Economic Perspectives

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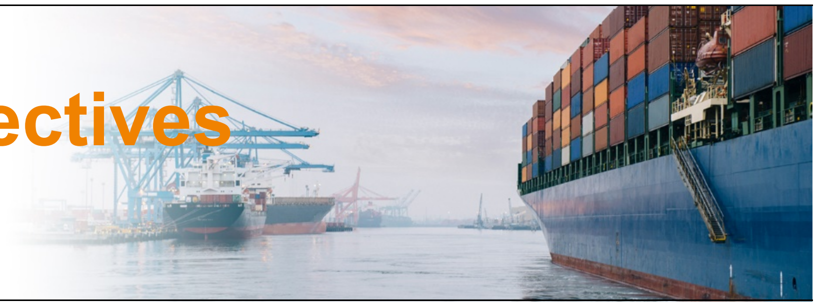


Challenging times for South America

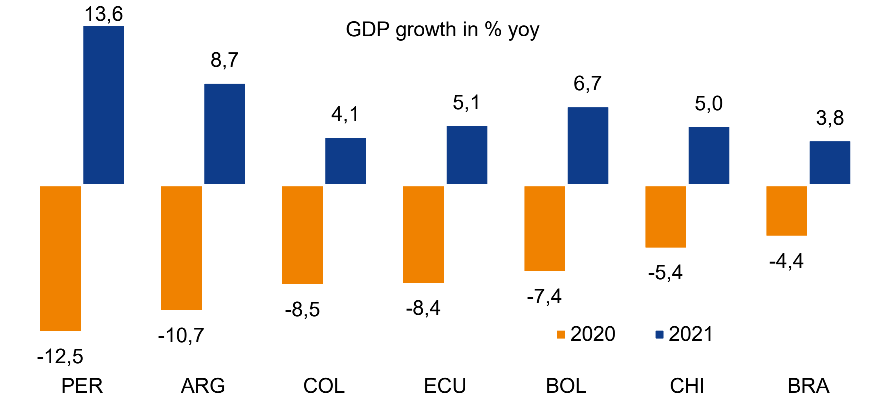
» **The further course of the corona pandemic also plays a major role for the economic outlook in South America. Furthermore, there is a strong dependence on agricultural and crude material exports.**

» **Brazil, Chile and Peru benefit from the demand pull from China. The ratification of the Mercosur Free Trade Agreement, on the other hand, is now being strongly questioned by the European side.**

» **The unstable political situation in the region poses a risk to the medium-term outlook. Corruption and income inequality also repeatedly cause social tensions.**

Summary
So far this year, South America's high infection rates in the wake of the Corona Pandemic, Brazil's controversial environmental policy and Argentina's recent debt cut have been at the center of attention. However, there are a number of other interesting aspects that will continue to influence the economic development of the region in the future. These include the increased importance of China as a trading partner in almost all countries, as well as the ratification of the Mercosur Agreement with the European Union, which is now being strongly questioned. In most cases, unstable political conditions prevent the necessary reforms to reduce dependence on raw materials exports. For Brazil and Chile, however, industrial goods already play an important role as export goods. In some countries, the very poor performance of the "Ease-of-Doing-Business Index" deters international investors. In this study, we look at eight economies on the South American continent, outlining the most important influencing factors and the recent developments in each country.

IN MOST COUNTRIES, A SIGNIFICANT ECONOMIC DOWNTURN IS LIKELY TO BE FOLLOWED BY A VISIBLE RECOVERY



Source: Oxford Economics, DZ BANK

MACROECONOMICS

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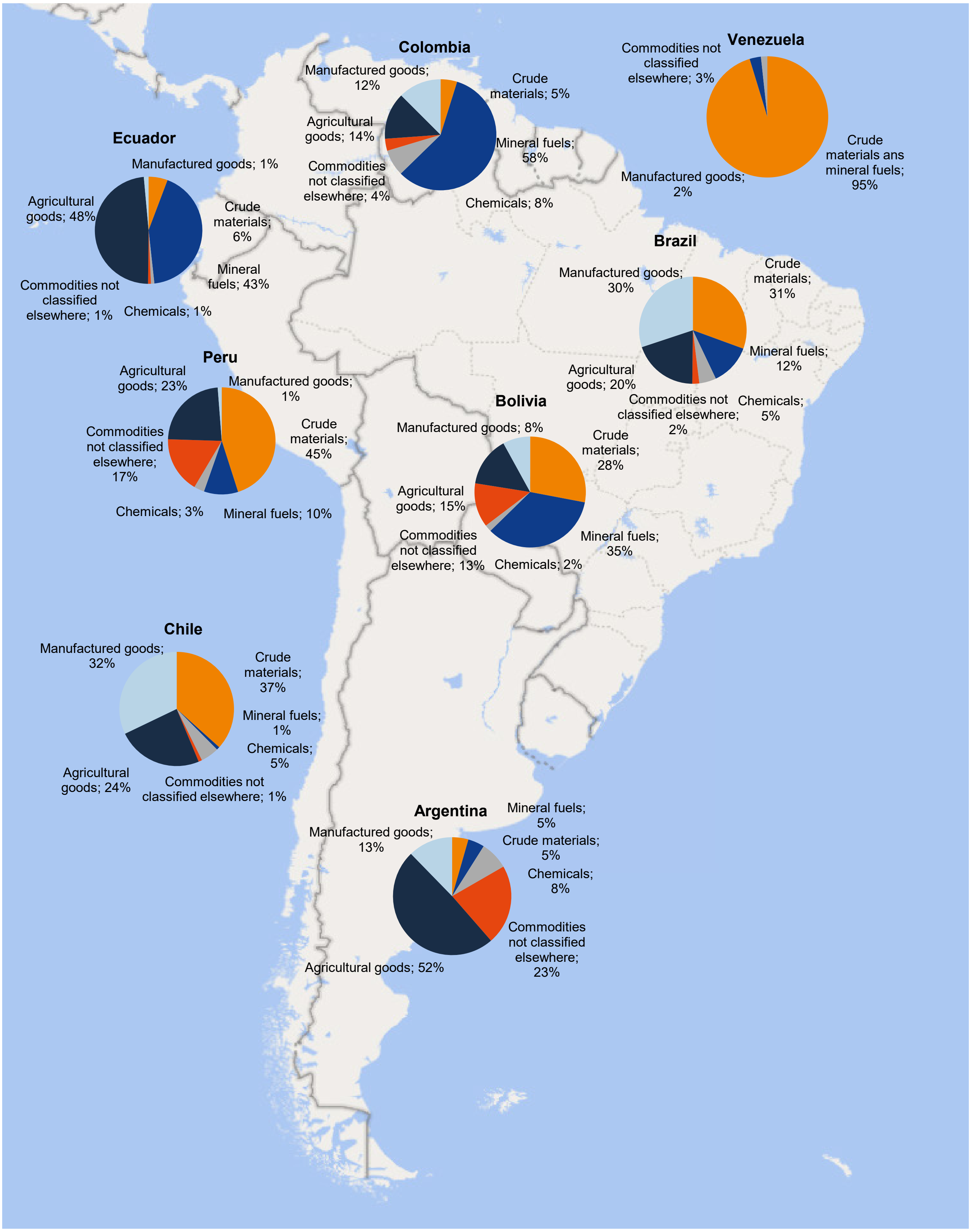
Strong dependence on exports of crude materials



Source: UN Comtrade Database, WTO, DZ BANK; share in goods exports, data from 2018

Economic slump and great uncertainty due to Covid-19

High infection rates make headlines, as does Brazil's environmental policy

So far this year, South America's high infection rates in the wake of the Corona Pandemic, Brazil's controversial environmental policy and Argentina's recent debt cut have been at the center of attention. However, there are a number of other interesting aspects that will continue to influence the economic development of the region in the future. In this study, we look at eight of the larger economies of the South American continent, outlining the most important influencing factors and recent developments in each country.

The citizens of South America have been severely affected by Covid-19, …

The corona pandemic, which has dominated all economic and political activity since the beginning of the year, has hit Latin America particularly hard. With Brazil, Peru, Colombia, Mexico and Argentina, five of the ten most affected countries in the world in absolute terms are in this region. There are many reasons for the severe course of events: weak health care systems, precarious housing situations in many metropolitan and surrounding areas, and a lack of political strategies. In addition, the number of new infections in many countries continues to soar. The resulting uncertainty is hampering economic recovery.

