2. Outlook and Policy Challenges for Latin America and the Caribbean

Growth in Latin America and the Caribbean slowed to 1.3 percent in 2014 and is projected to dip below 1 percent in 2015. The downturn in global commodity markets remains an important drag on South America's economies, even as lower oil prices and a solid U.S. recovery support activity elsewhere in the region. Country-specific factors, including weak private sector confidence in Brazil and the intensifying economic crisis in Venezuela, further weigh on the outlook for regional growth. Meanwhile, evidence of economic slack remains limited, underscoring the presence of supply-side bottlenecks. Flexible exchange rates can play a critical role in adapting to tougher external conditions, but policymakers will also need to ensure prudent fiscal positions, keep financial sector vulnerabilities in check, and tackle long-standing structural problems to raise investment, productivity, and potential growth.

Economic activity in Latin America and the Caribbean (LAC) continued to weaken in 2014 (Figure 2.1). With just 1.3 percent growth, regional output expanded at the slowest pace since 2002 (except for the short-lived recession in the midst of the global financial crisis in 2009). The weakness was concentrated in South America, where falling commodity prices reinforced a generalized sense of leaner times, weighing down on private demand. Domestic policy uncertainties further depressed confidence in some countries.

The challenging economic environment has also affected financial markets. The region's main currencies have depreciated by almost 20 percent on average against the U.S. dollar since mid-2014; equity prices have languished; and external bond spreads have widened, especially for companies and sovereigns exposed to commodities. Nonetheless, LAC continued to receive sizable portfolio inflows, and domestic bond markets generally held up well, in a context of very low global benchmark rates.
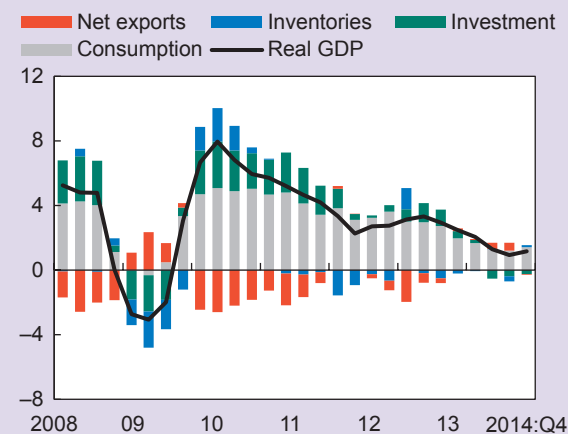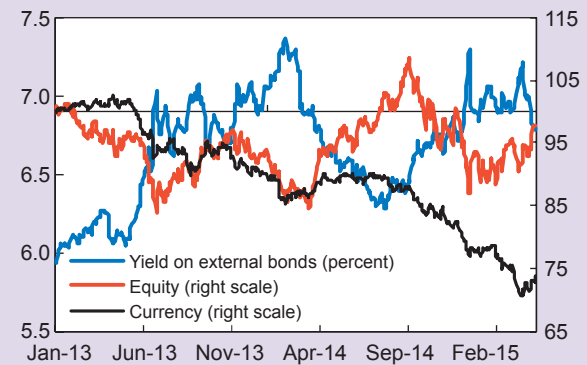
Figure 2.1

Economic activity has slowed further, led by weak investment. In this context, the region's floating currencies have depreciated markedly.

Selected Latin American Countries: Contributions to Real GDP Growth[1]
(Year-over-year percent change)

Latin America: Financial Markets[2]

Sources: Bloomberg, L.P.; Haver Analytics; national authorities; and IMF staff calculations.

[1] Seasonally adjusted. Purchasing power parity–weighted GDP averages of Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, Paraguay, Peru, and Uruguay. Inventories include statistical discrepancies. See Annex 2.1 for details on Argentina's GDP.

[2] Yield on external bonds is based on J.P. Morgan Emerging Markets Bond Index for Latin America. Equity index is MSCI Emerging Markets Latin America Index equity local net total return index. Currency index is Bloomberg J.P. Morgan Latin America Currency Index. The equity and currency indices are rebased to January 2, 2013 = 100.

Near-term prospects remain fairly dim for South America, with output contractions projected in three of the largest economies (Argentina, Brazil, and Venezuela) for 2015, while only Chile and Peru

13

would see a pick-up in growth. Elsewhere in LAC, growth is projected to be steady (Central America and the Caribbean) or strengthen (Mexico); see Figure 2.2. On balance, regional growth is expected to decline for a fifth consecutive year, bottoming out at just below 1 percent before staging a moderate recovery in 2016. The large downward revision to 2015 growth (almost 1.4 percentage points) relative to the October 2014 *World Economic Outlook* is driven by lower projections for South America—especially Brazil, Ecuador, and Venezuela—whereas prospects for Central America and the Caribbean have improved somewhat.

External factors play an important role in shaping the outlook for the region:

- *Broad-based weakness in commodity markets* is causing a protracted downward adjustment in corporate investment, well beyond the most exposed industries in commodity-dependent economies (see Chapter 4). Weaker long-term income prospects in these economies are also weighing on consumer sentiment and spending, even though labor markets have remained relatively tight to date.

- That said, *the sharp drop in oil prices since mid-2014* has provided divergent impulses to different parts of LAC which, on balance, should be broadly neutral for regional growth. While cheaper oil is intensifying terms-of-trade pressures for a handful of net oil exporters, it is creating significant relief elsewhere. Central America and the Caribbean are among the main beneficiaries, with average cuts to their import bills of 3–4 percentage points of GDP in 2015. In many economies, these savings will accrue at least partially to the private sector, boosting purchasing power, whereas governments in oil-exporting countries have tended to keep fuel prices stable, reducing effective subsidy levels (Figure 2.3).

- The *uneven recovery of the global economy*, where solid U.S. growth contrasts with still-subdued prospects for the euro area and Japan, and a secular slowdown in China, is set to benefit those LAC countries most closely linked to the U.S. economy. From a trade perspective, this
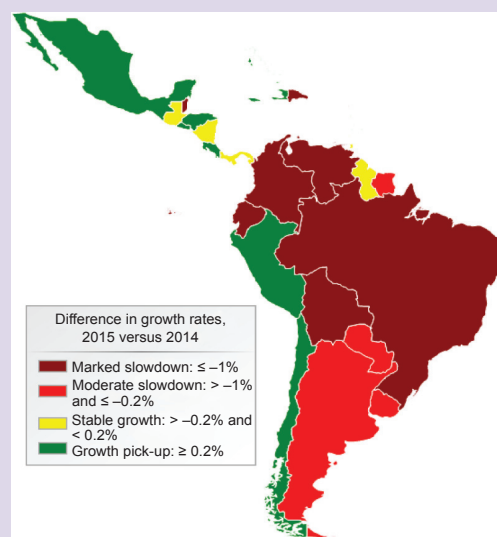
Figure 2.2

Regional growth is projected to decline for a fifth consecutive year in 2015, though prospects vary across subregions.

LAC: Real GDP Growth
(Percent)

	2013	2014	Projections 2015	Projections 2016
LAC	**2.9**	**1.3**	**0.9**	**2.0**
Financially integrated economies (LA6)	3.9	2.4	2.4	3.2
Other commodity exporters	6.0	2.0	0.6	1.6
CADR	4.2	4.4	4.2	4.2
Caribbean				
Tourism-dependent	1.1	1.5	2.0	2.4
Commodity exporters	3.1	2.8	2.4	3.2
Memorandum items:				
Brazil	2.7	0.1	−1.0	1.0
Mexico	1.4	2.1	3.0	3.3

LAC: Growth Momentum, 2014–15

Difference in growth rates, 2015 versus 2014

- Marked slowdown: ≤ −1%
- Moderate slowdown: > −1% and ≤ −0.2%
- Stable growth: > −0.2% and < 0.2%
- Growth pick-up: ≥ 0.2%

Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.
Note: CADR = Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama; LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay; LAC = Latin America and the Caribbean. For definitions of the other country groups and details on the aggregation method, see Table A2.1.

includes Mexico, much of Central America, and a few South American countries (Figure 2.4). However, the latter mostly export commodities to the U.S. market, and thus are primarily exposed to the global commodity cycle rather than specific U.S. demand conditions. For Mexico, Central America, and the Caribbean, in turn, positive spillovers from the United States also arise from remittance and tourism flows.

Figure 2.3

Worsening terms of trade have hit South America hard, weighing on capital spending. The growth effect of cheaper oil is more differentiated, as many economies stand to benefit, either through lower private sector fuel bills or through fiscal savings in countries with a history of high energy subsidies.
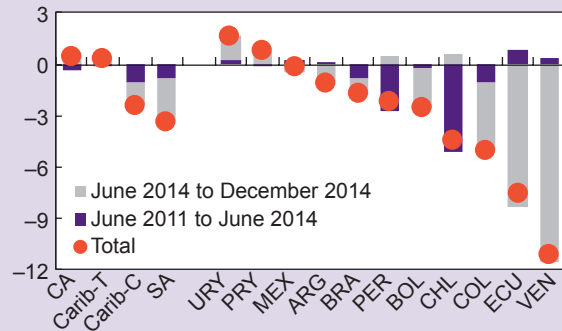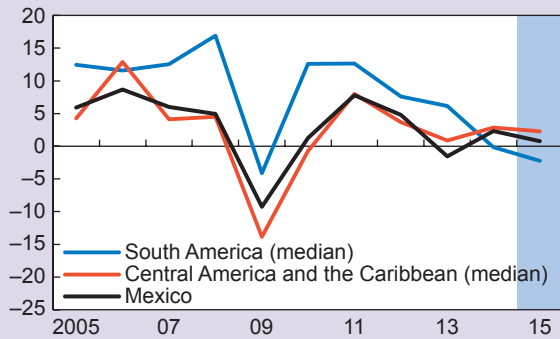
Commodity Exports[1]
(Percent of GDP)

Legend: South America, Central America, Caribbean
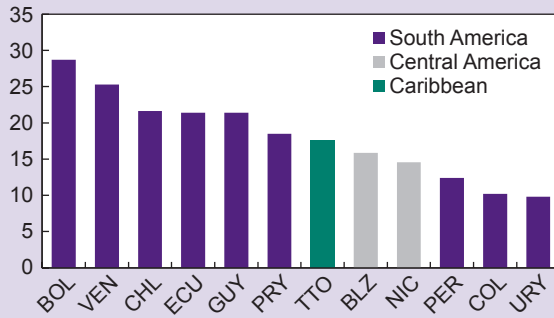
Change in Commodity Terms of Trade, 2011–14[2]
(Cumulative log change, percent)

Legend: June 2014 to December 2014; June 2011 to June 2014; Total

Real Fixed Investment Growth
(Percent change)

Legend: South America (median); Central America and the Caribbean (median); Mexico

Recent Growth Revisions versus Net Oil Exports[3]

y-axis: 2015 growth revisions (percent)
x-axis: 2013 net oil exports (percent of GDP)

Labeled points: COL, BOL, BRA, ECU, VEN
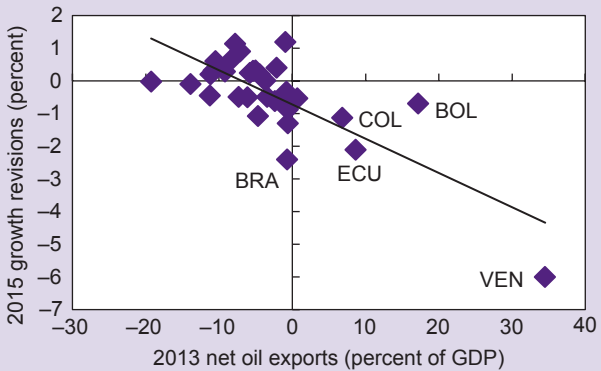
Adjustment Mechanisms for Domestic Fuel Prices with Respect to Global Oil Price Changes
(Proportion of total sample, 32 countries)

