

LATIN AMERICA and THE CARIBBEAN



Growth in Latin America and the Caribbean is projected accelerate moderately, from 0.8 percent in 2017 to 1.7 percent in 2018 and 2.3 percent in 2019, largely reflecting accelerating growth in commodity exporters. A cyclical recovery is underway in Brazil, and conditions are improving in Chile, Colombia, Mexico, and Peru. Downside risks to the growth outlook are significant, however. External risks include an abrupt tightening of financing conditions and an escalation of trade protectionism. Domestic risks, including policy uncertainty and disruptions from natural disasters, also stand to inhibit growth.

Recent developments

Growth in Latin America and the Caribbean has been accelerating, driven by generally favorable domestic and external financing conditions, strengthening growth in the United States, and higher prices of key commodities relative to a year ago. Except in Brazil and, to a lesser degree, Colombia, negative output gaps are nearly closed.¹

Private consumption was the main contributor to regional growth of 0.8 percent in 2017, and is estimated to have strengthened further in early 2018 amid supportive confidence and the effect of previous interest rate cuts. Regional investment has been recovering after a deep, prolonged contraction, supported by a strong recovery in commodity prices last year (Figure 2.3.1).

Robust global demand has boosted exports and helped narrow current account deficits as a share of GDP in some countries (e.g., Brazil, Mexico). At the regional level, however, import growth is outpacing export growth, owing to the recovery of domestic demand in commodity exporters, and as a result net exports still contribute slightly negatively to regional growth.

Note: This section was prepared by Dana Vorisek. Brent Harrison provided research assistance.

¹ Output gaps are calculated, using a multivariate filter, for seven LAC economies: Argentina, Bolivia, Brazil, Chile, Colombia, Mexico, and Peru.

In Brazil, Argentina, and Chile—three of the largest commodity-exporting economies—industrial production growth was considerably higher in the first quarter of 2018 than a year before, and retail sales growth was higher in Brazil and Chile, supporting activity. However, a drought is disrupting agricultural production in Argentina, and the recent market volatility may have inhibited activity in the second quarter. In República Bolivariana de Venezuela, an economic and humanitarian crisis continues, and an increasing number of Venezuelans are migrating to neighboring countries.

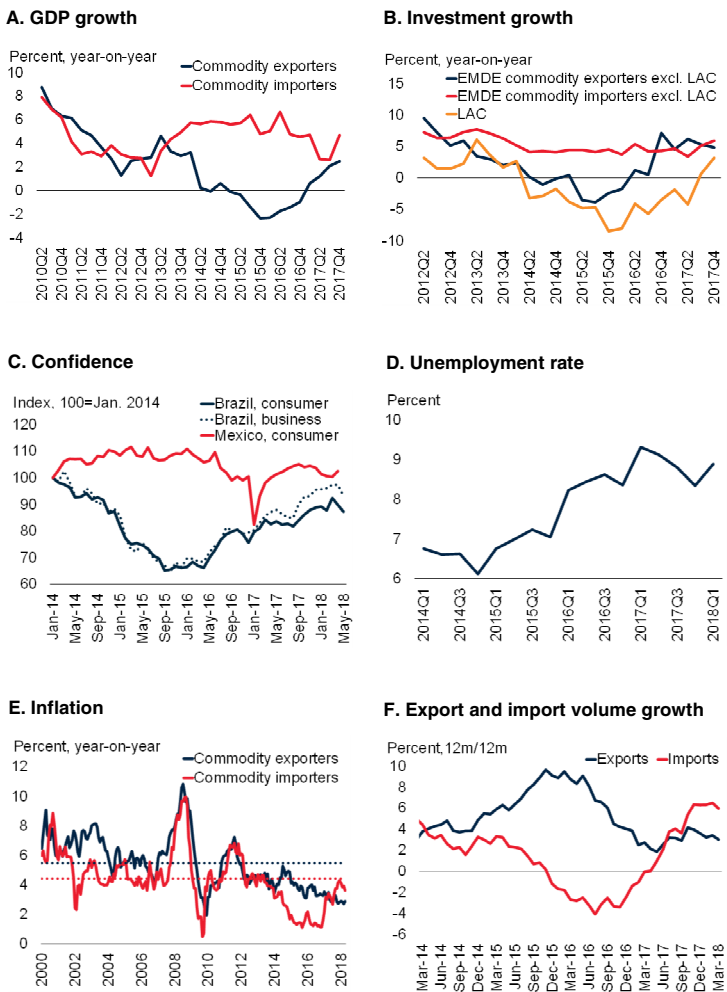
In Mexico, the largest commodity-importing economy in the region, high-frequency indicators have been mixed. Trade is becoming more supportive of growth, and the contraction in investment in 2017 is fading, but sluggish retail sales point to slightly moderating private consumption growth.