...but a PPP aims to provide the region with a vaccine

However, positive signals regarding combating the virus are coming from Argentina. There, a domestic biotechnology company is working on a vaccine together with the pharmaceutical company AstraZeneca within the framework of a public-private partnership. This vaccine is to be made available to the population of the entire Latin American region (except Brazil) at a very reasonable price, if possible in the first half of 2021.

Massive decline in economic activity

Meanwhile, the economic consequences of the Corona crisis cannot be overlooked in South America either. Due to lockdowns and closures of stores and factories, the collapse of world trade and the standstill of international tourism, the economic activity in all countries of the continent declined significantly in the course of the year. As a result, unemployment is rising and more citizens are dependent on state support. This shows the great dilemma that many politicians now face. Effectively containing the pandemic in the midst of a deep economic crisis is becoming more and more a trade-off between health and economic growth. In addition, very limited fiscal leeway in some countries impedes generous short-time work schemes and rescue packages for the economy.

"Ease-of-Doing Business Index" - a poor record for the region

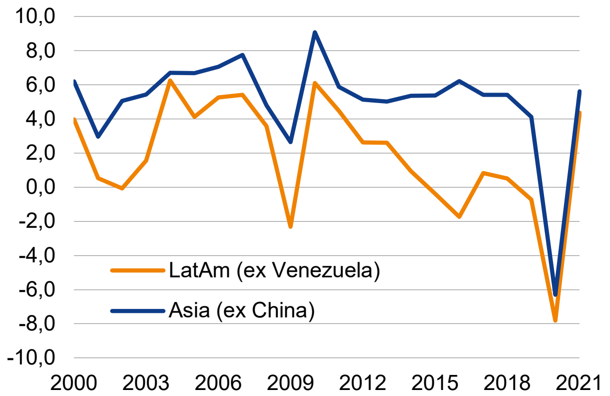
Corruption, political crises and social tensions…

Moreover, there are the "old" problems of many countries in the region. Widespread corruption and great social disparities create social tensions. This favors populist parties and weakens democratic processes. The mass protests in Chile, Peru and Ecuador, which last peaked in the fall of 2019, are likely to be in a kind of hibernation only because of corona and could quickly flare up again after the pandemic.

... negatively affect the regions appeal to foreign investors

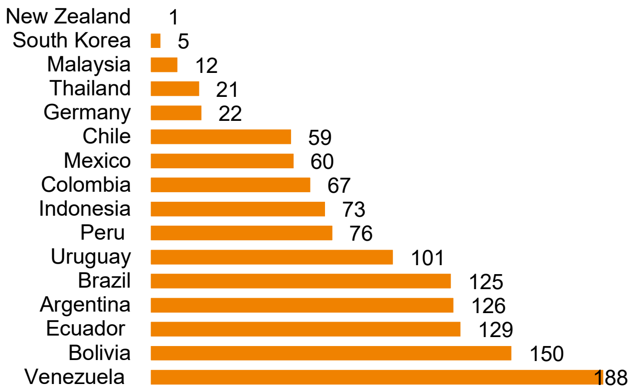
Symptomatic for the structural weaknesses is the below-average economic development of the national economies in the past ten years. Brazil, Argentina and Mexico, for example, grew only very weakly compared with the emerging markets in Asia. Since 2014, the region has not had a year of significant economic growth, see the following left-hand chart. In addition, there is high public-sector debt and a regulatory framework that is often not very investor-friendly. Ecuador and Argentina have already negotiated with their creditors this year and agreed to restructure part of their debt. The World Bank's Ease-of-Doing Business Index illustrates the limited appeal of many South American countries to foreign investors compared to Asian emerging markets. The index assesses business friendliness and the degree of corporate regulation in 190 economies and influences the location decisions of many international companies. While Chile and Colombia are still in midfield in the World Bank's ranking, Brazil and Argentina are only just ahead of Iran, and behind Lesotho and Senegal.

GDP GROWTH IN %: LATIN AMERICA AND ASIA IN COMPARISON



Source: Oxford Economics, DZ BANK

WORLD BANK'S EASE-OF-DOING- INDEX



Source: World bank, DZ BANK, Rankings ends at 190

Crude materials - a growth model for the future?

Commodity prices are often a plaything of the world markets

Another common characteristic of South American countries is their continuingly high dependence on agricultural and crude material exports. In principle, the continent's large deposits of crude materials hold the potential for prosperity. However, the revenues from exports are hardly ever passed on to the general population. Moreover, the one-sided dependence on crude material exports means being exposed to price and demand volatility on the world market. Price collapses could quickly put the stability of the entire economy at risk and can hardly be absorbed by other sectors.

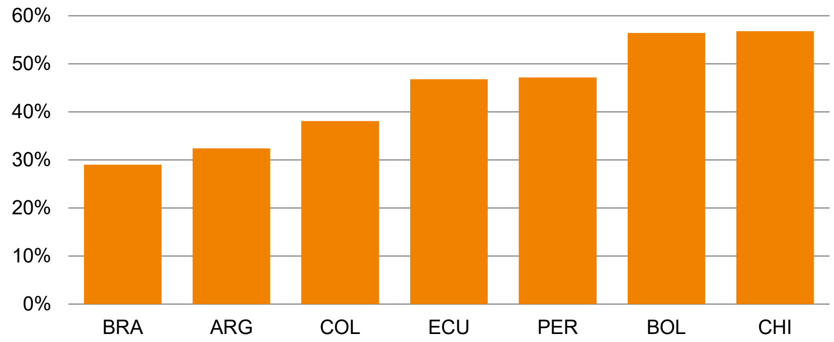
For Brazil and Chile, industrial goods play already an important role as export goods

Increased exports of manufactured goods could reduce this dependence. From this point of view, Brazil and Chile are already doing quite well, as the export share of industrial products in both countries was around 30 percent in 2018 (see figure on page 2). A higher value-added share in the processing of crude materials at home ultimately ensures more sustainable economic growth. However, this requires significant investment in education and infrastructure in most of the countries examined here.

The transition to electromobility favours countries with lithium and copper deposits

With an average annual growth rate of around 4.5 percent, Peru and Bolivia have enjoyed above-average growth over the past ten years. It is noticeable that both countries have a fairly high degree of openness with regard to international trade, which, however, is largely based on the exploitation of domestic crude material deposits. In the future, the transformation towards electromobility and the energy turnaround will cause a significant increase in demand for lithium, copper and other metals worldwide. This will particularly benefit countries with large deposits of these industrial metals. This is especially true for Chile, but Argentina, Bolivia and Peru would also profit from this.

FOREIGN TRADE RATIO 2019 (IMPORTS + EXPORTS IN % OF GDP)



Source: World bank, DZ BANK

Population growth provides positive outlook for domestic demand

The region's economic development is supported by natural population growth, which in turn should support domestic demand. Including Mexico and the Caribbean islands, the population already stands at around 630 million, and the United Nations expects a significant increase to around 750 million by 2050.

China is already an important trading partner for exports from Brazil, Chile and Peru,...

...particularly soy, oil and ores are in the center of interest

It is not surprising that the importance of China as a trading partner for this crude material exporting region has increased significantly in the last 10 years. In particular, Peru, Chile and Brazil each trade around 30 percent of their exports to China. This summer, too, the rapid recovery of Chinese demand for soya, copper and other metals had a supportive effect on the economy in these countries, but the strong concentration on one trading partner also carries risks. This is not only a matter of dependence on the Chinese economy. For Venezuela, Ecuador and Bolivia, for example, it has been shown that China also creates a strong financial dependency through credit lines. In contrast to loans from the International Monetary Fund (IMF), these loans are often of short duration and have clauses stipulating repayment via raw materials supplies if the recipient's creditworthiness is poor. Experts estimate that the three countries mentioned above are already indebted to China with 8 to 16 percent of their economic output.

The free trade agreement with the EU would benefit the agricultural industry in Argentina and Brazil

In contrast, the European public's focus has been particularly on the Free Trade Agreement between the European Union and the Mercosur states. The agreement, which was finally negotiated after 20 years, is currently under threat of a silent death. At first glance, the agreement offers opportunities for both sides. In return for considerable tariff reductions on the part of the South American states, Europe would open up part of its agricultural market. Considering that the average import duties in Brazil and Argentina are around 14 percent, their reduction would certainly be beneficial to European companies. On the other hand, the agricultural industry in Argentina and Brazil in particular would benefit from easier market access.

