

Latin America shines: Is it for real this time?

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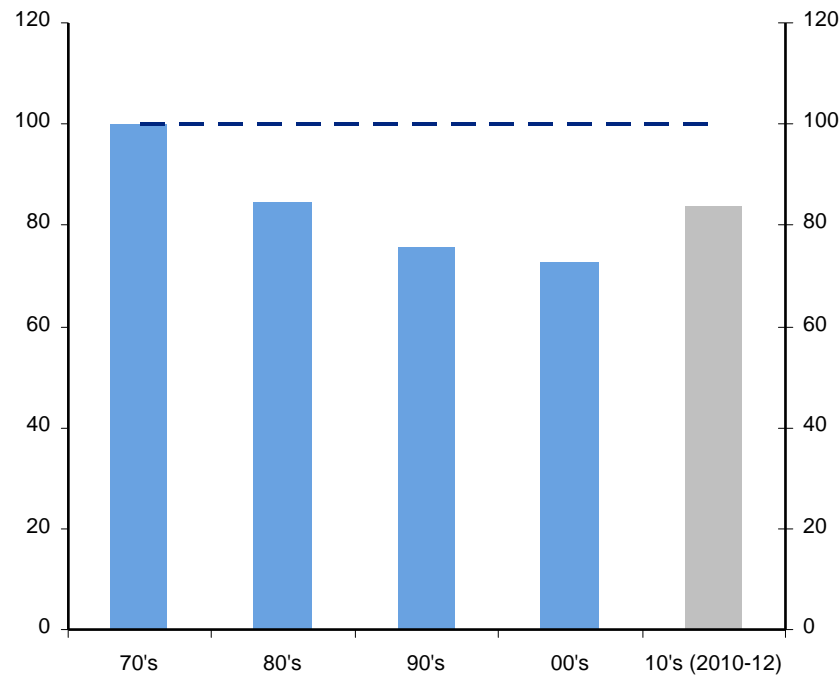
Latin America’s diverse realities

1. Latin America breaks with the past

After decades of disappointing economic performance, Latin American growth has resumed and the region has proven remarkably resilient to the largest financial crisis in half a century

LatAm, GDP per capita, relative performance to US, decade average. 70's=100

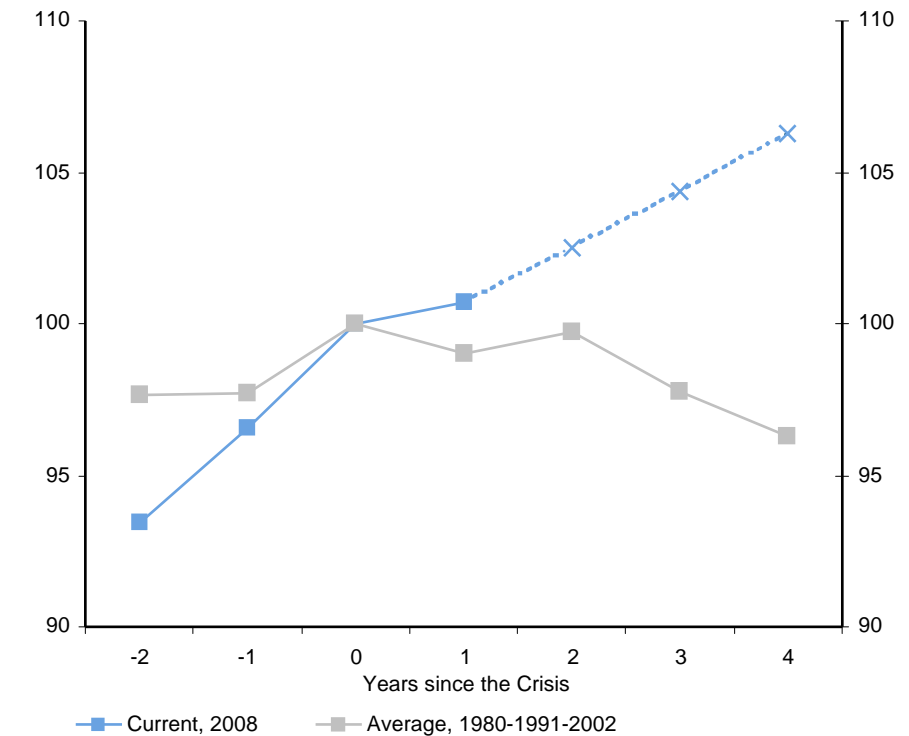
Source: BBVA Research



LatAm, GDP per capita, relative performance to US, crisis(*) comparison

(*) US recession in terms of GDP pc

Source: BBVA Research

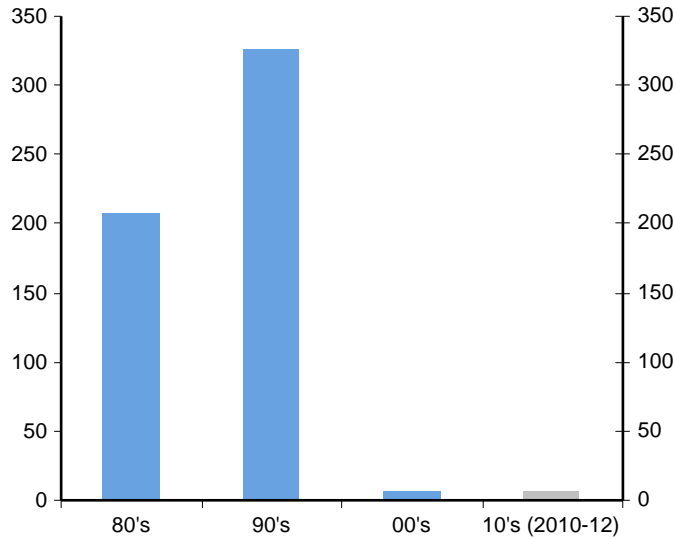


1. Latin America breaks with the past

While taming inflation in the late 90s, the region made sustained progress in external and public solvency over the years

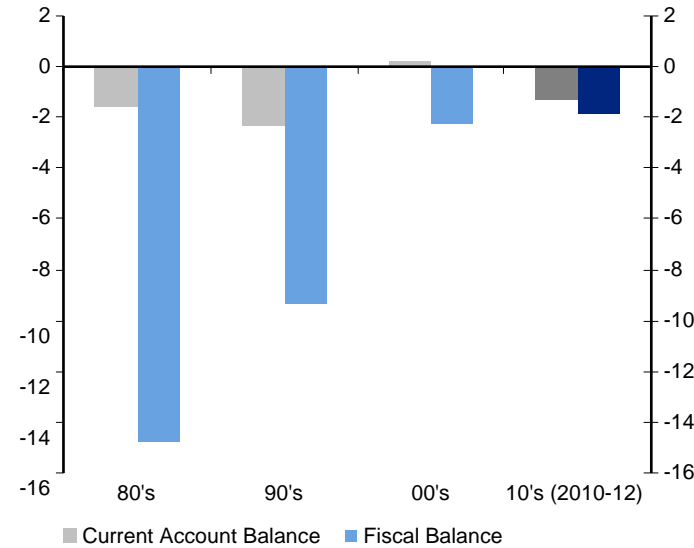
LatAm, Inflation
CPI, %, yearly average

Source: BBVA Research



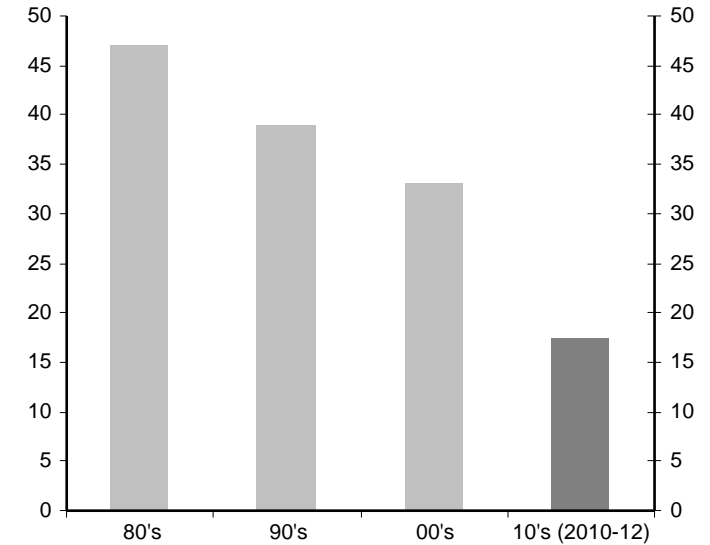
LatAm, External and Fiscal Balance
As % of the GDP

