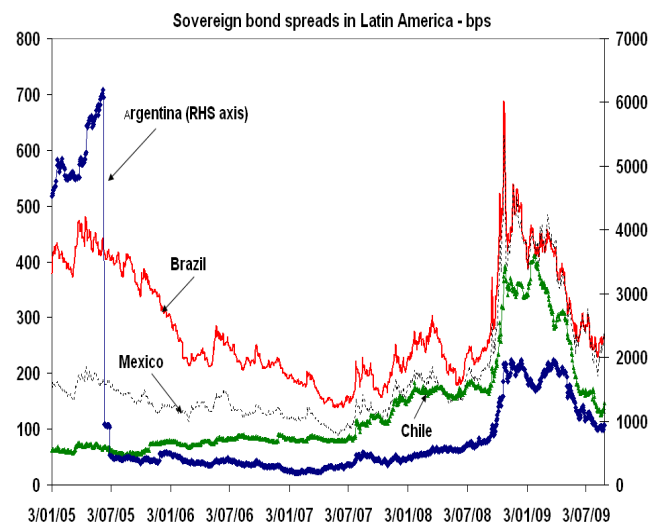


Recession Hits Latin America But No Crisis

Key trends

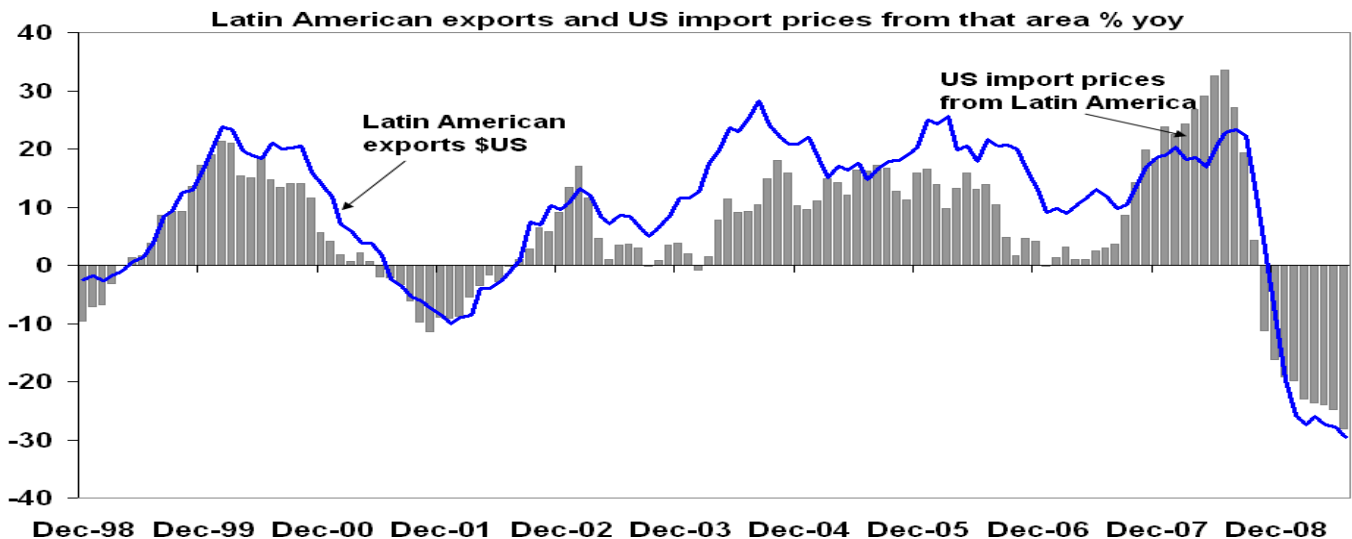
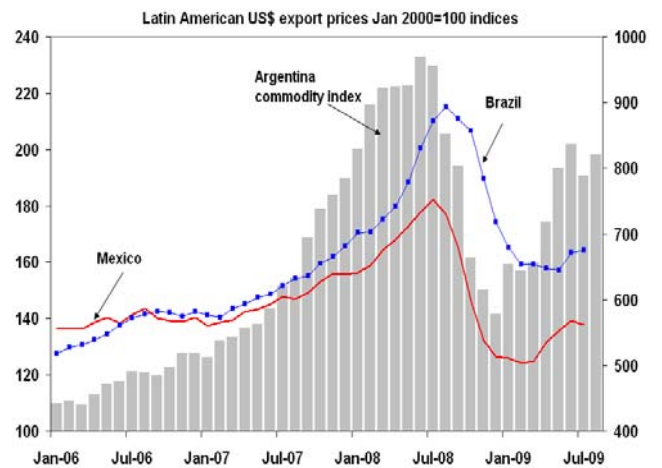
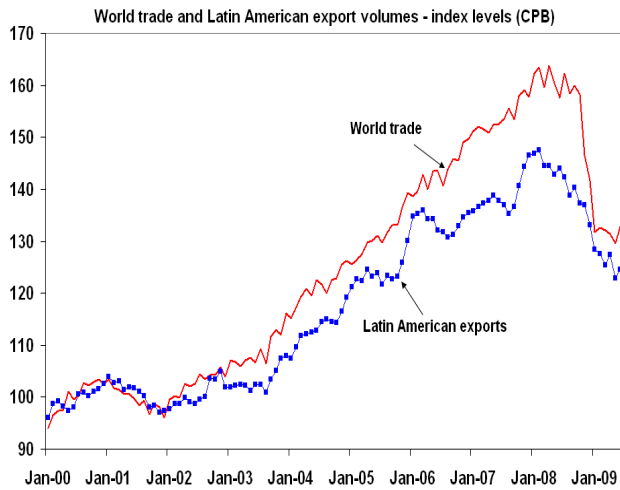
- Latin America has been hit by a series of very adverse economic shocks that have driven the region into recession - but the downturn is not as bad as would have been the case before. Sharp declines in commodity export prices, higher foreign debt funding spreads on sovereign bonds, depressed export markets and lower remittances from emigrants to the US have combined in late-2008/early-2009 to produce the worst external environment for the region since the debt crisis of the early-1980s.
- We expect regional GDP to fall by around 2% this year, broadly in line with the 1½% drop in global output. Next year GDP should rise by over 4%, partly reflecting the bounce-back in Mexico from the effects of the flu-related shutdowns in 2009. This is actually a good performance for a region that has a record of full blown crises when the world enters recession. The steep decline in Mexican output due to the swine flu epidemic has worsened the figures - without that the recession would probably have seen output fall by 1% to 2%.
- The reason why much of Latin America has fared better in this world recession is because the region went into the downturn in far better shape than before. Economies like Brazil have conducted very sensible economic policies, reducing their vulnerability to sudden stops of foreign capital and lower export commodity prices. They also had more scope to boost demand to offset weaker export earnings.



