Connor Bugni | HGT #2 | Latin America

Sources:

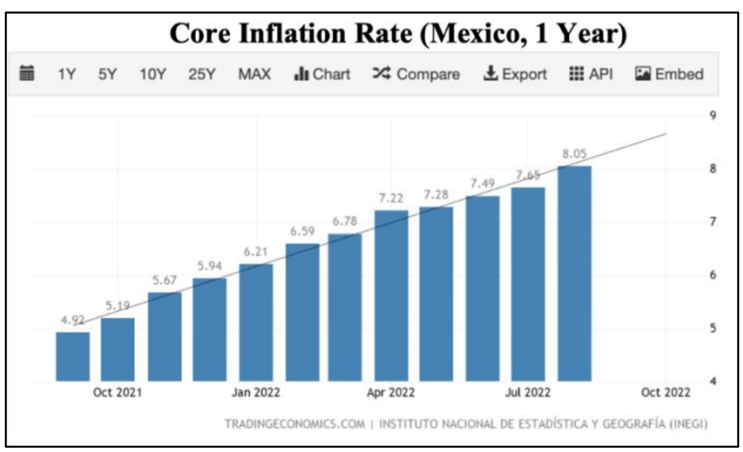
1. *Recession Fears, Europe Supply Woes Weigh on North American Natural Gas Markets Ahead of Winter* – Natural Gas Intel (Baker)
2. *Mexico Unemployment Rate* – Trading Economics (Instituto Nacional De Estadistica Y Geografia (INEGI))
3. *Unemployment Remains in Decline and Reaches 9.1% in the Quarter Ended July* – Agencia de Noticias (Belandi)
4. *Mexico's Economy Grows for Third Straight Quarter; Outlook Improves* – Federal Reserve Bank of Dalles (Cañas, Pranger)
5. *Brazil GDP Growth Rate* – Trading Economics (Instituto Brasileiro de Geografia E Estatistica (IBGE))

Introduction: Latin America has not been immune to the macroeconomic events happening around the world. From the war in Ukraine to the liquidity tightening measures being implemented in the U.S., countries in Latin America have experienced both the economic benefits and pitfalls of the current events happening all around us. Despite the expansiveness of the countries that compose Latin America, two in particular play especially important roles on the world's stage: Mexico and Brazil. In spite of turbulent global economic conditions, all hope has not been lost and, in fact, the Latin American economy is overall well-geared to weather the current economic climate.

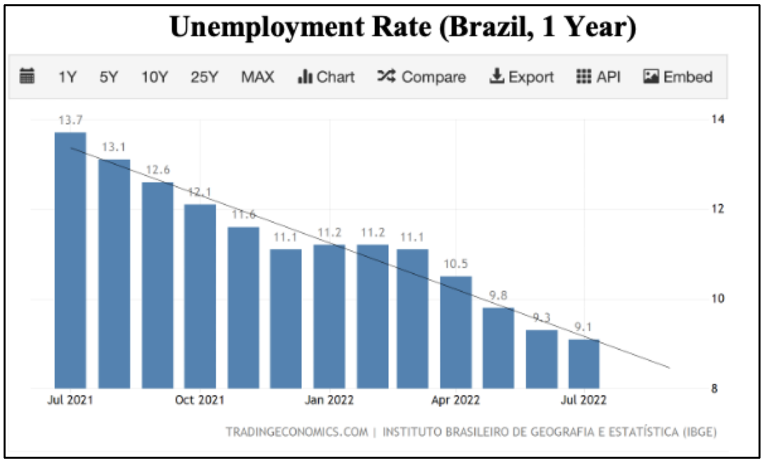
Facts:

- International Monetary Fund forecasts 1.2% economic growth for Mexico in 2023, revised from 2.5% in April. (Baker)
- Unemployment in Mexico fell to 3.4% in July 2022, down from 4.4% in the previous year (INEGI)
- Unemployment in Brazil decreased 1.4% to 9.1% in the most recently ended quarter (Belandi)
- Mexico's Consumer Price Index is up 8.1% year-over-year (Cañas)
- For the Quarter ending June 2022, Mexico's real GDP grew 0.9%, down from 1% growth the previous quarter (INEGI)
- For the Quarter ending June 2022, Brazil's real GDP grew 1.2%, up from 1.1% growth the previous quarter (IBGE)

Analysis: Within Mexico, inflation is clearly on the rise. The Consumer Price Index is up over 8% relative to the same period last year (Cañas) and still appears to have some room to run. Given the valuable trade relationship between Mexico and the U.S., both economies are closely linked. The U.S. posted lower-than-expected inflation in August and thus, it is practical to forecast Mexico will be reaching peak inflation in the near future. Although inflation is well above the Central Bank's (Banxico) target of 3% annually, this is not a surprise considering the supply chain shortages caused as a result of the Covid-19 pandemic, which



all economies are still in the process of recovering from. In this context, inflation in Mexico is not overly worrisome. Furthermore, the demand for labor is strong in Mexico and has led to the unemployment rate dropping to 3.4%, down 1% from 2021 (INEGI). Looking at the most recent drop in unemployment and rise in inflation, it is reasonable to gauge Mexico's economy as somewhat healthy. Mexico will likely perform in line with other Latin American countries, posting low single digit GDP growth.



Looking to Brazil, there are many similar indicators as with Mexico. Brazil saw a decline of 4.7% in their unemployment rate over the past 12 months (Belandi) and posted a positive GDP growth of 1.2% over the quarter ending June 2022 (IBGE). Although GDP is positive, the rate of growth has slowed from previous quarters and will be important to follow moving forward, especially in the event it turns negative. As an emerging market, Brazil faces greater susceptibility to investor sentiment and current events. The upcoming presidential election could have significant fiscal policy implications as well. Overall, Brazil's economy is of equal health as Mexico's, although it could experience greater equity volatility, particularly if the U.S. reports negative GDP growth. Expectations should not be overly optimistic, nor should they be overly pessimistic for Brazil over the coming periods, as it is also likely to perform in line with Mexico and other emerging markets.

Lessons Learned: Using the information addressed in the aforementioned paragraphs, it can be reasonably asserted the economy in Latin America is adequately healthy, with a slight bias toward an upside scenario. While neither Mexico nor Brazil is the healthiest it has ever been, taking macroeconomic conditions, such as pandemic recovery and the war in Ukraine, into account suggests these economies are doing well under the circumstances. The data are trending in favor of these economies continuing to grow, albeit at a slower pace. While economic expansion is great, countries in Latin America are still emerging and are consequently fragile. Reactions in these countries will be more severe than in developed economies, such as the U.S., so negative economic news will have amplified affects. Although it seems inflation has nearly peaked, it is impossible to tell when the causal pressures will begin to subside. In any event, investors, businesses, and consumers would be better off preparing for elevated inflation to persist for the remainder of 2022.

Implications: Even in the presence of an upside bias, it would be naïve to accept this outcome with certainty. Latin American economies are highly dependent on the performance of the U.S. economy, as well as those of developed Europe and Asia. Each of these continents is experiencing global liquidity constraints as policymakers tighten access to financing to combat inflation. Traditionally, such fiscal tightening has preceded economic downturns in emerging markets, such as those in Latin America. That said, I believe Mexico and Brazil to be properly situated to handle these punches as they come. Again, labor demand remains strong and real GDP continues to grow at sustainable rates. Price and currency stabilization will likely take priority over GDP growth in these countries, as that is what we have seen in the U.S. Ultimately, the economy of Latin America is fairly healthy now, but is highly susceptible to global risks (recessions, sociopolitical challenges etc.).