In the Caribbean, strong external demand is benefiting most services-exporting economies (e.g., the Dominican Republic, Jamaica, St. Lucia, Grenada). Despite the hurricanes in the autumn of 2017, tourist arrivals to the Caribbean reached an all-time high last year.

Inflation is decelerating in most LAC economies, with the key exceptions of Argentina and the extreme case of Venezuela. Median inflation in commodity exporters is well below its historical

FIGURE 2.3.1 LAC: Recent developments

Growth in LAC is accelerating, driven in large part by a cyclical recovery in Brazil and improving conditions in other large commodity-exporting economies. Investment is picking up after an extended period of contraction, while private consumption is strengthening amid supportive confidence and the effect of previous interest rate cuts, despite an uptick in unemployment. Net exports in the region are still contributing negatively to growth, in part due to rapid import growth as domestic demand rises.



Sources: CPB Netherlands Bureau for Economic Policy Analysis, Haver Analytics, International Labor Organization, Oxford Economics, World Bank.

A. 2010 GDP-weighted averages. Sample includes 13 commodity exporters and three commodity importers. Last observation is 2017Q4.

B. Investment is gross fixed capital formation. Aggregate investment rates calculated using constant 2010 investment-weighted averages. Last observation is 2017Q4.

C. Last observation is May 2018 for Brazil and April 2018 for Mexico.

D. Regional average weighted by size of labor force in 2014. Sample includes Argentina, Belize, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Mexico, Peru, and Uruguay. Last observation is 2018Q1.

E. Lines show medians of 14 commodity exporters and eight commodity importers, and horizontal lines the averages from January 2000 to present. Last observation is April 2018.

F. Sample includes 13 economies. Last observation is March 2018.

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average. Policy interest rates in almost all commodity exporters have been cut during the first half of 2018. Brazil, Colombia, and Peru have cut rates repeatedly. Recent monetary policy statements, however, suggest that the easing cycle may be coming to an end. Among commodity importers, inflation has eased somewhat since early 2018 (e.g., in Mexico, El Salvador, Jamaica), after accelerating rapidly in 2017 on fuel and food price increases.

Although external financing conditions remain supportive, sovereign bond yields have risen modestly in the large economies in the region since the start of 2018, consistent with the trend across emerging markets. Yields have risen by a larger amount in Argentina, where the central bank hiked interest rates sharply in April and May in response to currency pressures.

Fiscal deficits in the region have narrowed slightly relative to levels seen during the commodity price plunge, yet are still high. There is significant need for fiscal consolidation, especially in light of high debt levels in many countries (Végh et al. 2018). Brazil's government debt, for instance, recently reached record levels, and critical pension reform legislation has been delayed until after the new administration takes office in early 2019. Government debt is also high in El Salvador, Uruguay, Venezuela, and most Caribbean countries. In Grenada and Jamaica, however, fiscal rules have provided the discipline needed to begin reducing debt.

Outlook

Regional growth is projected to accelerate during the forecast horizon, to 1.7 percent in 2018 and to 2.5 percent by 2020, still below the long-term (1990–2017) average of 2.7 percent. This outlook is lower than that produced in January, mostly due to large downward revisions to projections for Venezuela, but also to downgrades for Argentina (Tables 2.3.1 and 2.3.2). Regional growth through 2020 will come almost exclusively from private consumption and investment (Figure 2.3.2).

