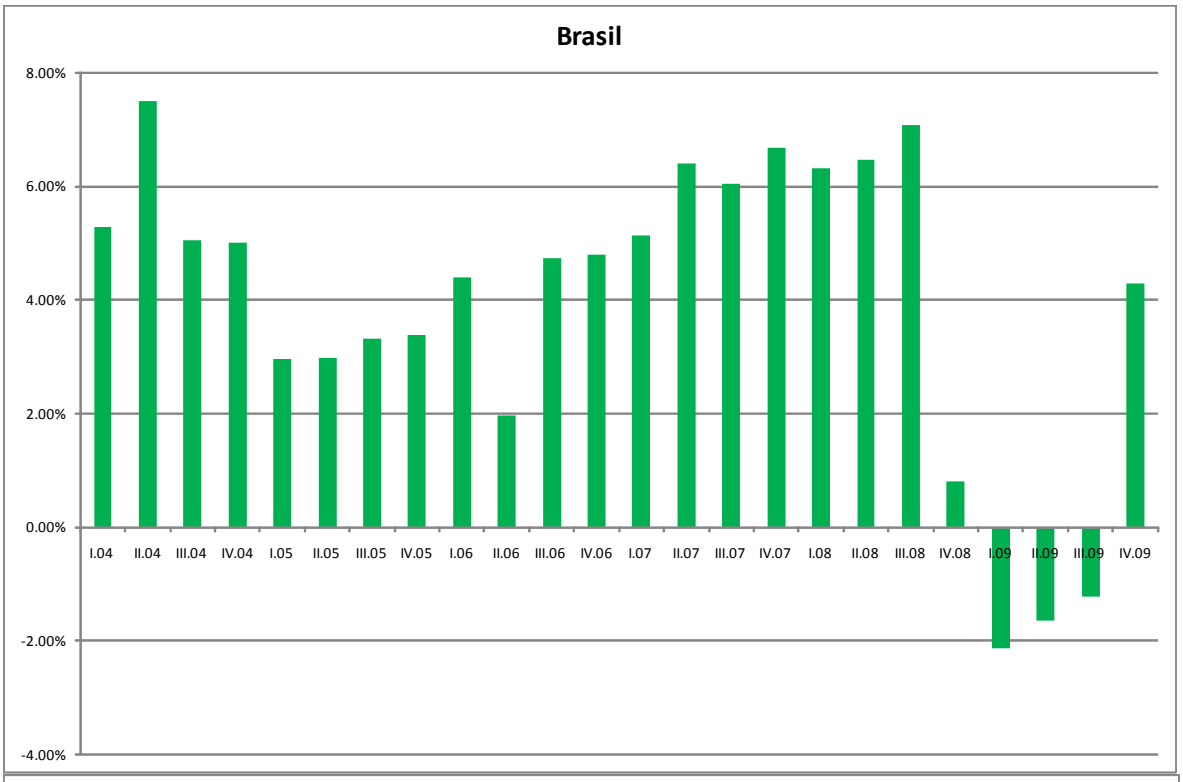
[4] Paul L. Freedman and Reid W. Click, "Banks That Don't Lend? Unlocking Credit to Spur Growth in Developing Countries", Development Policy Review, 2006, vol. 24, issue 3, pages 279-302

- The global recession impacted our countries primarily through three external sector paths – exports, remittances, and foreign direct investment, with the fall in exports being the single most important source.
- Countries with exports dominated by one commodity (copper or oil) were initially hardest hit – however, the prices of both commodities recovered rapidly so the exports of these countries have recovered.
- Countries where exports were less important or where exports were not concentrated in a few items showed less vulnerability and volatility, *e.g.*, Brazil.
- All our countries except for Ecuador and Venezuela used monetary and fiscal policies to counter the global recession. Ecuador could not afford a stimulus package while the impetus behind Venezuela's policies is unclear.
- Central banks with inflation-targeting policies are already considering interest rate increases in the belief that the recession is over. For example, Brazil raised interest rates last week.
- Credit spreads have recently fallen for all our countries except Argentina and Venezuela. The high spreads in these two countries reflect international misgivings over government policies.
- All of our countries with the exception of Venezuela will show positive GDP growth in 2010, but projected growth rates will be far below those registered before the global recession hit. This could in some way be a blessing inasmuch as growth rates for most of our countries in the 2006 – 2007 period were probably not sustainable.

DATA APPENDIX

QUARTERLY EVOLUTION OF REAL GDP BY COUNTRY BASED ON CENTRAL BANK DATA FOR EACH COUNTRY.