Market: 25.0
Regulated: Discretion 43.8, Formula 31.3, total 75.0
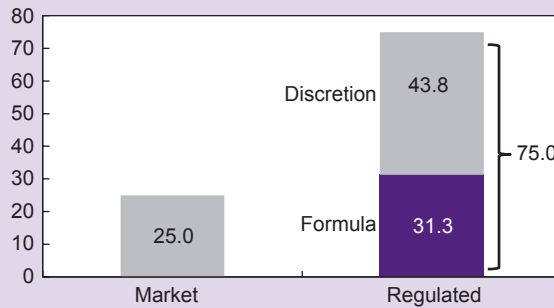
Expected Pass-Through Ranges Associated with the Recent Decline in Oil Prices[4]
(Proportion of total sample)

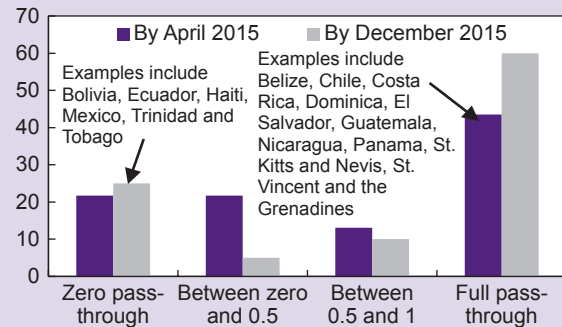Legend: By April 2015; By December 2015

Examples include Bolivia, Ecuador, Haiti, Mexico, Trinidad and Tobago

Examples include Belize, Chile, Costa Rica, Dominica, El Salvador, Guatemala, Nicaragua, Panama, St. Kitts and Nevis, St. Vincent and the Grenadines

Categories: Zero pass-through; Between zero and 0.5; Between 0.5 and 1; Full pass-through

Sources: Gruss (2014); Haver Analytics; IMF, World Economic Outlook database; UN Comtrade; and IMF staff calculations and projections.

Note: CA = Central America; Carib-T = tourism-dependent Caribbean; Carib-C = commodity-exporting Caribbean; SA = South America. For country name abbreviations, see page 79.

[1] Average ratios to GDP for 2010–12. Excludes precious metals and re-exports. Venezuela data refer to net oil exports.

[2] Commodity terms of trade are weighted by the share of commodity exports/imports in GDP, so a 1 percent increase can be interpreted approximately as an income gain of 1 percent of GDP. Indices exclude precious metals, except for Bolivia, Colombia, and Peru. See also Annex 3.1 and Gruss (2014).

[3] Growth data refer to the difference between the 2015 growth projections from the April 2015 *World Economic Outlook* and October 2014 *World Economic Outlook*. Net oil export data for Bolivia include natural gas.
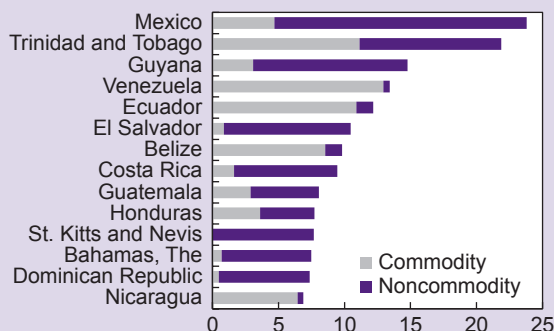
[4] Sample includes 23 countries for April 2015 and 20 countries for December 2015. Pass-through computations based on domestic-currency prices of oil and fuel.

Figure 2.4

The U.S. recovery will have the greatest positive impact on countries featuring close linkages via trade, tourism, and remittances.
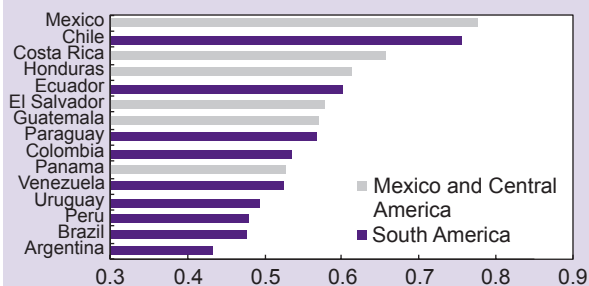
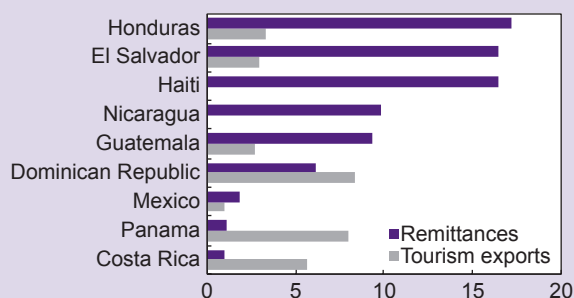**Exports of Goods to the United States[1]**
(Percent of GDP)

Mexico
Trinidad and Tobago
Guyana
Venezuela
Ecuador
El Salvador
Belize
Costa Rica
Guatemala
Honduras
St. Kitts and Nevis
Bahamas, The
Dominican Republic
Nicaragua

■ Commodity
■ Noncommodity

0   5   10   15   20   25

Business Cycle Comovement with the U.S. Economy, 2002–14[2]
(Correlation coefficient for monthly industrial output series)

Mexico
Chile
Costa Rica
Honduras
Ecuador
El Salvador
Guatemala
Paraguay
Colombia
Panama
Venezuela
Uruguay
Peru
Brazil
Argentina

■ Mexico and Central America
■ South America

0.3   0.4   0.5   0.6   0.7   0.8   0.9

Remittances and Tourism Exports, 2013–14[3]
(Average, percent of GDP)

Honduras
El Salvador
Haiti
Nicaragua
Guatemala
Dominican Republic
Mexico
Panama
Costa Rica

■ Remittances
■ Tourism exports

0   5   10   15   20

Sources: Haver Analytics; IMF, *Direction of Trade Statistics*; IMF, World Economic Outlook database; national authorities; UN Comtrade; and IMF staff calculations.
[1] Average ratios to GDP for 2011–13 or latest available. Countries not shown have ratios below 6 percent of GDP.
[2] Correlation calculated using the U.S. Industrial Production Index with the corresponding IP/Manufacturing/Economic Activity index for each country.
[3] Remittance data for Costa Rica and Dominican Republic end in September 2014. Panama refers to 2013. Tourism exports for Dominican Republic and Guatemala refer to latest eight-quarter data.

Beyond these external influences, there are important country-specific factors that will differentiate economic developments across the region. Most prominent among these are the persistent weakness of private sector confidence in Brazil and the intensifying crisis in Venezuela. More broadly, the capacity to respond to adverse external developments depends on domestic policy space, which is more ample in the Andean economies (Chile, Colombia, and Peru) than in most other countries of the region.

Together, these factors underscore the significant challenges facing South America, notably those economies with weaker macroeconomic fundamentals.
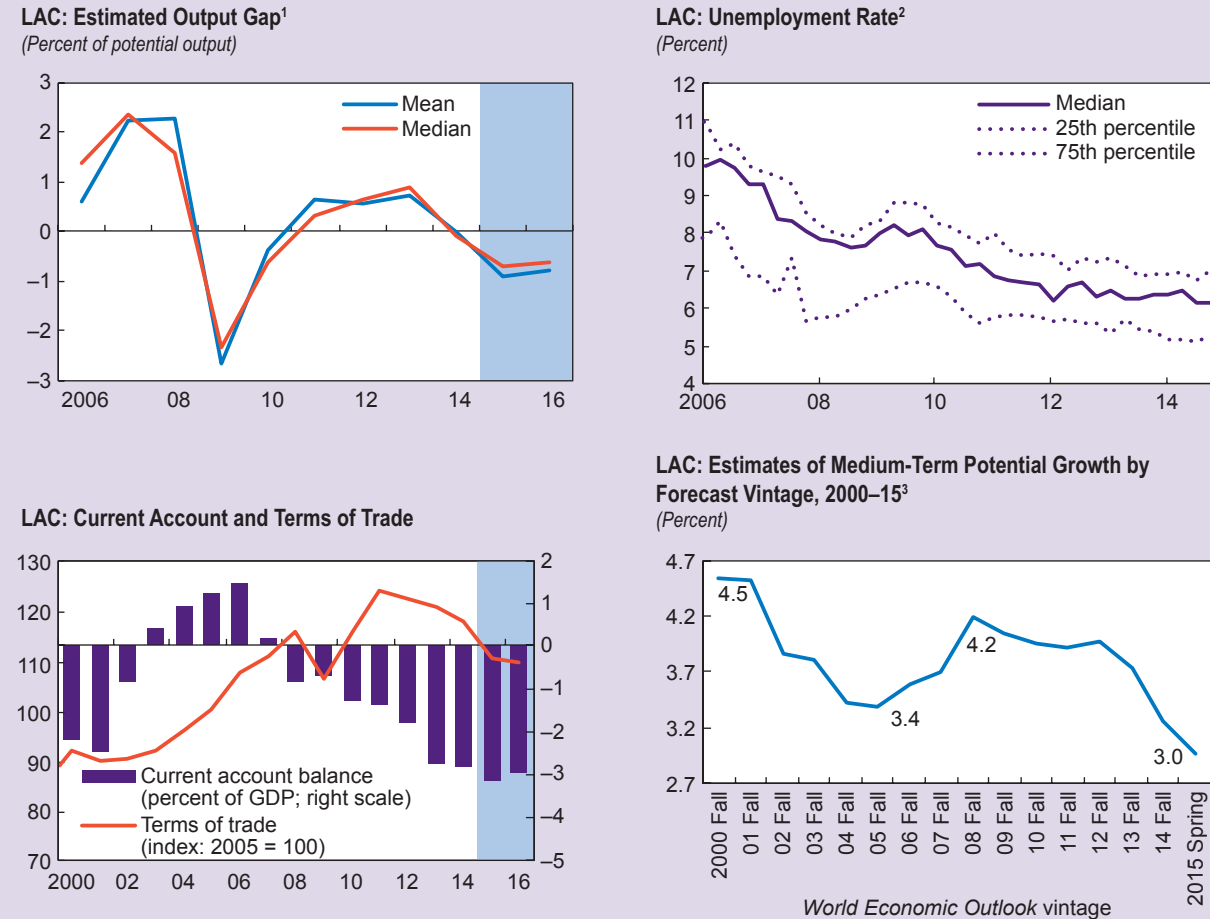
Despite the pronounced slowdown over the past several years, there are few indications of significant economic slack in LAC. Labor markets have started to weaken, but unemployment remains at historically low levels in most of the larger economies;[1] inflation is projected to decline only gradually toward midpoint targets, as the impact of lower commodity prices is balanced by currency depreciation and broadly closed output gaps; and current account deficits have generally widened further (Figure 2.5). Coupled with the drop in investment and chronically sluggish productivity growth, these observations point to a deeper problem of low potential growth, which in the absence of significant structural reforms could jeopardize the region's catch-up process. Indeed, projections for medium-term growth have fallen to their lowest level in at least 15 years.

Risks around the outlook are directly related to the factors mentioned previously and, overall, are still weighted to the downside. Further weakness in commodity prices, perhaps related to a more pronounced deceleration of investment in China, would heighten pressures on South America's net commodity exporters. Stronger-than-expected

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[1] Employment statistics might conceal a weakening in labor demand that occurs chiefly through reduced hours worked by workers in the informal sector. Yet, other indicators, including wage growth, have also remained robust. More broadly, Box 2 in the October 2014 *Regional Economic Outlook: Western Hemisphere Update* shows that labor market developments through mid-2014 were generally consistent with Okun's law.