Source: BBVA Research



LatAm, External Debt
As % of the GDP

Source: BBVA Research



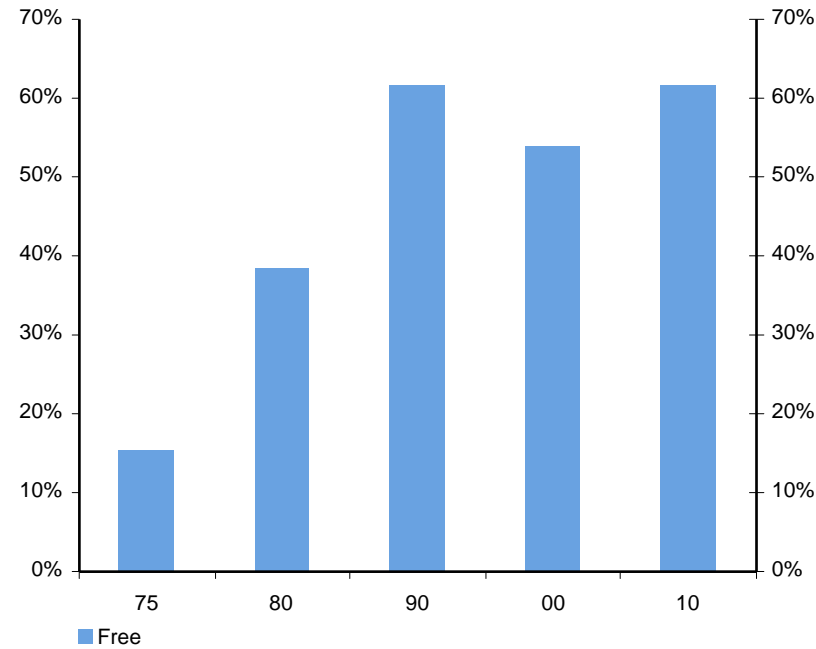
1. Latin America breaks with the past

Economic change has come along with institutional progress

LatAm, Political Freedom

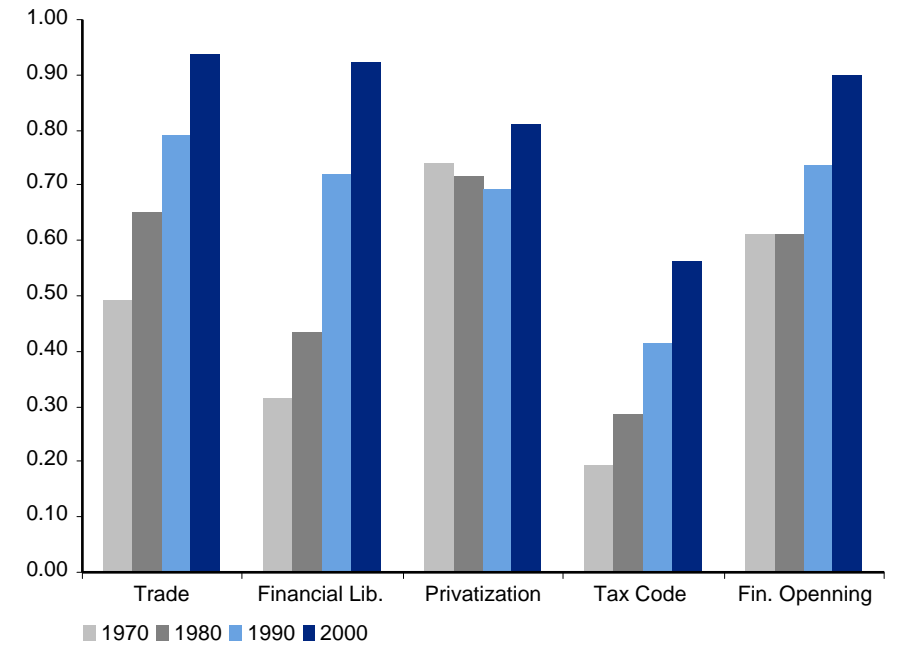
Freedom House Index, % of free countries

Source: BBVA Research with Freedom House data



LatAm, Economic reforms

Source: BBVA Research based on IADB and ECLAC data

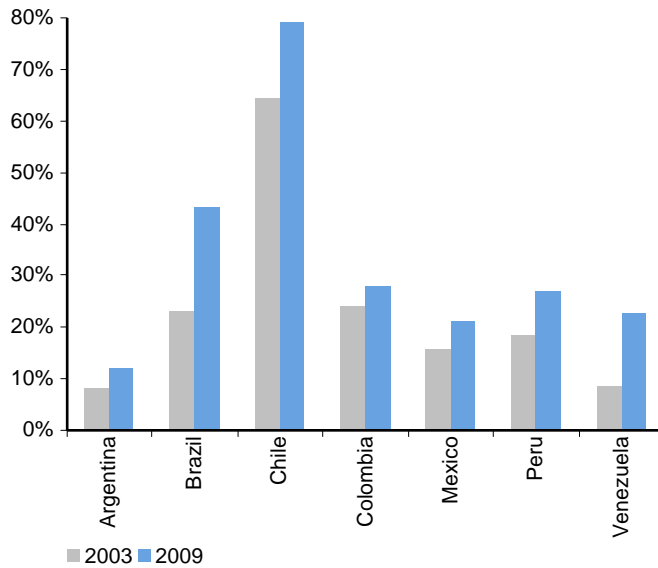


1. Latin America breaks with the past

The banking systems have been able to speed up credit supply, to cut NPL losses and to preserve high capital to assets levels