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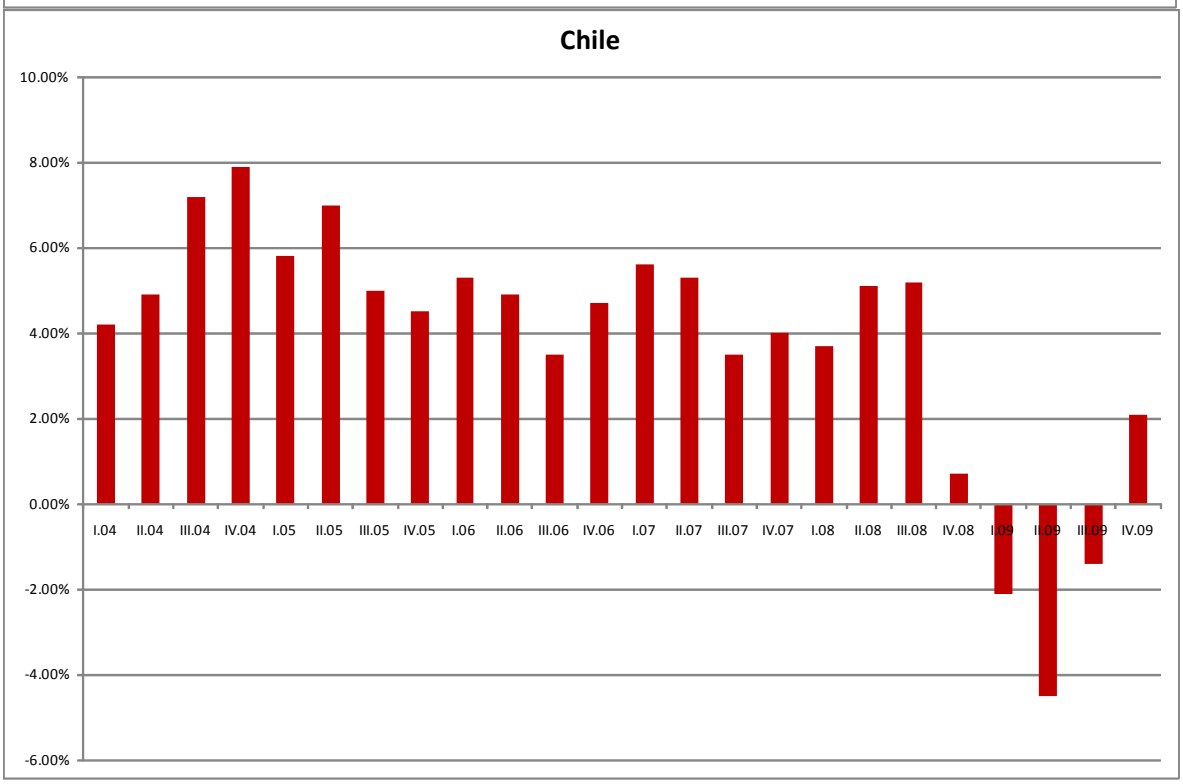
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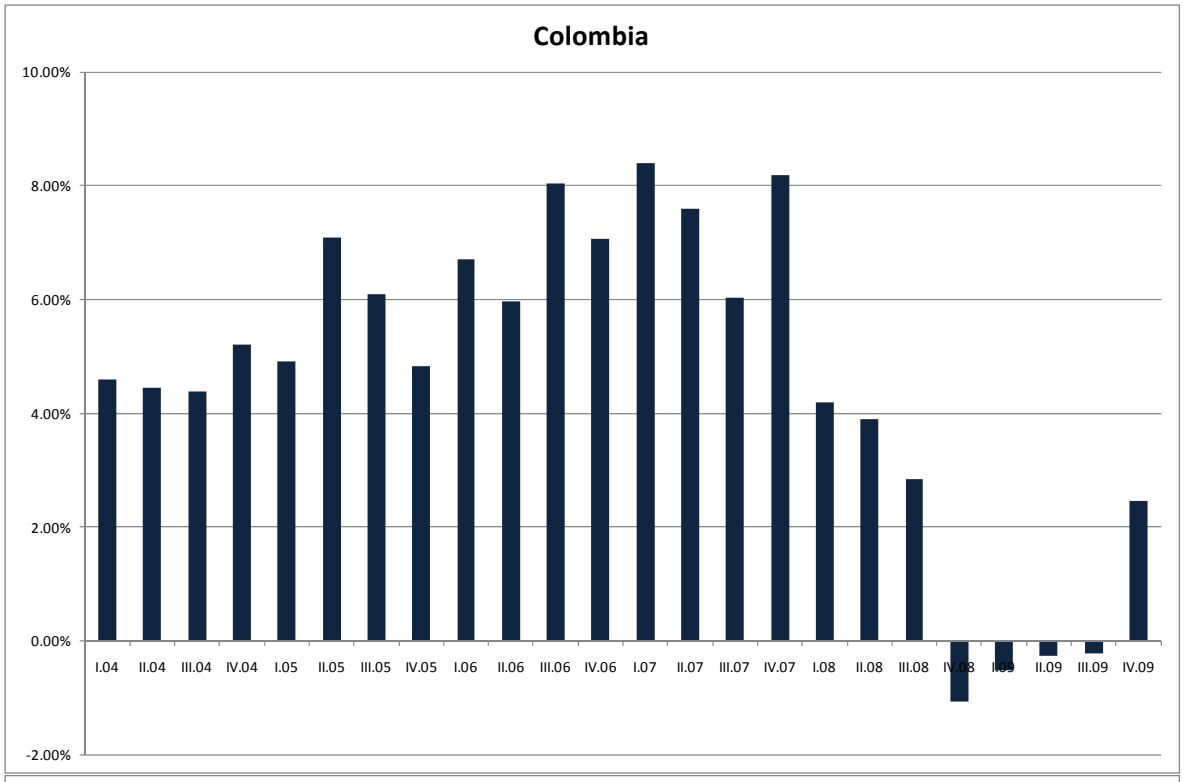
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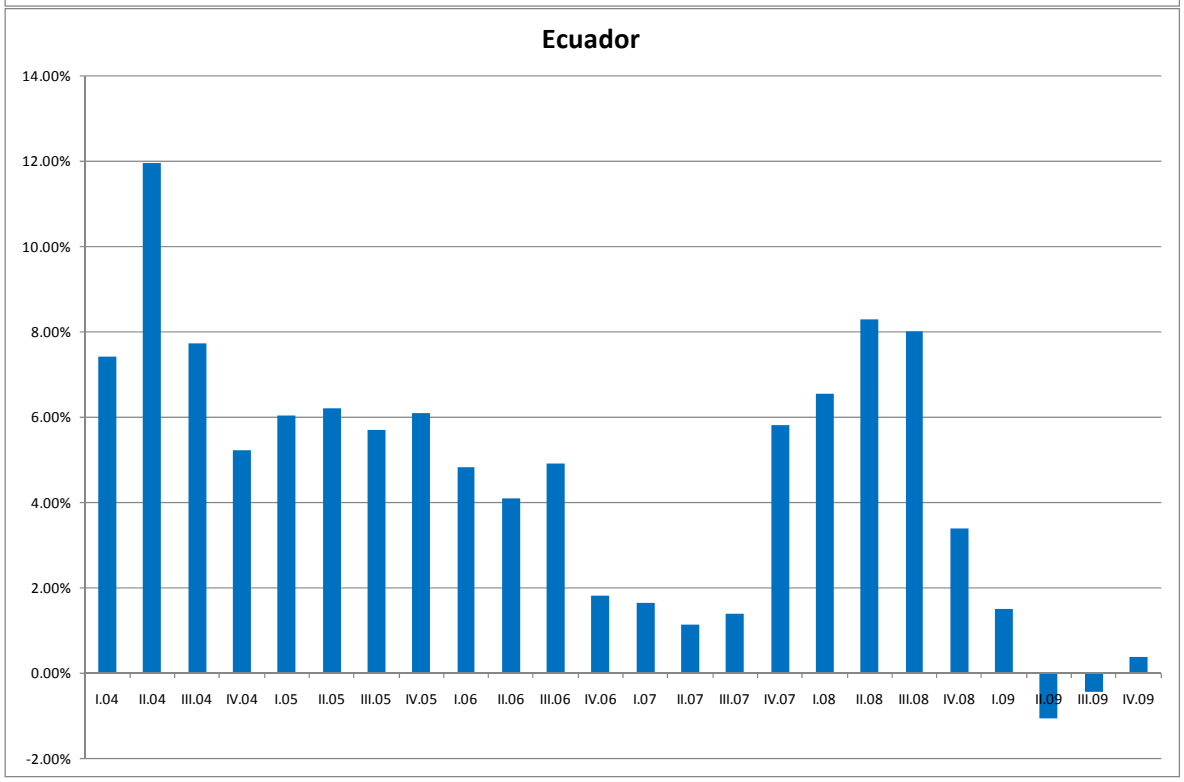
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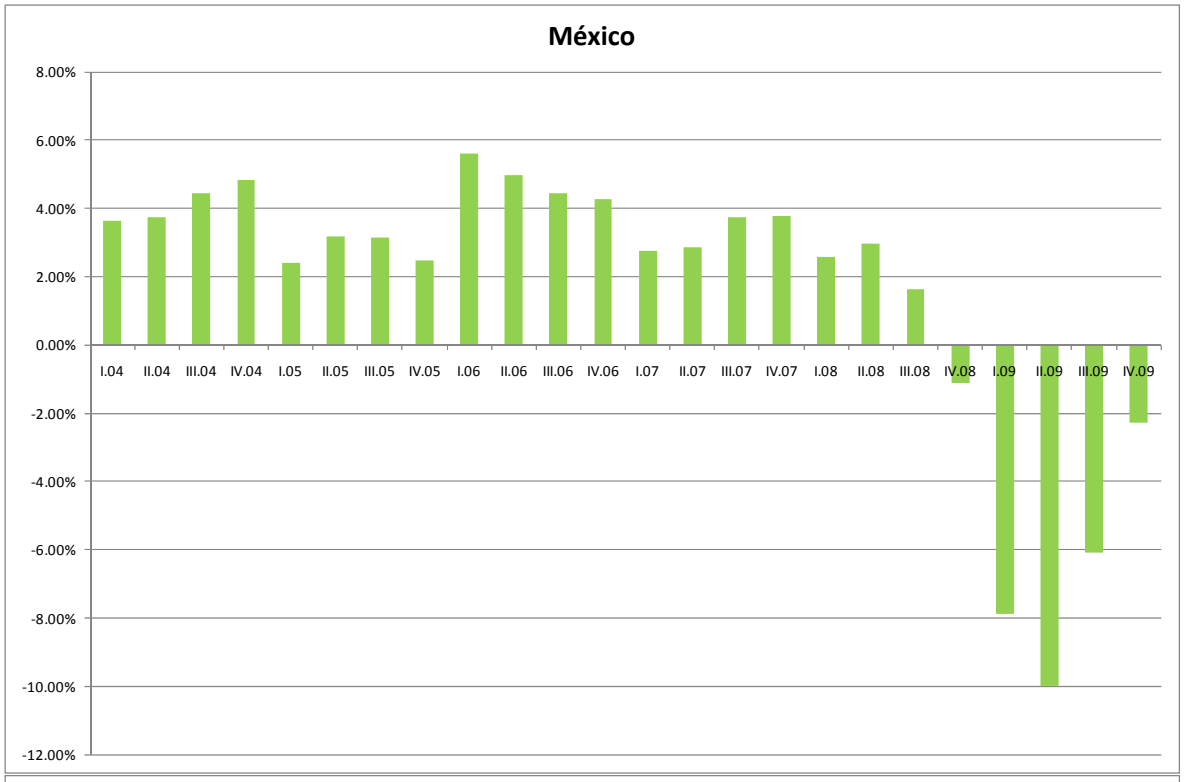
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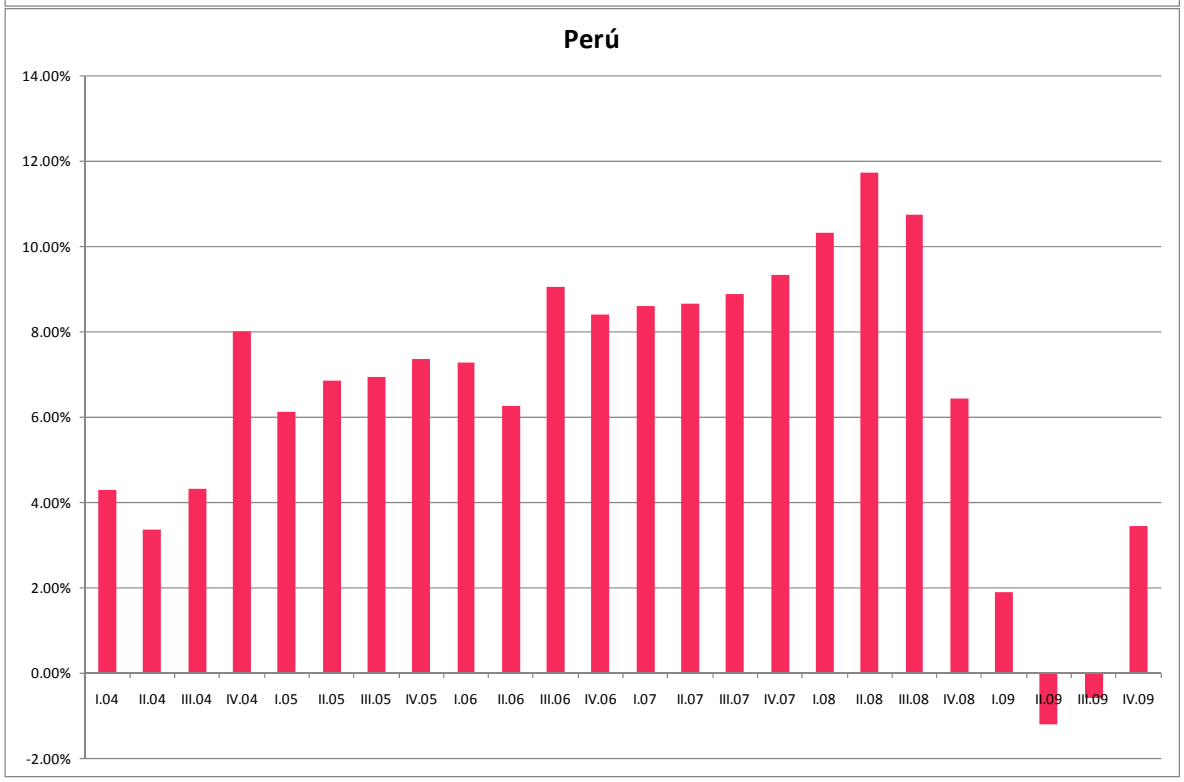
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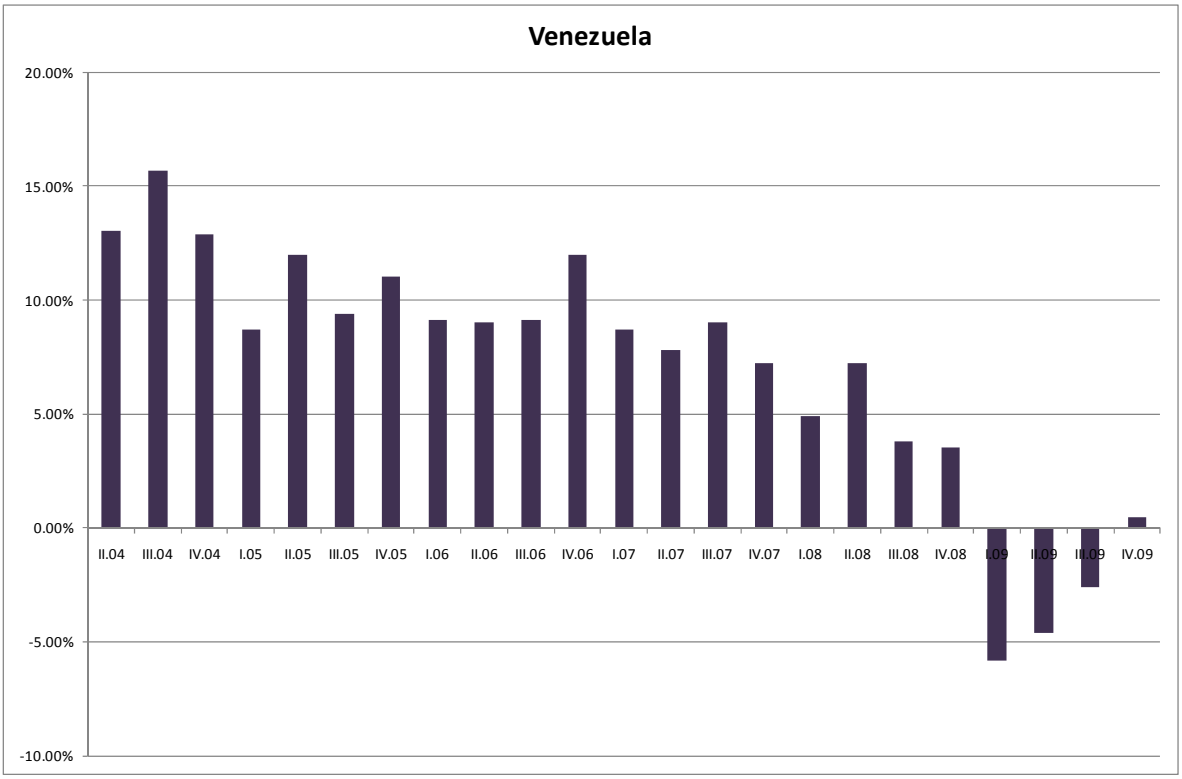
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Argentina: Effects of Global Recession and Future Prospects

by Marcela Gonzalez[5] and Elliott Morss

Executive Summary

The credit freeze had little impact in Argentina. While the stock market fell 65% resulting in asset loss of US$22 billion, that loss has almost been erased with the market down less than 1% from its earlier highs. But the reduction in export demand resulting from the global recession has had a greater impact. In 2009, investment is expected to fall 12% with consumption lower as well. Unemployment in 2009 will approach 10% by the end of the year. 2010 looks better, with most forecasts predicting GDP growth of 2%.

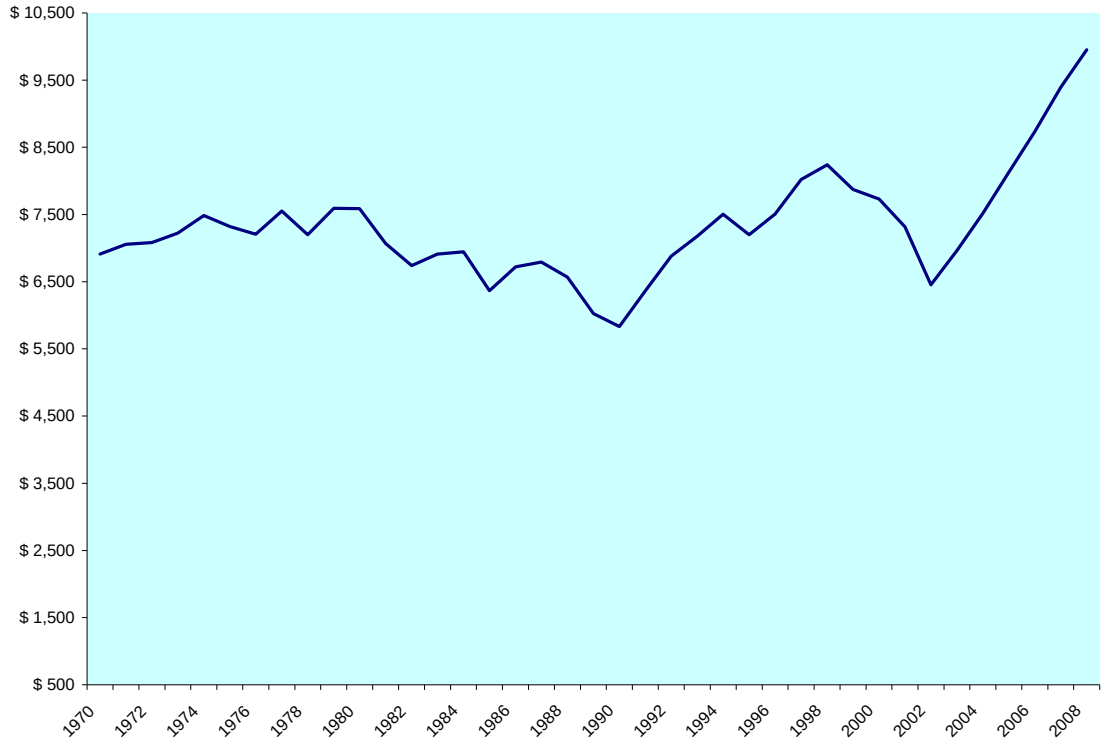
Introduction

Argentina is one of the most paradoxical countries in Latin America. Its GDP per capita was slightly above US$ 8,000 in 2008 current dollars, standing fourth in South America, and its Human Development Index was the second of the region. However, Argentina is a country with a high level of poverty, informal unemployment and corruption. Argentina ranks 106th in the world (low rankings mean low corruption), which is high by global standards and third only to Ecuador (Perception Index, third only to Ecuador (146) and Venezuela (162) in Latin America.

Argentina's growth was disappointing in 1980-2002. Hyperinflation in the 'eighties and massive unemployment and bank panic in the 'nineties were the consequences of bad policies and political instability. Since 2002, the Argentine economy has been steadily growing. From 2003 to 2008, the annual rate of growth of the GDP per capita, in constant terms, was 7.4 %. The following graph shows the evolution of GDP per capita since 1970.

[5] MBA student, University of Palermo.