Global recession hits the region

The global recession has hit Latin America hard with a sharp fall in regional export volumes and much weaker commodity export prices. The volume of world trade fell by over 20% through the latter half of 2008 and the early months of this year - a fall comparable to that seen going into the 1930s depression. Since then, world trade has stabilised but at a very low level. Latin American exporters were not immune from this shock but the magnitude of the drop in export volumes has not been as large - around 15%.

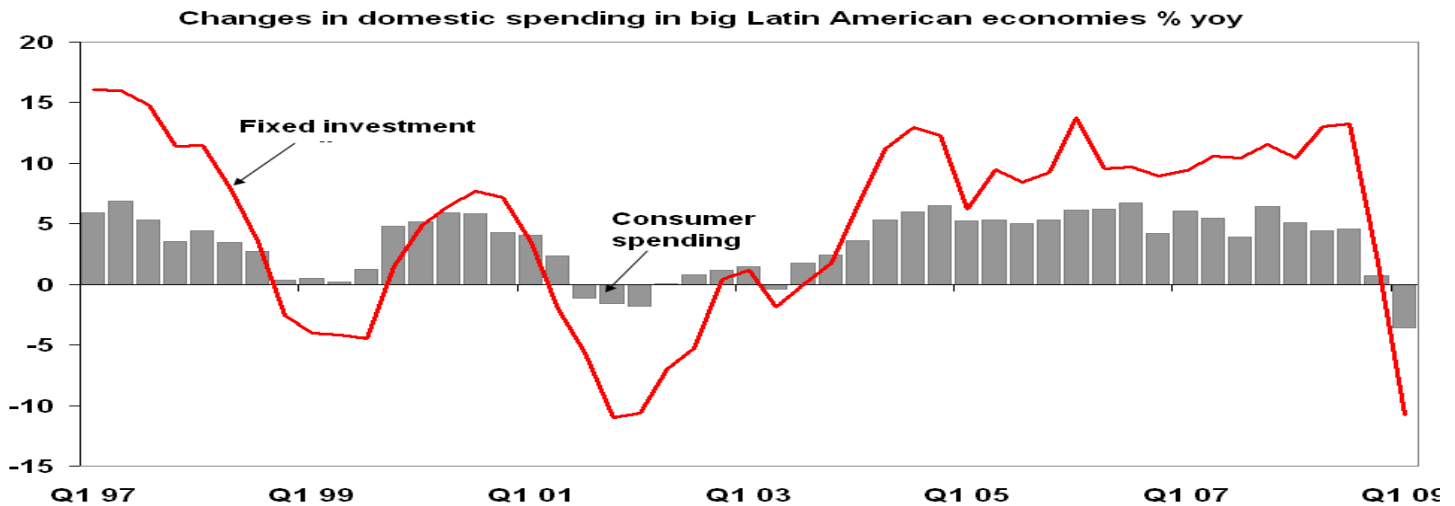
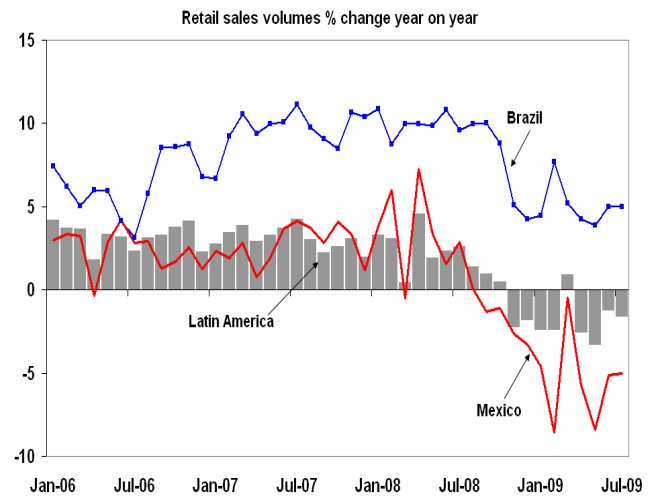
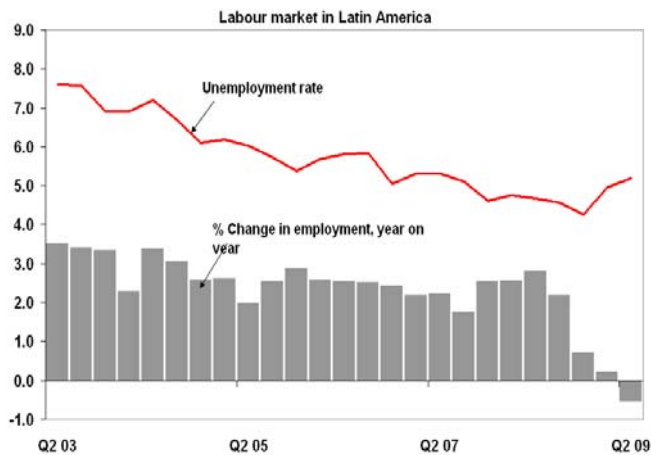
As the Latin American economies have a high degree of dependence on exports of commodities, they have been hit hard by the fall in global primary product markets. The Economist index of commodity prices fell by 45% between mid-2008 and early-2009 and that decline fed through into much lower returns for Latin American exporters. World prices for a basket of Argentinian commodity exports almost halved through the latter half of 2008 but they have since recouped some of those losses to be down by around one-third. The impact of the decline in commodity markets on export earnings has been severe with US\$ earnings down by around one-third yoy in mid-2009 and a similar drop in US import prices from Latin America.



Domestic demand falls

The increased difficulty in accessing foreign capital combined with the drop in export earnings has impacted adversely on incomes and domestic demand across the region. Although unemployment has not risen particularly sharply - unlike the US, Japan or Western Europe - the labour market has suffered. Employment growth was running at around 3% annually in the 5 years before the onset of the crisis but that fell to practically nothing by early-2009 and by mid-year the number of jobs was running below year-earlier levels. Clearly, therefore, the jobless numbers under-estimate the severity of the labour market stress with many workers leaving the official workforce rather than appearing in the unemployment register.