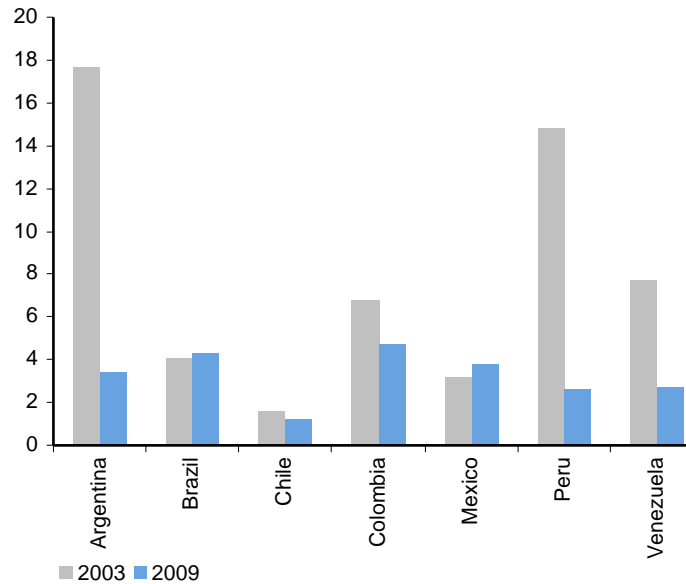
LatAm, Credit As % of the GDP

Source: BBVA Research, GSFR



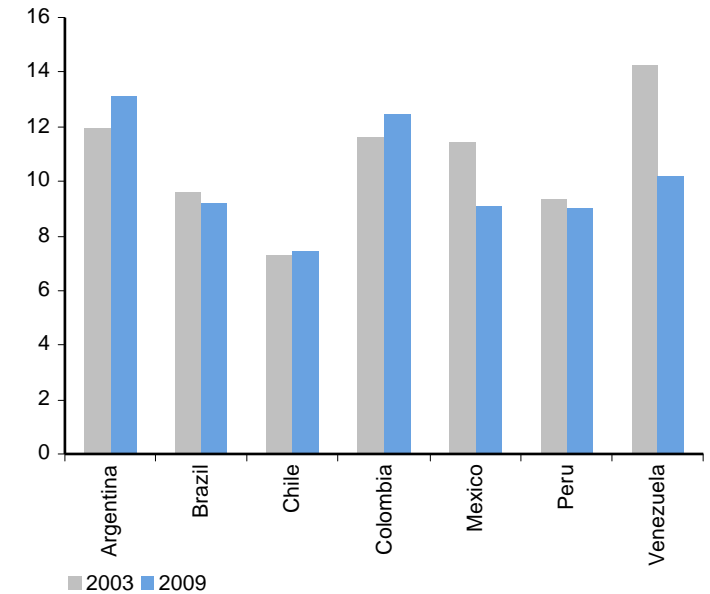
LatAm, NPL %

Source: BBVA Research, GSFR

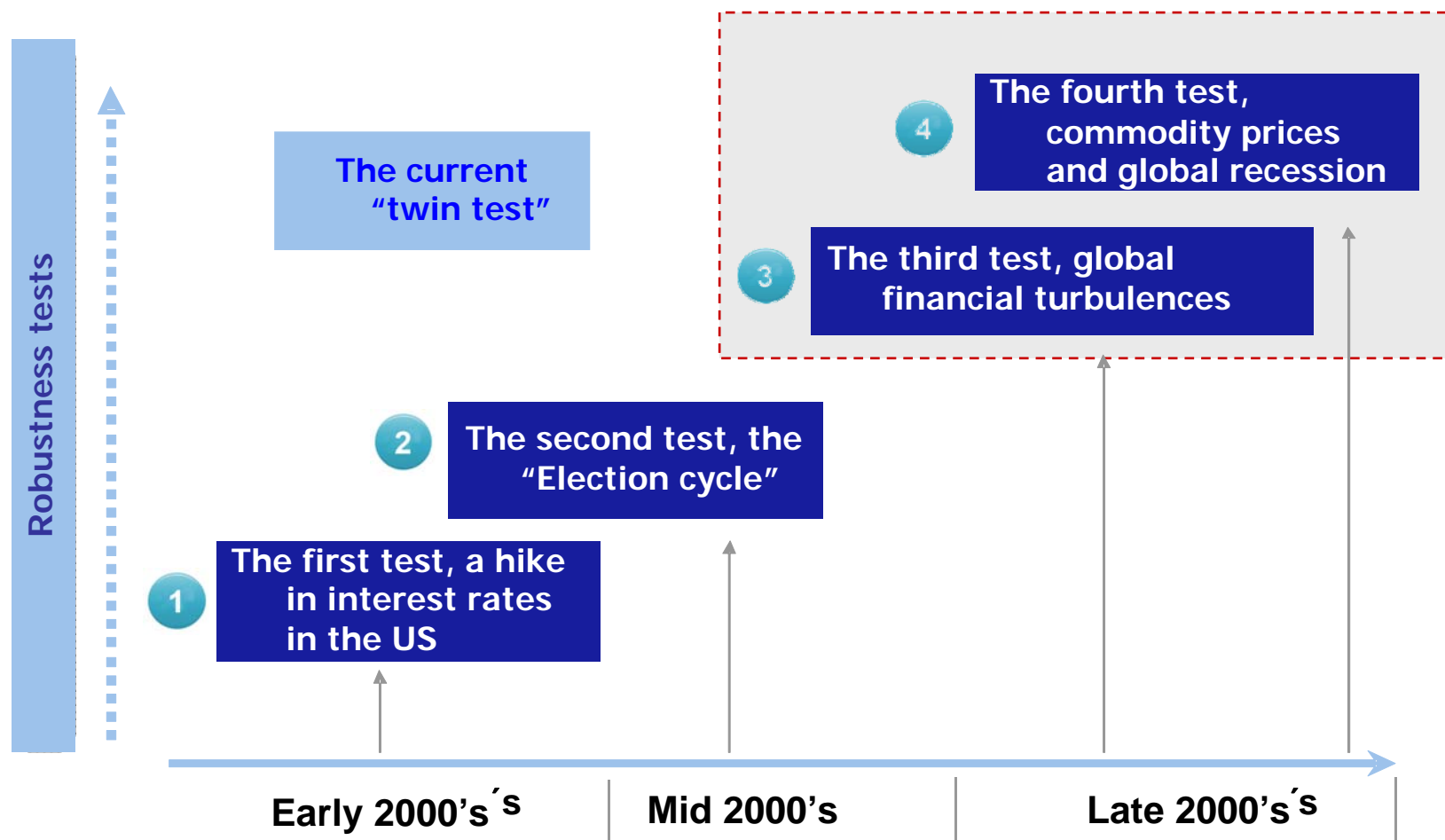


LatAm, Bank Capital to Assets %

Source: BBVA Research, GSFR



2. The region has passed a demanding sequence of tests since the 90s



2. The region has passed a demanding sequence of tests since the 90s

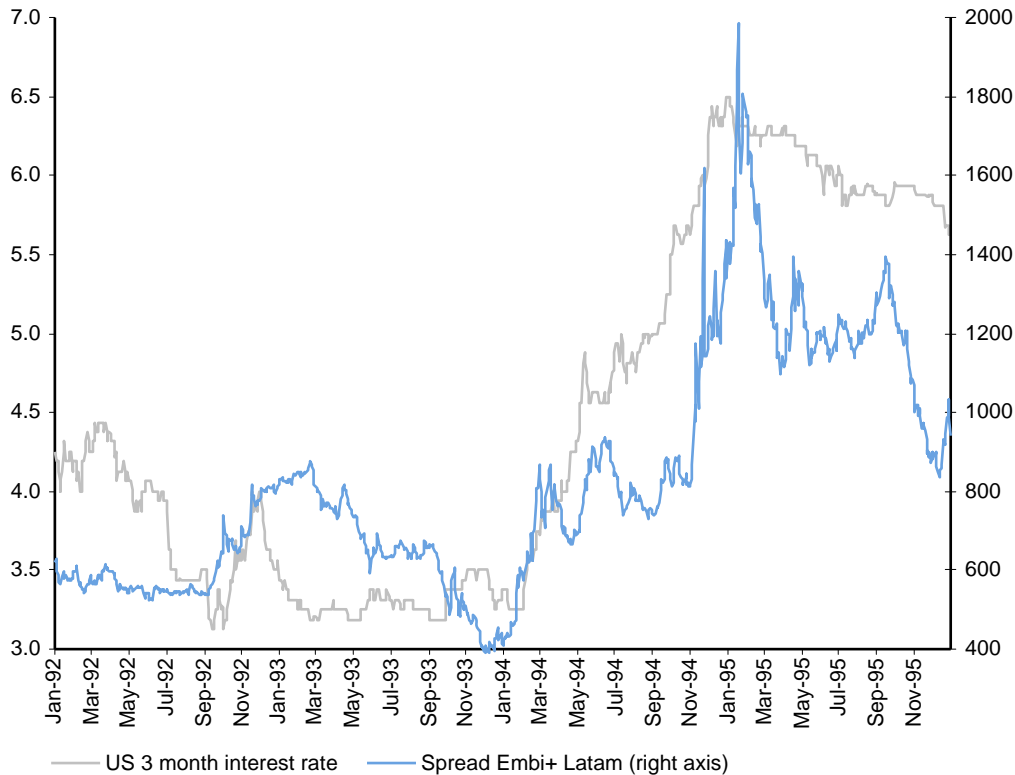
First test: increase on global interest rates

2.1. Response to an increase on global interest rates: decoupling based on enhanced financial soundness

1994

Spread EMBI Latam vs. US 3 month interest rate

Source: JP Morgan, Datastream and BBVA Research



2004

Spread EMBI Latam vs. US 3 month interest rate

Source: JP Morgan, Datastream and BBVA Research



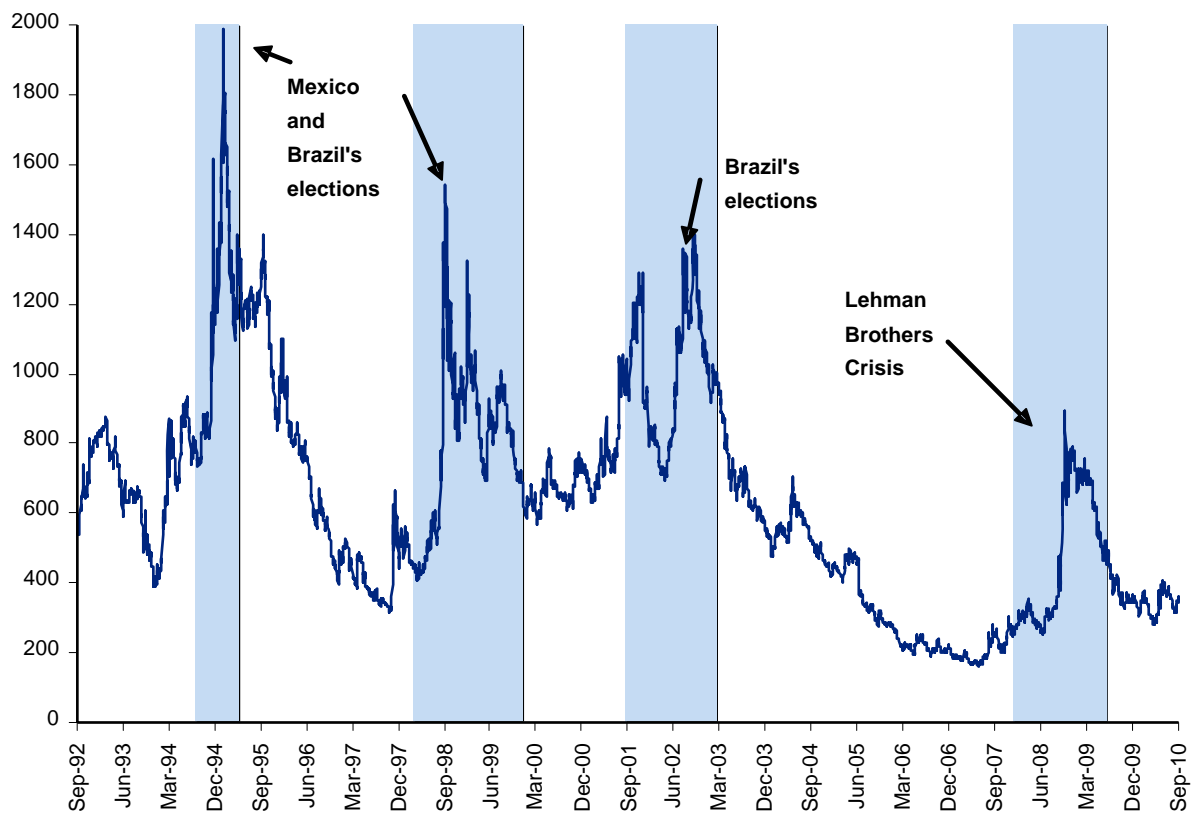
2. The region has passed a demanding sequence of tests since the 90s Second test: the “Election cycle”