Graph 1: The Evolution of Real GDP Per Capita in Argentina (1970-2008)



Source: CEPAL (2009)

Argentina's growth in 2003-2008 was driven by high commodities prices, especially agricultural commodities. The consequence has been that Argentine exports have almost 80 % since 2003. The main challenge for Argentina is growing inflation, which private analysts estimate at about 30% for the year 2010.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. The world lost $36 trillion in stock market losses directly following the credit freeze. Globally, markets have recovered cutting stock losses to $22 trillion. Latin American stock markets have recovered dramatically. And after being down 40% for a loss of $22 billion, the Argentine market is now less than 1%.

Impact of Declining Global Demand

Argentine exports have been adversely hit by the global recession. They are down 26.8% in the first 3 quarters of 2009 as compared with the same period in 2008.

Table 1. – Argentina Export Performance

	First 9 Months 2008	**First 9 Months 2009**	**First 9 Months 2008-2009 % Change**
Total Exports	54.8	41.1	-26.7%
Primary Products	13.7	7.3	-47.0%
Processed Agriculture	18.5	16.2	-12.0%
Manufacturing	16.3	13.3	-13.3%
Energy	6.3	4.3	-31.0%

Sources: http://www.bcra.gov.ar, http://www.indec.gov.ar/

A more complete understanding of export performance can be obtained from Table 2.

Table 2. Export Performance

Selected Exports	**Ten Months**		**Absolute Difference**	**% Change**
	US$ mil.			
	2008*	**2009[e]**		
Total Exports	**60,971**	**45,965**	**-15,006**	**-24.6%**
Planted Products	**22,597**	**14,679**	**-7,918**	**-35.0%**
Soy Flour	6,099	7,028	929	15.2%
Soybean Oil	4,231	2,739	-1,492	-35.3%
Soy Derivatives	4,381	1,674	-2,707	-61.8%
Wheat Flour	389	261	-128	-32.9%
Maize	3,263	1,220	-2,043	-62.6%
Wheat	2,228	789	-1,439	-64.6%
Barley	237	136	-101	-42.6%
Sunflower Oil	1,322	606	-716	-54.2%
Sunflower Seed	59	83	24	40.7%
Lemons	388	143	-245	-63.1%
Meat	**1,170**	**1,250**	**80**	**6.8%**

Wine	**431**	**470**	**39**	**9.0%**
Other Agriculture	**937**	**547**	**-390**	**-41.6%**
Fertilizers	379	186	-193	-50.9%
Leather	558	361	-197	-35.3%
Gold	**610**	**738**	**128**	**21.0%**
Vehicles and Parts	**4,473**	**3,659**	**-814**	**-18.2%**
Autos	2,414	2,156	-258	-10.7%
Trucks	1,551	1,131	-420	-27.1%
Gear Boxes	508	372	-136	-26.8%
Fuels	**5,474**	**3,987**	**-1,487**	**-27.2%**
Metals	**1,837**	**1,487**	**-350**	**-27.2%**
Steel Pipes	1,107	856	-251	-22.7%
Raw Aluminum	523	389	-134	-25.6%
Iron Products	207	242	35	16.9%
All Other	**23,442**	**19,148**	**-4,294**	**-18.3%**

Source : INDEC

As can be seen from this Table, all major exports fell sharply in the first ten months of 2009. Only meat, wine and gold increased over this period.

The Domestic Economy

Consumption growth slowed by 6.3% in the last quarter of 2008 and first quarter 2009 when compared to the same period in the earlier years. Consumption is expected to fall by 1.4% for all of 2009. Investment is down by 11.5% in the last quarter of 2008 and first quarter 2009 when compared to the same period in the earlier years. Investment is expected to decline by 11.6% for the entire year. It is estimated that the unemployment rate will increase to 9.9% in 2009 from 7.3% in 2008.

External Sector

As Table 3 indicates, Argentina's trade balance remains strong, even with the fall in exports. International reserves have fallen a bit, but they are still quite adequate.

Table 3. – External Sector (in millions of US$)

Item	**2007**	**2008**	**2009 Est**
Trade Balance (US$ billion)	11.1	12.7	13.6
Exports (US$ billion)	55.8	70.1	54.1
Imports (US$ billion)	44.7	57.4	40.5
International Reserves (US$ billion)	46.2	46.4	43.4
Total External Debt (US$ billion)	124.6	124.7	122.8
Total External Debt (% GDP)	47.8	37.9	51.1
Current Account Balance (US$ billion)	7.1	7.0	7.1

Source: LatinFocus

The country's primary problem here concerns its 2001 default. After defaulting on $95 billion of debt, holders of approximately $75 billion settled in 2005 at 35 cents on the dollar. Argentina has had on and off talks to settle up on the remaining $20 billion, but there is nothing definitive yet. Since then, the country has relied on local markets (it sold $8.5 billion of bonds in the local market) and loans from Venezuela ($7.6 billion) to meet financing needs. Last year, it seized about $24 billion in pension assets possibly to compensate for falling tax revenues.

Could Argentina afford to pay off its international debts? At 35 cents on the dollar, it would cost $7 billion. In addition, it has approximately $ billion in debt coming due this year. The country is estimated to have over $40 billion in international reserves. It is not clear whether the creditors who refused 35 cents on the dollar earlier would accept it now. Some estimate that 75% of the defaulted debt holders will. Settling this debt would allow Argentina to borrow again in international markets where it would probably have to pay less than the 15% charged by Venezuela now. It is reported that the government is at least talking to the IMF.

Government Policy More Generally

It appears that for some time, the country has not had a sound economic strategy. Instead, everything appears to be happening on an *ad hoc basis*. Argentina has some excellent economists. It is too bad one or more of them is not in a position of power. The country needs "a steady hand on the tiller".

There is talk of corruption. Corruption exists everywhere. If it is predictable, businessmen will build it in as a cost of doing business. Unpredictability is another matter: if you don't know whether your company or pension funds will be seized, you try to keep your assets out of the country. Unpredictability is in part the reason the country´s EMBI spread against the US Treasury rate approaches the spreads of Ecuador and Venezuela.

Looking Ahead

Does any of that really matter? Probably not. Like Russia, Argentina is a natural resource rich country. And a lot of its exports are food. The global population is growing and it has to have food. Argentina now exports more wine than Australia - see http://www.morssglobalfinance.com/the-global-economics-of-wine-past-present-and-future/.

The size and role of government will probably continue to grow (it has grown from 20% of GDP in 2002 to more than 30% now). And political power grabs will probably continue.

At least the first quarter of the 21st Century will be good to natural resource rich countries. And it is hard to imagine things will be bad in Argentina in the long run.
Its exports will rebound.

For the short run, consider first the projections made by World Bank. World GDP is expected to fall 2.9% in 2009 and increase 2.0% in 2010. That means Global GDP will not get back to 2008 levels until 2011. Latin America overall will fall somewhat less in 2009 before increasing 2% in 2010.

Table 4. - World Bank Global GDP Growth Estimates

Region	2007	2008	2009	2010
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
Developing Countries	8.1	5.9	1.2	4.4
South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	1.6

Argentina's GDP is projected to drop only 1.5% in 2009 before growing by 1.9% in 2010.

Table 5. - World Bank Latin American GDP Growth Estimates

Country	1995-2005	2006	2007	2008	2009	2010
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7
Argentina	**2.3**	**8.5**	**8.7**	**6.8**	**-1.5**	**1.9**
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4
Colombia	0.7	6.8	7.5	2.5	-0.7	1.8
Chile	4.2	4.3	4.7	3.2	-0.4	2.7
Peru	3.3	7.6	9.0	9.8	3.0	4.3

LatinFocus (http://www.latin-focus.com/) collects projections from a wide variety of organizations. Its Consensus GDP Percent Change Forecast for Argentina –2.3% for 2009 and 2.2% for 2010. The LatinFocus Consensus Unemployment Rate Forecast for Argentina is 9.9% in 2009 going to 10.3% in 2010. That will mean some pain and increased political pressure on the government.

Brazil: Effects of Global Recession and Future Prospects

by Roberto Flamini, Paula Gomez, and Elliott Morss

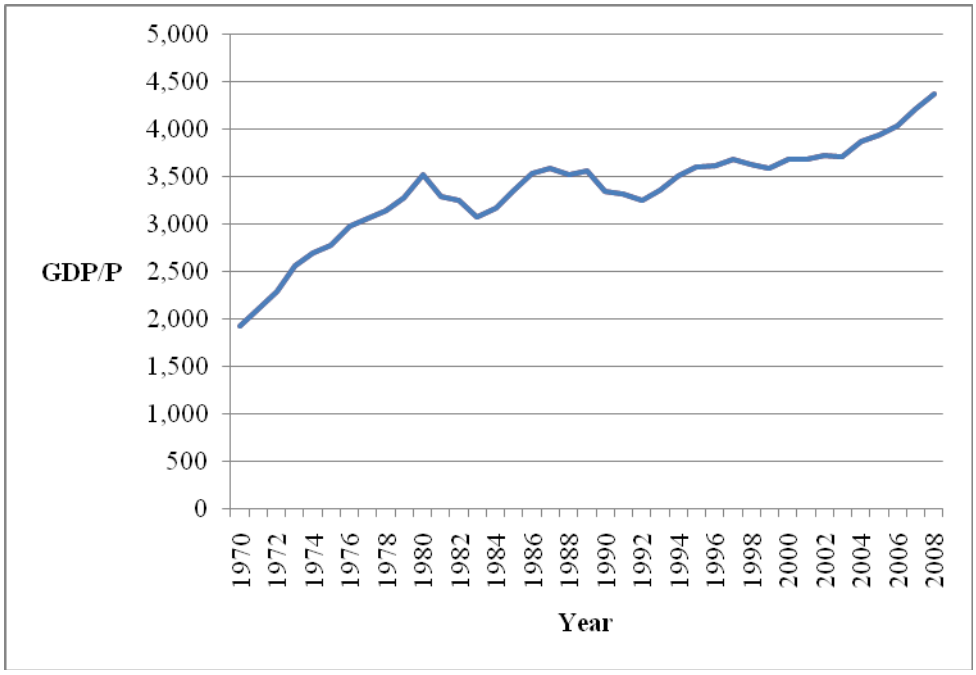
Executive Summary

The credit freeze had little effect in Brazil. The economic impact of the global recession in Brazil has been mild compared with previous global downturns. GDP could contract by up to 1% in 2009, far less than what would have been the case in Brazil in a global recession similar situation only a few years ago. Overall, Brazil has become one of the soundest economic powers in the world. With diverse exports, a growing middle class, and a broad natural resource base, Brazil's prospects are excellent.

Introduction

Measured by both geographic area and GDP, Brazil is the largest country in Latin America. Venezuela, Chile, and Mexico have higher per capita incomes than Brazil, where it is US$8,000 in current dollars. As Graph 1 indicates, per capita income in real terms has increased about 125% since 1970. The graph also indicates there have been two major downturns, one in the 1981-1984 period and also at the beginning of the 1990s.

Graph 1: The Evolution of Real GDP Per Capita in Brazil (1970-2008)



Source: CEPAL (2009)

Brazil has always been a natural resource rich country. And with a population density of only 22.5 per square kilometer, there is still little pressure on the land.

Brazil's ranks 2nd to Mexico in exports among Latam countries. Its exports have evolved from being primarily commodity-based to a point where in 2008, 47% were manufactured goods. Despite strong exports, Brazil is the most self-sufficient of all Latin American countries, with an export/GDP ratio of only 14%. Unlike many Latam countries, Brazil is not is not dependent on one export market. In 2008, 26% of its exports went to other Latam countries, 23% to Europe, 19% to Asia, and only 14% to the US. Exports to Asia are growing most rapidly, as the natural resource poor countries of China and India are buying more commodities.

Brazil has a rapidly growing middle class which will continue to be a major engine for its growth. And over the last decade, it has had more foreign direct investment than any other nation in Latin America. However, Brazil has a relatively low "Doing Business" rating among Latam countries. On the other hand, its sovereign interest spread is quite low.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. Global stock markets lost $36 trillion directly following the credit freeze. Global markets have recovered somewhat, cutting stock losses to $22 trillion. Latin American stock markets have risen dramatically. Brazil is no exception. The BVSP fell 60 % for a loss of US$642 billion. The Brazilian market has recovered somewhat but is still down 8.30 %.

Impact of Declining Global Demand

From 2003 through 2008, Brazil's exports grew at an amazing average annual rate of 22%. As a result of the global recession, exports fell by 26% in the first six months of 2009 as compared to the same period last year. Compared to the January-June 2008 period, the export of basic goods decreased by 7.4%, while semi-manufactured goods and manufactured goods decreased by 26.9% and 30.6%, respectively.

But there are early, tentative signs that recession effects are weakening. Between May and June of this year, basic goods exports have grown by 20.2%, semi-manufactured goods by 11.4%, and manufactured goods by 10%. It is expected that Brazil's exports will gain 11.5% in 2010.

Brazil is the world's largest exporter of beef, iron ore, sugarcane ethanol, and the second largest exporter of soy products. Other leading exports include wheat, minerals, oil, and transportation equipment (cars and airplanes). Brazil has just discovered large offshore oil deposits that will add to its large natural resource base in coming years.