In Europe, however, the agreement hardly finds approval anymore

In the meantime, clear resistance to the agreement has formed in France and Austria. While in France the agricultural lobby is very critical of the agreement, Austria is demanding binding environmental and social standards. In view of the devastating fires in the Amazon rainforest and the environmental policy of the current Brazilian government, Chancellor Merkel recently also expressed "considerable doubts" about a rapid ratification of the free trade agreement.

Political instability prevents necessary reforms

Zersplitterte Parlamente und anstehende Wahltermine sprechen eher gegen Reformen in naher Zukunft

Not only the corona pandemic, but also the elections scheduled for the next two years make a medium-term outlook for the countries of South America difficult. Will the recovery momentum after the deep recession be used for structural reforms to generate sustainable economic growth and better income equality? In particular, the sometimes highly fragmented parliaments and also the upcoming election dates speak against it. In addition, the rapidly rising prices for metals and agricultural commodities are supporting the economy and masking the urgency of the reforms.

But political stability is the be-all and end-all,…

...to benefit also from a reorganization of the supply chains

However, the recent vaccine initiative of Argentina and Mexico in collaboration with an international pharmaceutical company shows the potential already existing in the region. Some South American countries could well benefit from a worldwide reorganization of supply chains, which is to be expected not only as a result of the corona pandemic, but also because of the ongoing trade conflict between the USA and China. Chile, Colombia and Peru are often mentioned in this context, but Brazil and Argentina could also be among the winners. The "be-all and end-all" for this to succeed is a stable political situation in the respective country and, as a result, a concept for investment in education and infrastructure. It remains to be seen whether the upcoming elections in Bolivia, Chile, Peru and Ecuador will provide the necessary political majorities to make this happen.

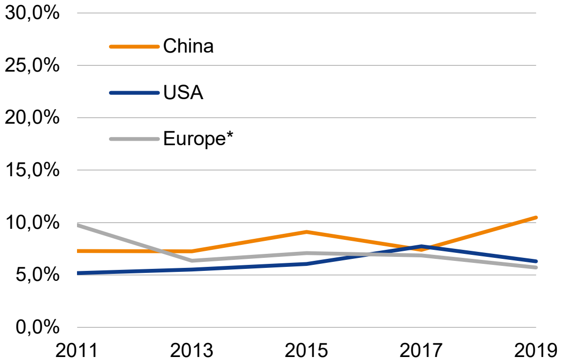
OVERVIEW PARLIAMENTARY ELECTIONS

	upcoming election	political position of the current government
Bolivia	Oct 2020	centre-right
Ecuador	Feb 2021	centre-left
Peru	Apr 2021	centre to centre-right
Chile	Nov 2021	centre-right
Brazil	2022	right
Colombia	2022	centre-right to right
Argentina	2023	left
Mexico	2024	left
Venezuela	2024	left

Source: DZ BANK, listed are regular elections

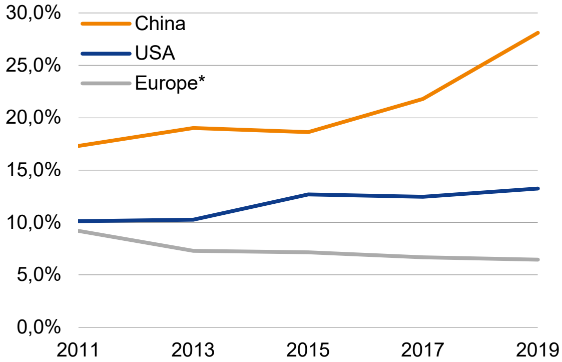
China is an important Trade Partner

ARGENTINA: EXPORT SHARE OF CHINA, EUROPE* AND THE USA



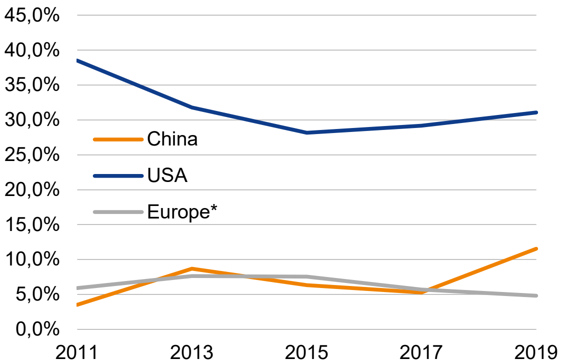
*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK;

BRAZIL: EXPORT SHARE OF CHINA, EUROPE* AND THE USA



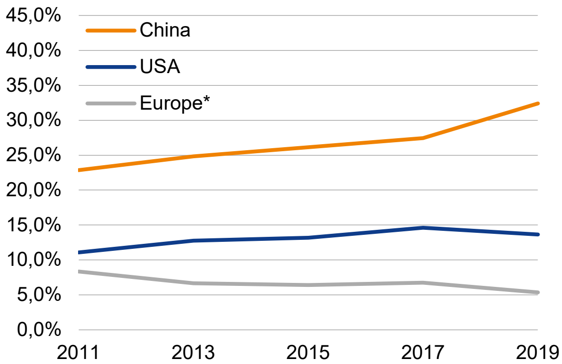
*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK

COLOMBIA: EXPORTANTEIL VON CHINA,EUROPA* AND THE USA



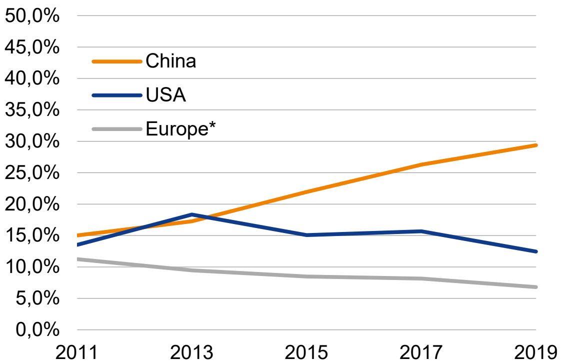
*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK

CHILE: EXPORT SHARE OF CHINA, EUROPE* AND THE USA



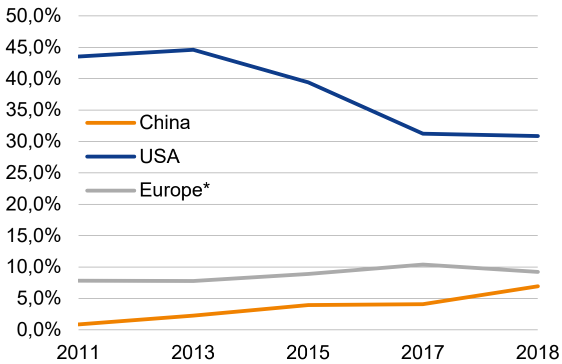
*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK

PERU: EXPORT SHARE OF CHINA, EUROPE* AND THE USA



*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK

ECUADOR: EXPORT SHARE OF CHINA, EUROPE* AND THE USA



*Europe = Germany, France, Spain and Italy
Source: UN Comtrade Database, DZ BANK

Argentina

The government has so far been very strict in combating the virus

Even before the corona pandemic, South America's second largest economy was in recession. After GDP had already contracted slightly in 2018 and 2019, a sharp decline in economic output of around 10 percent is expected this year. Since the government imposed strict contact bans at a very early stage, it was initially quite successful in keeping the incidence of infection under control. In the meantime, however, more than 600,000 people have been infected in the country, which has a population of almost 45 million.

A PPP together with Mexico is to secure the supply of a vaccine for LatAm

Great hopes are therefore pinned on the bilateral strategy with Mexico to provide Latin America with a corona vaccine announced in mid-August. In a public-private partnership, the Argentinean biotech company mAbxience is working on a vaccine together with the pharmaceutical company AstraZeneca. This vaccine is to be available for the population of the entire Latin American region (except Brazil) at a very favourable price, if possible in spring/summer 2021. The vaccine is to be distributed through Mexico and will be financed by Mexican billionaire Carlos Slim.