2.2. Presidential elections are losing their negative impact on risk premium they used to have in the past

Uncertainty during Electoral Periods

Embi spread Latin America, bps

Source: JP Morgan and BBVA Research



2. The region has passed a demanding sequence of tests since the 90s

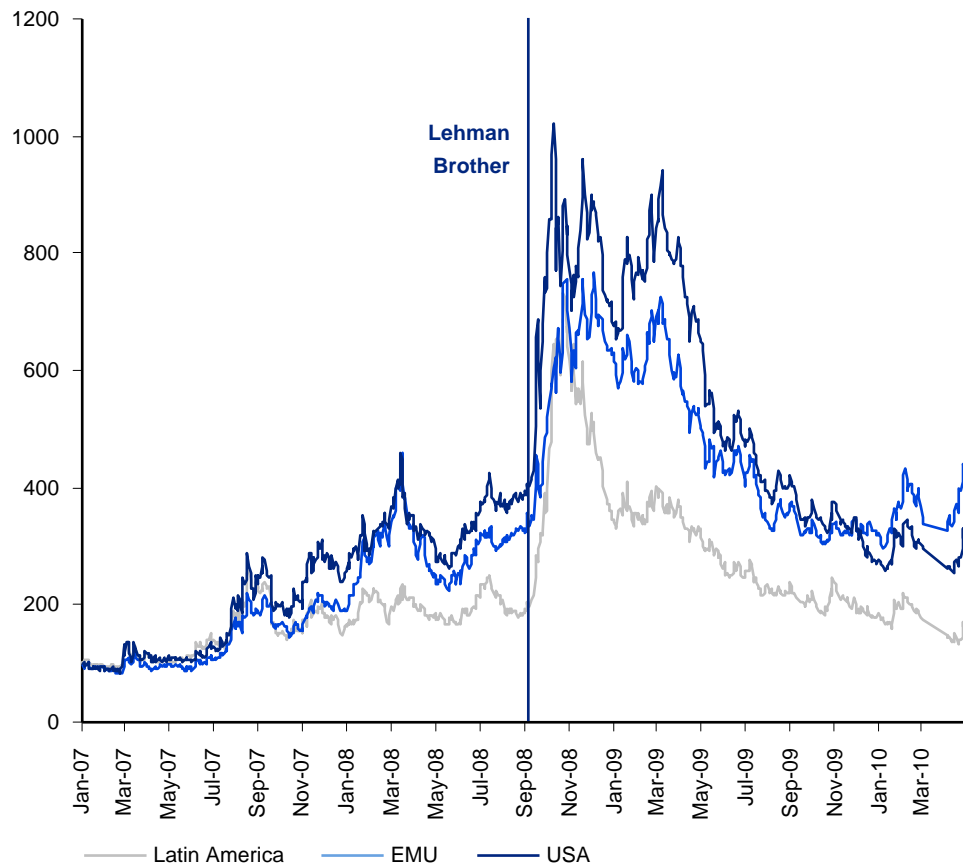
Third test: global financial turbulences

2.3. The region resisted the global financial crisis, and has come financially stronger: lower spreads and less volatility without net foreign outflows

BBVA Research Financial Stress Indicator

Jan07=100

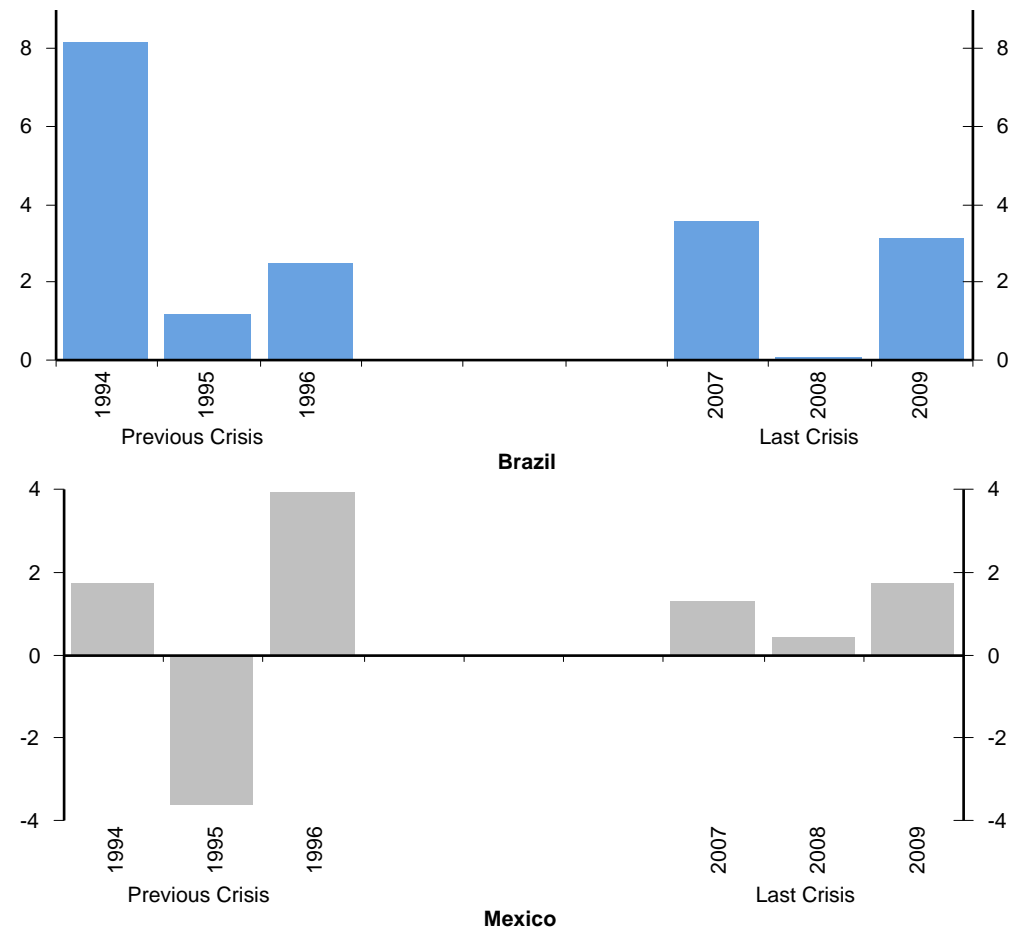
Source: BBVA Research



Portfolio Foreign Investment

Net Inflow, as % of GDP

Source: BBVA Research

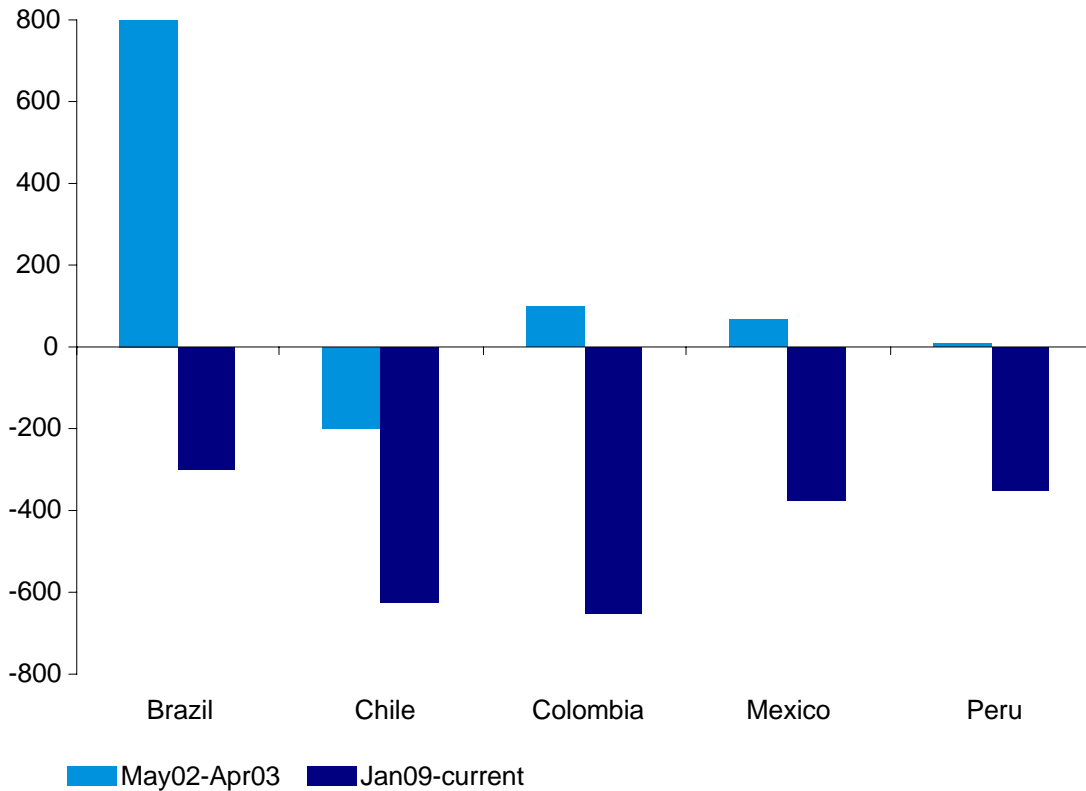


2.The region has passed a demanding sequence of tests since the 90s Fourth test: commodities prices and global recession

2.4. Economic resilience built across time allowed the implementation of countercyclical policies in most of the region, marking a major departure from previous negative shocks.