The Domestic Economy

LatinFocus (http://www.latin-focus.com/) estimates that Brazil's GDP will fall by only 0.1% in 2009, with investment falling 12.3%. Unemployment will increase from 6.8% in 2008 to 8.1% in 2009.

But even with the global recession, consumption grew by 2.3% in 2009. Like China and India, Brazil has a rapidly growing middle class. According to the Fundacion Getulio Vargas, this class has grown from 42% of the population in 2004 to 52% in 2008 (Economist Sept. 11, 2009). This class wants all the luxuries enjoyed now in developed nations, and consumer credit has expanded by 28% in nominal terms in each of the last 3 years.

The spending of this growing middle class will be a major deterrent to extended effects from the global recession.

Government Policies

The Brazilian Government has enacted a small ($3.6 billion – only 0.2% of GDP) stimulus package to boost domestic spending. This was done by reducing income tax rates on middle income families and lowering the tax on manufactured products. It has also lowered interest rates and eased capital requirements for the banking system. While no banks have failed in Brazil as a result of the global credit freeze and recession, there has been some bank consolidation as healthier banks took over weaker banks.

Like China and Japan, Brazil is concerned about the growing value of its currency – the Real – against the US dollar. Like most currencies, the Real weakened in the immediate aftermath of the global credit freeze, but it is now strengthening. To hold down further Real appreciation, the government has just imposed a 2% tax on new currency transactions. And

because it does not want its competitive export position to erode further, it could resort to buying US dollars.

The relatively mild recession has strengthened the public position of President Luiz Inácio Lula da Silva. He has pursued prudent macroeconomic policies in recent years. The government deficit as a percent of GDP has been kept under control. It will increase to 2.9% in 2009 in response to the global recession but is expected to fall back to 2.2% in 2010.

Looking Ahead

At least the first quarter of the 21st Century will be good to natural resource rich countries. And Brazil, with its rich export base, should do very well.

For the short run, consider first the projections made by World Bank. World GDP is expected to fall 2.9% in 2009 and increase 2.0% in 2010. That means Global GDP will not get back to 2008 levels until 2011. Latin America overall will fall somewhat less in 2009 before increasing 2% in 2010.

Table 1. - World Bank Global GDP Growth Estimates

Region	**2007**	**2008**	**2009**	**2010**
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
Developing Countries	8.1	5.9	1.2	4.4
South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	1.6

According to World Bank Estimates, Brazil's 's GDP is projected to drop by only 1.1% in 2009 before growing by 2.5% in 2010.

Table 2. - World Bank Latin American GDP Growth Estimates

Country	**1995-2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Brazil	**2.4**	**3.7**	**5.7**	**5.1**	**-1.1**	**2.5**
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7

Argentina	2.3	8.5	8.7	6.8	-1.5	1.9
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4
Colombia	0.7	6.8	7.5	2.5	-0.7	1.8
Chile	4.2	4.3	4.7	3.2	-0.4	2.7
Peru	3.3	7.6	9.0	9.8	3.0	4.3

LatinFocus collects projections from a wide variety of organizations. Its Consensus GDP Percent Change Forecast for Brazil is –0.1% for 2009 and 4.6% for 2010. The LatinFocus Consensus Unemployment Rate Forecast for Argentina is 8.1% in 2009 going to 7.8% in 2010.

Brazil is well on its way to becoming one of the strongest world economies in the 21st Century. With a low population density (22.5 persons/sq. km) versus China (141.7) and India (380.0), and abundant natural resources, the future is bright.

Chile: Effects of Global Recession and Future Prospects

by Elise Baros[6], Ceres Corro[7], and Elliott Morss

Executive Summary

The credit freeze had little impact in Chile. While the stock market fell 40% resulting in an asset loss of US$149 billion, that loss has almost been erased with the market down now only 1% from its earlier highs. But the reduction in export demand resulting from the global recession has had a greater impact. In 2009, investment is expected to fall 13% with consumption lower as well. Unemployment in 2009 will approach 10% by the end of the year. 2010 looks better, with most forecasts predicting GDP growth of 4%.

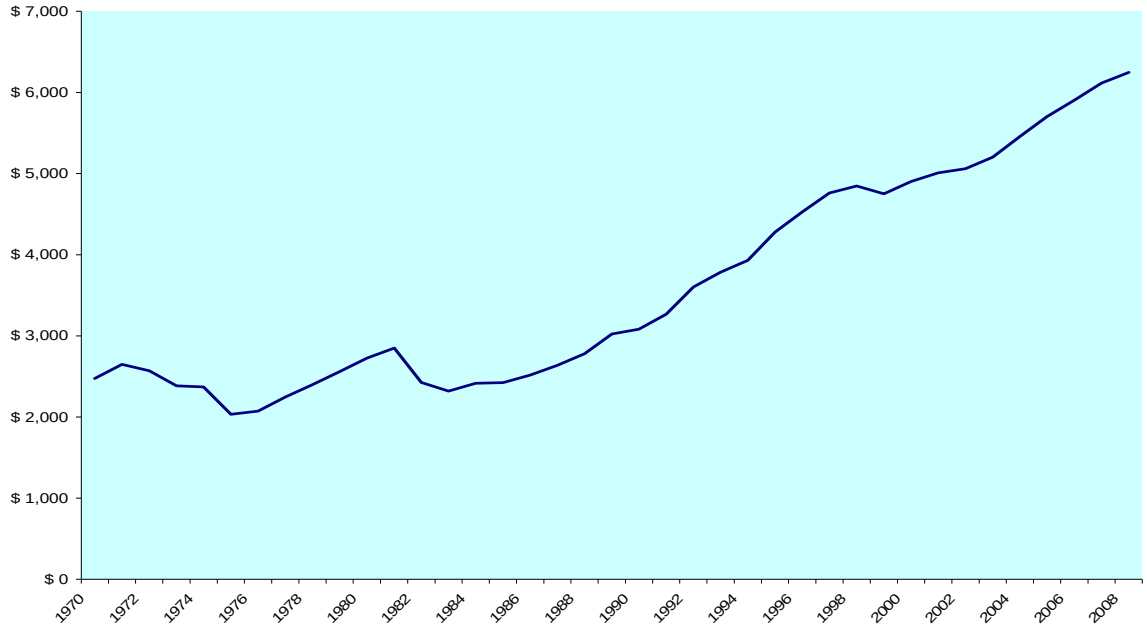
Introduction

With a per capita income of about US$10,000 (current 2008 US$), Chile, with Mexico, are just below Venezuela as the richest countries in Latin America. Between 1970 and 2008, Chile's GDP per capita grew more rapidly than any other Latin country (2.47% in 2008 constant dollars). This can be explained primarily by the "golden age" of the 'nineties, when the growth rate was 4.75%. The following graph shows the evolution of GDP per capita since 1970.

Graph 1: The Evolution of GDP Per Capita in Chile (1970-2008)

[6] MBA student, University of Palermo

[7] MBA student, University of Palermo



Source: CEPAL (2009)

Exports constitute a greater percentage of GDP in Chile than in any other Latam Country (47%). And with copper constituting more than half of its exports (52.5% in 2008), the economy is quite sensitive to fluctuations in the price of copper.

Chile is highly regarded by foreign investors. It ranks second only to Colombia in the Doing Business Ranking for South American countries. It also has the lowest Sovereign Interest rate spread of any Latin American country. In addition, Chile ranks tenth in the world and first in Latin America in the *"Index of Economic Freedom"* of the Heritage Foundation.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. The world lost $36 trillion in stock market losses directly following the credit freeze. Globally, markets have recovered cutting stock losses to $22 trillion. Latin American stock markets have recovered dramatically. And after being down 40% for a loss of $149 billion, the Chilean market is now only down 1%.

Impact of Declining Global Demand

Chilean exports have been adversely hit by the global recession. They are down 30.1% for the last quarter of 2008 combined with the first 3 quarters of 2009 as compared with the same period in 2007-2008.

Table 1. – Chile Export Performance (in bil. US$)

				(4thQtr 2008+1-3 Qtrs2009)

	2006	2007	2008	vs Same Period 2007-8 % Change
Total Exports	56,43	65,08	63,28	-30.1%
Copper	32,71	37,58	32,80	-39.1%
Molybdenum oxide	2,78	3,83	3,36	-57,5%
Salmon/Trout	2,15	2,16	2,32	-6,9%

Source: http://www.bcentral.cl/estadisticas-economicas/series-indicadores/index_se.htm

The Domestic Economy

Consumption growth slowed from an average of 5.8% for the last quarter of 2007 plus the first two quarters of 2008 to only 0.1% for the same period in 2008-2009. It is expected to be down by only 0.4% for all of 2009. Investment is expected to decline by 13.4% in 2009. It is estimated that the unemployment rate will increase to 9.9% in 2009 from 7.5% in 2008.

External Sector

Chile had been receiving a significant amount of foreign direct investment, and this is projected to fall in 2009. Foreign remittances are not significant for Chile.

Table 2. – External Trade (in millions US$)

Item	2006	2007	2008	2009 est.
Exports of Goods and Services	56,430	65,081	63,281	35,438
Imports of Goods and Services	35,899	44,030	57,609	28,344
Trade Balance	20,530	21,050	5,672	7,093

Source: http://www.bcentral.cl/estadisticas-economicas/series-indicadores/index_se.htm

Government Policies

In the spring of 2008, the Chilean peso was strengthening relative to the US dollar. In response, the Central Bank started buying US dollars with pesos. Its goal was to purchase $8 billion and thereby end the peso appreciation. This program was stopped in September after the Bank had purchased $6 billion. As the credit freeze took hold and the demand for liquidity increased the Bank launched a program in which it would use pesos and US dollars to buy various financial contracts (swaps and repos). http://www.bcentral.cl/eng/studies/economic-policy-papers/pdf/dpe30eng.pdf

The Bank also reduced its interest rate from 8.25% to 2.25%.

Partially as a result of the global recession, the government's overall balance as a percent of GDP is expected to go from a surplus of 5.4% in 2008 to a deficit of 4.2%.

Looking Ahead

The World Bank estimates World GDP will fall 2.9% in 2009 before recovering 2.0% in 2010. That means Global GDP will not get back to 2008 levels until 2011. Latin America overall will fall somewhat less in 2009 before increasing 2% in 2010.

Table 3. - World Bank Global GDP Growth Estimates

Region	2007	2008	2009	2010
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
Developing Countries	8.1	5.9	1.2	4.4
South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	1.6

Chile's GDP is projected to drop only 0.4% in 2009 before growing by 2.7% in 2010.

Table 4. - World Bank Latin American GDP Growth Estimates

Country, Region	**1995-2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7
Argentina	2.3	8.5	8.7	6.8	-1.5	1.9
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4
Colombia	0.7	6.8	7.5	2.5	-0.7	1.8
Chile	**4.2**	**4.3**	**4.7**	**3.2**	**-0.4**	**2.7**
Peru	3.3	7.6	9.0	9.8	3.0	4.3

LatinFocus (http://www.latin-focus.com/) collects projections from a wide variety of organizations. Its Consensus GDP Percent Change Forecast for Chile is 1.5% for 2009 and 4.0% for 2010.

Part of the reason for projected the strong rebound is attributable to the fact Copper prices have recovered 57% of their losses from previous highs. This is important inasmuch as copper constitutes approximately 50% of Chile's exports.

Table 5. – Copper Price Index

Index	**Index High**	**Index Low**	**Index Now**	**Hi-Low % Loss**	**Hi-Now % Loss**	**Percent Recovery**
Copper	8.71	3.1	6.3	-64.4%	-27.7%	57.0%

As a result, the LatinFocus consensus is that exports will grow 12.8% in 2010 after falling 25.3% in 2009. The LatinFocus Consensus Unemployment Rate Forecast for Chile is 9.9% in 2009 and 9.3% in 2010.

Chile's external debt is 38.6% of its GDP which is high, but the Sovereign Spread it has to pay on borrowings is extremely low by Latin American standards.

COLOMBIA: Effects of Global Recession and Future Prospects

by Maria Victoria Vasquez[8], Carlos Uribe, and Elliott Morss

Executive Summary

The 2008 credit freeze caused major asset losses around the world, both in equity and real estate. The resulting "wealth effect" caused consumption and investment expenditures to fall, triggering a global recession. Consumption, investment, and employment fell in most regions of the world.

However, the credit freeze and its resulting wealth effect had little long run impact in Colombia, and the country weathered the resulting recession better than any other large economy in Latin America. But recovery will be modest, subject to depressed export markets.