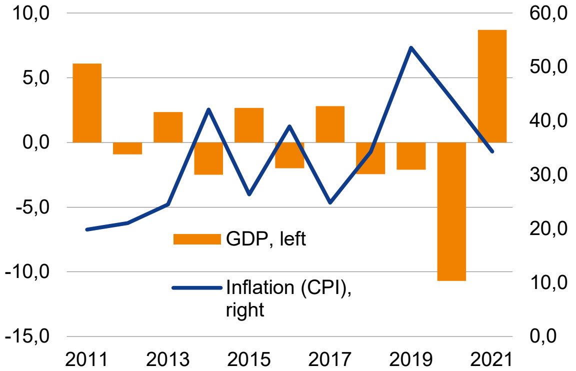
But the headlines tend to focus on the desperate state of the state budget

However, Argentina is making bigger headlines in Europe, mainly because of the still fragile budgetary situation of the state. Last year, the debt ratio already climbed to the high level of around 88 percent of GDP. It was not until the beginning of August that a new debt cut had to be made, which creditors were fortunately able to agree on at fairly short notice. The currently falling tax revenues and also, for example, the emergency financial aid programme for low-wage earners are likely to widen the chronic budget deficit to around eight percent of economic output this year.

Fernández has so far had no opportunity to realign economic policy

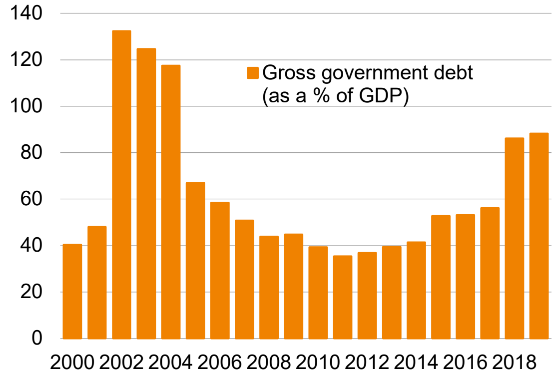
Despite the strong biomedical sector, the highly technological agricultural industry is the main driver of the export economy and also an important source of foreign exchange for the G20 country. When the Peronist Alberto Fernández took office as president in December, the agricultural sector feared the introduction of export taxes. However, the current crisis management has left Fernández little room for a reorientation of economic policy. On the contrary: the fact that he approached the liberal-conservative mayor of Buenos Aires, his political adversary, to coordinate corona-related measures brought him recognition from the opposition.

ARGENTINA: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

NOT ONLY THE RECESSION WEIGHS ON THE BUDGET



Source: FERI, DZ BANK

Bolivia

Political instability and high infection rates

Bolivia currently has to deal with many problems at the same time. One is the corona pandemic, which is also rampant in Bolivia with high infection rates. On the other hand, after the army forced the resignation of left-wing President Evo Morales in November 2019, Bolivia is still without a legitimate government and finds itself in a power-political vacuum. The announced new elections have now been postponed three times (currently to October 18) due to the corona crises. While the government argues that it is not possible to guarantee secure elections during the pandemic, the opposition continues to push for elections as soon as possible. In addition, the conservative interim president Anez faces a parliament in which Morales' party is still the strongest force, which significantly limits the government's ability to act. At the same time, roadblocks set up by radical Morales supporters threaten the supply of some cities and paralyze large parts of the country. Bottlenecks in food, medicine and gasoline are the result.

New civil unrest paralyzes large parts of the country

Severe downturn in economic activity...

In the stranglehold of this political crisis, Bolivia is in the middle of a deep recession. While over the past 10 years the country has been one of the fastest growing economies in Latin America, for the year 2020 as a whole, we expect economic output to decline by 7.4 percent. However, due to the pandemic and the very unstable political situation, this estimate is subject to great uncertainty. A further sign of a deteriorating overall economic situation is rising unemployment. The urban unemployment rate rose in May from 5.3 to 8.1 percent year-on-year. Nevertheless, it should be noted that in Bolivia, according to a working paper from the International Monetary Fund (IMF), the informal sector accounts for over 60 percent of gross domestic product.

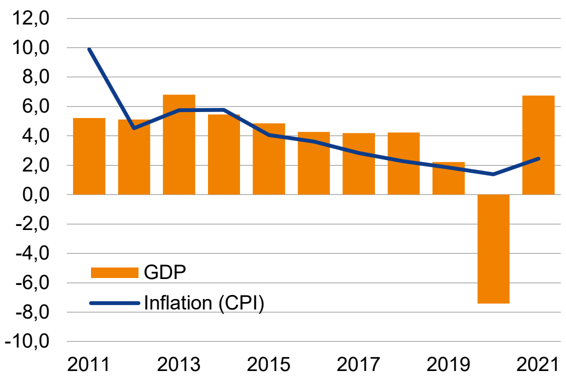
...but very large informal sector

Peg to the dollar poses medium-term risks

Another interesting aspect is the fixed peg of the Boliviano to the US dollar. While a fixed exchange rate offers some advantages, such as low inflation and a stabilizing effect on the country's own currency, a country needs high currency reserves and foreign exchange revenues to support the exchange rate when capital is withdrawn. Bolivia's main source of income is the export of natural gas to its neighboring countries. Similar to the oil price, the price of natural gas has fallen significantly since 2015. As a result, Bolivia has had a current account deficit and declining currency reserves since 2015. Although the latter are currently still relatively large in relation to imports, the negative trend could be significantly accelerated by rising budget deficits. This would bring the question of the long-term stability of the peg into greater focus. It is therefore all the more surprising that Congress has so far rejected a new unconditional credit line from the IMF.

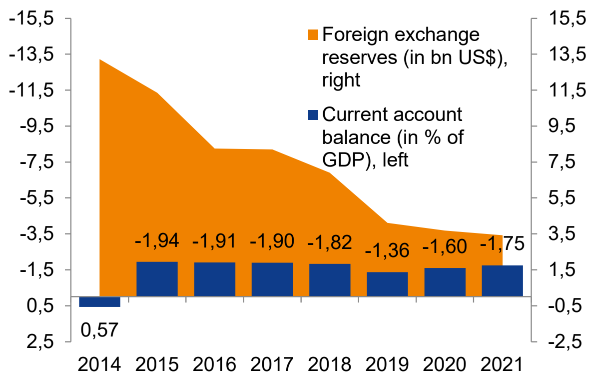
Strong dependence on gas exports

BOLIVIA: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

BOLIVIA: RAPIDLY DECLINING CURRENCY RESERVES



Source: Oxford Economics, DZ BANK

Brazil

Brazil has become the hotspot of the Corona pandemic,...

...uncertainty in the economy is likely to remain high

The most populous country in South America suffers severely from the effects of the corona pandemic. With now more than 4.5 million people infected and almost 140,000 dead, Brazil is one of the hotspots of the global health crisis. The number of daily new infections is also still very high. After a deep slump, the economic climate has recently brightened somewhat. However, not only because of the completely misguided health policy, we assume that uncertainty among the population and the economy will remain high in the coming months. The criticism of numerous foreign investors of the government's environmental policy is now also finding support in the domestic business. The economic recovery in the current and coming quarters is likely to be slow.

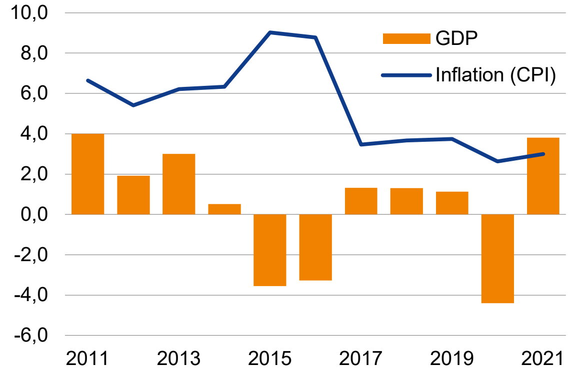
In Q2, GDP shrank by 9.7 %

Despite the serious health crisis, the Brazilian economy still seems to be coming through the crisis relatively unscathed by international comparison. In the second quarter, Brazilian GDP contracted by 9.7 per cent compared with the previous quarter. However, initial indicators for the current quarter - especially the industrial climate - point to visible growth. A stronger decline in overall economic output in Q2 was prevented by a surprisingly sharp rise in exports. Following a 4.4 per cent decline in gross domestic product this year, we anticipate economic growth of just under four per cent in 2021, driven strongly by catch-up effects.