Interest Rate changes during crises (2002 compared to 2009)

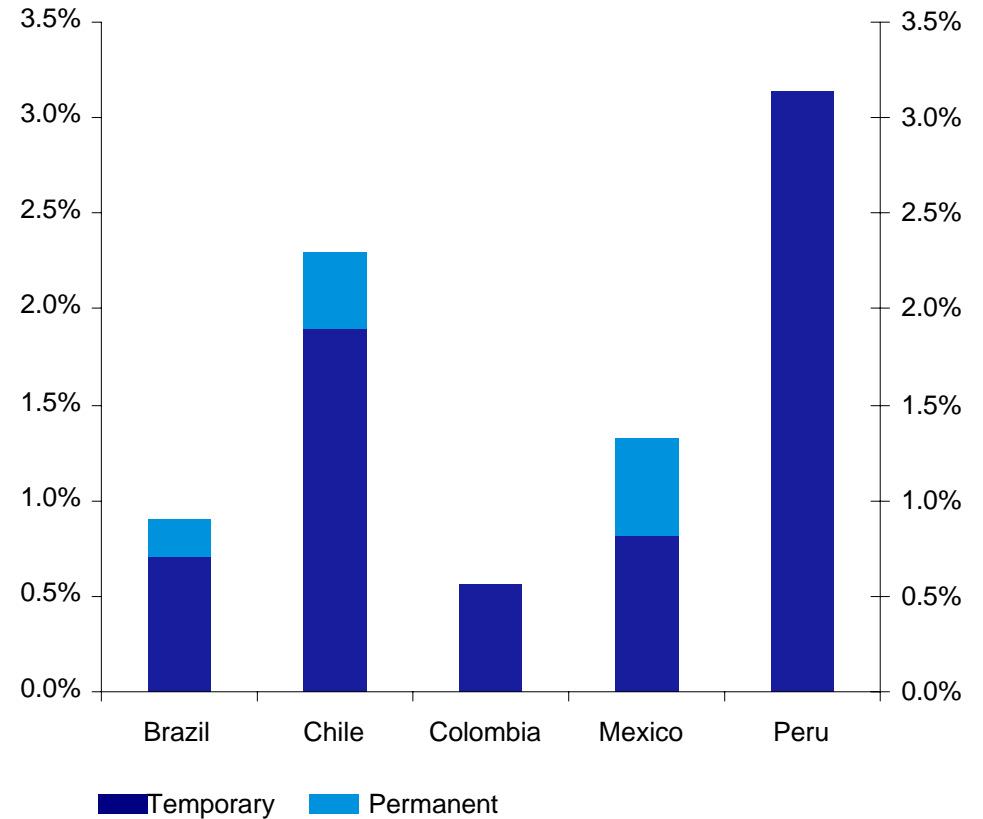
Source: BBVA Research



LatAm, Fiscal Stimulus

as % of the GDP

Source: BBVA Research

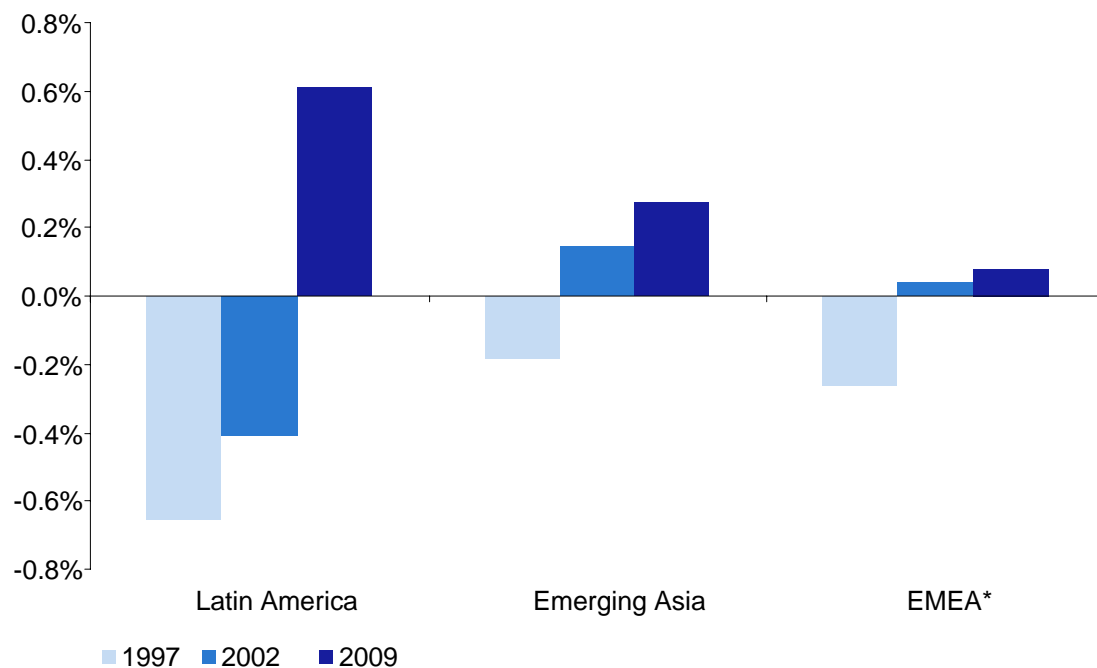


3. A bright future, if the right road is taken

A more open region, both to trade and investment, is benefiting from Asian dynamism

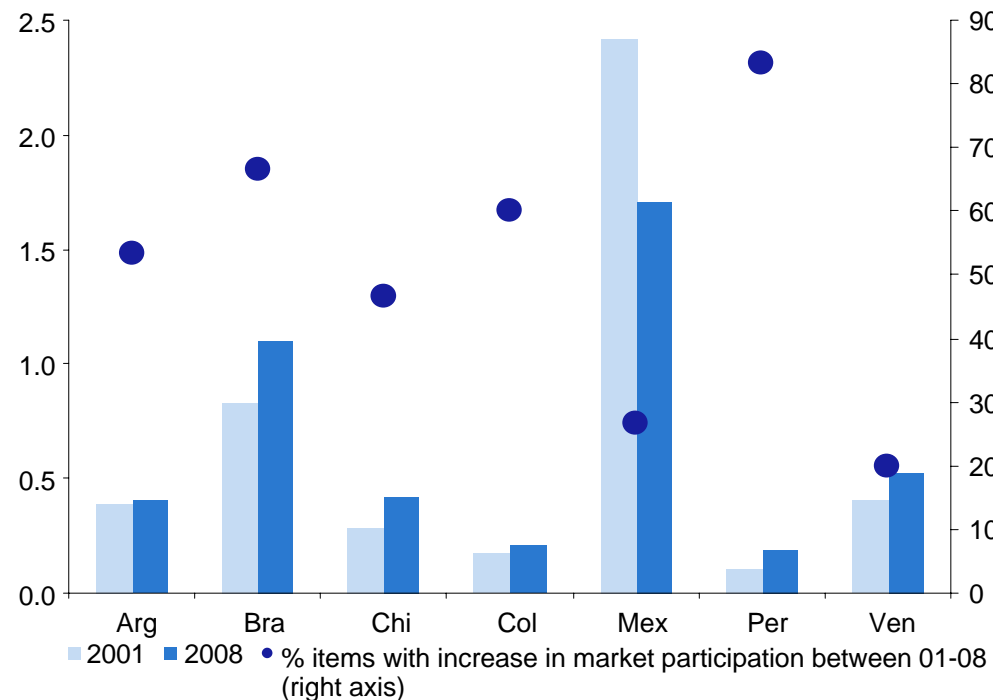
Emerging Markets Net Equity Inflows (Yearly Flows as % of Total Regional Assets)

Source: EPFR and BBVA Research. *EMEA: Emerging Europe, Middle East and Africa



Changes in markets participation*

Source: Unions Nations and BBVA Research. *Markets participation by main 30 items of export in each country