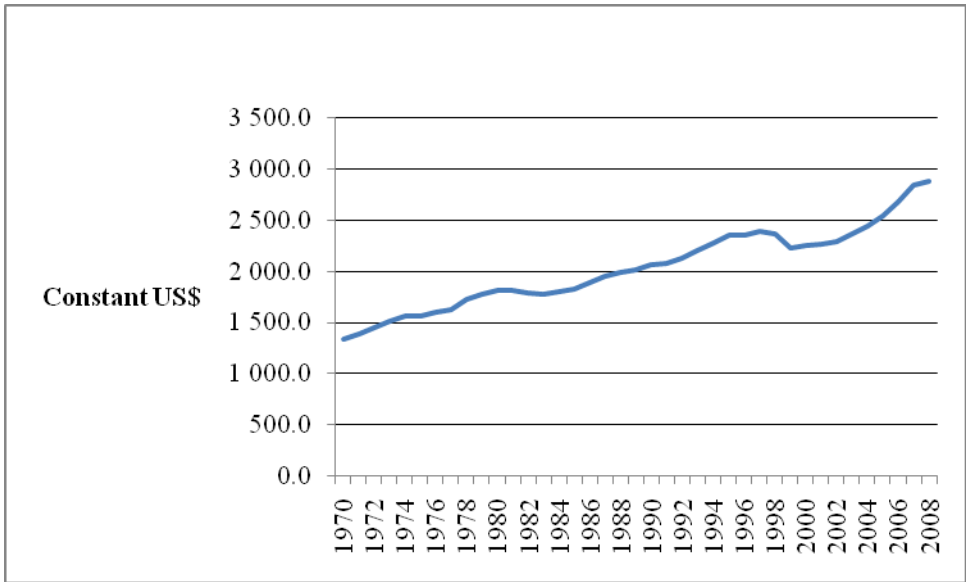
Introduction

As measured by GDP and land area, Colombia is one of the smaller Latin American countries in our survey. However, it ranks second only to Mexico with a population density of 43 people per square kilometer. Its per capita income (US$4,724 in current US$) is the lowest in our group with the exception of Peru.

As Graph 1 indicates, per capita income in real terms has more than doubled since 1970. The graph also indicates there has been a major downturn, in the 1998-2000 period.

[8] MBA student, University of Palermo.

Graph 1: The Evolution of Real GDP Per Capita in Colombia (1970-2008)



Source: CEPAL (2009)

Colombia is quite self-sufficient, with only 17% of its economy derived from trade. More than 60% of its exports are commodities, with about half of these being oil based. Colombia also exports coffee and coal. Its major trading partners are the US and Venezuela.

Remittances from overseas workers are important in Colombia constituting 2.4% of income in 2007.

Colombia is highly regarded by overseas investors. It has the highest "Doing Business" rating of any Latam country. It also has a relatively low sovereign interest spread.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. Global stock markets lost $36 trillion directly following the credit freeze. Global markets have recovered somewhat, cutting stock losses to $22 trillion. Latin American stock markets have risen dramatically.

Colombia is no exception. In fact, The IGBC fell 43% resulting in asset losses of US$6,5 billion. Nonetheless, losses have already been recovered with the stock market recently reaching new highs. Table 1 illustrates IGBC performance since January 2007.

Table 1. – IGBC monthly performance (high)

Month	2007	2008	2009
January	10,203	8,251	7,456
February	9,901	8,813	7,515
March	10,052	8,561	7,611
April	10,548	9,200	8,042

May	10,011	9,823	8,468
June	10,138	9,158	9,312
July	10,609	8,719	9,628
August	9,960	8,833	10,375
September	10,291	9,010	10,279
October	10,166	6,461	10,687
November	10,638	6,812	10,537
December	10,041	7,174	

Market capitalization in Colombia is roughly 49% - a very low figure when compared to other economies in the region. Therefore, the overall economy is not as vulnerable to stock market crashes.

With respect to construction, overall activity fell 11% after Q3/08, but quickly returned to all-time highs on account of increasing levels of public construction programs. Construction accounts for 5.9% of the economy. Table 2 illustrates overall construction activity (both private and public) in Colombia since Quarter 1, 2007.

Table 2. – Construction activity in millions of constant pesos (2000)

Period	2007	2008	2009
Q1	3,529,483	3,545,789	3,497,568
Q2	3,596,587	3,554,047	4,151,502
Q3	3,273,665	3,735,884	
Q4	3,795,591	3,322,870	

Source: DANE, Colombia

The picture is somewhat gloomier when considering Foreign Direct Investment. FDI fell almost 21% in Q1/09 with respect to the same period in 2008. However, as some confidence returned to international markets, FDI recovered in Q2/09, and was only 1% lower than in the same period in 2008. Foreign direct investment accounts for 4.4% of the Colombian economy. Table 3 illustrates quarterly FDI in Colombia since Q1/07.

Table 3. – Colombia, Foreign Direct Investment

Quarter	2007	2008	2009	08-09 % Change
1	2,059	2,874	2,377	-17.3%
2	2,226	2,543	2,519	-0.9%
3	2,364	2,603		
4	2,400	2,580		

Remittances to Colombia decreased significantly after Q4/08 as a result of worsening conditions in the US economy. Remittances account for 2.4% of GDP. In fact, most monthly data in 2009 show a substantial decrease when compared to the same period in 2008, as indicated in Table 4.

Table 4. – Remittances to Colombia (in mil. US$)

Month	2008	2009	% change
January	385.0	324.2	-18.75
February	362.0	379.5	4.59
March	393.7	389.8	-0.99
April	411.1	338.9	-21.30
May	410.6	340.7	-20.54
June	367.8	312.2	-17.81
July	469.2	313.3	-49.79
August	373.0	303.5	-22.90
September	480.0	313.2	-53.24
October	427.5		
November	323.8		
December	438.4		

Impact of Declining Global Demand

Colombian exports have been adversely hit by the global recession, especially because Colombia's main trading partners (US and Venezuela) are among the weakest performers world-wide.

Overall exports are down 24% since reaching a high in Q2/08 on account of declining demand. However, export Activity accounts for only 17% of the Colombian economy – one of the lowest in the region. Table 5 summarizes overall export behavior:

Table 5. – Colombian Exports by Sector and Destination

	Jan-Sept		
	2008	**2009**	**% Change**
Total Exports	29,273	23,853	-18.5%
by sector			
Oil	10,178	6,764	-33.5%
Coal	3,854	4,173	8.3%
Petrochemicals	1,996	1,834	-8.1%
Food/Bevs.	1,852	1,796	-3.0%
Coffee	1,479	1,168	-21.0%
by country			
USA	10,540	9,017	-14.4%
Venezuela	4,569	3,514	-23.1%
Ecuador	1,125	894	-20.5%
Mexico	463	379	-18.1%
Japan	279	253	-9.3%

Source: DANE, Colombia

The Domestic Economy

Overall, Colombia's downturn in 2009 was more shallow than the average for Latin America on account of a relatively closed economy (exports of goods and services accounted for 18% of GDP in 2008), aggressive monetary easing by the government, and a

relatively stable banking system. However, Colombia's recovery in 2010-11 will lag behind regional leaders such as Brazil, as a result of fiscal deterioration and an external reliance on the US and Venezuela, two of the hemisphere's weak performers.

On the supply side, manufacturing, which contributed strongly to GDP growth in recent years but fell by 8.2% in January-July, and retail sales, which dropped by 4.7% in the period, are expected to have bottomed out in July or August but will remain relatively weak in 2010-11. Construction will continue to gain some support from accelerated execution of public infrastructure projects and expansion in productive capacity in mining and energy, but will suffer from the end of the residential boom of 2004-07 until confidence returns. (Economist Intelligence Unit). Table 6 illustrates economic performance in 2008 and 2009.

Table 6. – Economic Performance

Sector	**2008**				**2009**	
	1 qtr.	2 qtr	3 qtr	4 qtr	1 qtr.	2 qtr
GDP	4.2%	3.9%	2.8%	-1.1%	-0.4%	-0.5%
Imports	12.8%	10.0%	7.8%	8.8%	-1.5%	-9.7%
Consumption	3.7%	2.8%	1.4%	1.2%	-0.3%	-0.3%
Private	4.3%	2.9%	1.4%	1.6%	-0.5%	-0.7%
Government	1.5%	2.5%	1.5%	-0.1%	0.3%	0.9%
Investment	8.4%	10.2%	12.8%	-0.1%	-3.7%	-7.3%
Exports	4.8%	4.6%	4.1%	0.9%	-1.1%	-2.1%
	14.1%	9.2%	2.9%	2.4%	2.0%	-5.7%
Sector						
Agriculture/Fishing	4.0%	5.5%	2.1%	-0.6%	-0.8%	-1.8%
Mining	4.6%	7.9%	10.4%	6.4%	10.6%	10.2%
Manufacturing	2.1%	1.2%	-2.5%	-7.9%	-7.9%	-10.2%
Elect, Gas, Water	0.7%	1.7%	1.2%	1.0%	1.9%	0.1%
Construction	0.4%	-0.2%	21.1%	-11.3%	4.1%	16.8%
Retail, hotels, Rest.	2.2%	4.0%	1.1%	-0.6%	-2.7%	-3.9%
Transport & Communications	9.0%	4.6%	2.3%	0.4%	-2.0%	-1.2%
Financial Services	7.0%	4.9%	6.5%	3.9%	4.7%	4.3%
Social Services	3.4%	2.9%	1.7%	0.3%	-0.2%	0.5%

.Government Policies

In late 2008, the government asked private banks to “voluntarily” save 43% of current profits to maintain liquidity. As a result, by August, 2009, banks had liquidity levels of 15.1%, way above the 9% required by the Superintendencia Bancaria (Colombian bank regulatory agency).

Short-term fiscal policy has revolved around the financing of a worsening budget deficit provoked by the economic slowdown and delays in Colombia’s privatization program. Therefore, in order to finance the additional fiscal slippage (a total of Ps4.4trn), the Uribe administration plans to resort to issuing additional Titulos de Tesoreria (TES, government bonds) in the amount of Ps6trn (or US$3bn) - 2trn of which will be auctioned as pre-financing for the 2010 budget.

With respect to monetary policy, as inflation worries eased in 2009, Banco de la República (Banrepublica, the central bank) loosened monetary policy by slashing rates to 4% in order to promote the recovery of domestic demand and to alleviate currency-appreciation pressures. The bank is also actively participating in the foreign exchange market. Therefore, foreign exchange reserves continue to rise.

Nevertheless, both government and monetary authorities remain under pressure from exporters to curb the appreciation of the peso, which has nominally appreciated by 17% against the US dollar since December 2008.

Looking Ahead

As previously stated, Colombia recovery will by slowed by fiscal deterioration and an external reliance on the US and Venezuela, two of the hemisphere's weak performers. Tables 7 and 8 depict estimates for Colombia's GDP growth. The World Bank estimates GDP in 2009 falling 0.7% and growing 1.8% in 2010.

Table 7. - World Bank Global GDP Growth Estimates

Region	2007	2008	2009	2010
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
Developing Countries	8.1	5.9	1.2	4.4
South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	1.6

Table 8. - World Bank Latin American GDP Growth Estimates

Country, Region	1995-2005	2006	2007	2008	2009	2010
Latin America and Caribbean			5.8	4.2	-2.2	2.0
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7
Argentina	2.3	8.5	8.7	6.8	-1.5	1.9
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4
Colombia	**0.7**	**6.8**	**7.5**	**2.5**	**-0.7**	**1.8**
Chile	4.2	4.3	4.7	3.2	-0.4	2.7
Peru	3.3	7.6	9.0	9.8	3.0	4.3

The consensus forecast of LatinFocus is more optimistic: it sees a 2.3% growth of GDP in 2010. However, it estimates unemployment rising to 13.3% at the end of 2009 and remaining there throughout 2010.

Ecuador: Effects of Global Recession and Future Prospects

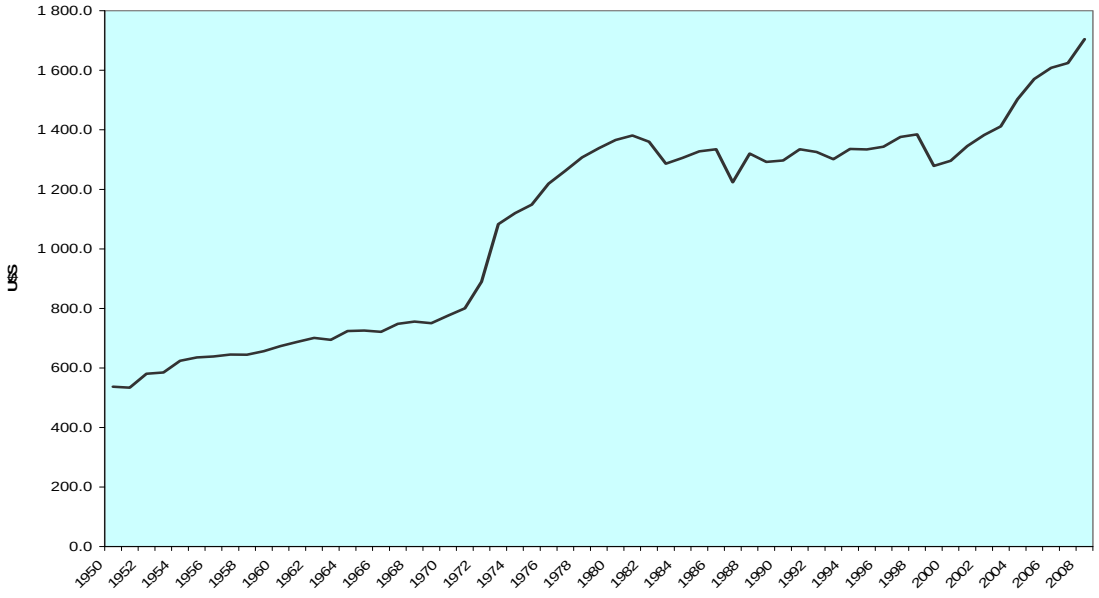
by Diego Gauna

Introduction

Ecuador is one of the poorest countries in Latin America. Excluding Bolivia and Paraguay, it has the lowest GDP per capita in South America.

