A Critical Look at Neglect and Opportunity in Latin America and the Caribbean

Canadian Investment & Trade in Latin America: Obstacles & Opportunities

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Vice-President & Head of International Research
Latin America in Emerging Markets Context

**MIDDLE EAST:** Heightened Security Tensions – Iraq out of control – Ongoing Israel/Palestine conflict – Iran’s Nuclear Development Programme: crisis in sight

**EUROPE:** Russia as global (de)stabilizing force in energy markets – Turkey as geo-strategic link for US & Europe – EU enlargement fatigue? – Avian flu outbreak

**ASIA:** Robust growth in China & India – Quest for global resources – US-India nuclear deal – Massive foreign exchange reserves – China’s banks & currency reforms

**AMERICAS:** Heavy electoral calendar – Low-inflation Growth & Debt sustainability – Energy (in) security? – US foreign policy – Intense Bilateralism ➤ FTAA failure
Net Capital Flows to Emerging Market Economies

Source: Institute of International Finance Sep 2005

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Foreign Direct Investment by Receiving Country

By Major Region
- Asia: 49%
- Latin America: 31%
- Emerging Europe: 11%
- Middle East & Africa: 9%

By Country (6-yr annual average)
- China
- Hong Kong
- Brazil
- Mexico
- Argentina
- Poland
- South Korea
- Russia
- Chile
- Czech Republic
- India
- Hungary

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Comparative Global Financial Sector Strength

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Moody's Financial Strength Index

Jan-06

May-99

Argentina

Venezuela

China

Russia

South Korea

Turkey

India

Brazil

Poland

Czech Republic

South Africa

Mexico

Hungary

Chile

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Changing Leadership in South America
## Electoral Calendar in the developing Americas

<table>
<thead>
<tr>
<th>Country</th>
<th>Regional Elections</th>
<th>Congressional</th>
<th>Presidential</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>HIGH</td>
<td>Oct-05</td>
<td>Mar-07/Oct-07</td>
</tr>
<tr>
<td>Bolivia</td>
<td>HIGH</td>
<td>Dec-05</td>
<td>Dec-05</td>
</tr>
<tr>
<td>Chile</td>
<td>LOW</td>
<td>Dec-05</td>
<td>Dec-05/Jan-06</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>LOW</td>
<td>Feb-06</td>
<td>Feb-06</td>
</tr>
<tr>
<td>Colombia</td>
<td>MEDIUM</td>
<td>Mar-06</td>
<td>May-06</td>
</tr>
<tr>
<td>Peru</td>
<td>HIGH</td>
<td>Apr-06</td>
<td>Apr-06/Jun-06</td>
</tr>
<tr>
<td>Dom. Rep.</td>
<td>LOW</td>
<td>May-06</td>
<td></td>
</tr>
<tr>
<td>Mexico</td>
<td>HIGH</td>
<td>Jul-06</td>
<td>Jul-06</td>
</tr>
<tr>
<td>Brazil</td>
<td>HIGH</td>
<td>Oct-06</td>
<td>Oct-06/Nov-06</td>
</tr>
<tr>
<td>Ecuador</td>
<td>HIGH</td>
<td>Oct-06</td>
<td>Oct-06</td>
</tr>
<tr>
<td>Venezuela</td>
<td>MEDIUM</td>
<td>Dec-05</td>
<td>Dec-06</td>
</tr>
</tbody>
</table>
Changing Leadership in Mexico

Felipe Calderon

Andres-Manuel Lopez-Obrador

Roberto Madrazo

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NAFTA+ Zone Convergence – Equity Securities Markets

Mexico has substantially outperformed its peer North American stock markets, increasing its vulnerability to a sudden asset price adjustment.
The Global Quest for Yield ► Booming Latin American Markets

- North American Stocks (MSCI)
- Latin American Stocks (MSCI)
- Latin American Bonds (EMBI+)

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Core Latin America GDP (ppp-based)