Accelerating private consumption growth in the region reflects the effect of previous interest rate cuts and supportive consumer confidence in some

large economies. Investment growth in LAC is expected to reach 3.7 percent in 2018, and to firm to 4.6 percent in 2020. The investment recovery will be supported by a broad-based cyclical recovery in Brazil, rising copper prices and fading disruptions in the mining industry (e.g., Chile, Peru), large infrastructure projects (e.g., Argentina, Colombia, Panama, Peru), and stable capital inflows.

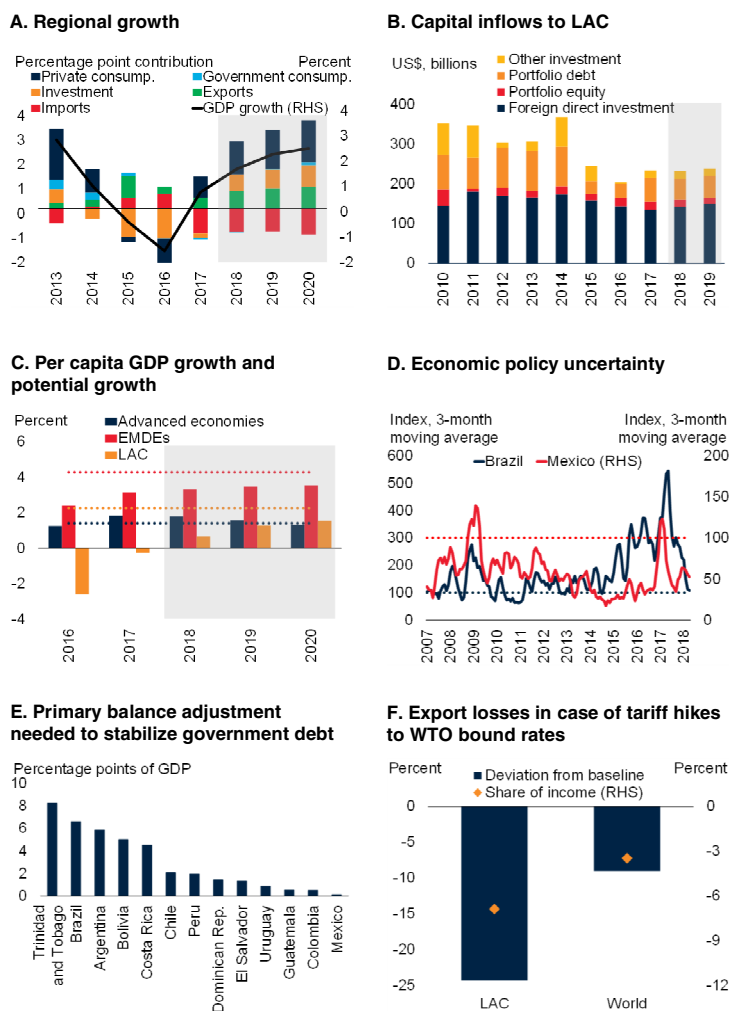
In most large commodity exporters, including Brazil, Chile, Colombia, and Peru, growth is projected to accelerate in 2018 and 2019. In these economies, the recovery is expected to reflect upward momentum in private consumption, continued acceleration in investment growth, and, in all except Colombia, a modest contribution from net exports. In Argentina, on the other hand, growth is expected to slow in 2018 as monetary and fiscal tightening, together with the effects of the drought on the agricultural sector, counter strong momentum at the start of the year. In Ecuador, growth is expected to moderate during the forecast horizon in the context of gradual fiscal consolidation. For oil exporters across the region, the upward revision to oil prices will provide a boost to growth.

Growth in commodity importers, which are geographically concentrated in the Mexico and Central America and the Caribbean subregions, is also expected to strengthen in 2018, in part due to rising demand for exports as growth picks up in the United States. In Mexico, a reversion to positive investment growth is also projected to support growth through the forecast horizon, while private consumption growth is expected to stall at a lower rate than in recent years. The outlook for Central America is mixed, with growth in some agricultural exporters (e.g., Costa Rica, Guatemala) expected to accelerate moderately through 2020 and that in commodity importers (El Salvador, Panama) expected to stabilize or decelerate.