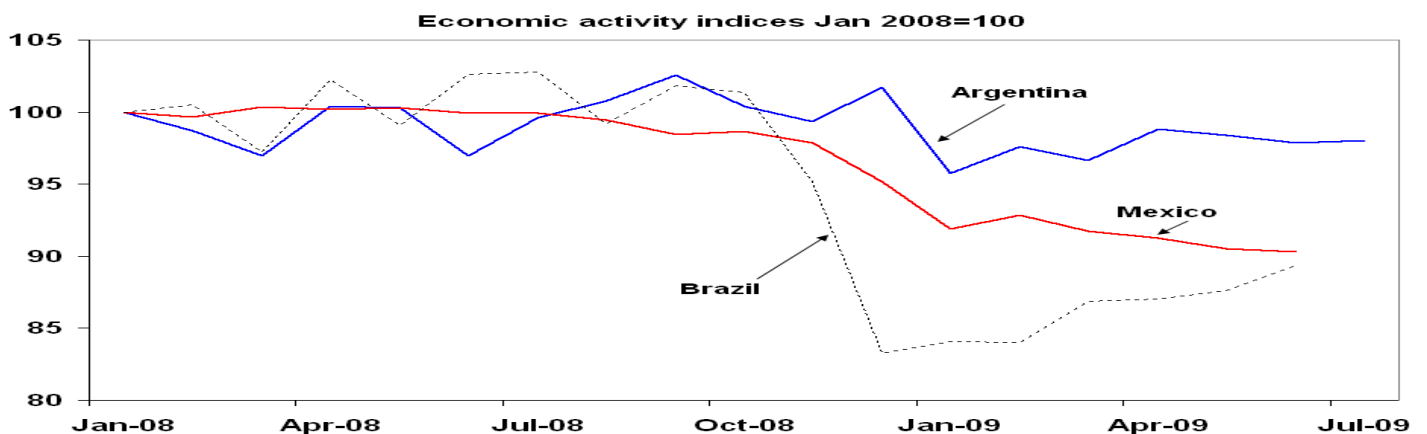
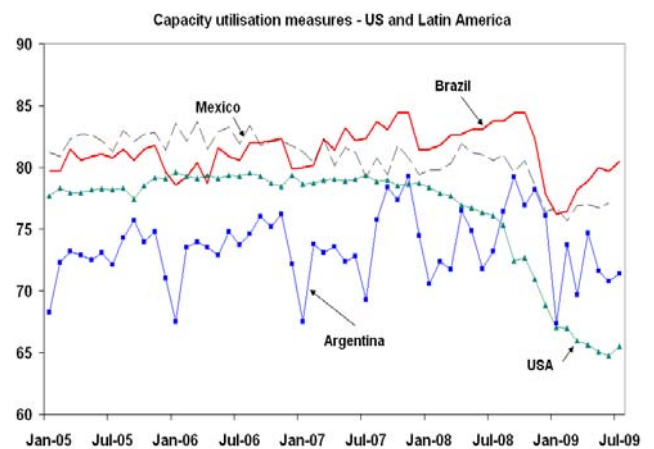
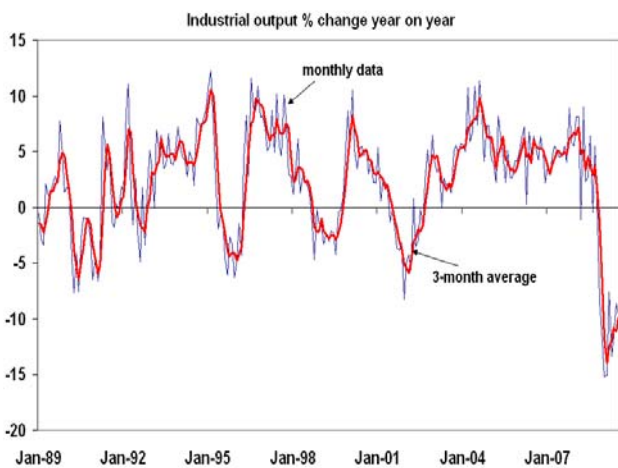
Although there is not much data on aggregate household income, it seems likely that the downturn in employment levels has cut spending power. Consumer spending has clearly suffered with the national accounts across 4 big Latin American economies (Chile, Argentina, Mexico and Brazil) showing a reduction of almost 3½% yoy in real consumer spending. There is, however, a very marked variation between economies with the impact of the swine flu on Mexican economic activity being very obvious. In early-2009, Mexican real consumer spending was down by almost 10% yoy, Chilean figures were slightly negative but Brazil and Argentina still had growth of around 1½% yoy. The retail trade figures show the persistence of these differences between individual economies persisting into mid-2009. Investment spending has also fallen heavily.



Output stabilises in mid-2009

The monthly industrial output numbers give the most timely indication of output trends across the region. These showed that output was generally maintained across the region until October 2008 but then fell sharply through the closing months of last year and into early-2009. Since then, output seems to have recovered slightly but it was still down by around 10% yoy in July. This weakness in industrial production is also found across all of the main economies - there is far less differentiation between them than was true for consumer spending. Predictably, industrial output was down the most in Mexico (by 11% yoy) but it was also down by 10% yoy in Brazil, 9% yoy in Argentina and 7% in Chile.

Broader indices of economic activity show the extent to which activity in Argentina has been maintained while Brazil has suffered in the downturn. Despite the impact of the global recession on output in almost all economies in the region, a comparison of capacity utilisation measures with those in other parts of the world shows the extent to which Latin America has suffered less than them. US capacity utilisation has dropped by around 12 percentage points in the downturn so far and the fall in Japan has been nearly 30 points. However the declines in capacity utilisation in Latin America - imperfect though the data is - looks much smaller - in the order of 5 percentage points. This should help promote a faster turnaround in business investment spending in the region as it moves out of recession.



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