Figure 2.5

Despite the marked slowdown in growth, output remains close to its estimated potential, consistent with the observation of historically low unemployment rates and wide current account deficits. Meanwhile, estimates of medium-term potential growth have fallen further.

LAC: Estimated Output Gap[1]
(Percent of potential output)

LAC: Unemployment Rate[2]
(Percent)

LAC: Current Account and Terms of Trade

LAC: Estimates of Medium-Term Potential Growth by Forecast Vintage, 2000–15[3]
(Percent)

Sources: Haver Analytics; IMF, World Economic Outlook database; and IMF staff calculations and projections.
Note: LAC = Latin America and the Caribbean.
[1] Purchasing power parity–weighted GDP statistics; sample includes all 27 LAC countries for which IMF staff estimates output gaps.
[2] Includes Argentina, Brazil, Chile, Colombia, Dominican Republic, Ecuador, Mexico, Peru, Uruguay, and Venezuela.
[3] Reflects projected real GDP growth for the last year ($t + 5$) of the forecast horizon.

U.S. growth would benefit its closest trading partners in the region, but could also accelerate the normalization of U.S. monetary policy. In a scenario of rapidly rising U.S. bond yields, renewed financial turmoil in the euro area, or other global shocks, disruptive moves in Latin American currency and capital markets cannot be ruled out, even as monetary expansion proceeds in the euro area and Japan (see also Chapter 3 of the April 2014 *Regional Economic Outlook: Western Hemisphere*, which analyzes spillovers from U.S. monetary policy in detail). The most exposed are

countries with large current account deficits and heavy reliance on U.S. dollar debt, although high levels of official foreign exchange reserves should provide a significant buffer.

The protracted weakening of economic activity also heightens the risk of domestic policy missteps, especially attempts to stave off a structural slowdown with excessive policy stimulus. At present, most countries seem to be resisting this risk, and fiscal stimulus is generally limited to economies with strong public balance sheets, such as Chile and Peru.

However, commitments to fiscal prudence could come under political pressure as expectations for continued economic and social progress become harder to fulfill in a less favorable environment.

Further risks to macroeconomic stability could arise from a sharper-than-expected worsening of asset quality in the banking system, as lower earnings take their toll on corporate and household borrowers (Box 2.1). Policymakers will therefore have to monitor closely indicators of financial vulnerability and ensure that lenders maintain sufficient balance sheet buffers to manage the downswing in the credit cycle.

Financially Integrated Economies

Developments and Outlook

Growth trends among the financially integrated economies (LA6, comprising Brazil, Chile, Colombia, Mexico, Peru, and Uruguay) are projected to diverge over the period ahead, reflecting distinct exposures to global commodity markets and other country-specific factors (Figure 2.6):

- *Brazil* is undergoing its most serious economic downturn in more than two decades, with output projected to contract by 1 percent in 2015. Private investment remains an important drag, as long-standing competitiveness problems are being compounded by weaker terms of trade and high uncertainty, including about the fallout from the Petrobras investigation and the impact of a protracted drought on electricity supply. Consumer sentiment has also worsened sharply, amid elevated inflation, tighter credit supply, and an incipient weakening of the labor market. The authorities' move to tighten macroeconomic policies adds to the short-term weakness of demand, but is critically needed to contain the rise in public debt and rebuild trust in the macroeconomic policy framework. Similarly, the ongoing realignment of key relative prices, including the real exchange rate, should help to improve prospects for investment over time.

- *Mexico*, the second-largest economy in the region, faces a comparatively favorable outlook, even though earlier growth forecasts have been pared back once again. GDP is projected to expand by 3 percent this year. Stronger external demand from the United States has started to support activity, whereas domestic confidence and demand have yet to perk up. The immediate impact on growth from lower oil prices is limited, given the relatively small share of hydrocarbon sector activity in GDP. However, the drop in government revenue has prompted a modest fiscal tightening for 2015. Potential longer-term gains from reforms in the telecommunications and energy sector remain significant, though persistently low oil prices could dampen investor interest over time.

- Among the other financially integrated economies, *Chile*, *Colombia*, and *Peru* are all facing headwinds from lower commodity export prices and the related cuts to corporate investment. In Chile and Peru, these headwinds have been felt for some time, as metal prices started to decline more than three years ago. More recently, cheaper oil imports have provided some offset. Growth is likely to rebound this year, helped by expansionary policies and the removal of short-term brakes on activity, notably last year's delays in Peruvian mining production. Still, important uncertainties cloud the horizon in both countries, related to external conditions, the impact of ongoing reforms in Chile, and slow investment execution at the subnational level in Peru. For Colombia, in turn, terms of trade pressures have mounted recently, as the oil price collapse has hit the country's largest export sector. Growth is projected to ease below 4 percent but remain fairly resilient, as the sharp depreciation of the peso should support noncommodity exports over time. *Uruguay*, meanwhile, continues to post solid growth but is undergoing a gradual slowdown, linked to weak activity in neighboring Argentina and Brazil.
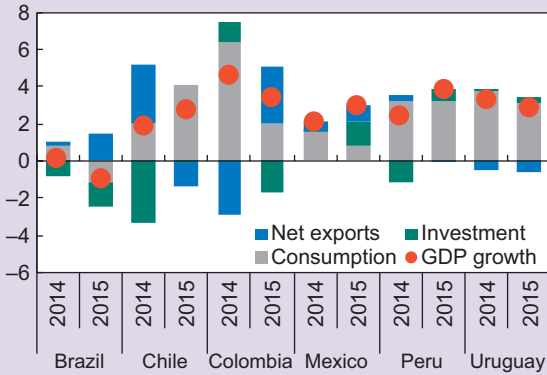
Across most of the LA6, employment growth has slowed. At the same time, persistently low unemployment rates and still-solid wage growth suggest that economic slack generally remains

Figure 2.6

Although growth dynamics across the financially integrated economies are expected to diverge, labor markets remain relatively firm in most countries. Depreciated currencies should help reduce current account deficits over time, though they contribute to keeping inflation above target over the near term.
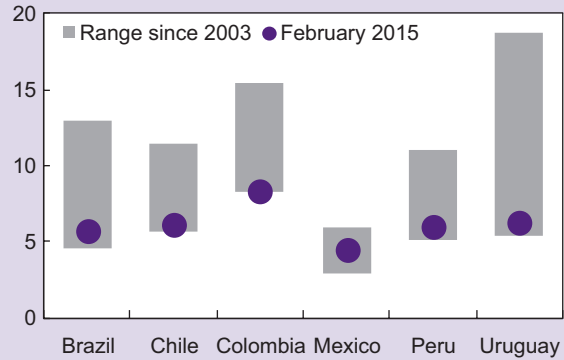
**LA6: Real GDP Growth Contributions**
(Percentage points)

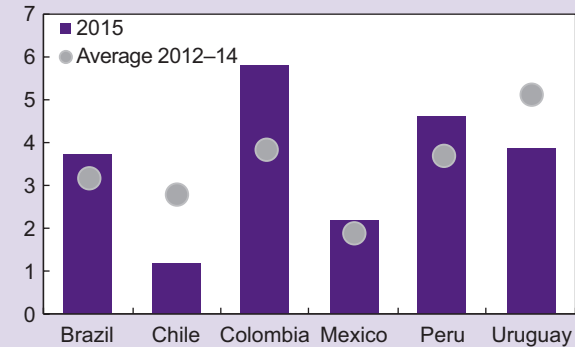Legend: Net exports, Investment, Consumption, GDP growth

Categories: Brazil, Chile, Colombia, Mexico, Peru, Uruguay (2014, 2015)

LA6: Unemployment Rate[1]
(Percent)

Legend: Range since 2003, February 2015

Categories: Brazil, Chile, Colombia, Mexico, Peru, Uruguay

LA6: Nominal Wage and Employment Growth
(Median, 12-month percentage change, seasonally adjusted)

Legend: Nominal wage[2], Employment
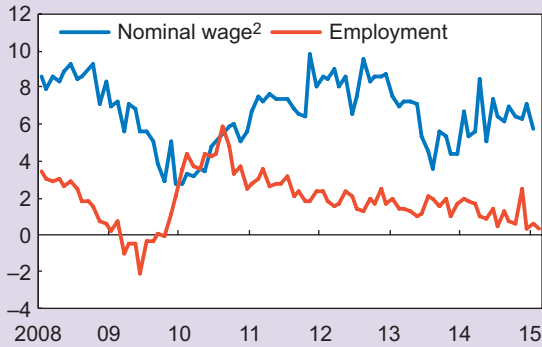
LA6: Current Account Deficit
(Percent of GDP)

Legend: 2015, Average 2012–14

Categories: Brazil, Chile, Colombia, Mexico, Peru, Uruguay

LA6: Change in NEER versus Change in Commodity Terms of Trade Since April 2013[3]

Axes: Change in nominal effective exchange rate (percent) vs Change in commodity terms of trade (percent)

Legend: LA6, Other countries
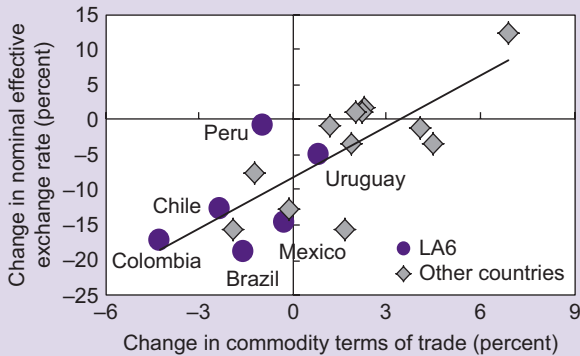
LA6: Headline Inflation Less Inflation Target
(12-month percentage change)

Legend: Brazil, Uruguay, Mexico, Average, Chile, Colombia, and Peru
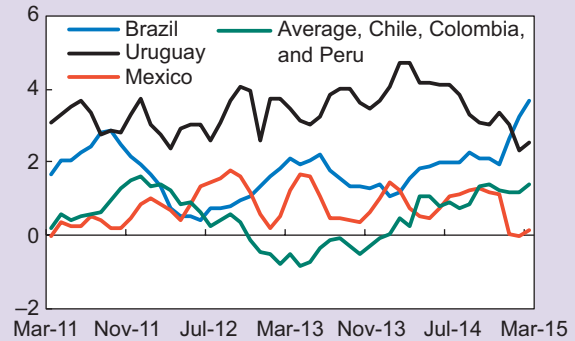
Sources: Bloomberg, L.P.; Haver Analytics; IMF, *Information Notice System*; IMF, World Economic Outlook database; national authorities; UN Comtrade; and IMF staff calculations.

Note: LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay; NEER = nominal effective exchange rate.

[1] Seasonally adjusted. Latest observation for Uruguay is January 2015.

[2] Peru data are minimum wage.

[3] Data are through end-February 2015. Other countries include Hungary, India, Indonesia, Israel, Korea, Malaysia, Philippines, Poland, Romania, South Africa, Thailand, and Turkey. Commodity terms of trade are weighted by the share of commodity exports/imports in GDP, so a 1 percent increase can be interpreted approximately as an income gain of 1 percent of GDP. Indices exclude precious metals, except for Colombia and Peru. See also Annex 3.1 and Gruss (2014).

limited. Large deficits in external current accounts and above-target inflation rates support this view, even though they have also been affected by other important factors of late:

- External deficits have continued to widen in several of the LA6 economies (Chile being a notable counterexample) as lower commodity prices have reduced export proceeds. In response, exchange rates have depreciated, and typically more so in countries hit by larger terms-of-trade shocks. Over time, these weaker exchange rates— some currencies have depreciated as much as 25 percent against the U.S. dollar in six months, though movements in trade-weighted terms have been much less extreme—should help to boost net exports. Yet, IMF staff research suggests that much of this adjustment typically occurs through the compression of imports, as domestic demand cools, rather than a rise in export volumes (see Chapter 3; see also Box 2.2 on the broader implications of U.S. dollar strength for Latin America).