In the Caribbean, post-hurricane reconstruction, robust tourism, and supportive commodity prices are expected to lift growth in 2018. Some commodity-reliant economies (Suriname, Trinidad and Tobago) are expected to register their highest growth rates since before the 2014–

FIGURE 2.3.2 LAC: Outlook and risks

Growth in Latin America and the Caribbean is projected to continue to accelerate during the forecast horizon, driven almost exclusively by domestic demand—in particular, private consumption and investment. Although per capita GDP growth is projected to rise after a long period of contraction, it will only marginally exceed that in advanced economies by 2020, resulting in stalled convergence. Significant downside risks to the growth outlook remain, including an abrupt tightening of external financing conditions, increased trade protectionism, policy uncertainty, and the effects of natural disasters.



Sources: Baker, Bloom, and Davis (2016); Haver Analytics; Institute of International Finance; Kutlina-Dimitrova and Lakatos (2017); Végh et al. (2018); World Bank.

A. Bars show contribution of each of the components of GDP to regional growth.

A.C. GDP-weighted averages.

B. Sample includes Argentina, Brazil, Chile, Colombia, Mexico, and Venezuela. Estimates as of May 2018.

C. Bars show annual per capita growth and lines average potential growth during 2016–20.

D. For Brazil, the index is normalized to equal 100 at its 1991–2011 median. For Mexico, the index is normalized to equal 100 at its 1996–2016 median. Horizontal lines show medians during these periods. Last observation is April 2018.

E. Calculated using methodology described in Végh et al. (2018). Venezuela, not shown in the figure, is estimated to need a primary balance adjustment of 26 percentage points of GDP to stabilize debt.

F. Based on simulations using the GDyn computable general equilibrium model. Results show cumulative decline by 2020, relative to a business-as-usual scenario, assuming that tariff hikes start in 2018. The scenario is defined as a worldwide increase in tariffs up to legally allowed bound rates coupled with an increase in the cost of traded services of 3 percent. World Trade Organization (WTO) bound tariffs are the maximum tariffs under WTO commitments.

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16 oil and metals price drop. Rapid development of an offshore oil industry is expected to boost Guyana's growth sharply in 2020.

Despite the cyclical recovery underway in the region, potential growth is expected to moderate in the medium term, averaging 2.3 percent in 2018–22, compared to an estimated 2.7 percent in 2013–17 (World Bank 2018c). This projection reflects slower labor force growth and capital accumulation, as well as continued weakness in total factor productivity, and raises doubts about the region's ability to deliver sustained progress on per capita income convergence with advanced economies. Per capita GDP growth in the region is projected to exceed that in advanced economies only in 2020, following a long stretch of contraction, but remain well below the EMDE average. This outlook reinforces the need for reforms to counter less favorable demographics, boost investment growth after the extended period of weakness, and raise persistently low productivity (World Bank 2018c).

Risks

Risks to the regional growth outlook continue to be predominantly downside, through external and domestic channels. However, the possibility of favorable spillovers as the United States implements fiscal stimulus cannot be ruled out.

Externally, an abrupt tightening of financing conditions or changes in investor sentiment regarding EMDEs as advanced economies unwind monetary policy accommodation, such as that experienced by Argentina recently, could set back capital inflows and growth in the region. This is a particular risk for countries with large current account deficits (e.g., Argentina, Bolivia, Nicaragua, Panama) or significant fiscal adjustment needs (e.g., Argentina, Brazil), and for those where credit quality has deteriorated. A marked tightening of the external financing environment or a softening of global commodity prices could also contribute to a growth slowdown, which may not be sufficiently addressed with countercyclical fiscal policy given the lack of fiscal space (Végh et al. 2018).