The performance of Ecuadorian economy had been disappointing. It entered the new Century with the same per capita income it had in 1980, reflecting a long period of stagnation and economic downturn. During the local financial crisis in 2000, the local currency was eliminated and the US dollar was made the official currency. The following graph shows the evolution of GDP per capita since 1950.

Graph 1: The Evolution of Real GDP Per Capita in Ecuador (1950-2008)



Source: CEPAL (2009)

Historically, the economy was based on commodity production, especially crude oil and bananas. In 2008, agriculture and mining's share of GDP was 30.4% and the primary export share of total exports was 76%. Clearly, the Ecuadorian economy has a high degree of vulnerability to commodity price fluctuations. Periods of high growth in Ecuador coincide with periods of high commodities prices (1973-1978; 2001-2008).

Ecuador has the highest percentage of remittance inflows in Latin America. In 2007, remittances as a percent of GDP were 6.9%. The main sources of remittances are the US (47%) and Spain (41%) followed by Italy (7.5%).

In trade, Ecuador is highly dependent on US. In value terms, 45% of Ecuador exports went to the US and 20% of its imports came from there in 2008.

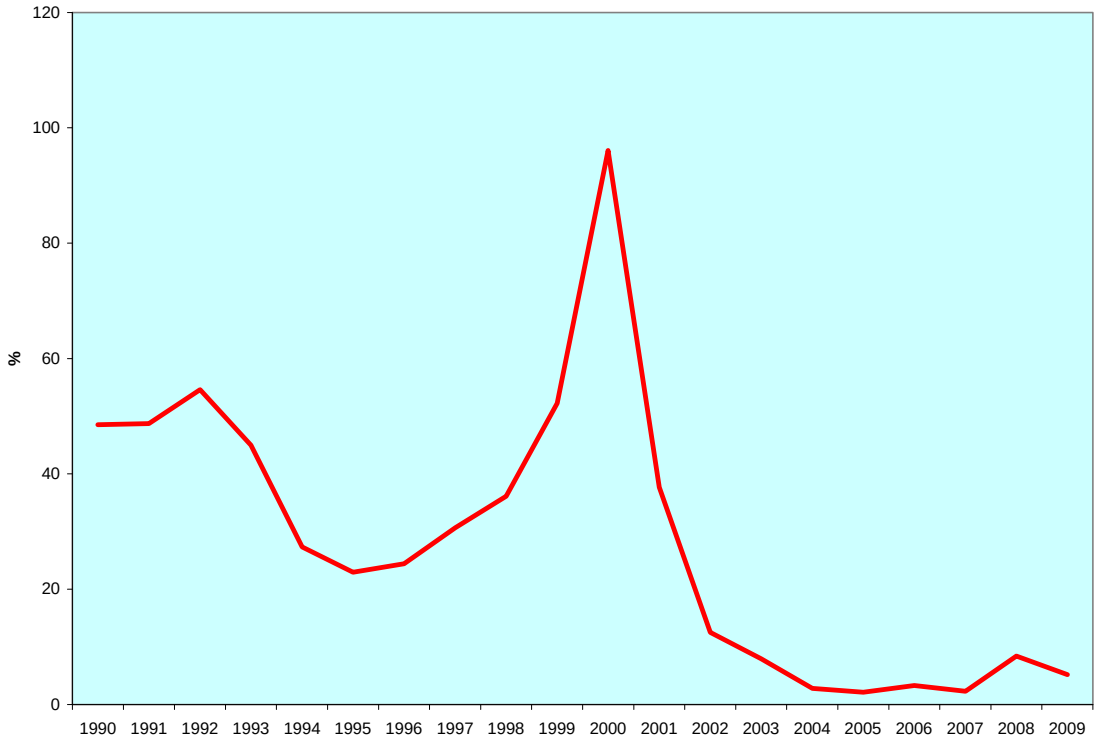
Ecuador has one of the most underdeveloped stock markets in Latin America. The stock markets of Quito and Guayaquil are extremely narrow, with few firms and low levels of liquidity. Excluding Paraguay, Uruguay and Venezuela for no data, Ecuador has the lowest ratio of stock market capitalization to GDP in Latin America. In 2008, this ratio was only 9% (World Development Indicators, 2009).

Ecuador has one of the worst investment climates in Latin America. Ecuador ranks 133rd in the Doing Business Index (World Bank) with only Bolivia and Venezuela lower. It interest spread is higher than any other Latam country.

The most notorious characteristic of Ecuadorian economy is the dollarization regime. Because of the dramatic financial crisis by the end of 1999 and the los of confidence in the local currency, Ecuador adopted the US dollar as the official currency. This policy reduced the inflation rate and stimulated economic growth after the year 2000, but at the same time, the government lost control of fiscal and monetary policy to stabilize the economy. It could reduce aggregate demand by increasing taxes or reducing expenditures, but its ability to stimulate the economy was limited by its holdings of US dollars.

Ecuador has experienced large and volatile rates of inflation. During the nineties, the inflation rate was above 20% every year, reaching almost a 100% in 2001. With the dollarization regime, the inflation rate fell steadily. In 2004-2007 period, the average rate of inflation was less than 3%. Inflation pressures emerged during 2008, mainly because of the rise in international commodities prices. The following graph provides inflation data.

Graph 2: Ecuador's Inflation Rate (1990-2009)



Source: CEPAL (2009)

Crisis Effects

The global recession impacted Ecuador via the following channels:

a. Sharp drop in commodities prices, especially oil prices.
b. The lower demand for exports resulting from the US credit crisis.
c. Lower remittances resulting from higher unemployment in Spain and USA.

Commodity prices fell sharply. The Ecuadorian crude oil price, which had hit almost US$120 per barrel in June 2008, dropped to US$27 per barrel in December. That means the primary export commodity of Ecuador lost more than of 75% of its value in only six months.

The oil price drop caused a marked fall in export values. 2009 exports were 25.6% less than in 2008. The average price fell 23.8% while volume was down by 2.5%. Oil export prices fell 40.3% and volume was down 7.6%. The average price of non-oil exports did not

change while they increased in volume by 10%, primarily as a result of an increase in banana exports.

This has led to a downturn in Ecuador. Demand has fallen almost 7% between the third quarter of 2009 and the same period of 2008, mainly because of the drop in value of oil exports. The effects of global crisis started in the second quarter of 2009 and, since the first quarter of 2009, government policy has been to increase its expenditures.

Table 1 shows that public consumption was 5.35% higher in the second quarter of 2009 than it was in the same quarter in 2008 and 2.45% higher in the third quarter.

Table 1. – Ecuador: 2008- 2009 Changes in Expenditures (%)

2008-09 Change	Internal Demand	Consumption		Investment	Exports	Total Demand
		Private	Public			
1st Qtr.	2.60%	2.14%	0.02%	4.77%	-6.64%	0.04%
2nd Qtr.	-3.60%	-1.34%	5.35%	-4.02%	-9.17%	-5.13%
3rd Qtr.	-7.57%	-3.04%	2.45%	-8.06%	-4.91%	-6.88%

Source: Central Bank of Ecuador

Table 2 shows that with the exception of one quarter, public consumption has grown quarter to quarter starting in the third quarter of 2008.

Table 2. – Ecuador: Quarterly Changes in Expenditures (%)

Percent Change	Internal Demand	Consumption		Investment	Exports	Total Demand
		Private	Public			
2008: II-III	5.38%	2.25%	2.97%	5.43%	-4.07%	2.78%
2008: III-IV	-0.11%	0.85%	2.75%	0.98%	-0.91%	-0.31%
2008-09:IV-I	-5.70%	-2.48%	-0.57%	-7.58%	-3.86%	-5.23%
2009: I-II	-2.89%	-1.91%	0.14%	-2.46%	-0.60%	-2.30%
2009: II-III	1.04%	0.48%	0.14%	1.00%	0.43%	0.88%

Source: Central Bank of Ecuador

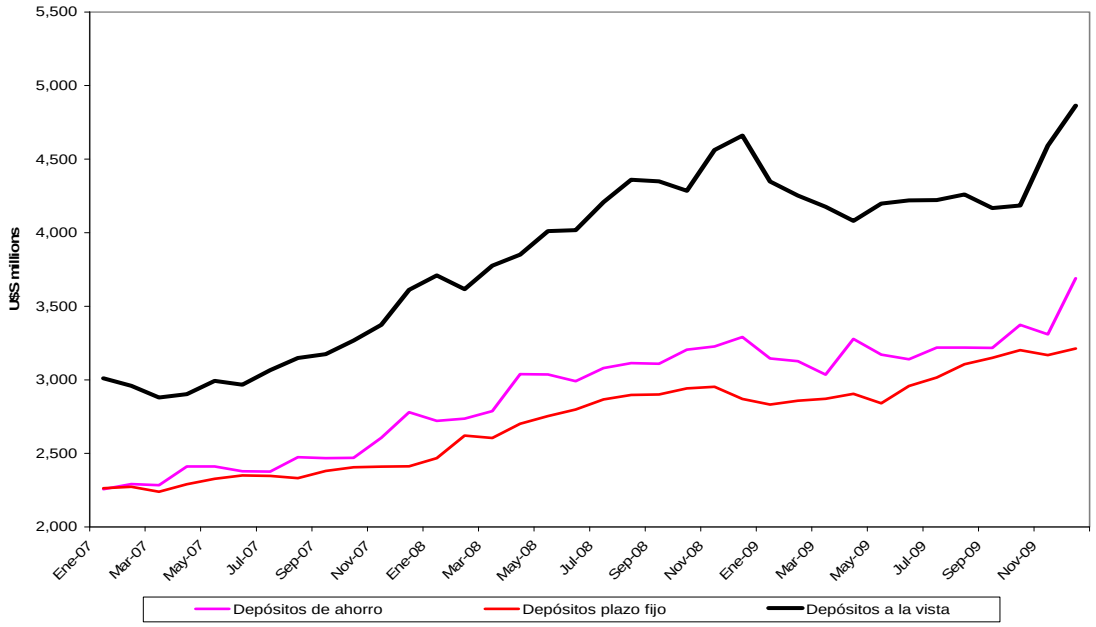
The dollarization regime in Ecuador has impeded the use of exchange rate as policy instrument. The current account deficit moved from a surplus of US$1.6 billion in 2007 (3.6 % of GDP) to a deficit of US$427 million in 2009 (up to September). To correct this disequilibrium, Ecuador could not depreciate their currency to reduce the outflow and increase domestic expenditures.

Urban unemployment has increased from 7.1% in September of 2007 to 9.1% in September of 2009 *("Evolución de la Economía Ecuatoriana", Enero de 2010, Banco Central de Ecuador).*

Ecuador's government depends on oil revenues: the oil revenue share in total revenues was 25% in 2000-2008. For this reason, the sharp fall in oil prices during global crisis contributed to the growing government deficit. The Central Bank of Ecuador estimates the government deficit at 3.5% of GDP in 2009, which is higher than the 1.5% deficit in 2008. It important to understand that unlike countries that have their own currencies, Ecuador is limited in what it can do to stimulate its economy to its US$ reserves. CEPAL estimated Ecuador's international reserves at US$2.7 billion at the end of June, 2009. For all of 2009, LatinFocus estimates the government deficit at 4% of GDP, or approximately US$2 billion, leaving it with only US$700 million for stimulus in 2010 and following.

The Ecuadorian banking system was not significantly threatened by the Western banking collapse. As indicated in Graph 3, private bank deposits fell in early 2009 but then recovered to previous levels.

Graph 3: Ecuador: Private Deposit Volume (2007-2009)



Source: Central Bank of Ecuador (2009)

The stock market index of Ecuador fell 26% between December of 2007 and December of 2009. Ecuador' stock market is not recovering to levels attained prior to the crisis. This contrasts with most Latin American countries where stock prices have recovered. (excluding Venezuela). It is important to keep in mind that Ecuador's stock market is precarious and index movements have little economic significance.

Policy Responses

As indicated above, the dollarization regime in Ecuador limits what the government can do to mitigate the consequences of the global recession. The only way the government can run a deficit to stimulate the economy is to draw down its international holdings of dollars, and these holdings are limited.

It is important to note that maintaining a fiscal and external equilibrium is the key factor to sustain the dollarization regime.

As table 2 shows, Ecuador chose to increase public spending in 2008, but then held them steady because of the sharp deterioration in government revenues. In 2008, President Correa got a new article enacted into law that eliminated the independence of the Central Bank.

Ecuador introduced restrictions on imports to restore the equilibrium in the current account. These policies included an increase in the import tariff rate (December ’08), quantitative restrictions (January ‘09) and tariff barriers (July ’09).

Prospects

Table 3 provides World Bank growth estimates for Latin American countries. Ecuador is expected to recover as oil exports increase.