- Depreciated exchange rates have also put some upward pressure on consumer prices. However, estimated pass-through rates are moderate (below 0.1), and lower commodity prices have had a countervailing effect.

On balance, macroeconomic data do not yet point to a significant shortfall in aggregate demand, cautioning against excessive macroeconomic stimulus even where policy space would be available in principle.

Amid persistent current account deficits, the structure of external financing has been broadly stable (Figure 2.7). Both foreign direct investment (FDI) and portfolio inflows have remained sizable, while other investment has edged up. Thus, foreign holdings of domestic-currency government bonds have reached new record levels in Colombia and Mexico. Simultaneously, corporate bond issuance has continued at a rapid clip, albeit below 2013 peak rates.
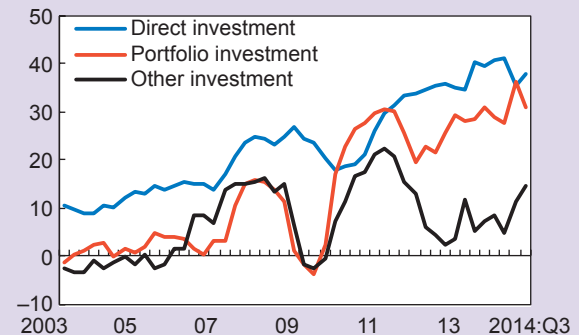
Countries' considerable reliance on non-FDI inflows could foreshadow further volatility in currencies and broader asset markets.

Figure 2.7

Capital inflows have remained strong, supporting high foreign holdings of local-currency bonds and robust corporate issuance.

LA6: Gross Capital Inflows[1]
(Billions of U.S. dollars, four-quarter moving average)

LA5: Nonresident Holdings of Domestic Debt
(Percent of total)
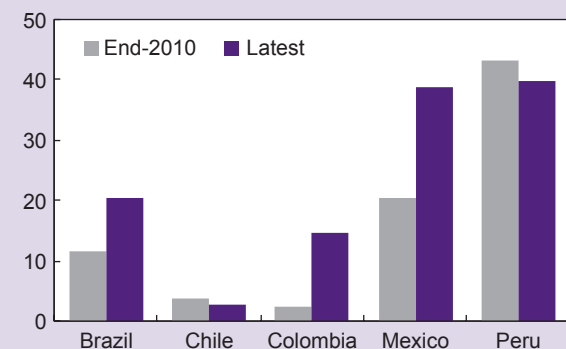
LA6: Foreign Bond Issuance: Nonfinancial Firms[2]
(Billions of U.S. dollars, 12-month moving average)
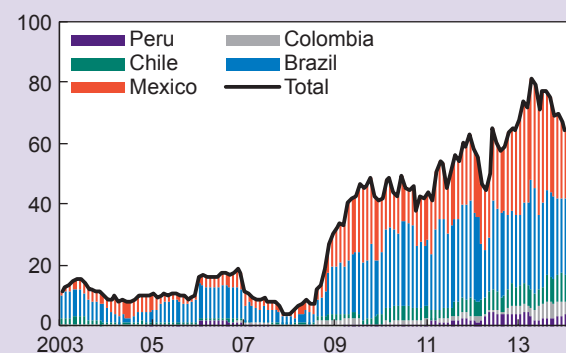
Sources: Dealogic; IMF, *Balance of Payments Statistics Yearbook*; national authorities; and IMF staff calculations.
Note: LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay; LA5 excludes Uruguay.
[1] Excludes Peru.
[2] Residency-based issuance criterion for all countries except Brazil, which is based on nationality criterion.

This also entails the risk that external financing conditions for Latin American borrowers might tighten abruptly, whether in response to specific news from the region or because of external developments, notably the anticipated tightening of U.S. monetary policy.

Concerns are focused on firms from the financially integrated economies that have ramped up their bond issuance in international capital markets since the global financial crisis. Immediate repricing and rollover risks are limited by the fact that many firms used the favorable market conditions of recent years to issue longer-maturity bonds with fixed-rate coupons.

Question marks remain, however, over the possibility that some firms may have built up foreign-currency liabilities that are not matched by foreign-currency claims or revenue streams. To date, there is no evidence that such open positions have led to financial difficulties among LA6 firms, despite the sharp recent depreciation of domestic currencies. Nonetheless, this risk requires close monitoring, especially since firms' debt-servicing capacity is already being pressured by lower earnings (Figure 2.8). In this context, some commodity sector firms have seen a notable increase in credit spreads, and corporate investment budgets have been trimmed across the board.

Reflecting the more challenging outlook, domestic credit growth has also slowed. Lower loan demand has been a principal factor, but in some cases (notably, loans extended by public banks in Brazil) a deliberate tightening of credit supply is playing a role as well. Thus far, the share of nonperforming loans has generally remained moderate (at or below 3 percent), but asset quality is likely to worsen over the period ahead, especially in economies that saw credit grow at a rapid clip in recent years and are now facing a sharp economic slowdown (Box 2.1). In these economies, the unanticipated weakening of activity is likely to catch some borrowers off guard. For households, the main concerns relate to a higher risk of unemployment, while relatively underdeveloped mortgage markets limit the risks associated with falling house prices.

Figure 2.8

Weaker corporate earnings have reduced interest coverage ratios and prompted cuts to investment plans. Credit growth has slowed.

Recent Evolution of the Interest Coverage Ratio and Return on Equity[1]
(Median; x-axis: ratio; y-axis: percent)
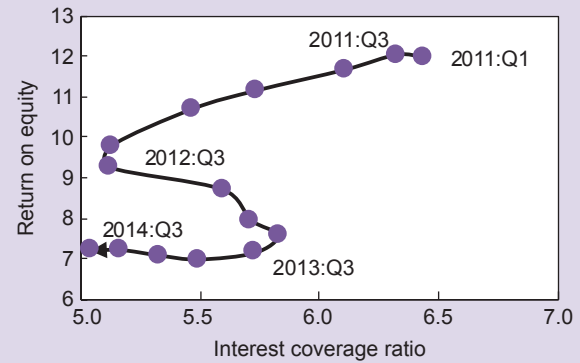
Capital Expenditure of Selected Large Firms[2]
(Index: 2005 = 100)
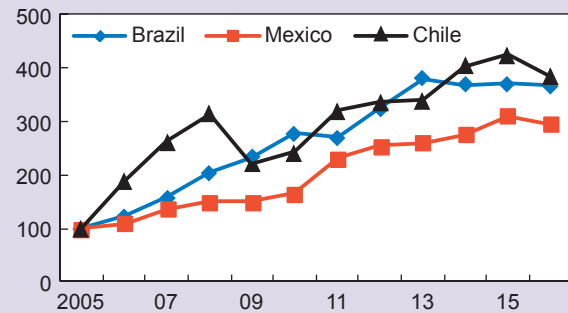
LA6: Credit to the Private Sector in Real Terms
(12-month percentage change)
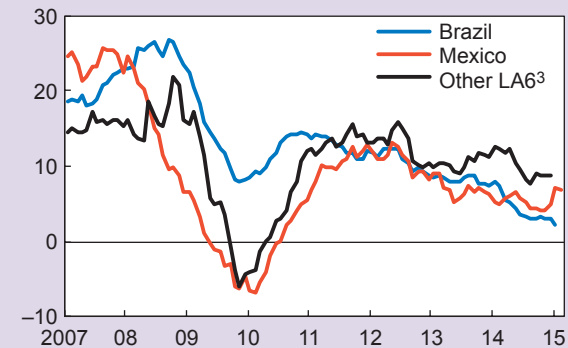
Sources: Bloomberg, L.P.; Haver Analytics; IMF, Financial Soundness Indicators database; national authorities; and IMF staff calculations.
[1] Sample includes about 400 nonfinancial firms from Brazil, Chile, Colombia, Mexico, and Peru. Four-quarter rolling averages of median values.
[2] Index based on sum of nominal capital expenditures (in local currency) of 26 large companies from Brazil, Chile, and Mexico; historical data up to 2013, and analyst forecasts for 2015 and 2016; 2014 refers to outturns where available, and otherwise analyst forecasts.
[3] Simple average of Chile, Colombia, Peru, and Uruguay.

Policy Priorities

The combination of subdued growth, limited economic slack, and growing financial risks presents significant challenges to policymakers. Although the extent of these challenges varies across the LA6 economies, a core set of five policy considerations applies to all of them.

First, flexible exchange rates can play a crucial role in the adjustment to a more difficult external environment. In particular, weaker currencies help to redirect demand toward domestically produced output, thereby reducing external deficits.

Strong official reserve buffers allow the authorities in the LA6 to mitigate acute depreciation pressures (Figure 2.9), but interv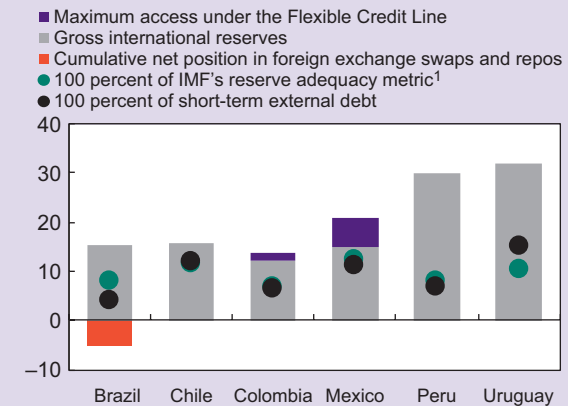ention should be limited to cases where exchange rate volatility becomes excessive, market conditions turn disorderly, or other significant financial stability risks emerge. Thus far, currency movements have been large but orderly, and in general have reduced, rather than amplified, concerns about currency misalignment. It is therefore judicious that authorities have mostly allowed their exchange rates to adjust, despite relatively frequent intervention in Peru (a highly dollarized economy, where sharp exchange rate movements could have more disruptive effects on the real economy). The Brazilian authorities' decision to end their long-running foreign exchange swap program, which had accumulated a synthetic short position in foreign currency of more than $113 billion by end-March, is welcome.

Second, vigilant monitoring of financial stability risks has gained further importance in an environment of sharp exchange rate movements, lower earnings and, in some cases, rising interest rates. Banking systems in the financially integrated economies generally continue to post solid levels of capitalization and profitability, yet the challenges ahead argue for a clear focus on maintaining or even strengthening existing buffers. In this regard, it is welcome that the authorities in Peru recently raised further the reserve requirement on foreign-currency-denominated deposits. Regarding the corporate sector, further efforts

Figure 2.9

Reserve buffers remain strong across the LA6 economies. Central banks have recently cut rates in Chile and Peru, but hiked in Brazil.

LA6: Official Foreign Exchange Reserves, 2014
(Percent of GDP)

- ■ Maximum access under the Flexible Credit Line
- ■ Gross international reserves
- ■ Cumulative net position in foreign exchange swaps and repos
- ● 100 percent of IMF's reserve adequacy metric[1]
- ● 100 percent of short-term external debt

LA5: Monetary Policy Rates[2]
(Percent)

- ■ Sample range
- — End-August 2014
- ▲ Latest
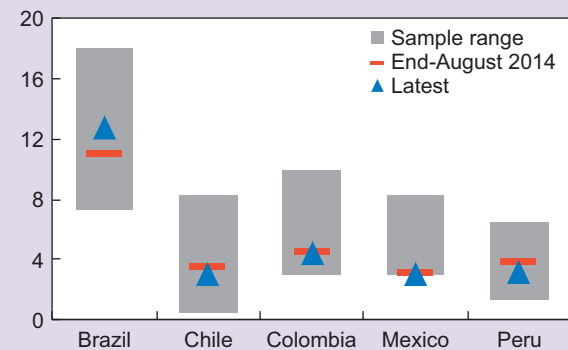
Sources: Bloomberg, L.P.; IMF, *International Financial Statistics*; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
Note: LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay; LA5 excludes Uruguay.
[1] Methodology described in Moghadam, Ostry, and Sheehy (2011).
[2] Sample period is January 2006 to April 13, 2015

are needed to gather granular data on unhedged currency exposures.