Downside risks also emanate from international trade channels. Adverse outcomes of the NAFTA renegotiations could hold back growth in Mexico. Additional trade-restricting actions by China and the United States could have negative effects on the region through trade, confidence, financial, and commodity market channels, and may encourage policy support for increased protectionism (Huidrom, Kose, and Ohnsorge 2017; Kose et al. 2017). Protectionism in the form of increases in actual tariffs to bound tariffs would reduce exports from LAC significantly (Kutlina-Dimitrova and Lakatos 2017). However, for some specific agricultural products, such as soybeans, and maize, tariff increases by China on U.S. exports could raise demand for LAC exports. Furthermore, the region has recently become more active in pursuing new trade agreements, most prominently between Mercosur and the European Union.

On the domestic front, a key downside risk is an escalation of policy uncertainty. The medium-term policy environment in the two largest economies in the region, Brazil and Mexico, could shift following presidential and legislative elections in the second half of the year. Significant delays in key reforms could lead to sudden changes in investor sentiment and derail a still-fragile investment recovery.

Recent years have also demonstrated the vulnerability of the region to floods, droughts, hurricanes, earthquakes, and wildfires, which threaten to become more common in the medium to long term as climate conditions change (Bello 2017).

An upside risk to the regional outlook is the possibility of stronger-than-expected favorable spillovers from the United States as it implements fiscal stimulus. This would tend to benefit Mexico and Central America the most. However, any boost would likely be short-lived given that U.S. fiscal stimulus is slated to fade later in the forecast horizon, and that the stimulus will occur in the context of expected monetary policy tightening.

TABLE 2.3.1 Latin America and Caribbean forecast summary

(Real GDP growth at market prices in percent, unless indicated otherwise)

Percentage point differences
from January 2018 projections

	2015	2016	2017e	2018f	2019f	2020f	2018f	2019f	2020f
EMDE LAC, GDP¹	-0.4	-1.5	0.8	1.7	2.3	2.5	-0.3	-0.3	-0.2
(Average including countries with full national accounts and balance of payments data only) ²									
EMDE LAC, GDP ²	-0.4	-1.5	0.8	1.7	2.3	2.5	-0.3	-0.3	-0.2
GDP per capita (U.S. dollars)	-1.5	-2.6	-0.3	0.7	1.3	1.5	-0.3	-0.3	-0.2
PPP GDP	0.2	-0.9	1.1	1.9	2.4	2.6	-0.3	-0.3	-0.2
Private consumption	-0.3	-1.7	1.4	2.1	2.5	2.7	0.0	-0.2	-0.2
Public consumption	0.9	0.0	-0.4	-0.2	0.2	0.7	-0.2	-0.7	0.0
Fixed investment	-5.5	-6.0	-0.9	3.7	4.0	4.6	1.1	0.4	0.9
Exports, GNFS ³	4.3	1.3	2.0	3.2	3.7	3.9	-0.7	-0.3	0.1
Imports, GNFS ³	-2.0	-2.9	4.8	4.3	4.1	4.6	0.8	-0.1	0.6
Net exports, contribution to growth	1.3	0.9	-0.6	-0.2	-0.1	-0.2	-0.3	-0.1	-0.2
Memo items: GDP									
South America ⁴	-1.8	-3.2	0.2	1.3	2.1	2.3	-0.6	-0.4	-0.4
Mexico and Central America ⁵	3.4	3.1	2.2	2.5	2.7	2.8	0.1	-0.1	0.1
Caribbean ⁶	3.7	2.6	2.4	3.5	3.5	3.8	0.0	0.0	0.4
Brazil	-3.5	-3.5	1.0	2.4	2.5	2.4	0.4	0.2	-0.1
Mexico	3.3	2.9	2.0	2.3	2.5	2.7	0.2	-0.1	0.1
Argentina	2.7	-1.8	2.9	1.7	1.8	2.8	-1.3	-1.2	-0.4

Source: World Bank.

Notes: e = estimate; f = forecast. EMDE = emerging market and developing economy. World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not differ at any given moment in time.

1. GDP at market prices and expenditure components are measured in constant 2010 U.S. dollars. Excludes Cuba.

2. Aggregate includes all countries in notes 4, 5, and 6 except Grenada, St. Kitts and Nevis, and Suriname, for which data limitations prevent the forecasting of GDP components.