Economic climate improved, but service providers still slightly pessimistic

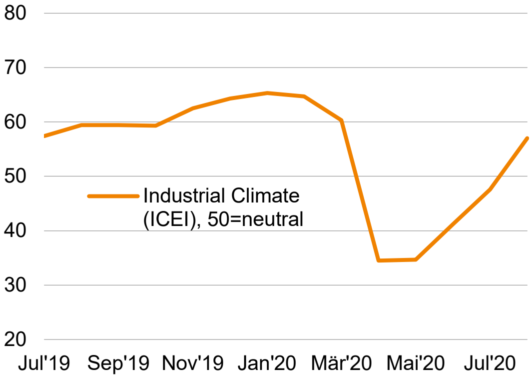
As a result of regional curfews, but also due to consumer restraint, retailers' sales in the second quarter were significantly lower than in the same period last year. Industrial companies also had to cope with a 20 per cent decline in production. However, the mood in the economy brightened again in July and August. The business climate of the national industry association (ICEI) recently stood at 57.0 points. The Markit survey (PMI) in the industrial sector now even shows a value of 64.7 points, visibly above the growth threshold of 50 points. Service providers, on the other hand, are not quite as optimistic about the future: the PMI for this sector has so far only worked its way up to a value of 49.5 points and is thus still slightly in the contractionary range. Accordingly, the recovery on the labour market is likely to proceed only slowly.

BRAZIL: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

STRONG REBOUND ACROSS THE INDUSTRY



Source: National Industry Confederation (CNI), DZ BANK

Chile

Unprecedented collapse of economic activity

Chile has the highest GDP per capita in Latin America. After the Chilean economy had already grown only weakly in 2019 due to mass protests and social unrest, Chile's GDP in the second quarter was 14.1 percent below the level of the same quarter of the previous year. Despite the positive development expected for the second half of the year, we anticipate a 5.4 percent decline in economic output for the year as a whole. However, there were also positive developments in the second quarter. The crucial mining industry in particular was even able to grow slightly thanks to strong demand from China. With the world's largest deposits of lithium, Chile's mining industry should visibly benefit from the electrification of mobility.

Mining industry defies the economic crisis

Support from strong export demand from China

On the other hand, Chile depends very heavily on its copper exports, which account for about 50 percent of all exports. After the copper price on the world market had slumped sharply in mid-March, the price of a ton of copper rose again significantly, driven by strong demand from China, and in mid-September was quoted above the pre-Corona level. Due to the solid development of exports, Chile even recorded a temporary current account surplus in July, resulting in important foreign exchange earnings.

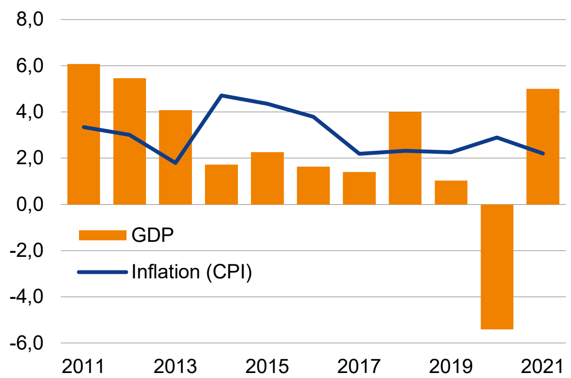
Strong fiscal support for the economy

Chile has reacted to the economic crisis with three major fiscal packages. These amount to a total of around 10 percent of GDP and are scheduled to run until the end of 2021. In addition to tax cuts and aid payments for the unemployed, a very controversial measure has been adopted: every citizen is allowed to have up to 10 percent of his or her pension rights paid out. While the scheme is very well received by citizens in the current situation, in the long run the measure carries the risk that the pension entitlements of many citizens will not be sufficient in retirement.

Widespread corruption and strong social disparities cause social tensions

Chile's economic outlook could be adversely affected by the great discontent among large sections of the population, with mass protests already having occurred in fall 2019. High costs of living, expensive education, widespread corruption and a high level of income inequality continue to hold great social explosive power and must be addressed by politicians. The announced referendum on a new constitution (the current one dates from the time of dictator Pinochet) is a first step in the right direction, but further measures are needed.

CHILE: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

CHILE: THE COPPER PRICE SUPPORTS THE ECONOMIC RECOVERY (IN USD PER TON)

Source: Bloomberg, DZ BANK

Ecuador

The Corona crisis and low oil prices are weighing on the economy

Ecuador's economy is also severely affected by the Corona pandemic. The strict lockdown and the decreed curfew led to a collapse in economic activity. As a result, the indicator for manufacturing production fell from 96 points in February to 71 points in April. After the economy was already barely able to grow in 2018 and 2019, we expect economic output to fall by 8.4 percent in 2020. In particular, the low oil price means substantial income losses for the country, as the export share of petroleum products in 2018 was over 40 percent. In addition, agricultural exports are an important pillar of the economy.

"Dollarization" as a curse and blessing at the same time

Ecuador is the only nation in Latin America that uses the US dollar as its own currency. While this stabilizes the economy and keeps inflation low, there are also some negative effects. Especially in times of crisis, when the dollar is considered a safe haven and tends to appreciate against currencies from developing and emerging countries, this greatly reduces the competitiveness of Ecuador's export sector. In addition, Ecuador has no opportunity to pursue its own monetary policy. Bond purchase programs to increase liquidity in the financial sector, such as those now being implemented by many countries around the world, are not possible.

High budget deficits and the immense public debt...

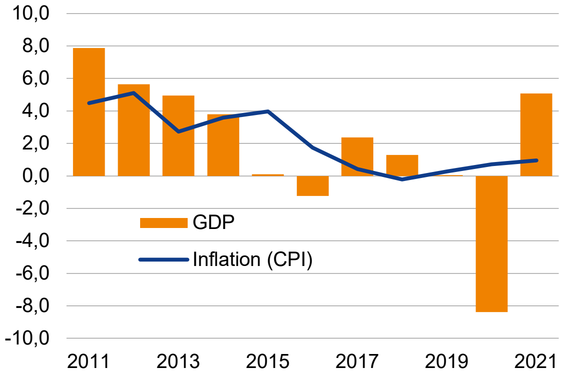
At the same time, Ecuador has great difficulty in servicing outstanding loans and interest. After already in 2008 debts could not be serviced, Ecuador, like Argentina, has agreed with creditors on a debt cut in 2020. In addition, repayment and interest payment periods have been extended significantly to ease the strain on public finances during the crisis. Before the agreement, gross financing requirements (debt repayment + budget deficit) amounted to 14 % of economic output in the current year alone, an amount Ecuador could not even begin to meet. Nevertheless, despite the agreement, the liabilities remain immense. Especially in view of declining revenues, rising social spending and a current account deficit, it seems questionable how sustainable the agreement reached is. Urgently needed additional capital will probably only come from the IMF and Chinese banks for the time being.

...severely restrict fiscal policy leeway

Upcoming elections cause further uncertainty

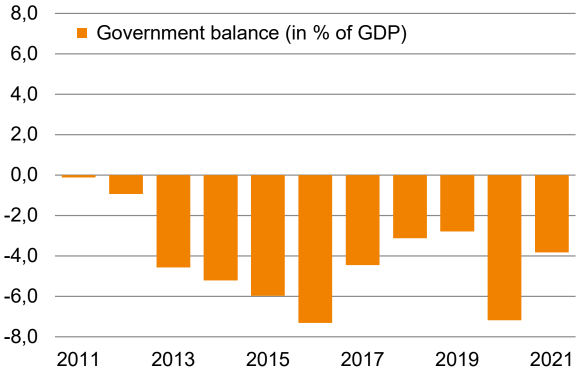
Getting the economy on a growth path sufficient to stabilize debt without much room for fiscal maneuver will be an enormous challenge. In addition, there are political uncertainties, since the 2021 presidential elections will have a major impact on the country's future course. The incumbent Moreno has already announced that he will not run again.

ECUADOR: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

ECUADOR: LARGE BUDGET DEFICITS



Source: Oxford Economics, DZ BANK

Colombia

Colombia's economy collapses dramatically in Q2 and...

Colombia's economy is heavily influenced by the corona pandemic in 2020. Economic output recorded an unprecedented slump in the second quarter and was 15 percent below the level of the previous quarter. Despite a very consistent response to the onset of the corona pandemic in March, especially compared to some neighboring countries, infection rates in Colombia rose sharply from June onwards, after some of the restrictions were lifted. Now, in the midst of a deep recession and high infection rates, new lockdowns have been imposed on some regions of the country and large parts of the capital Bogota. This is likely to have severely hampered the expected economic recovery in the current quarter.

...current developments may slow down the hoped-for recovery

Strong dependence on the oil price

Colombia was also strongly influenced by the massive slump on the oil markets. With a crude oil export share of over 50 percent, Colombia's foreign trade is heavily dependent on the world market price and on the economic development of its by far most important trading partner, the USA. At the same time, the Colombian peso has depreciated significantly since the beginning of the year, making imports more expensive. This illustrates how vulnerable hardly diversified economies are to external shocks.