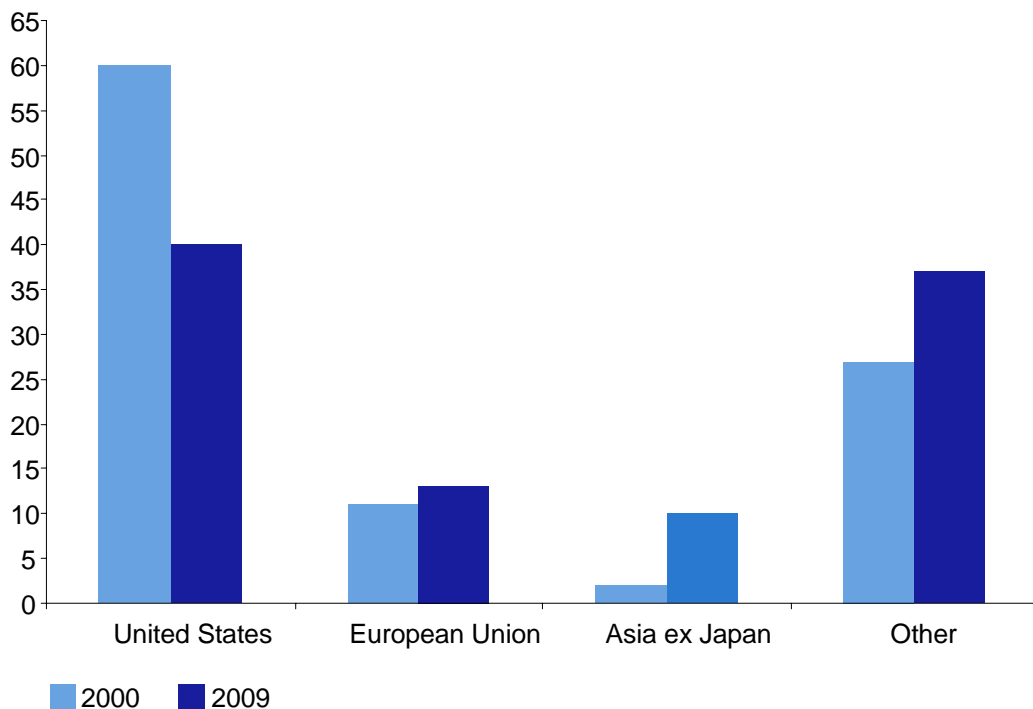
- **The region has increased significantly its trade integration with Emerging Asia during the last decade, mainly at the expense of traditional trade partners (U.S.).**
- **Gains in competitiveness show up in gains in market share in the main exports items**

3. A bright future, if the right road is taken

A more open region, both to trade and investment, is benefiting from Asian dynamism

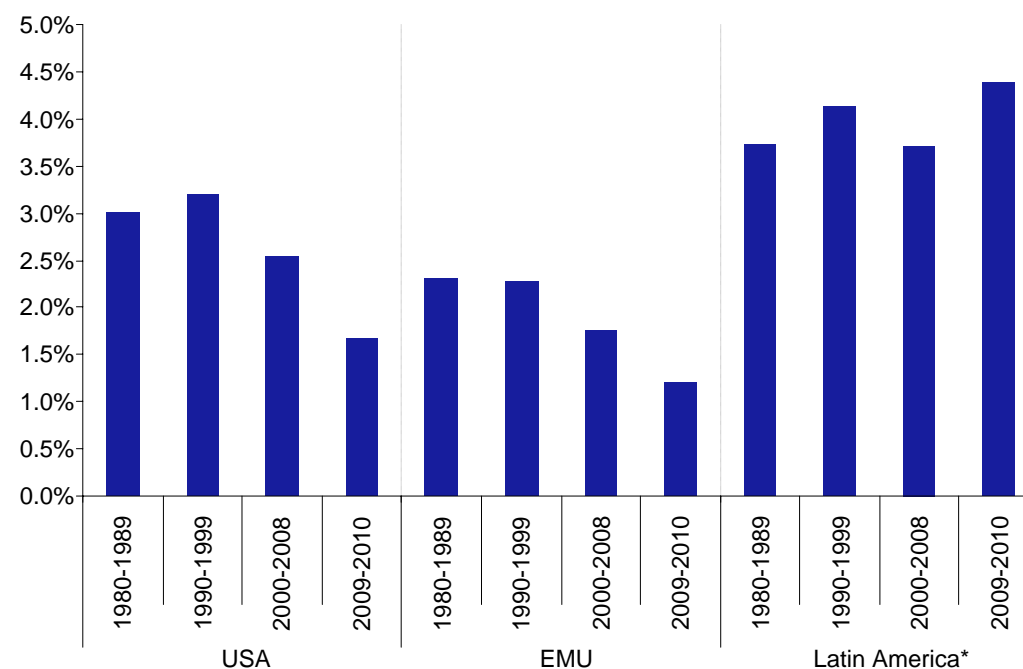
Exports Breakdown (% over total)

Source: MF and BBVA Research



Potential Output Growth (% yoy change)

Source: BBVA Research. *Latin America: Arg, Bra, Chi, Col, Mex, Per and Ven.



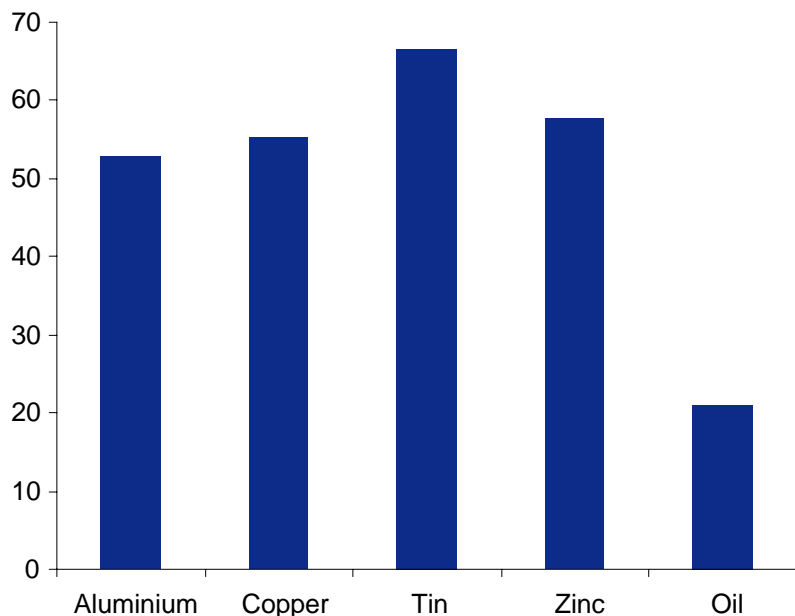
- **The region has increased significantly its trade integration with Emerging Asia during the last decade, mainly at the expense of traditional trade partners (U.S.)**
- **In the coming decade we expect major impulse from Asia due to urbanization and industrialization, taking advantage of low labor costs and growing integration into global markets**

3. A bright future, if the right road is taken

Asian development is putting pressure on most commodity markets

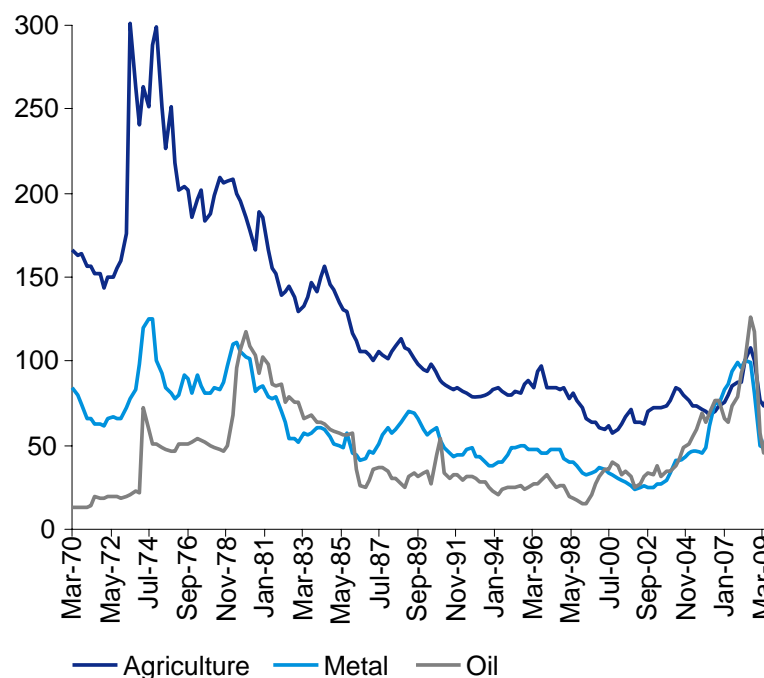
Asia: share in world consumption of raw materials (%)

* As of 2008
Source: BBVA Research, WMS and IEA



Long-term trends in commodity prices (US cents 2009/pound)

Source: IADB (2010) and BBVA Research



- **Rising incomes, urbanization and fast industrialization in China put a lot of pressure on all kind of commodity markets. India is just at the beginning of a similar process**
- **Commodity prices have been resilient to the financial crisis. A new cycle of high prices seem to be starting, fueled by fast Asian development. There is a similarity with the post WWII reconstruction in Europe and Japan**

3. A bright future, if the right road is taken

	GDP (% y/y)			
	2003-2008*	2009	2010	2011-2012*
Argentina	8.2	-2.1	6.5	4.2
Brazil	4.2	-0.2	6.9	5.0
Chile	4.7	-1.5	4.8	5.2
Colombia	5.0	0.8	4.2	5.1
Mexico	3.1	-6.6	4.5	3.5
Peru	7.0	0.9	6.8	5.9
Venezuela	7.3	-3.3	-3.8	1.3
LATAM	4.7	-2.4	5.2	4.3