Third, monetary policy should remain focused on keeping expected inflation in line with official targets. Unlike many emerging markets in Asia and Europe, where inflation rates have fallen to very low levels, the LA6 generally still face above-target inflation, partly reflecting sharp recent currency depreciation. As a result, policy easing has been

more limited, with only Chile and Peru recently enacting modest rate cuts (Figure 2.9). Meanwhile, central banks in Brazil and Uruguay continue to face the task of strengthening the credibility of their monetary frameworks, as inflation persists in high single digits. The determined further tightening of monetary policy in Brazil since late 2014 is appropriate in this regard.

*Fourth, fiscal policy* choices need to weigh not only what is *desirable* from a cyclical perspective, but also what is *feasible* without jeopardizing debt sustainability. Given still-limited slack in most economies, the case for policy stimulus appears tenuous from the outset. Even where rising output gaps are in prospect due to the recent terms-of-trade shock, policymakers must consider the likelihood that much of that shock is likely to be permanent (see Chapter 3). As such, fiscal policy can soften but not prevent the impact of the shock, consistent with the design of structural fiscal rules like those in Chile and Colombia. For several economies, cyclical considerations are, in any event, outweighed by the reality of limited fiscal space. Indeed, the average structural deficit across the LA6 has gradually widened in recent years and is now 2 percentage points of GDP higher than in 2004 (Figure 2.10), when the terms of trade were much weaker than they are today. This deficit bias has been particularly apparent in Brazil, where, as a consequence, the authorities now have little choice but to tighten fiscal policy in the midst of a downturn. Tighter fiscal stances are also impending in Mexico, Uruguay, and, by 2016, in Colombia. Chile and Peru, in turn, have the most latitude to smooth the inevitable adjustment to a weaker terms-of-trade environment, reflecting low public debt levels.

Last but not least, the above considerations underscore the central importance of *structural reforms* to restore robust, sustainable growth. With the tailwinds of the commodity boom decidedly over, long-standing problems of low saving, investment, and productivity have come back to the fore in many economies. Addressing these problems is becoming ever more urgent to avoid an extended period of low growth. Efforts should focus on eliminating critical bottlenecks

Figure 2.10

Fiscal policy in the financially integrated economies has tended to be countercyclical in recent years, however with a deficit bias. As a result, debt has risen in several countries.

LA5: Real GDP Growth and Structural Fiscal Balance[1]
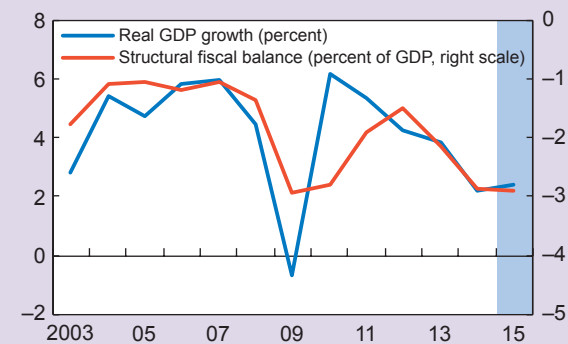
LA6: General Government Gross Debt and Net Lending[2]
(Percent of fiscal year GDP)
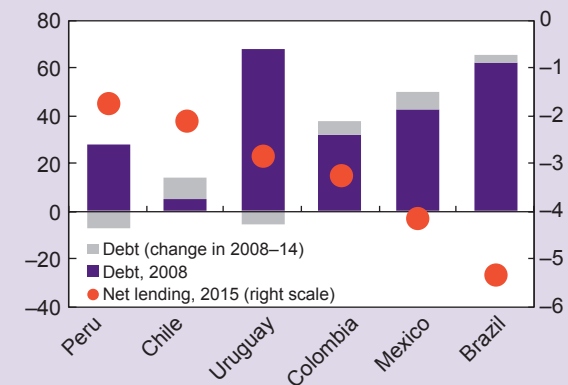
Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.
Note: LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay. LA5 excludes Uruguay.
[1] Simple average of Brazil, Chile, Colombia, Mexico, and Peru.
[2] For definitions of government coverage, see Table A2.2.

in infrastructure and human capital—both areas where private investment can play a role but where some reprioritization and reoptimization of public spending will also be required (Figure 2.11).[2] These efforts need to be supported by steps to improve the business environment, with the goal of fostering more diversified, resilient, and prosperous economies (see also Chapter 5).

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[2] On the challenge of raising domestic saving rates, see Grigoli, Herman, and Schmidt-Hebbel (2014).

Figure 2.11

LA6: Structural Performance Indicators
(Percentile ranks)
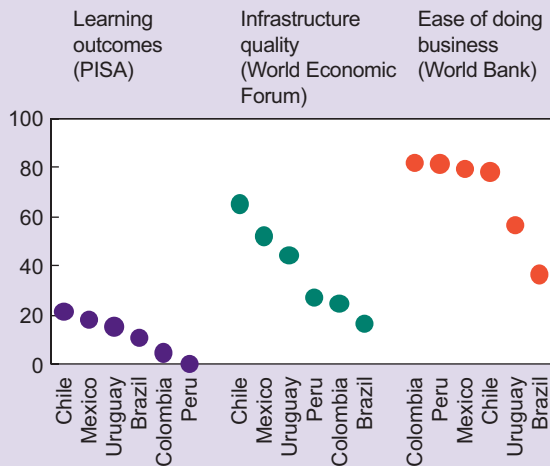
Sources: Organisation for Economic Co-operation and Development, *2012 Programme for International Student Assessment* (PISA); World Bank, 2015 Ease of Doing Business database; World Economic Forum, *2014–15 Global Competitiveness Report*; and IMF staff calculations.
Note: LA6 = Brazil, Chile, Colombia, Mexico, Peru, and Uruguay. The scale reflects the percentile distribution in all countries for each respective survey; higher scores reflect higher performance.

Several countries have already launched reforms in these areas, but more work is needed in many of the LA6 economies to strengthen governance, reduce excessive bureaucratic burdens, and promote competition.

Other Commodity Exporters

Developments and Outlook

Economic developments across the remaining (less financially integrated) commodity exporters of South America have continued to diverge (Figure 2.12). The halving of oil prices since mid-2014 has caused major setbacks for Bolivia, Ecuador, and especially Venezuela, whereas Paraguay—which exports agricultural products and electricity but imports all of its fuel needs—has benefited. Beyond these external shocks, domestic policies have played a crucial role in determining the country-specific outlook.

For *Venezuela*'s economy, the massive terms-of-trade shock suffered over the past few months has made

Figure 2.12

Growth prospects differ markedly across the other South American commodity exporters, as solid activity in Bolivia and Paraguay contrasts with a deepening crisis in Venezuela.

Other Commodity Exporters: Real GDP Growth, 2015
(Percent)
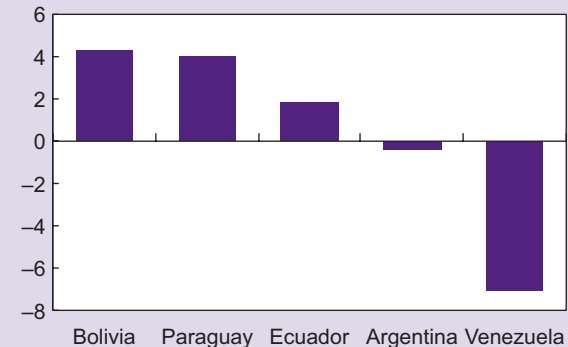
Inflation and Parallel Market Exchange Rates, 2012:Q1–2014:Q4[1]
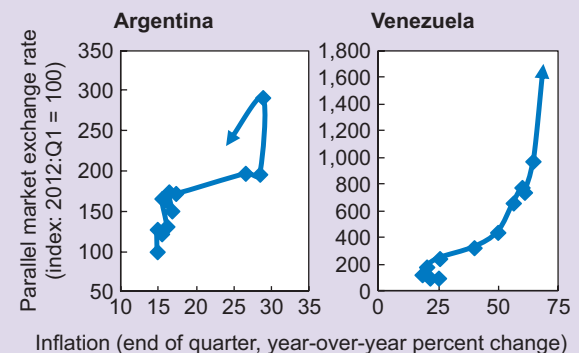
Other Commodity Exporters: Sovereign Credit Spreads[2]
(Basis points)
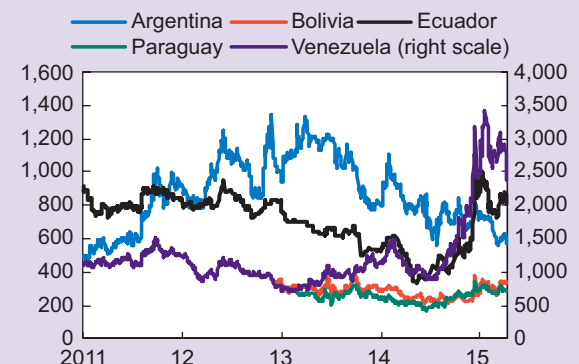
Sources: Bloomberg, L.P.; Haver Analytics; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
[1] Inflation data for Argentina reflect staff estimates through 2014:Q3 and official IPCNu data thereafter.
[2] Refers to J.P. Morgan Emerging Market Bond Index.

an already difficult situation even worse. Years of unsustainable macroeconomic expansion and heavy-handed microeconomic intervention have created a mix of high double-digit inflation, acute scarcities, and depressed private sector confidence that prompted a slide into recession in early 2014. All of these problems have recently been aggravated by a sharp drop in government revenue from oil exports, which has further intensified the shortage of foreign currency and driven the informal exchange rate up to a level of 280 bolivars per U.S. dollar, more than 40 times higher than the lowest official exchange rate in Venezuela's complex multiple-exchange-rate system. Simultaneously, financial markets have started to signal a high risk of default. The authorities have responded to the deepening economic crisis by further tightening price and quantity controls and nationalizing more enterprises. Amid the ensuing disruptions, Venezuela is projected to face both the highest inflation rate (95 percent) and third-largest output contraction (−7 percent) of any economy in the world in 2015.

Argentina's macroeconomic imbalances also remain significant, following an extended period of fiscal expansion that has increasingly relied on central bank financing. Intrusive restrictions on trade and currency markets have also created a significant gap between the official and the informal exchange rate of the peso. That said, the exchange rate gap has stabilized at 40–50 percent since late 2014, and inflation appears to have eased back into the lower double digits. Financial investor sentiment toward Argentina has also recovered some ground, even though the ongoing standoff with holdout investors leaves the country shut off from global bond markets. Investors' relative optimism appears linked to Argentina's moderate external indebtedness along with an expectation that some of the most disruptive economic policies might be relaxed following elections in October. Recent legal changes have also improved the investment climate for international oil companies, holding out the prospect of tapping Argentina's large potential in the energy sector. However, adverse terms-of-trade developments (notably the sharp drop in soy prices), weak activity in Brazil, and the renewed

appreciation of the real effective exchange rate have added fresh headwinds to growth. Thus, output is projected to decline 0.3 percent in 2015, extending last year's slowdown.