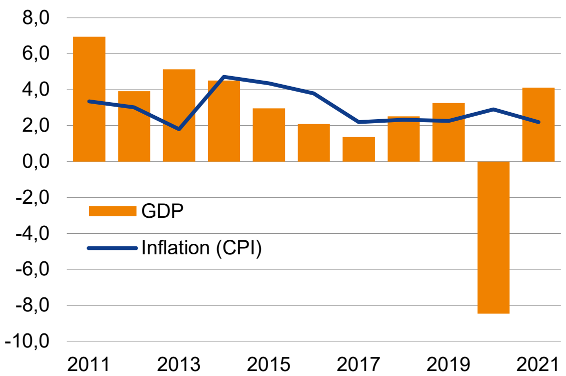
Little leeway for fiscal stimulus

In addition, there is a very limited scope for fiscal packages. According to figures from the International Monetary Fund (IMF), the aid agreed upon amounts to just 1.5 percent of gross domestic product. This is also a very low amount even by regional standards. Despite a new credit line from the IMF, the government is hesitant to take any major fiscal measures. A closer look at public debt reveals that even without a major fiscal package, public debt will increase significantly in the current year. Foreign currency debt in particular will become significantly more expensive due to the weak currency.

1.6 million refugees from Venezuela are now in Colombia

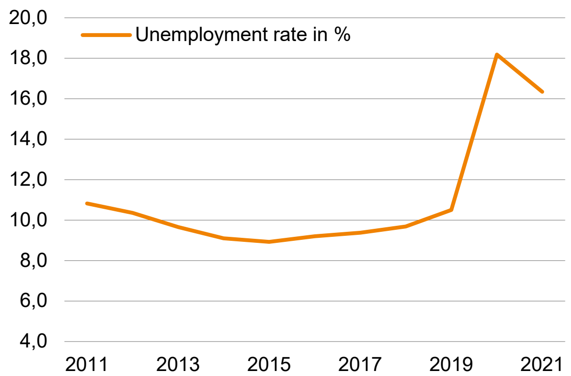
In addition, Colombia is hosting by far the largest number of refugees from Venezuela and is at the center of the largest refugee crisis in Latin America. According to the UN, the approximately 1.6 million, predominantly poor Venezuelans in Colombia need a lot of support and at the same time are pushing down local wages. Since many of them have no official papers, they work in the informal sector and have no access to state social benefits. The labor market in Colombia, meanwhile, has deteriorated considerably, with the unemployment rate in July standing at 20.2 percent.

COLOMBIA: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

COLOMBIA: SHARP RISE IN UNEMPLOYMENT



Source: FERI, DZ BANK

Peru

Massive political crisis ...

Similar to some neighboring countries, the political situation in Peru is anything but stable. After former President Kuczynski resigned in early 2018 due to accusations of corruption, Peru has had six different prime ministers under his successor Vizcarra. The climax of the political crisis was the dissolution of Congress in 2019 and the subsequent new elections at the beginning of 2020. The election resulted in a highly fragmented Congress with nine parties, in which none of the parties managed to win over 11 percent of the votes. Since these were early elections, the period of office is also limited until the next regular election in 2021. Overall, the election results can be interpreted as confirmation of President Vizcarra's anti-corruption policy, although the strong fragmentation limits the government's ability to act. In September 2020, Vizcarra and his minister of finance, María Alva, both faced a vote of confidence but remained in office.

...inhibits the government's ability to act

Economy collapses to a much greater extent than in the neighboring countries...

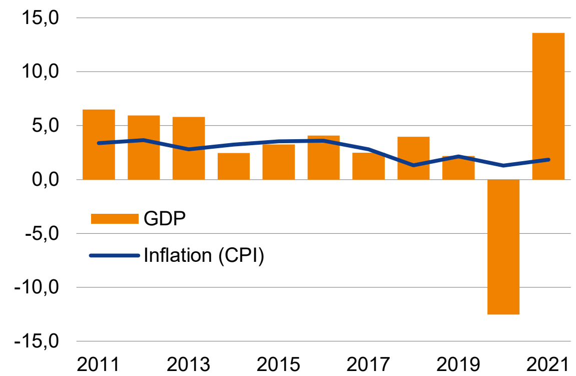
Peru's economy finds itself in a deep recession in 2020. In the second quarter, economic output fell by an unprecedented 30.2 percent compared to the same period of the previous year. We forecast a slump of 12.5 percent for the year 2020 as a whole. This means that Peru's economy is one of the hardest hit worldwide. Large parts of the service sector in particular came to an almost complete standstill as a result of the 100-day lockdown. However, after the restrictions were eased on June 30, the number of cases rose again and some restrictions were re-introduced. The Peruvian economy was supported by the rapidly recovering demand for metals and ores, which account for over half of exports. In addition, China, the most important export destination with over 27 percent, has recovered surprisingly quickly.

...but demand pull from China indicates strong recovery

This trade contact in particular, but also the moderate economic downturn in neighboring Brazil, point to a strong economic recovery in the coming year. To support the economy, the government has passed a fiscal package of seven percent of GDP. In addition, in order to increase liquidity in the financial sector, the key interest rate has been lowered to 0.25 percent. Like Chile, Peru has also decided that citizens can have part of their public pension entitlements paid out. While this will boost consumption in the short term, pension funds will have to sell assets at a very unfavorable time in order to be able to service the payouts. This decision was already highly controversial among the ruling party of President Vizcarra. This applies even more to a recently passed law that provides for a similar regulation for private pension funds. As a reaction, Vizcarra threatened to deny his approval and initiate legal action against the bill.

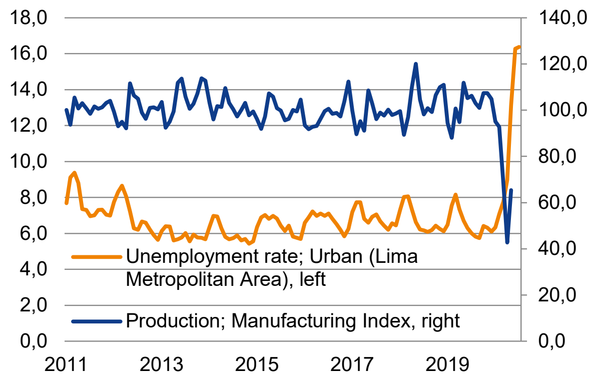
Withdrawals from the pension fund are expected to support private consumption

PERU: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

PERU: LABOUR MARKET AND INDUSTRY UND PRESSURE



Source: FERI, DZ BANK

Venezuela

The economy had hit rock bottom even before the corona crisis and ...

Venezuela, the fifth largest country in Latin America in terms of population, has been in a deep economic and political crisis since 2013. Looking at the country's economic output, GDP fell by 67 percent between 2013 and 2019. For the current year, we forecast a further decline of 37 percent. In addition, there is hyperinflation and a supply crisis for many groceries, petrol and medicines. While eight percent of the population will be living in extreme poverty in 2012, current studies estimate the figure to be around 80 percent. This extreme decline in the economy and the political situation led to an unprecedented exodus, resulting in the largest wave of refugees in Latin America. According to UNHCR and IOM, a total of more than 5 million people, or over 15 percent of the population, left the country. Most fled to neighboring countries, especially Colombia (1.8 million refugees), Peru (0.86 million) and Chile (0.45 million).

...the current crisis is further exacerbating the already precarious situation in the country

The ailing oil industry is hardly productive anymore

Decisive for the economic misery are the government's mismanagement and the harsh sanctions imposed by the United States. According to a study by BP from 2016, Venezuela has the world's largest oil reserves. However, due to sanctions, outdated technology and a massive investment backlog, the production volume has been falling steadily for years and the number of active rigs was down to one in June 2020. While Venezuela produced 3.5 million barrels/day in 1998, in August 2020 the figure was only around 100-200 thousand barrels/day, and the downward trend continues.