Table 3. - World Bank Latin American GDP Growth Estimates

Country	95-05	2006	2007	2008	2009	2010 est.	2011 est.
Argentina	2.3	8.5	8.7	6.8	-1.5	1.9	2.1
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5	4.1
Chile	4.2	4.3	4.7	3.2	-0.4	2.7	3.6
Colombia	2.1	6.8	7.5	2.5	-0.7	1.8	4.0
Ecuador	**3.2**	**3.9**	**2.5**	**6.5**	**-2.6**	**1.8**	**3.1**
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7	3.0
Peru	3.3	7.6	9.0	9.8	3.0	4.3	6.0
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4	1.2

But serious problems remain. LatinFocus estimates that the countries unemployment rate will increase to 10% and stay there, at least through 2011.

Ecuador has difficult choices in the short run. If Ecuador continues with the dollarization regime, the recovery will be slow and painful for their economy and their workers. The radicalization of Correa polices the bad investment climate and the volatility in oil markets

lead to pessimism about the country's future. Ending dollarization would allow the government to again exercise monetary and fiscal policy. But introducing a new currency will not be easy and could generate panic and instability in local financial markets.

Mexico: Effects of Global Recession and Future Prospects

By Elliott Morss

Executive Summary

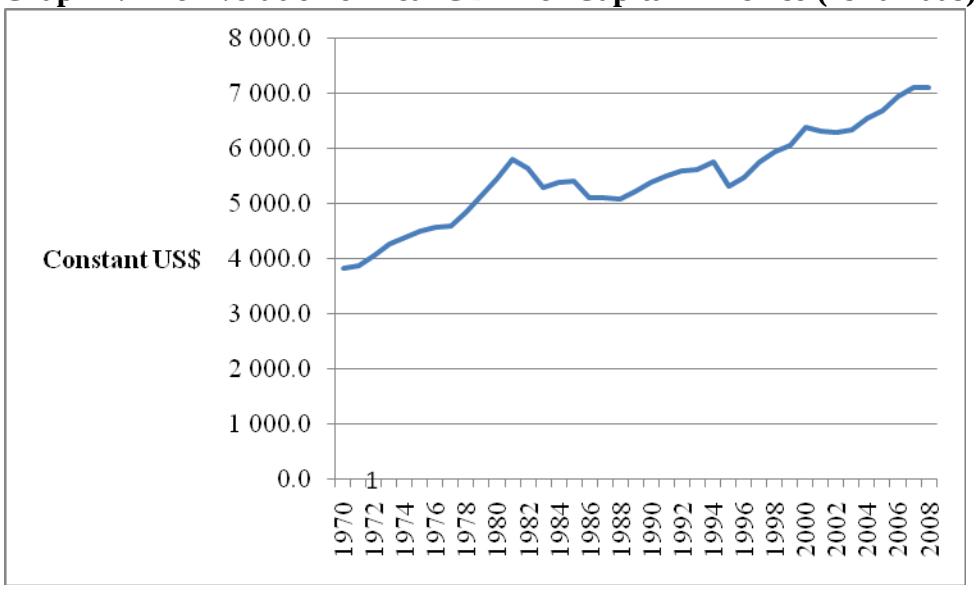
The credit freeze had a significant impact in Mexico. The stock market fell 48%; that loss has recently been pared to 5%. The reduction in export demand resulting from the global recession has had a greater impact. Exports fell an estimated 25% in 2009, with investment down more than 10% and consumption off nearly 7%. Unemployment jumped from 4.3% in 2008 to 5.6% in 2009. 1010 looks better, with GDP growth of expected to increase by 3.0% after falling 7.1% in 2009.

Introduction

As measured by GDP and land area, Mexico is the second largest country (Brazil is the largest) among Latin American countries. It has the highest population density of any Latam nation (56 people per square kilometer). And a per capita income of US$10,160 (current 2008 US$), it is second only to Chile among countries in this survey. It is the largest exporter of all Latam countries.

As Graph 1 indicates, per capita income in real terms has almost doubled since 1970. The Graph also shows there have been two downturns, in the late 1980's and 1990's.

Graph 1: The Evolution of Real GDP Per Capita in Mexico (1970-2008)



Source: CEPAL (2009)

79% of Mexico's exports are manufactured goods. Its major commodity export is oil (17%). 80% of its exports go to the United States. Remittances from workers overseas are important, constituting about 2.6% of GDP.

Mexico's external debt is 22% of its GDP; this is moderate by Latin American standards. The Sovereign Spread over US Treasuries is only 200bps, making second only to Chile as the lowest in Latin America. Mexico also has a good "Doing Business" rating.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. Global stock markets lost $36 trillion directly following the credit freeze. Global markets have recovered somewhat, cutting stock losses to $22 trillion. Latin American stock markets have risen dramatically. And after being down almost 48% for a loss of $227 billion, the Mexican market is now only down a little more than 5%.

Impact of Declining Global Demand

As shown in Table 1, Mexico's leading exports are electrical machinery, oil, vehicles and nuclear reactors. All have been adversely affected by the global recession.

Table 1. – Mexico Export Performance (in mil. US$)

Item	2006	2007	2008	2009 (11 mos.)	2008 (1st 9 mos.)	2009 (1st 9 mos.)
Total Exports	249.9	271.9	291.3	206.8	228.0	162.5
Electrical Machinery	61.7	70.3	75.2	55.2	57.8	43.8
Oil	39.0	43.0	50.6	27.5	43.3	21.6
Vehicles	39.5	41.9	42.8	29.8	32.2	22.1
Nuclear Reactors, Boilers, Machinery	32.7	33.9	33.7	26.2	25.9	20.7

Source: http://www.banxico.org.mx/sitioingles/tipo/estadisticas/index.html.

Overall, exports are down 29% (Table 2), with oil exports hardest hit.

Table 2. – Mexico: Change in Exports

Percent Change	2006 - 2007	2007 - 2008	2008 - 2009 (1st 9 mos.)
Total Exports	9%	7%	-29%
Oil	10%	18%	-50%
Vehicles	6%	2%	-32%
Electrical Machinery	14%	7%	-24%
Nuclear Reactors, Boilers, Machinery	4%	-1%	-20%

Table 3 provides data on Mexico's leading exports. Using 2008 data, these 4 export categories comprise 69% of Mexico's total exports.

Table 3. – Mexico – Leading Exports

Export Composition	**2006**	**2007**	**2008**	**2009 (11 mos.)**	**2008 (1st 9 mos.)**	**2009 (1st 9 mos.)**
Electrical Machinery	25%	26%	26%	27%	25%	27%
Fuels	16%	16%	17%	13%	19%	13%
Vehicles	16%	15%	15%	14%	14%	14%
Nuclear Reactors, Boilers, Machinery	13%	12%	12%	13%	11%	13%

Mexico's export performance depends primarily on US demand. As Table 4 indicates, more than 80% of Mexico's exports go to the US.

Table 4. – Mexico – US Export Share

US Export Share	**2006**	**2007**	**2008**	**2009 (11 mos.)**	**2008 (1st 9 mos.)**	**2009 (1st 9 mos.)**
Non-Fuels	85%	83%	80%	80%	80%	80%
Fuels	81%	80%	82%	84%	81%	84%

According to the CIA, Mexico produces 3.186 million bbl of oil daily. It has proved reserves of 10,500 million bbl. At this rate of production, Mexico has only 9 years of oil production capacity left. Of course, with increased investment oil, reserves can be raised. But The Mexican situation is far different than Venezuela that has 99 million bbl of proved reserves.

The Domestic Economy

Consumption fell sharply in 2009. According to the LatinFocus Consensus Forecast (http://www.latin-focus.com/), consumption was down 7.1%. Investment was down by 10.5%. Overall, GDP, which had been growing by more than 3% over the last half decade, fell by an estimated 7.1% in 2009. The unemployment rated increased from 4.3% in 2008 to 5.6% in 2009.

External Sector

Mexico has traditionally run both a trade and current account deficit. These have in part been covered by workers' remittances which constituted approximately 2.6% of GDP in 2008. As Table 5 indicates, the trade and current account balances have been increasing over time. The global recession will probably cut workers' remittances by more than 50%.

Table 5. – Mexico: Trade and Current Account Balances

Item	2006	2007	2008	2009
Current Account Balance	-0.5	-0.8	-1.5	-1.6
Trade Balance	-0.6	-1.0	-1.6	-1.3

Source: LatinFocus.

Government Policies

According to the International Labor Organization, the Mexican Government has launched a stimulus package of $54 billion or 4.7% of GDP to counter the global recession. This package, coupled with deteriorating government revenue resulting from the recession, has prompted concern over the government deficit. LatinFocus projects that it will grow to more than 2% for both 2009 and 2010. To counter the effect of the global recession in Mexico, interest rates have been reduced and the money supply increased.

Looking Ahead

The World Bank estimates World GDP will fall 2.9% in 2009 before recovering 2.0% in 2010. That means Global GDP will not get back to 2008 levels until 2011. Latin America overall will fall somewhat less in 2009 before increasing 2% in 2010.

Table 6. - World Bank Global GDP Growth Estimates

Region	2007	2008	2009	2010
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
Developing Countries	8.1	5.9	1.2	4.4
South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	1.6

The World Bank estimates that Mexico's GDP will fall by 5.8% in 2009 before growing by 1.7% in 2010.

Table 7. - World Bank Latin American GDP Growth Estimates

Country, Region	1995-2005	2006	2007	2008	2009	2010
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5
Mexico	**3.6**	**4.8**	**3.3**	**1.4**	**-5.8**	**1.7**
Argentina	2.3	8.5	8.7	6.8	-1.5	1.9
Venezuela	1.6	1.3	8.4	4.8	-2.2	-1.4
Colombia	0.7	6.8	7.5	2.5	-0.7	1.8
Chile	4.2	4.3	4.7	3.2	-0.4	2.7
Peru	3.3	7.6	9.0	9.8	3.0	4.3

LatinFocus (http://www.latin-focus.com/) collects projections from a wide variety of organizations. Its Consensus GDP Percent Change Forecast for Peru is –7.1% for 2009 and 3.0% for 2010.

Peru: Effects of Global Recession and Future Prospects

by Margarita Benavides[9], Luis Enrique Povea[10], and Elliott Morss

Executive Summary

The credit freeze had a significant impact in Peru. The stock market fell almost 72% resulting in an asset loss of US$68 billion. That loss has recently been pared to 35% and a US$ loss of $33 billion. The reduction in export demand resulting from the global recession has had a greater impact. In 2009, investment is expected to fall less than 1%. Consumption growth will be lower – only 2.5% versus 7.9% in both 2007 and 2008. The unemployment rate in 2009 will increase to 8.5% by the end of the year. 1010 looks better, with GDP growth of 4.3%.

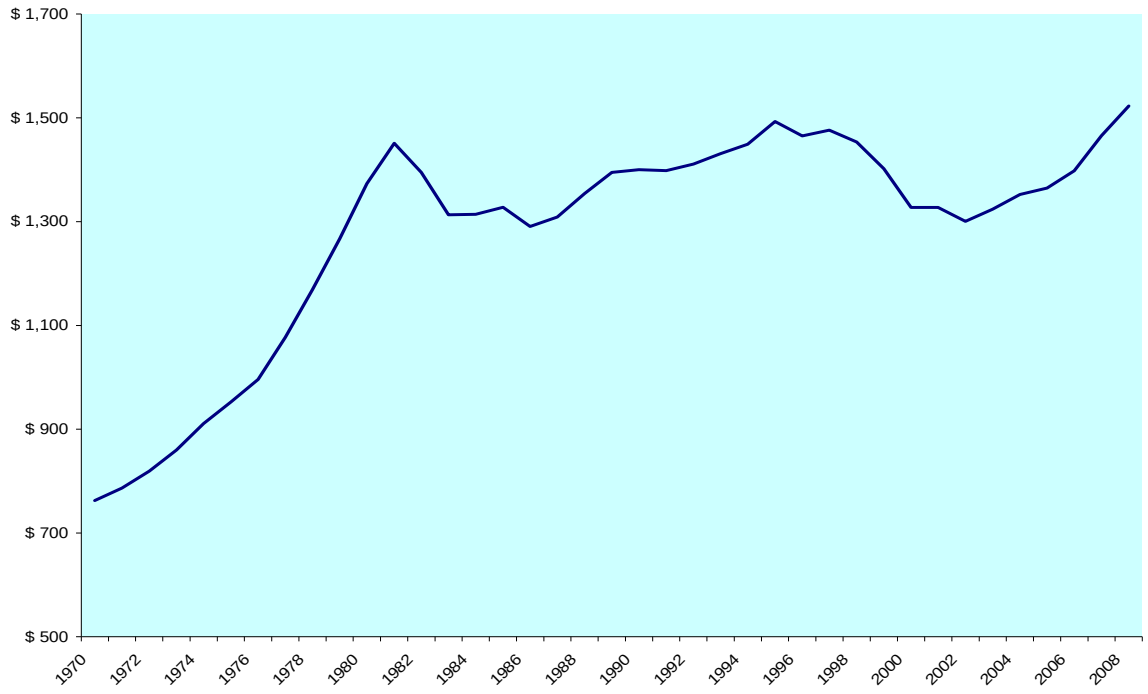
Introduction

After decades of slow and negative growth, with several institutional and political conflicts, the Peruvian economy has been on a steep growth path. Over the last decade, Peru has had more rapid economic growth than any other South American country. The average annual (geometric) rate of growth in GDP per capita in the 1999 - 2008 period was 3.8%, the highest in South America and one of the highest in the world. However, even with this growth, Peru has a GDP per capita of only $4,421 (current 2008 US$), one of the lowest in Latin America. The following graph shows the evolution of GDP per capita since 1970:

Graph 1: The Evolution of Real GDP Per Capita in Peru (1970-2008)

[9] MBA student, University of Palermo

[10] MBA student, University of Palermo



Source: CEPAL (2009)

Like Ecuador, Peruvian growth is highly correlated with commodity prices: higher commodities prices mean more rapid economic growth. The level of exports in 2008 was more than four times higher than the level of exports in 2000. The mining sector has been growing relative to other exports. In 2008, mining exports constituted 60% of total exports.