Ecuador is projected to suffer a marked deceleration, with growth at 1.9 percent in 2015, while *Bolivia*'s growth rate would ease to a still-robust 4.3 percent. Both economies have large hydrocarbon sectors and are undergoing the adjustment to much lower oil and gas prices after a decade of boom-like conditions. For Ecuador, which has seen the largest expansion of primary government spending of all economies in the region since 2004, the absence of fiscal buffers poses a particular challenge. As a fully dollarized economy, Ecuador also cannot benefit from nominal exchange rate depreciation to help the adjustment to weaker external conditions. In this context, the authorities have recently imposed import surcharges (subject to review by the World Trade Organization), citing concerns over balance of payments pressures. In Bolivia, fiscal reserves are available to smooth the downturn, but several ongoing policy initiatives—including steps to expand central bank lending to public enterprises—are likely to accelerate the weakening of public balance sheets. Moreover, the authorities have resisted any currency depreciation, hampering the necessary rebalancing of demand (Figure 2.13).

Figure 2.13

Other Commodity Exporters: Real Effective Exchange Rates
(Index: January 2012 = 100)
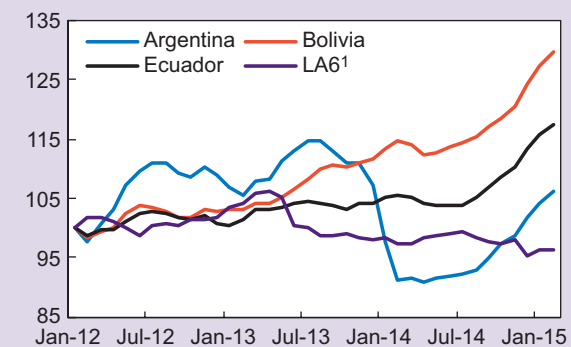
Source: IMF, *Information Notice System*.
[1] Simple average of Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.

Paraguay, in turn, is projected to sustain growth at about 4 percent in 2015, spurred by cheaper oil, a projected rebound in electricity generation, and the launch of several infrastructure projects. Solid macroeconomic fundamentals, including moderate public sector debt and a recently established inflation targeting regime, underpin the comparatively favorable outlook, and have manifested themselves in external borrowing costs well below those of many regional peers.

Policy Priorities

Necessary policy adjustments mirror the distinct circumstances of each country, although fiscal consolidation, eliminating energy subsidies, and greater exchange rate flexibility are common priorities in all of the economies where macroeconomic imbalances have been mounting.

In Venezuela, the damage caused by years of economic mismanagement will be impossible to reverse in a short time. Yet, any successful stabilization of the situation will have to involve further depreciation of the (average) official exchange rate, a reduction of the large fiscal deficit, and an end to monetary financing, as well as the unwinding of a host of dirigiste measures that have choked private sector activity.

Although its economic disruptions are less extreme, Argentina will require a similar mix of tighter macroeconomic policies, a weaker exchange rate, and less microeconomic distortion to lay the foundation for a return to stability and growth.

For Bolivia and Ecuador, the principal challenge is to rein in fiscal and external deficits that have opened up with the drop in oil and gas prices. The very large expansion of government spending in recent years has arguably created areas of inefficiency where savings can and should now be sought. Greater flexibility of the exchange rate and, failing that, of domestic prices would facilitate the adjustment. Paraguay, in turn, will need to integrate the envisaged buildup of public infrastructure into a prudent medium-term

fiscal plan. Across all three economies, resolute efforts to address governance issues and enhance educational outcomes are also crucial.

Central America and the Dominican Republic

Developments and Outlook

Unlike South America, Central America's economies are expected to benefit from the current external environment (Figure 2.14). The global pattern of U.S.-led recovery is particularly favorable for the region, given its strong real-sector linkages to the U.S. economy through exports and remittances, which are likely to outweigh the tightening of financial conditions resulting from orderly U.S. monetary policy normalization.[3] Windfall gains from the decline in oil prices are also important, as all Central American countries are net oil importers (Box 2.3). At the same time, there are country-specific headwinds to growth; and many economies cope with long-standing fiscal and external vulnerabilities as well as deep-seated problems of governance and security, that leave some clouds on an otherwise brighter outlook.

Growth in 2015 is projected at a solid 4¼ percent, close to last year's outturn. However, this headline number masks important country differences. In the Dominican Republic, growth is set to slow after several years of above-trend expansion. Guatemala's economy should continue to grow at a broadly unchanged rate, as the effect of a more favorable external environment makes up for a negative base effect, related to last year's launch of several new mining projects. Elsewhere in the region, growth will also be steady or increase modestly, despite a number of idiosyncratic factors that dampen the boost from external conditions—these include the normalization of the public investment cycle in Panama, reduced financing from Venezuela's Petrocaribe program, and welcome fiscal consolidation in Honduras and possibly Costa Rica.

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[3] See the April 2014 *Regional Economic Outlook: Western Hemisphere*, Chapter 3.

Figure 2.14

Growth prospects for Central America have brightened, owing to cheaper oil and a solid U.S. recovery.

CADR: Revisions to Growth and Current Account Projections, 2015
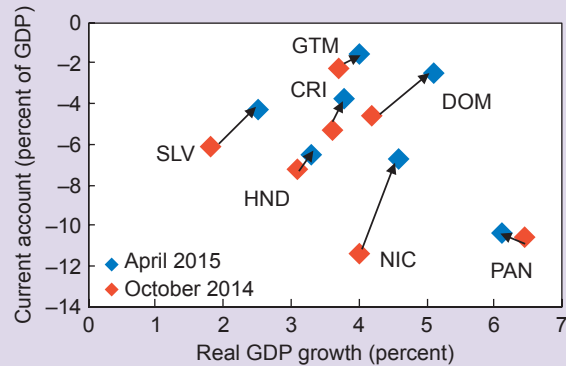
CADR: Destination of Goods Exports, 2013[1]
(Percent of GDP)
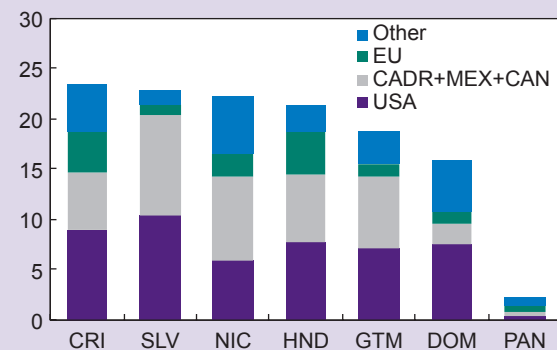
Workers' Remittances[2]
(12-month percentage change, 3-month moving average)
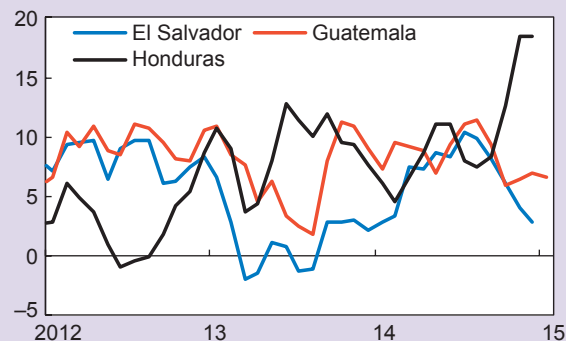
Sources: Haver Analytics; IMF, *Direction of Trade Statistics*; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
Note: CADR = Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama; EU = European Union. For country name abbreviations, see page 79.
[1] Many countries also export significant amounts of services to the United States, which are not captured in this chart owing to data constraints.
[2] Measured in U.S. dollars.

Headline inflation across Central America has fallen much more sharply in the wake of lower global oil prices than in larger Latin American countries. This reflects both greater pass-through to domestic energy prices and the absence of depreciation pressures in the region.

However, fiscal vulnerabilities render some Central American countries susceptible to downside risks, especially since public debt levels are projected to stay elevated and, in some cases, increase further under current policies.

External bond spreads have widened again during the recent period of volatility in emerging markets, highlighting the risks associated with large financing needs (Figures 2.15 and 2.16).

External vulnerabilities are tempered by the prospect of narrower current account deficits that should be fully financeable by foreign direct investment in several countries. Current account deficits will shrink due to both lower oil prices and higher U.S. growth, and could approach 5 percent of GDP in 2015 on average, down from nearly 6 percent of GDP in 2014 and 7 percent of GDP in 2013. Foreign direct investment and portfolio flows have remained steady, with sovereigns continuing to tap international markets in significant amounts. International reserve coverage has improved somewhat, although buffers generally remain modest.

Credit growth has eased in most countries from the peaks reached in recent years, with the Dominican Republic a notable exception. Slower growth in foreign-currency-denominated loans has been an important factor in Central America, possibly reflecting some greater internalization of exchange rate risks by borrowers—particularly in Costa Rica, following a period of exchange rate volatility in early 2014—as well as greater use of alternative funding sources, notably external corporate bond issuance in the case of Guatemala. Although banks are generally well capitalized and already meet Basel III liquidity requirements, vulnerabilities to credit risks from unhedged borrowers have increased after a period of strong growth in foreign currency loans.

Figure 2.15

Fiscal and external vulnerabilities remain significant in several countries, although current account deficits are set to shrink.

CADR: Gross Public Sector Financing Needs and External Debt Spreads[1]

HND
SLV
CRI
DOM
BRA
PER
PAN
MEX
GTM
CHL
COL
CADR
LA5

EMBI spreads (basis points)

Gross financing needs, 2015–16
(average, percent of GDP)
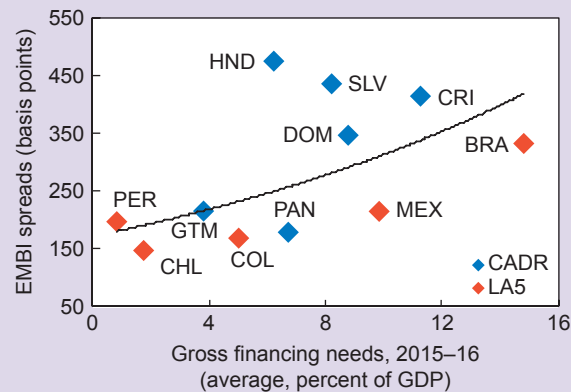
CADR: Net Capital Flows[2]
(Four-quarter moving average, percent of GDP)

Other
Portfolio
Foreign direct
Financial account

2005   07   08   10   11   13   14:Q3
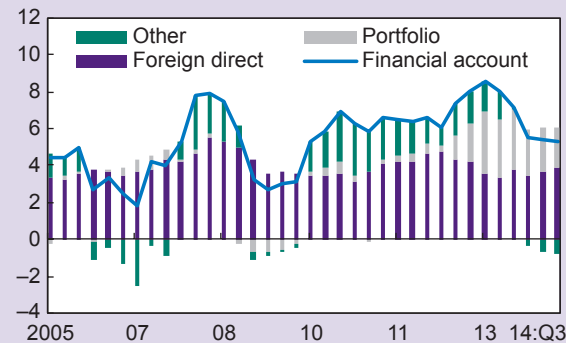
CADR: Reserve Coverage, 2014
(Percent of GDP)

Gross international reserves
100 percent of short-term external debt
100 percent of IMF's reserve adequacy metric[3]
3 months of imports

CRI   DOM   SLV   GTM   HND   NIC   PAN
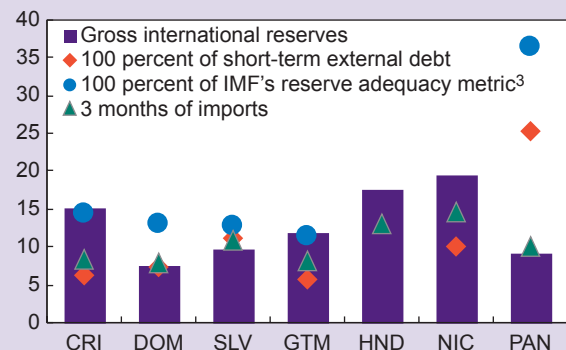
Sources: IMF, *Balance of Payments Statistics Yearbook*; national authorities; and IMF staff calculations.
Note: CADR = Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama; EMBI = Emerging Markets Bond Index. For country name abbreviations, see page 79.
[1] Definition of the public sector varies by country.
[2] CADR excluding El Salvador and Panama.
[3] Methodology described in Moghadam, Ostry, and Sheehy (2011).