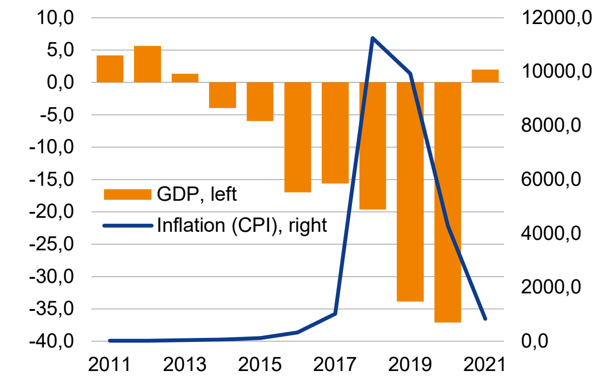
On the drip from China and Russia

This has a significant impact, oil accounted for almost 90 percent of exports in 2018. Without the important foreign exchange from exports, Venezuela is forced to reduce imports further, as the country is virtually insolvent since 2017 and is mainly supported by China and Russia. The decreasing imports then in turn aggravate the supply situation in the country, since the domestic production is not sufficient to supply the population.

Maduro consolidates his power - Guaido domestically without progress

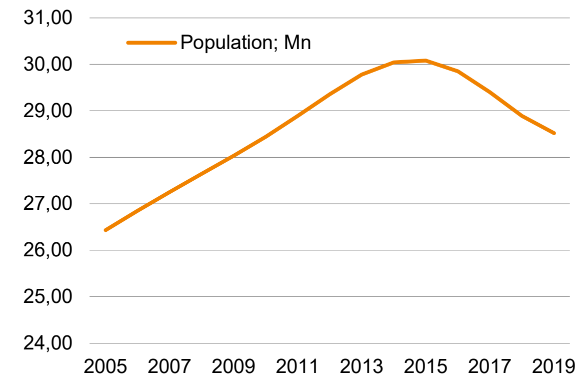
Nevertheless, with the support of the military and the police, President Maduro is able to stay in power and further expand his control. Although the self-proclaimed interim president Guaido is recognized by more than 50 nations, he has been on the retreat domestically since 2018, and the opposition-dominated National Assembly is largely disempowered. Norway's attempts to create a basis for dialogue between the two parties also showed how divided the opposition is. A political solution is still not in sight.

VENEZUELA: GDP GROWTH AND INFLATION (Y/Y, IN %)



Source: Oxford Economics, DZ BANK

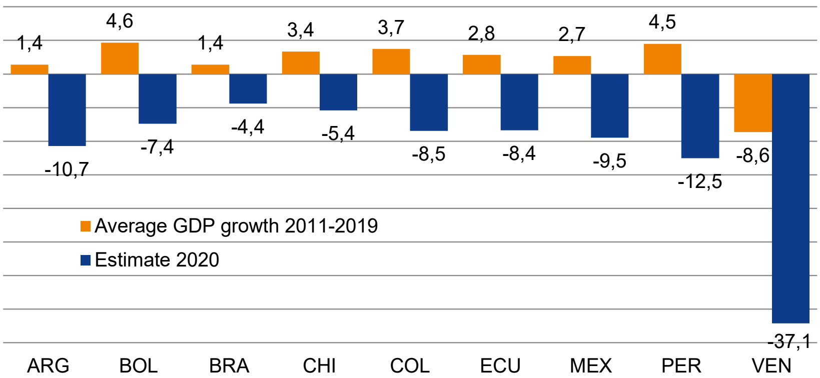
VENEZUELA: THE EXODUS IN NUMBERS



Source: FERI, DZ BANK

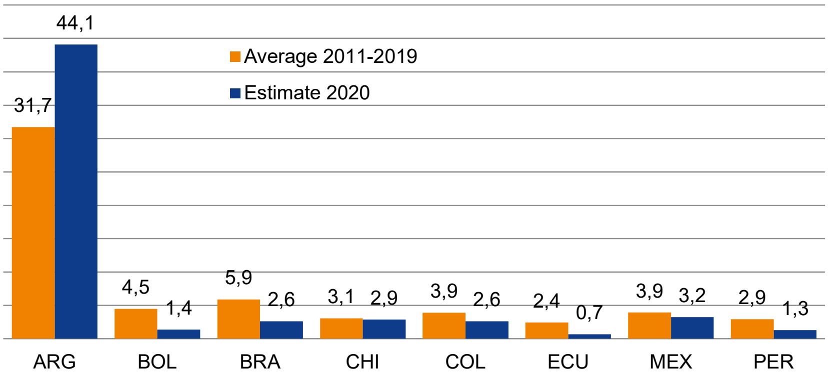
Graphical Overview

ECONOMIC GROWTH (IN %)



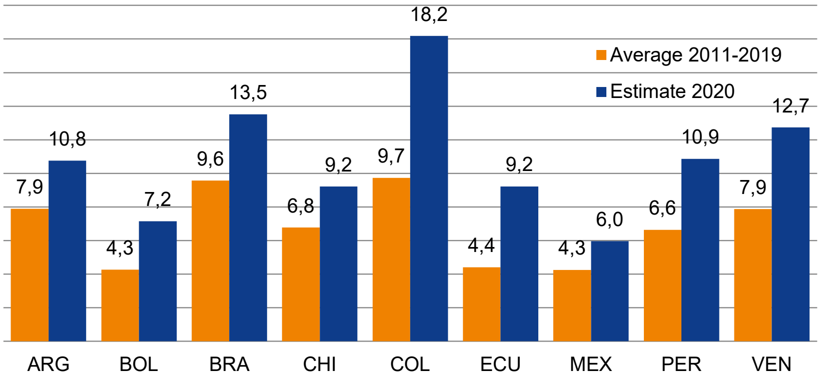
Source: Oxford Economics, DZ BANK

INFLATION RATE (IN %)



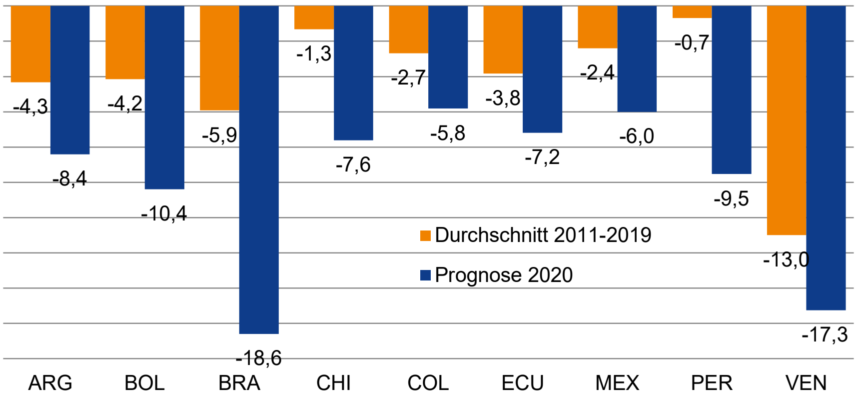
*Geschätzte Inflation in Venezuela 2020: 4275%, Source: Oxford Economics, DZ BANK

UNEMPLOYMENT RATE (IN %)



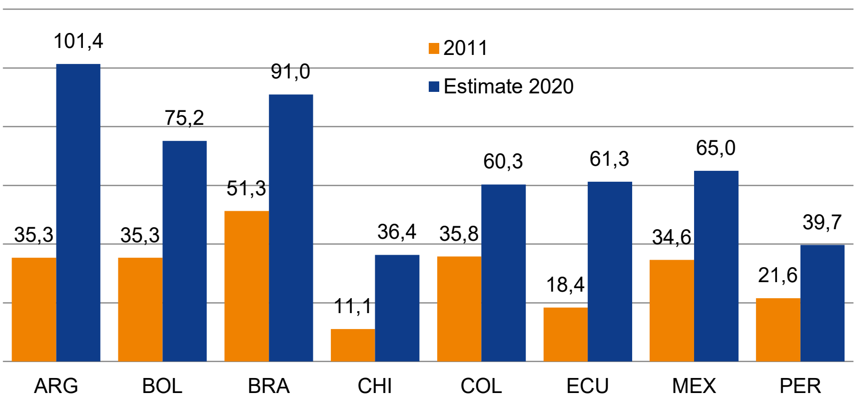
Source: Oxford Economics, DZ BANK

GOVERNMENT BALANCE (% OF GDP)