*average

	Inflation CPI (% y/y, average)			
	2003-2008*	2009	2010	2011-2012*
Argentina	9.5	6.3	10.4	12.0
Brazil	7.0	4.9	5.2	4.8
Chile	3.9	0.4	1.5	2.9
Colombia	5.8	4.2	2.4	3.1
Mexico	4.3	5.3	4.5	3.8
Peru	2.9	3.0	1.6	2.4
Venezuela	22.1	28.6	31.6	30.3
LATAM	7.1	6.4	6.7	6.6

*average

	Current Account (% GDP)			
	2003-2008*	2009	2010	2011-2012*
Argentina	3.3	3.6	1.4	0.4
Brazil	0.6	-1.6	-2.7	-3.7
Chile	1.7	2.5	0.9	-3.7
Colombia	-1.8	-2.0	-2.1	-1.9
Mexico	-0.8	-0.6	-1.2	-2.1
Peru	0.1	0.1	-0.9	-1.7
Venezuela	13.3	2.4	11.2	11.2
LATAM	1.2	-0.2	-0.7	-1.6

*average

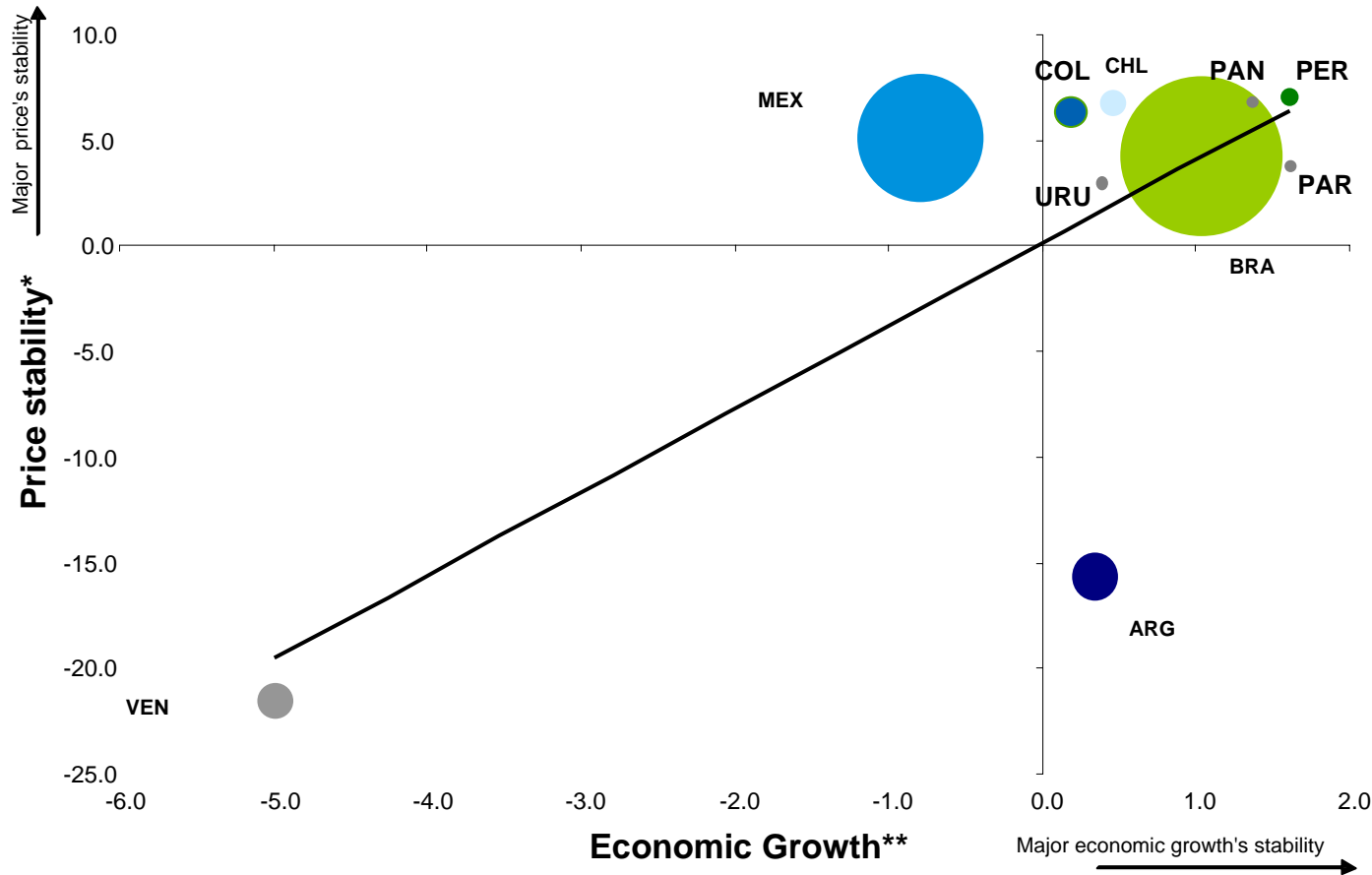
	Fiscal Balance (% GDP)			
	2003-2008*	2009	2010	2011-2012*
Argentina	1.5	-0.6	-0.3	-1.3
Brazil	-2.9	-3.3	-2.8	-2.0
Chile	4.7	-2.1	-1.5	-0.6
Colombia	-3.3	-3.8	-3.9	-3.1
Mexico	-1.5	-2.7	-2.3	-1.8
Peru	0.3	-1.9	-1.4	-0.6
Venezuela	-0.5	-5.4	-0.7	0.1
LATAM	-1.4	-2.9	-2.2	-1.7

*average

4. But Latin America is not one entity: there is diversity in the region

Diversity in the region (GDP and CPI forecast)

Source: BBVA Research. : *Price Stability: CPI 2010-2012 (spread % y/y average latam vs. average country). **Economic Growth: GDP 2010-2012 (spread % y/y average country vs. average latam) Bubble size: Total GDP based on purchasing-power-parity (PPP).



- The “two giants” (BRA, MEX)
- **Medium Size Emerging South America:** medium size countries combine good performance both in inflation and growth (CHL, COL, PER)
- The “heterodox” countries: most countries have achieved low inflation, but it remains a problem in ARG and VEN

4. The two giants

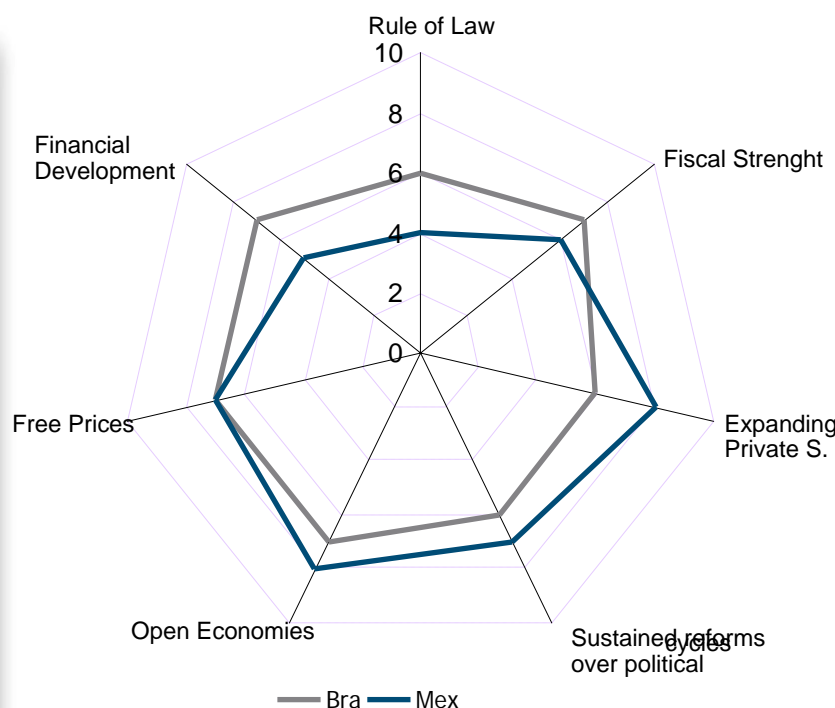
Brazil and Mexico have become reliable economies, but they face major challenges to step up growth

Strengths

- Reliable policies, large market size and commitment with market oriented economies
- Open economies in trade and financial areas
- Significant rise of middle classes has become a source of stability and economic progress
- Stronger fiscal and monetary institutions
- Financial system

The Two LatAm Giants

Source: WB, WEF and BBVA Research. 1 (negative valuation) and 10 (positive valuation). Rule of Law: World Bank Ranking 08, Fiscal Strength: low levels in CDS Sept, Financial Development: World Economic Forum Ranking 09 and rest of indicators: BBVA Research teams assessment.



