

How LatAm has Decoupled

LatAm is on a journey that will not be easily derailed by the global credit crunch, developed market slowdown or commodity corrections. The biggest risk lies at home.

by Manuel J. Balbontin*



What a difference a few years of discipline, responsible governments and learning from past mistakes make. We may be getting a lot of help from Asia and an ongoing secular global demand for commodities. Perhaps we go a little over the top when we talk about decoupling, but you have to agree that this time, we are watching a very different movie to the one we saw, over and over again, in the multiple crises of the last few decades.

Is this decoupling? I strongly believe so.

Today, as the US, Japan and many European countries are not only sneezing, but undergoing severe and lasting colds, LatAm, or at least over 80% of the region is barely sniffing. It is very well prepared to sustain further global deterioration.

Brazil, during the second quarter grew at an historic pace of 6.1%, exceeding even the most optimistic estimates. It is not alone. Peru, Colombia, Mexico and Chile also continue to show quite healthy levels of activity. There is domestic market growth, increased local consumption and infrastructure investment, all coupled with healthy demand for some exports, energy and food.

On the inflation front, Latin America has also made impressive advances over the past years. The countries mentioned above are all enjoying single digit inflation levels and are being subjected to increasing domestic interest rates imposed by very strict independent central banks in an effort to contain imported international inflationary trends due to increasing energy and food prices.

This is a good recipe for an optimistic assessment of the next few years. Latin America is better prepared than ever before to face a bigger and more protracted global slump.

More than a commodity/export story, this is a situation of real political and economic change. Discipline, growing reserves –regional international reserves exceed the amount of external debt by more than \$50 billion – fiscal and monetary obedience and strong banking sectors are all bullish. LatAm is increasingly an investment grade region, with Brazil, Chile, Colombia, Mexico and Peru all deserving the rating.

The Populist Menace

There is meanwhile a new middle class, strong corporate performance and rapidly developing local capital markets. This is a story of domestic growth, both in terms of existing and new consumers and investments, of people working with the people, for the people. Some of the less fortunate that had little reason to believe in it are starting to have faith and derive some of the benefits.

Unfortunately, even though this is the exception rather than the rule, some regional leaders have not learned. Populism, irresponsibility, empty promises, protectionism, and nationalism, are still rampant in Venezuela, Ecuador, Nicaragua and Bolivia.

The only good news for these countries is encapsulated by the Spanish saying “no hay mal que por bien no venga.” These populist leaders are drowning themselves, slowly but surely. Unfortunately, many innocent bystanders are also going down with them, and the resulting destruction will be long lasting.

Argentina is still lying in the middle, but it is being rapidly pushed to choose between a forward looking globalized country and an old fashion populist regime.

Today, the biggest risk that Latin America faces is inside the region. Is not about global slowdown, but internal wealth distribution and its effects on some of these new and fragile democracies.

Unlike most developed markets, every four or five years, some of these countries play Russian roulette. Capitalism, open markets, free trade, economic and political discipline hang in the balance with nationalism, protectionism and the most absurd levels of destruction and irresponsibility.

Let’s not forget that this is not just a Venezuelan, Bolivian and Ecuadorian problem. Many other countries, even investment grade, are not out of the woods. The risk of populist governments resurfacing in the near future is too high.

Think Ollanta Humala in Peru or Andres Manuel Lopez Obrador in Mexico. They and others like them are lurking in the background ready to strike. This is by far the biggest economic and political derailment risk that countries like Peru, Mexico, Brazil and Colombia face over the next 3-5 years.

Local and international governments, the private sector and multilateral organizations have to focus not just on discipline and responsible management of these countries, but also on hastening reform and making sure that new wealth created trickles down to those most in need. This is much easier said than done, but it is nonetheless crucial for Latin American stability over the next decade.

Equities and bonds will rise and fall, bubbles will inflate and burst, the US, Europe and Japan will oscillate in and out of recession. In the meantime, the fundamental well being of many LatAm economies and their citizens will be driven much more by positive and responsible domestic policy than the vicissitudes of external markets.

The world is suffering a serious cold, yet Latin America barely sneezes. Watch out for the poor who are not benefiting, elections are drawing closer.

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