Latin-8 GDP = US$4 trillion

- Brazil 38%
- México 26%
- Argentina 13%
- Venezuela
- Perú
- Chile
- Colombia

Latin-8 GDP per Capita

- Argentina
- Chile
- México
- Brazil
- Colombia
- Venezuela
- Perú

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<table>
<thead>
<tr>
<th>Economic Zone</th>
<th>95-04</th>
<th>2004</th>
<th>2005e</th>
<th>2006f</th>
<th>2007f</th>
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<tbody>
<tr>
<td>NAFTA zone</td>
<td>3.2</td>
<td>4.1</td>
<td>3.5</td>
<td>3.3</td>
<td>2.8</td>
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<tr>
<td>Europe</td>
<td>2.2</td>
<td>1.8</td>
<td>1.4</td>
<td>1.8</td>
<td>1.7</td>
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<tr>
<td>Japan</td>
<td>3.6</td>
<td>2.3</td>
<td>2.8</td>
<td>2.5</td>
<td>2.0</td>
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<tr>
<td>Developing Asia</td>
<td>5.5</td>
<td>6.6</td>
<td>7.1</td>
<td>6.6</td>
<td>6.3</td>
</tr>
<tr>
<td>Developing Europe</td>
<td>3.6</td>
<td>7.2</td>
<td>5.2</td>
<td>5.2</td>
<td>2.4</td>
</tr>
<tr>
<td>Developing Americas</td>
<td>2.2</td>
<td>6.8</td>
<td>4.4</td>
<td>4.3</td>
<td>3.8</td>
</tr>
</tbody>
</table>
While Mexico is structurally converging to NAFTA zone economic performance standards, the rest of the developing Americas is positioned to record higher than average economic growth rates.
NAFTA+ Zone Convergence – Economic Growth

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- Canada
- USA
- Mexico
- Chile
The Region has achieved remarkable success in containing and reversing inflationary pressures. With the exception of Argentina, all countries will post lower rates of inflation in the years ahead.
Central bank autonomy is at the core of the impressive control of inflation in Mexico & Chile.
NAFTA+ Zone Convergence – Short-term Interest Rates

- **US**
- **Canada**
- **Mexico**
- **Chile**

Consumer price inflation rate (year over year)

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Monetary Response to Energy & Demand Shock

Fed Funds
- Fut Jun 06
- Fut Sep 06

UK repo rate
- Fut Jun 06
- Fut Sep 06

Canada O/N
- Fut Jun 06
- Fut Sep 06

Euribor
- Fut Jun 06
- Fut Sep 06
NAFTA+ Zone Convergence – Long-term Government Bond Yields

- **US**
- **Canada**
- **Mexico**
- **Chile**

**Consumer price inflation rate (year over year)**

- **3.0**
- **3.5**
- **4.0**
- **4.5**
- **5.0**
- **5.5**
- **6.0**
- **6.5**
- **7.0**
- **7.5**
- **8.0**
- **8.5**
- **9.0**
- **9.5**
- **10.0**
- **10.5**
- **11.0**

**Dates:**
- Apr-05
- Jun-05
- Aug-05
- Oct-05
- Dec-05
- Feb-06
- Apr-06

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Strong export performance and exchange rate adjustments produced substantial improvement in the region’s current account whereas the most severe risk remains the sizable deficit in the United States.
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Commodity Market Boom

Regional Foreign Trade Bonanza

COPPER

Spot 12-month average

NICKEL

Spot 12-month average

GOLD

Spot 12-month average

ALUMINUM

Spot 12-month average
10-year FX Market Performance vs. USD (%) in the Americas

- Ecuadorian Sucre
- Venezuelan Bolivar
- Uruguayan peso
- Argentine peso
- Costa Rican Colon
- Colombian peso
- Brazilian real
- Peruvian New Sol
- Mexican peso
- Bolivian Boliviano
- Jamaican Dollar
- Canadian dollar
- Chilean peso
- South
- Center
- North

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NAFTA+ Zone Convergence – Currency Performance

Mexican peso
Chilean Peso
Canadian dollar
In search of a new Leverage Shock – USA Twin Deficits

Source: Scotiabank estimates + OECD

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NAFTA+ Zone Convergence – Fiscal (im) Balance

% of GDP - end of period (%)

Canada
USA
Mexico
Chile

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NAFTA+ Zone Convergence – Current Account Balance

% of GDP - end of period (%)

-7.0  -6.0  -5.0  -4.0  -3.0  -2.0  -1.0  0.0  1.0  2.0  3.0

Canada  USA  Mexico  Chile

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A Glance at Global Issues & Uncertainties

- Energy (In) Security in Global Leaders’ Agenda
- The Euro & European Leadership Transition
- Multilateral Trade Liberalization under siege?
- Sustained, yet slowing, Global Economic Growth
- Growing US-China Economic Interdependence
- Housing Markets in the US & UK on Red Alert?
- Synchronized Global Monetary Tightening
- Intensifying US Debt Build-up: Defensive USD?
- Paced Refinement Of China’s Currency Regime
- Persistent Global Equity Market Strength
- Emerging Debt/Equity Market Correction?
- Emergence Of A De-facto G12 Nations Group