Challenges

- Both of them: to reduce informality, create jobs, develop domestic financial markets and to further increase middle class weight
- Mexico: enhance rule of law and introduce reforms to foster competition and reduce fiscal vulnerabilities
- Brazil: Simplify tax structure to promote competitiveness, gain more credibility to reduce interest rates and avoid excessive interference of the public sector in economic activities

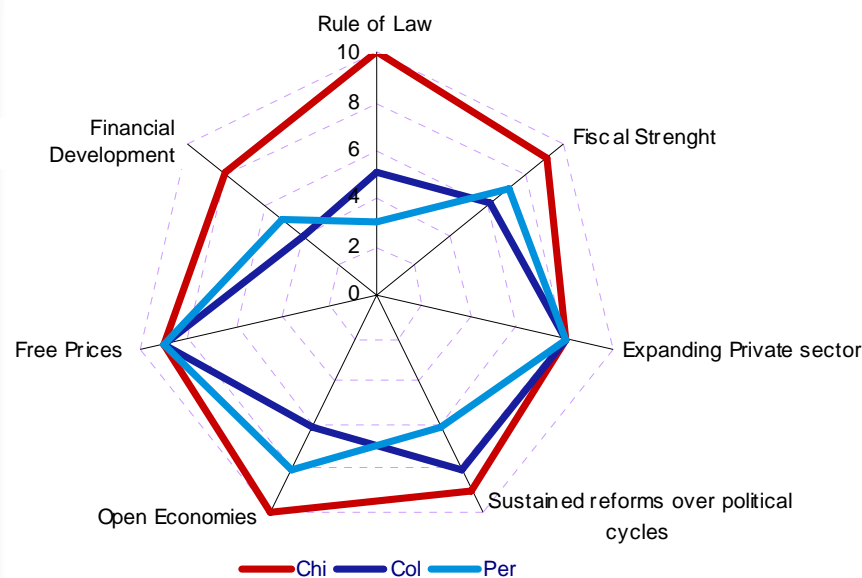
4. Medium Size Emerging South America

Strengths

- Consolidated democracies
- Growing importance of emerging middle classes with a positive impact on markets as well on politics
- Stronger economic institutions
- Economic stability
- Increasingly open economies with growing ties with Asia
- Favorable climate for FDI
- Rich in natural resources
- Financial system

Medium size Emerging South America

Source: WB, WEF and BBVA Research. 1 (negative valuation) and 10 (positive valuation). Rule of Law: World Bank Ranking 08, Fiscal Strength: low levels in CDS Sept, Financial Development: World Economic Forum Ranking 09 and rest of indicators: BBVA Research teams assessment.



Challenges

- Still large informal sectors
- Low quality of educational system might pose a problem in the medium term
- Coverage of Social Security, and pending issues in governance in Colombia and Peru
- Fiscal revenues too dependent on few natural resources rents (Chile and Peru)
- Fiscal vulnerability in Colombia

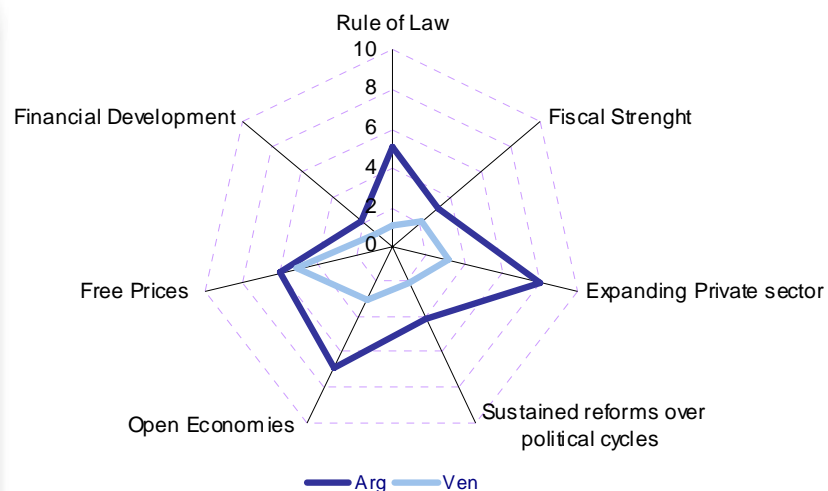
4. The “heterodox countries”

Strengths

- Rich in natural resources
- Very low asset prices
- Argentina is still the leading country in the region in terms of quality of human capital and has a sophisticated and well connected financial market
- Large stock of assets held abroad by the private sector could come back if conditions change
- Democratic institutions still in place in both countries
- Financial system

The Heterodox countries

Source: WB, WEF and BBVA Research. 1 (negative valuation) and 10 (positive valuation). Rule of Law: World Bank Ranking 08, Fiscal Strength: low levels in CDS Sept, Financial Development: World Economic Forum Ranking 09 and rest of indicators: BBVA Research teams assessment.

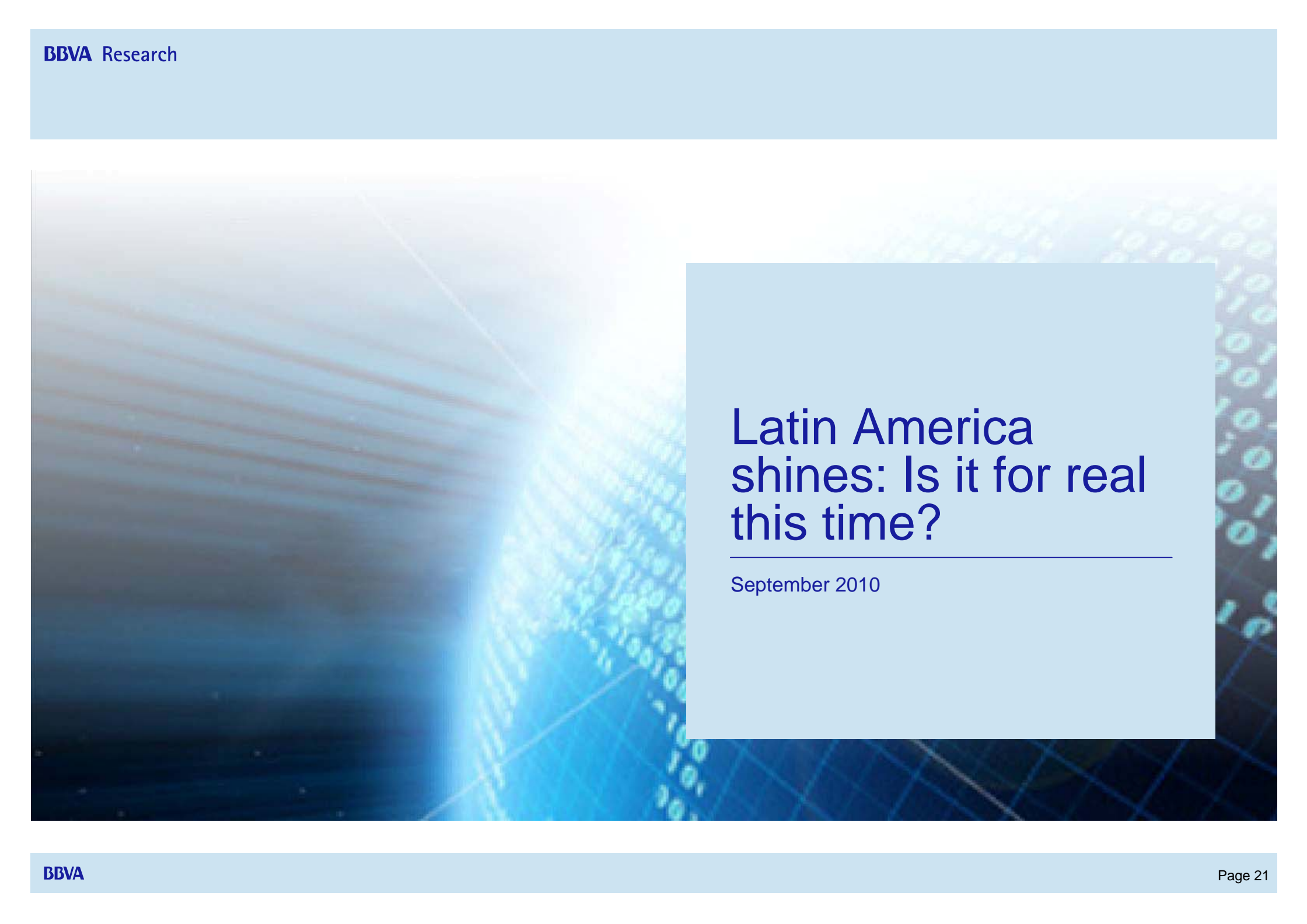


Challenges

- Fiscal and external accounts remain very vulnerable
- Decision making process largely arbitrary and unpredictable discourage investment
- Large relative price distortions and repressed inflation
- Growing weakening of economic and political institutions
- Both are rich in energy resources but power supply has become a constraint to economic growth

Closing Messages

- Latin America has changed, both politically and economically
- A great deal of macroeconomic stability has been achieved: inflation has been conquered in most countries and fiscal discipline is now widespread
- This, together with external factors such as growing ties with Asia and related benign terms of trade, have contributed to sustained growth in the region
- The region has passed major economic and political tests, and is emerging stronger from the current financial crisis: higher credit ratings and lower risk premiums are evidence of that
- There have been a few setbacks, but we believe they will be temporary
- Major challenges remain, but growing middle classes with an stake in the good performance of the economic system is a major source of stability
- There is room for further increases in potential growth in the case extra microeconomic reforms and more investments in infra-structure and education materialize
- We are convinced that this time is for real: Latin America is entering a path of sustained progress



Latin America shines: Is it for real this time?

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