Figure 2.16

Under current policies, public debt would continue to rise in several economies. Credit growth has eased in Central America recently.

CADR: General Government Gross Debt
(Percent of fiscal year GDP)

2014
2020
2008

SLV   CRI   HND   PAN   DOM   NIC   GTM
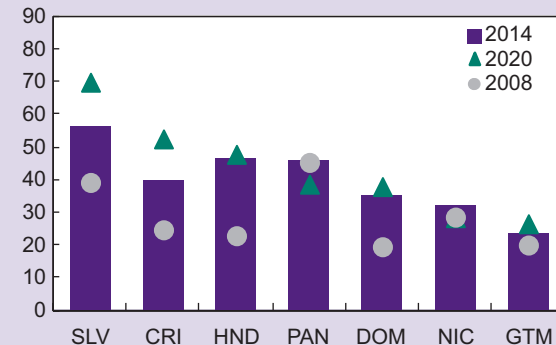
CADR: Credit to the Private Sector[1]
(Year-over-year percentage change)
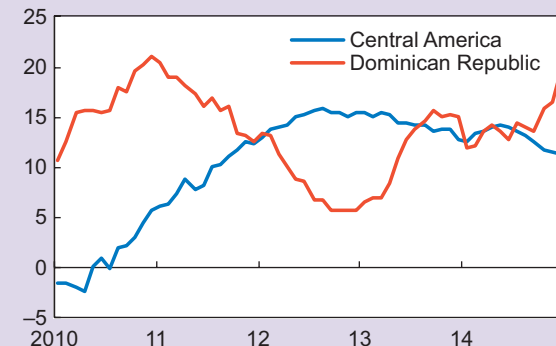
Central America
Dominican Republic

2010   11   12   13   14

Sources: IMF, World Economic Outlook database; national authorities; and IMF staff calculations.
Note: CADR = Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama. For country name abbreviations, see page 79.
[1] Central America is the simple average of Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

Policy Priorities

Policymakers in the region should take advantage of the opportunity provided by a more favorable external environment to further reduce fiscal vulnerabilities and foster inclusive growth. On the fiscal front, any direct windfall gains from faster growth and reduced public subsidies (resulting from lower oil prices) should be saved at least initially, given uncertainties about their durability as well as the need to rebuild policy space to respond to future negative shocks. This would be of particular importance in countries with large sustainability

gaps. Lower oil prices should also facilitate the implementation of measures foreseen in existing or recommended consolidation programs, including the phasing out of energy subsidies and increases in value-added tax rates. More generally, countries would benefit from strengthening policy frameworks, including through the introduction of fiscal rules and adoption of measures to enhance transparency and minimize contingent risks from public-private partnerships.

Central banks in the nondollarized economies should advance their efforts to strengthen inflation-targeting frameworks. In general, it seems appropriate to avoid responding to the first-round effects on headline inflation from lower commodity prices, especially in countries where underlying price pressures could soon reemerge due to limited spare capacity. Indeed, the fall in headline inflation provides an opportunity to better anchor inflation expectations that have persisted above official targets in some cases. Allowing greater exchange rate flexibility will also be important to underpin the credibility of inflation-targeting frameworks and facilitate the adjustment to external shocks. In this regard, the recent removal of the exchange rate band in Costa Rica marks a step in the right direction. Separately, further enhancements to prudential regulations are needed to reduce financial vulnerabilities, including those related to credit dollarization.

Further progress in structural reforms will also be critical to achieve sustained and inclusive growth. A key priority relates to tax reforms that create the fiscal space for higher public investment and education spending, helping to overcome existing supply bottlenecks and enhance human capital and productivity. These efforts should be supplemented by improvements in the business environment, which will help to attract private investment.

The Caribbean

Developments and Outlook

Prospects for economic growth in the Caribbean are the product of opposing forces. On the one hand, the projected recovery of the U.S. economy provides a positive impulse, especially to tourism-based economies that depend heavily on U.S. visitors. Even more important, all Caribbean economies, with the significant exception of Trinidad and Tobago, are net hydrocarbon importers and as such benefit from the sharp drop in oil prices. On the other hand, these positive impulses are clearly not powerful enough to overcome the long-standing structural weaknesses holding back the region. Moreover, the oil market rout has heightened the risk of disruptions to the Petrocaribe program through which Venezuela has been providing subsidized financing of oil imports to many partner economies in the Caribbean and beyond (Box 2.3).

On balance, the economic recovery is expected to continue, even as external, fiscal, and financial vulnerabilities remain high in several economies. In the tourism-dependent Caribbean, average growth reached 1.5 percent in 2014—the highest rate since 2007—and is projected to improve further, to 2.0 percent, in 2015 (Figure 2.17). The better momentum is led by The Bahamas and Jamaica, as well as several economies from the Eastern Caribbean Currency Union (ECCU). The commodity-exporting Caribbean, in turn, lacks the tailwinds from stronger terms of trade, but is still set to grow at 2.4 percent on average, only slightly below last year's outturn.[4]

Despite this moderately more favorable outlook, tremendous challenges remain. For many tourist destinations in the Caribbean, the recent rise in arrivals follows several years of stagnation or decline, reflecting competitiveness gaps that even a broad-based recovery in U.S. and European tourism demand is unlikely to offset. In fact, problems related to the Caribbean's high cost levels could worsen further, as the region's pegged currencies appreciate in lockstep with the U.S. dollar. Unless this effect is offset by other cost savings or significant upgrades to the tourism product,

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[4] These growth numbers refer to simple averages, which tend to be higher than GDP-weighted averages, given that the region's largest economy (Trinidad and Tobago) has one of the lowest growth rates.

Figure 2.17

Improving external conditions underpin a somewhat better outlook for growth in the Caribbean. However, significant fiscal, external, and financial vulnerabilities remain to be addressed.

Caribbean: Real GDP Growth[1]
(Percent change)
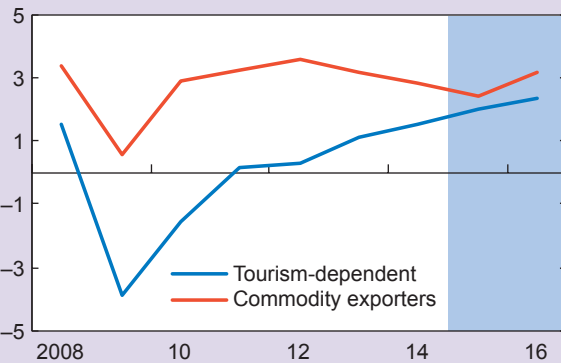
Caribbean: Tourist Arrivals
(Index: 2008 = 100; 12-month moving average)
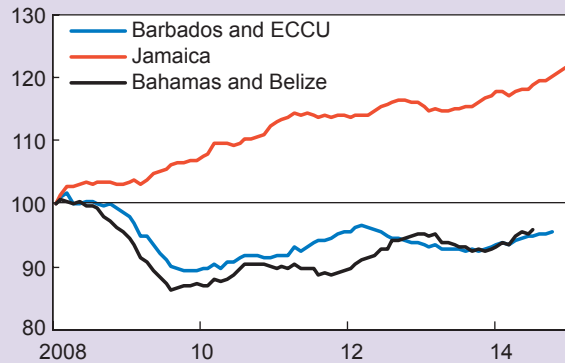
Caribbean: Fiscal Accounts
(Percent of fiscal year GDP)
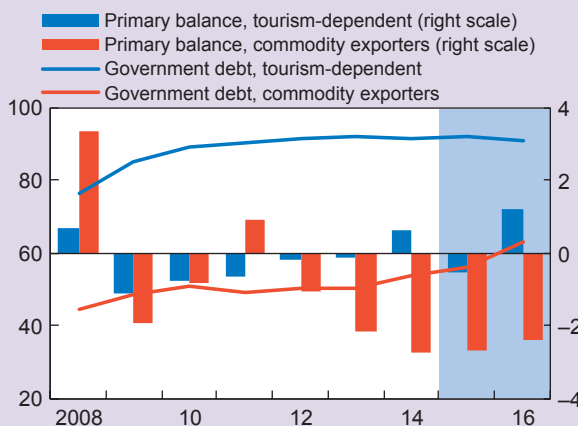
Caribbean: External Debt, 2014
(Percent of GDP)
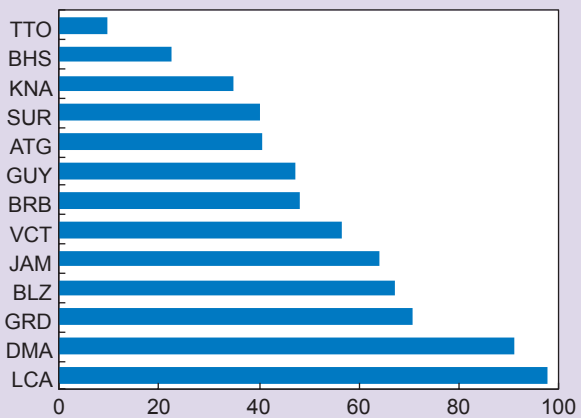
Caribbean: Petrocaribe Exposure
(Percent of GDP)
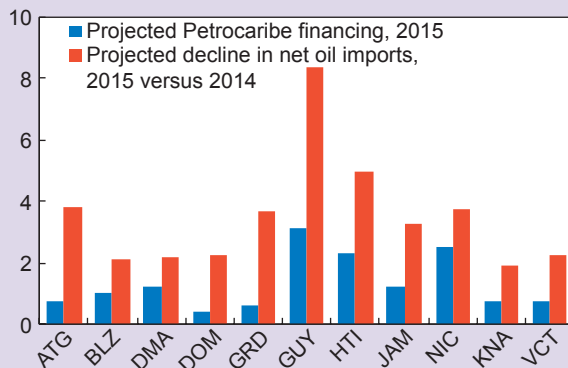
Caribbean: Nonperforming Loans
(Percent of total loans)
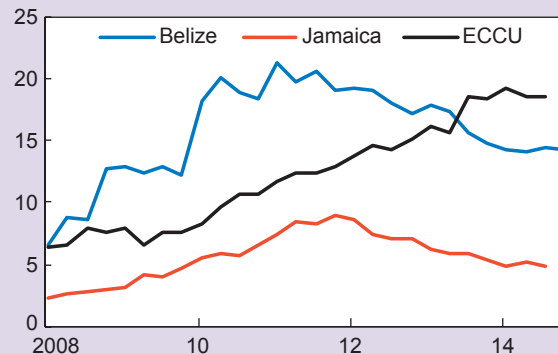
Sources: Caribbean Tourism Organization; Eastern Caribbean Central Bank; IMF, World Economic Outlook database; national authorities; and IMF staff calculations and projections.

Note: Commodity exporters = Belize, Guyana, Suriname, and Trinidad and Tobago; tourism-dependent economies = Antigua and Barbuda, The Bahamas, Barbados, Dominica, Grenada, Jamaica, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines; Eastern Caribbean Currency Union (ECCU) = Anguilla, Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines. For country name abbreviations, see page 79.
[1] Simple average.

many destinations are likely to lose further market share to competitors in Mexico, Central America, and beyond.[5]

The region's large external imbalances underscore the scale of the challenges. Even though cheaper oil imports provide significant relief, the average current account deficit among the tourism-dependent economies is still projected at more than 13 percent of GDP in 2015. In the commodity-exporting Caribbean, current account deficits are lower but still significant at about 6 percent of GDP. These deficits continue to be financed mainly through foreign direct investment and official flows, including in some cases from the IMF. For several countries, support through the Petrocaribe program also plays an important role, exposing them to the risk of sudden financing gaps should the ongoing crisis in Venezuela compromise its commitments to Petrocaribe partners (Box 2.3).