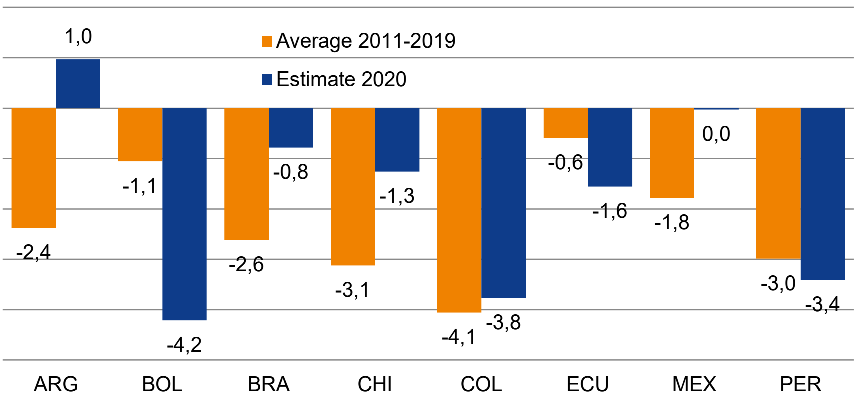
Source: Oxford Economics, DZ BANK

GOVERNMENT DEBT (% OF GDP)



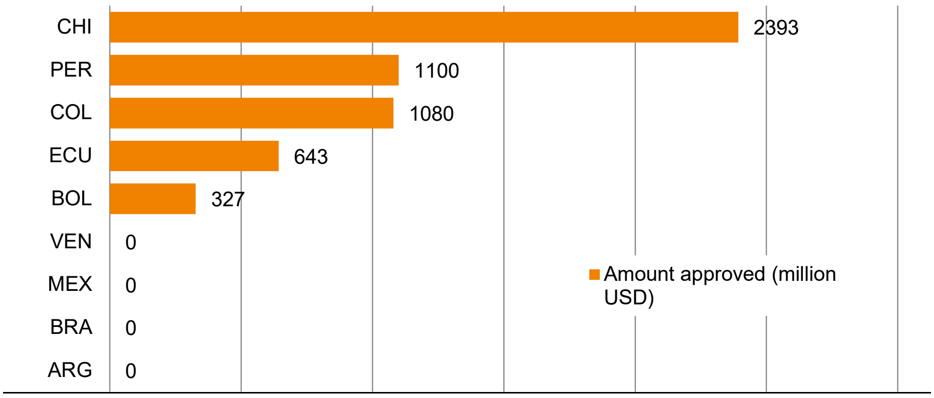
Source: Oxford Economics, DZ BANK

CURRENT ACCOUNT BALANCE (% OF GDP)



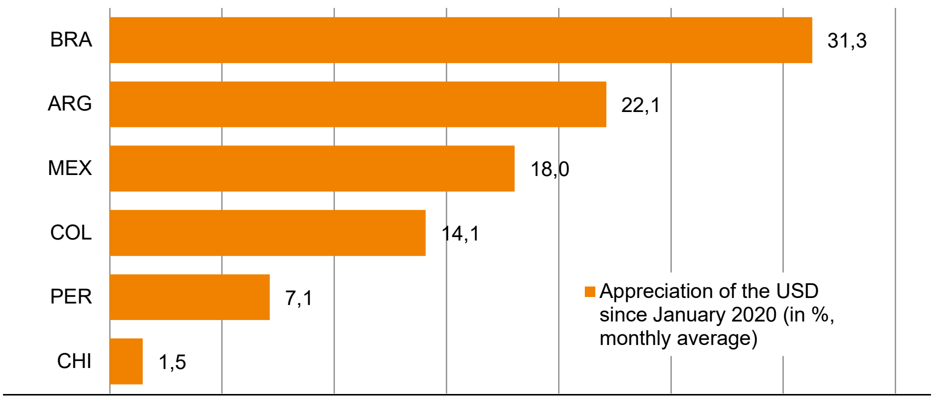
Source: Oxford Economics, DZ BANK

APPROVED CREDITS GRANTED BY THE IMF: PER, CHI AND COL (FCL), ECU AND BOL (RFI)



*FCL=Flexible Credit Line, RFI=Rapid Financing Instrument, Source: IMF, DZ BANK

EXCHANGE RATES: APPRECIATION OF THE US DOLLAR AGAINST THE LOCAL CURRENCY (AUGUST 2020)



Source: FERI, DZ BANK

Overview of economic data

	2018	2019	2020	2021
Argentina				
GDP (% year on year)	-2,4	-2,1	-10,7	8,7
Inflation (% year on year)	34,3	53,5	44,1	34,3
Unemployment rate (in %)	9,2	9,8	10,8	10,2
Public budget balance (as percentage of GDP)	-4,8	-3,7	-8,4	-5,0
Government debt (as percentage of GDP)	86,1	90,2	101,4	89,0
Current account balance (as percentage of GDP)	-4,8	-0,8	1,0	0,3
Bolivia				
GDP (% year on year)	4,2	2,2	-7,4	6,7
Inflation (% year on year)	2,3	1,8	1,4	2,5
Unemployment rate (in %)	4,8	5,2	7,2	5,9
Public budget balance (as percentage of GDP)	-8,1	-7,2	-10,4	-7,0
Government debt (as percentage of GDP)	53,8	60,3	75,2	75,8
Current account balance (as percentage of GDP)	-4,5	-3,3	-4,2	-4,2
Brazil				
GDP (% year on year)	1,3	1,1	-4,4	3,8
Inflation (% year on year)	3,7	3,7	2,6	3,0
Unemployment rate (in %)	12,3	11,9	13,5	12,0
Public budget balance (as percentage of GDP)	-7,1	-5,9	-18,0	-8,3
Government debt (as percentage of GDP)	76,5	75,8	86,2	92,2
Current account balance (as percentage of GDP)	-2,2	-2,7	-1,0	-2,3
Chile				
GDP (% year on year)	4,0	1,0	-5,4	5,0
Inflation (% year on year)	2,3	2,3	2,9	2,2
Unemployment rate (in %)	7,4	7,2	9,2	7,6
Public budget balance (as percentage of GDP)	-1,6	-2,8	-7,6	-7,0
Government debt (as percentage of GDP)	25,6	27,9	36,4	41,2
Current account balance (as percentage of GDP)	-3,6	-3,9	-1,3	-2,5
Ecuador				
GDP (% year on year)	1,3	0,1	-8,4	5,1
Inflation (% year on year)	-0,2	0,3	0,7	1,0
Unemployment rate (in %)	4,1	4,4	9,2	6,0
Public budget balance (as percentage of GDP)	-3,1	-2,8	-7,2	-3,8
Government debt (as percentage of GDP)	46,0	49,6	61,3	61,8
Current account balance (as percentage of GDP)	-1,4	0,0	-1,6	-0,9
Colombia				
GDP (% year on year)	2,5	3,3	-8,5	4,1
Inflation (% year on year)	3,2	3,5	2,6	2,4
Unemployment rate (in %)	9,7	10,5	18,2	16,3
Public budget balance (as percentage of GDP)	-3,1	-2,2	-5,8	-3,6
Government debt (as percentage of GDP)	51,8	50,3	60,3	59,8
Current account balance (as percentage of GDP)	-3,9	-4,2	-3,8	-4,0

Source: Oxford Economics, DZ BANK

	2018	2019	2020	2021
Mexico				
GDP (% year on year)	2,2	-0,3	-9,5	4,0
Inflation (% year on year)	4,9	3,6	3,2	3,5
Unemployment rate (in %)	3,3	3,5	6,0	5,6
Public budget balance (as percentage of GDP)	-2,2	-2,4	-6,0	-4,0
Government debt (as percentage of GDP)	53,6	54,0	65,0	64,0
Current account balance (as percentage of GDP)	-2,1	-0,3	0,0	0,2
Peru				
GDP (% year on year)	4,0	2,2	-12,5	13,6
Inflation (% year on year)	1,3	2,1	1,6	1,8
Unemployment rate (in %)	6,7	6,6	10,9	7,8
Public budget balance (as percentage of GDP)	-2,3	-1,6	-9,5	-3,4
Government debt (as percentage of GDP)	25,8	26,9	39,7	37,7
Current account balance (as percentage of GDP)	-1,7	-1,5	-3,4	-2,2
Venezuela				
GDP (% year on year)	-19,6	-33,8	-37,1	2,0
Inflation (% year on year)	1005131	17365	4557	4184
Unemployment rate (in %)	8,4	9,0	12,7	13,1
Public budget balance (as percentage of GDP)	-16,5	-14,0	-17,3	-10,5
Government debt (as percentage of GDP)	147,8	280,3	358,1	329,8
Current account balance (as percentage of GDP)	12,3	25,5	2,5	1,6

Source: Oxford Economics, DZ BANK

I. IMPRINT

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