3. Exports and imports of goods and non-factor services (GNFS).

4. Includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay, and Venezuela.

5. Includes Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Panama.

6. Includes Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Guyana, Haiti, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, and Trinidad and Tobago.

For additional information, please see www.worldbank.org/gep.

TABLE 2.3.2 Latin America Caribbean country forecasts¹

(Real GDP growth at market prices in percent, unless indicated otherwise)

							Percentage point differences from January 2018 projections		
	2015	2016	2017e	2018f	2019f	2020f	2018f	2019f	2020f
Argentina	2.7	-1.8	2.9	1.7	1.8	2.8	-1.3	-1.2	-0.4
Belize	3.8	-0.5	1.2	2.0	1.9	1.7	-0.2	0.2	0.0
Bolivia	4.9	4.3	4.2	3.9	3.6	3.4	0.1	0.2	0.1
Brazil	-3.5	-3.5	1.0	2.4	2.5	2.4	0.4	0.2	-0.1
Chile	2.3	1.3	1.5	3.3	3.4	3.5	0.9	0.7	0.7
Colombia	3.0	2.0	1.8	2.7	3.3	3.6	-0.2	-0.1	0.2
Costa Rica	3.6	4.2	3.2	3.4	3.6	3.6	-0.2	0.1	0.1
Dominican Republic	7.0	6.6	4.6	5.0	4.7	4.6	0.1	0.0	-0.1
Ecuador	0.1	-1.6	3.0	2.2	1.5	0.9	1.4	0.6	-0.1
El Salvador ²	2.4	2.6	2.3	2.3	2.2	2.2	0.5	0.4	0.3
Grenada	6.4	3.7	4.5	3.3	2.8	2.8	1.1	0.7	0.7
Guatemala	4.1	3.1	2.8	3.1	3.3	3.3	-0.3	-0.2	-0.2
Guyana	3.1	3.4	2.1	3.8	3.8	29.0	0.0	0.1	25.3
Haiti ³	1.2	1.5	1.2	1.8	2.4	2.4	-0.4	-0.1	-0.1
Honduras	3.8	3.8	4.8	3.5	3.6	3.8	-0.1	0.1	0.3
Jamaica	0.9	1.4	0.5	1.7	1.9	2.0	-0.1	-0.1	0.0
Mexico	3.3	2.9	2.0	2.3	2.5	2.7	0.2	-0.1	0.1
Nicaragua	4.8	4.7	4.9	4.7	4.5	4.4	0.3	0.1	0.0
Panama	5.6	5.0	5.4	5.6	5.6	5.6	0.0	0.0	-0.1
Paraguay	3.0	4.0	4.3	4.3	4.2	4.2	0.3	0.2	0.2
Peru	3.3	4.0	2.5	3.5	3.8	3.8	-0.3	0.0	-0.2
St. Lucia	2.0	0.9	2.1	2.8	2.3	2.3	0.6	0.5	0.5
St. Vincent and the Grenadines	1.4	1.9	1.0	2.1	2.5	2.7	-0.6	-0.3	-0.1
Suriname	-2.6	-5.1	0.1	1.1	1.7	2.1	-1.1	0.5	0.9
Trinidad and Tobago	1.5	-6.0	-2.3	1.6	1.9	1.2	-0.3	-0.3	-0.4
Uruguay	0.4	1.7	2.7	3.3	3.1	2.9	0.5	-0.1	-0.3
Venezuela	-6.0	-16.5	-14.5	-14.3	-7.0	-4.0	-10.1	-7.6	-4.9

Source: World Bank.

Notes: e = estimate; f = forecast. World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not significantly differ at any given moment in time.

1. GDP at market prices and expenditure components are measured in constant 2010 U.S. dollars.

2. A recent rebasing of El Salvador's GDP, from 1990 to 2014, has resulted in significant changes to historical growth rates compared to January 2018.

3. GDP is based on fiscal year, which runs from October to September of next year.

For additional information, please see www.worldbank.org/gep.