One of the challenges Peru faces in the coming years is to reduce corruption. The Corruption Perception Index (CPI) ranks Peru 75th in the world and fifth in South America.

Impact of the Credit Freeze

The credit freeze has had a dramatic impact worldwide. The world lost $36 trillion in stock market losses directly following the credit freeze. Globally, markets have recovered cutting stock losses to $22 trillion. Latin American stock markets have recovered dramatically. However, after being down almost 72% for a loss of $68 million, the Peruvian market is still down 35% for a loss of $32 million.

Impact of Declining Global Demand

Peru's leading exports are copper, gold, zinc, textiles and fish meal. They have been adversely affected by the global recession. As indicated in Table 1, they are down by 24% year to year, with mineral and petroleum exports the hardest hit.

Table 1. – Peru Export Performance (in mil. US$)

Exports	Oct 07-Sept 08	Oct08-Sept09	% Change
Total	32,993	25,089	-24.0%
Fish	1,779	1,655	-7.0%
Agricultural	586	640	9.3%
Mineral	19,947	14,813	-25.7%
Petroleum	3,000	1,576	-47.5%
Other	7,681	6,405	-16.6%

http://estadisticas.bcrp.gob.pe/index.asp?sFrecuencia=M

The Domestic Economy

Consumption growth slowed from an average of 7.9% in 2008 to 3.5% for 2009 as estimated in the LatinFocus Consensus Forecast (http://www.latin-focus.com/). Investment fell more sharply: it grew by 28% in 2008; it is estimated to be about the same in 2009. Overall, GDP growth fell from a growth rate averaging 8.3% over the last four years to an estimated growth rate of only 1.5% in 2009. However, LatinFocus estimates GDP will grow 4.3% in 2010.

External Sector

Peru has been running a significant positive trade balance over the last few years. But as Table 2 indicates, the global recession has cut into it as exports have fallen more rapidly than imports.

Table 2. – External Trade (in millions US$)

Item	2006	2007	2008	2009 (11 mos.)
Exports	23,830	27,882	31,529	23,719
Imports	14,844	19,595	28,439	18,996
Balance	8,986	8,287	3,090	4,723

http://estadisticas.bcrp.gob.pe/index.asp?sFrecuencia=M

Government Policies

The Peruvian Government has reacted to the global recession by launching a US$3.5 billion stimulus package. In addition, the Central Bank has kept its interest rate at an historically low 1,25%.

Partially as a result of the global recession and the government stimulus package, the government overall balance as a percent of GDP is expected to go from surplus of 2.1% in 2008 to a deficit of 1.8% in 2009.

Looking Ahead

The World Bank estimates World GDP will fall 2.9% in 2009 before recovering 2.0% in 2010. That means Global GDP will not get back to 2008 levels until 2011. Latin America overall will fall somewhat less in 2009 before increasing 2% in 2010.

Table 3. - World Bank Global GDP Growth Estimates

Region	2007	2008	2009	2010
World	3.8	1.9	-2.9	2.0
High Income	2.6	0.7	-4.2	1.3
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South Asia	8.4	6.1	4.6	7.0
India	9.0	6.1	5.1	8.0
East Asia and Pacific	11.4	8.0	5.0	6.6
China	13.0	9.0	6.5	7.5
Middle East and North Africa	5.4	6.0	3.1	3.8
Sub-Saharan Africa	6.2	4.8	1.0	3.7
Latin America and Caribbean	5.8	4.2	-2.2	2.0
Europe and Central Asia	6.9	4.0	-4.7	16

Peru's GDP is projected to grow by 3.0% in 2009 before growing by 4.3% in 2010.

Table 4. - World Bank Latin American GDP Growth Estimates

Country, Region	**1995-2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Brazil	2.4	3.7	5.7	5.1	-1.1	2.5
Mexico	3.6	4.8	3.3	1.4	-5.8	1.7
Argentina	2.3	8.5	8.7	6.8	-1.5	1.9
Venezuela	1.6	10.3	8.4	4.8	-2.2	-1.4
Colombia	0.7	6.8	7.5	2.5	-0.7	1.8
Chile	4.2	4.3	4.7	3.2	-0.4	2.7
Peru	**3.3**	**7.6**	**9.0**	**9.8**	**3.0**	**4.3**

LatinFocus (http://www.latin-focus.com/) collects projections from a wide variety of organizations. Its Consensus GDP Percent Change Forecast for Peru is 1.5% for 2009 and 4.3% for 2010.

Part of the reason for projected the strong rebound is attributable to the fact commodity prices are recovering rapidly. This is important inasmuch as copper and other commodities constitute a significant portion of Peru's exports.

The LatinFocus consensus is that exports will grow 11.4% in 2010 after falling 18.9% in 2009. The LatinFocus Consensus Unemployment Rate Forecast for Peru is 8.5% in 2009, falling to 8.2% in 2010.

Peru's external debt is 27% of its GDP is moderate while the Sovereign Spread it has to pay on borrowings is quite low by Latin American standards.

Venezuela: Effects of Global Recession and Future Prospects

by Diana Colmenares[11], Silvia Sandoval[12] and Elliott Morss

Executive Summary

The economy depends primarily on oil. Oil exports plummeted in 2009, but in recent months the oil price has recovered somewhat. However, major imbalances continue exist due to bad government policies. Inflation and the government budget deficit are very high. Venezuela is the riskiest Latin American country for foreign investors. But the government can continue in this manner because of tremendous oil reserves.

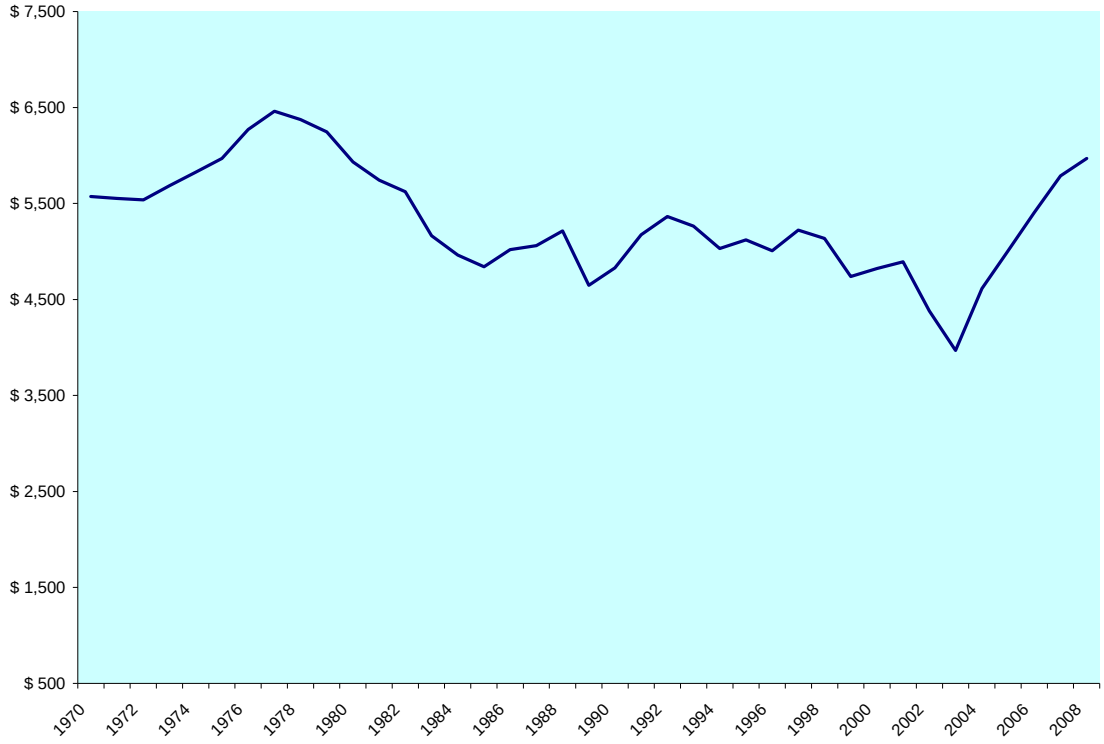
Introduction

Venezuela is the largest oil producer in Latin America. Its GDP per capita was above US$ 11,230 (in current 2008 dollars), the highest in South America. Venezuela's economy depends on the oil price: periods with high oil prices (1971-1977; 2002-2008) coincide with periods of high economic growth. The following graph shows the evolution of GDP per capita since 1970.

Graph 1: The Evolution of Real GDP Per Capita in Venezuela (1970-2008)

[11] MBA student, University of Palermo

[12] MBA student, University of Palermo



Source: CEPAL (2009)

Venezuela's economy is highly regulated. Hugo Chavez, the current president of Venezuela, has been increasing the role of the state in the economy over the last decade. For example, Venezuela nationalized international firms, closed independent media and reformed their National Constitution. Heritage Foundation ranks Venezuela 174 in the Index of Economic Freedom and Transparency International ranks Venezuela 162 in corruption level. Venezuela's sovereign interest spread is the second highest to Ecuador in Latin America.

Impact of Credit Freeze

The credit freeze has had a dramatic impact worldwide. $36 trillion was lost worldwide in stock markets directly following the credit freeze. Markets have recovered somewhat, cutting back stock losses to $22 trillion. Latin American stock markets have recovered dramatically.

While Venezuela still has a stock market, it is hardly significant. Because of exchange restrictions, companies prefer to list their stock on other markets. This means that Venezuelan stock market fluctuations had very little impact on incomes in Venezuela.

Impact of Declining Global Demand

According to LatinFocus, oil constitutes 93.5% of Venezuelan exports. Consequently the collapse in oil prices from a high of $140 in early 2008 to $30 in January 2009 had a devastating effect on exports. Oil prices have recovered some of their losses, but Venezuelan exports are still expected to fall 46% in 2009.

US/ Venezuelan Trade

For the first half of 2009, Venezuela exported US$ 12.1 billion to the US, a drop of 53% over the same period in 2008.

Domestic Economy

The fall in oil exports had wide ranging effects on the domestic economy. GDP will be down 2.1% in 2009. Consumption is expected to be off by 2.1% with investment falling by 6.7%. Unemployment is projected to increase in 2009 to 8.3% from 6.1% in 2008.

The government budget has been seriously affected by the loss in oil revenues. The deficit as a percent of GDP is expected to grow from 1.2% in 2008 to 4.8% in 2009.

Exchange Rates

Because of currency controls, there is a large gap between the government's pegged rate and the black market rate. In September, the black market rate for the Bolivar Fuerte was 5.55 per US$ while the official rate was exchange market the 2.15 Bolivar Fuertes for per US$. That means the official price is less than half the market price, an extremely serious imbalance. Spreads of this sort invite extensive black market profiteering.

In an attempt to sop up some of the excess demand for US dollars in Venezuela, Chavez issued US$3.0 billion in the sovereign debt bonds. The issue was oversubscribed, attesting to the internal demand to sell Fuertes for dollars.

Inflation

Inflation is expected to be 30% in 2009 and slightly higher in future years.

Foreign Investment

There will be little foreign investment as long as current policies are continued. Foreigners investing in Venezuela have little chance to get their money out. And the government regularly chooses which obligations to pay and which ones to ignore. The riskiness of Venezuela is reflected in its Sovereign Spread (bbs) of 884 in September, higher than any other Latin American country other than Ecuador.

The Future

Table 1 . – World Bank Latin American GDP Growth Estimates

Country, Region	1995-2005	2006	2007	2008	2009	2010
Brazil	2,4	3,7	5,7	5,1	-1,1	2,5
Mexico	3,6	4,8	3,3	1,4	-5,8	1,7
Argentina	2,3	8,5	8,7	6,8	-1,5	1,9
Venezuela	**1,6**	**10,3**	**8,4**	**4,8**	**-2,2**	**-1,4**
Colombia	0,7	6,8	7,5	2,5	-0,7	1,8
Chile	4,2	4,3	4,7	3,2	-0,4	2,7
Peru	3,3	7,6	9,0	9,8	3,0	4,3

Venezuela's economy is expected to continue down in 2010.

However, Venezuela exports about one billion barrels of oil annually. It has more than 50 billion barrels of oil reserves. This means Venezuela can live off its oil almost indefinitely under existing Chavez policies.

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