Public finances also remain under strain. Primary balances are projected to be broadly stable in many economies, although the recent large surplus in St. Kitts and Nevis is likely to shrink significantly as receipts from the citizenship-by-investment program decline. By contrast, both Grenada and Haiti have committed to rein in their previous high deficits, while Jamaica is set to maintain the high primary surplus that is needed to bring down public debt. On average, the tourism-dependent economies carry a debt burden in excess of 90 percent of GDP that has failed to lighten in recent years. Among the commodity-exporting economies, meanwhile, public debt continues to creep up, likely reaching 56 percent of GDP by end-2015. A relatively positive outlier is Trinidad and Tobago, which has kept gross debt below 40 percent of GDP while building up assets in its Heritage and Stabilization Fund. However, the sharp drop in energy prices is causing revenue declines that will require offsetting fiscal measures to achieve the authorities' original budget targets.

In the ECCU, external and fiscal vulnerabilities are compounded by acute financial fragilities, as many indigenous banks suffer from low capitalization, weak asset quality, and outsized exposures to their fiscally fragile sovereigns.

Policy Priorities

The critical challenge facing the Caribbean is to secure a sustained economic recovery while reducing still-high macroeconomic vulnerabilities, especially in tourism-dependent economies. The favorable recent shift in external conditions is creating a window of opportunity to make more decisive progress. Policymakers should take advantage of more buoyant economic activity to achieve sufficiently ambitious fiscal consolidation targets and put public debt on a downward path. Headwinds to growth from policy tightening can be mitigated through the careful design of fiscal measures, notably by redirecting scarce budget resources from current spending toward high-value public investment. Phasing out the level of tax waivers and concessions would assist the consolidation process. The recent adoption of a value-added tax in The Bahamas provides another encouraging example.

Lower public deficits will also support external rebalancing. However, a broader strategy will be needed to reduce the region's high current account deficits. The key is to raise competitiveness, notably in the tourism sector, by better aligning wages with productivity, reducing energy costs, and improving the quality of the supporting infrastructure and public services.

In the ECCU, progress toward resolving weak banks in an orderly and coordinated regional approach is urgently needed. Beyond addressing acute current problems, the authorities will also need to strengthen the general legal and regulatory framework to enhance supervision and facilitate crisis management in future.

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[5] See also the analysis in Laframboise and others (2014).

Box 2.1

Credit Gaps in Latin America: Keeping a Watchful Eye

Credit has grown rapidly over the past decade in much of Latin America and, despite the recent slowdown, generally remains above trend levels relative to GDP. Figure 2.1.1 shows the range of estimated credit gaps across Latin American countries, calculated as the difference between private credit to GDP and its long-term trend.[1] In South America, credit gaps have been positive since the mid-2000s in most countries. During the same period, Central American countries have typically had smaller or negative credit gaps, reflecting more subdued economic and financial conditions there. At end-2014, Venezuela, Paraguay, and Panama stood out with the largest stock of credit relative to estimated trend levels (Figure 2.1.2). Even these credit gaps were still below 10 percentage points of GDP, a threshold often considered an early warning indicator of banking crisis risk (Basel Committee on Banking Supervision 2010; Borio and Lowe 2002). Nonetheless, the legacy of rapid credit growth across South America underscores the need for vigilance.

Particular caution is warranted in countries where a long-running credit boom has now given way to a sharp downturn in growth. In such countries, borrowers took on increasing amounts of debt during the "good years" and are suddenly facing a much weaker economic environment that could put their repayment capacity to the test. Appealing to this basic argument, the arrow in Figure 2.1.2 points in the direction of rising vulnerabilities. Thus, the country with the most challenging combination of a large credit gap and significant growth slowdown[2] is Venezuela, followed (at some distance) by Argentina, Brazil, Panama, and Paraguay.[3] From a somewhat different perspective, Figure 2.1.3 combines information on estimated credit gaps and the total stock of credit at end-2014. The red-shaded area suggests higher risk, in the sense that countries in this area not only have experienced a stronger credit boom but also feature a larger overall stock of private debt, increasing the potential for losses should credit quality weaken.

Figure 2.1.1

Estimated Credit Gaps
(Percent of GDP)
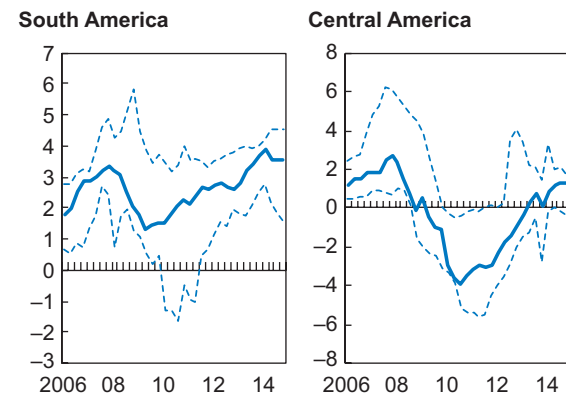
Sources: IMF, *International Financial Statistics*; IMF, World Economic Outlook database; and IMF staff calculations.
Note: Solid blue line shows the median; dotted lines show the 25th and 75th percentile of estimated credit gaps across individual countries in each regional group. South America includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay, and Venezuela. Central America includes Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Panama.

Note: This box was prepared by Natalija Novta, with excellent research assistance from Genevieve Lindow.

[1] The long-term credit-to-GDP trend is calculated using the one-sided Hodrick-Prescott (HP) filter, as in Borio and Lowe (2002) and the Basel Committee on Banking Supervision (2010). Starting in 2001, using quarterly data and a smoothing parameter (lambda) of 400,000, the HP filter is run recursively for increasingly longer time periods. Thus, the credit gap presented for time *t* uses only data up to time *t*. For Bolivia and Uruguay, the sample starts in 2005:Q1 to avoid apparent structural breaks in the series. Trend estimation inevitably requires specification choices that can affect estimated credit gaps.

[2] Slowdown in growth is measured as the difference between the average expected growth during 2015–16 and the observed average growth during 2008–13.

[3] Estimates for Venezuela need to be taken with caution, insofar as high inflation and the multiple exchange rate regime tend to distort macroeconomic statistics. Credit data for Panama, in turn, reflect the country's role as a regional financial center, making them somewhat less informative about strictly domestic credit developments.

Box 2.1 *(continued)*

Figure 2.1.2
Credit Gap and Growth Slowdown
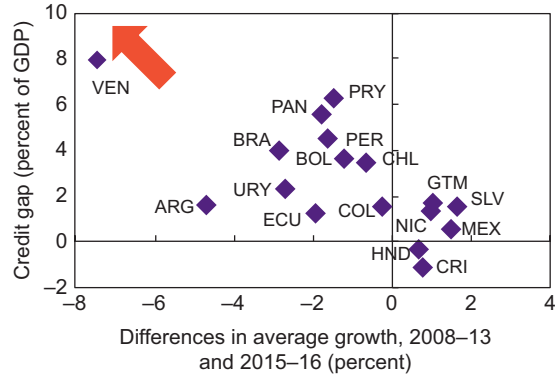
Sources: IMF, *International Financial Statistics*; IMF, World Economic Outlook database; and IMF staff calculations.
Note: For country name abbreviations, see page 79.

Figure 2.1.3
Credit Gap and Credit-to-GDP Ratio, 2014
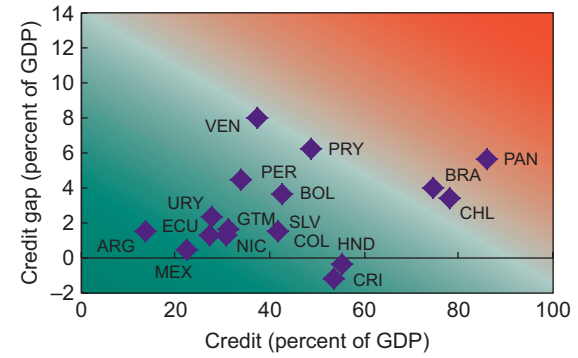
Sources: IMF, *International Financial Statistics*; IMF, World Economic Outlook database; and IMF staff calculations.
Note: For country name abbreviations, see page 79.

Reassuringly, the region still appears to have significant financial buffers to cope with the fallout of lower growth and rising asset quality pressures. Capital adequacy ratios, return on assets, and provisioning ratios remain relatively comfortable compared to other emerging market regions; and nonperforming loan (NPL) ratios typically do not exceed 3 percent (Figure 2.1.4). These indicators also do not show a significant recent deterioration, although the backward-looking nature of some indicators (especially NPL ratios) cautions against complacency.

Figure 2.1.4

Capital Adequacy Ratio
(Percent)

Nonperforming Loans
(Percent of total loans)

Return on Assets
(Percent)
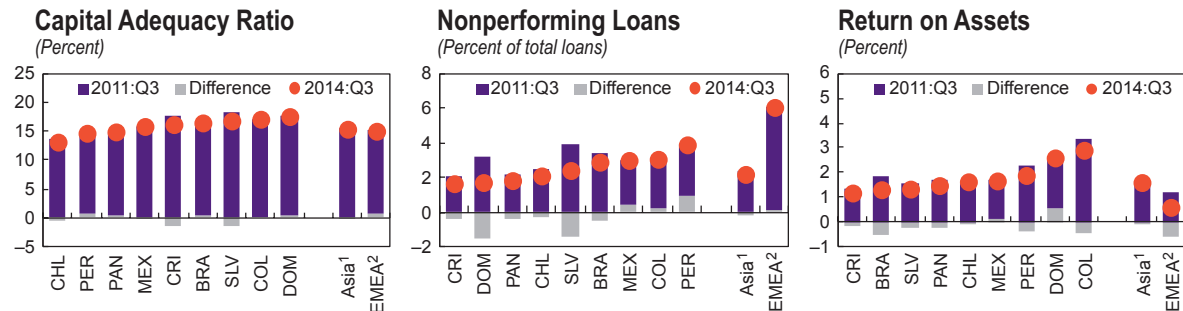
Sources: IMF, Financial Soundness Indicators database; and IMF staff calculations.
Note: Asia = India, Indonesia, Korea, Malaysia, and the Philippines. Europe, Middle East, Africa (EMEA) = Hungary, Israel, Poland, Russia, South Africa, and Turkey. For country name abbreviations, see page 79.
[1] Simple average. Due to missing data: Indonesia, average of 2011:Q2 and 2011:Q4 data used for 2011:Q3; Korea, 2014:Q2 data used for 2014:Q3.
[2] Simple average. Due to missing data: South Africa, 2014:Q2 data used for 2014:Q3.

The priority is to maintain strong capital levels and ensure swift recognition of bad loans. The negative terms-of-trade shock affecting many Latin American countries, the anticipated tightening of U.S. monetary policy, and the related strong appreciation of the U.S. dollar increase the likelihood of worsening credit quality going forward. To ensure that such a development would not undermine financial stability, regulators and supervisors should guide banks to maintain conservative provisioning standards, scrutinize credit quality trends and quickly recognize problem loans, and avoid outsized profit distributions that would compromise capital buffers. More broadly, the ongoing downturn in the credit cycle underscores the benefits of countercyclical macroprudential policies during the upswing. Regulators that appropriately tightened prudential standards during the boom years not only helped to curtail excesses at the time but also created additional buffers that should prove valuable over the period ahead.

Box 2.2

U.S. Dollar Strength and Economic Activity in Latin America

The U.S. dollar has appreciated by about 18 percent in real effective terms since June 2014, marking the fastest appreciation in over 40 years. Moreover, many observers expect the current dollar strength to continue, driven by favorable growth prospects and widening interest differentials vis-à-vis other major currencies. How might this appreciation trend affect growth in Latin America? Looking at the past 45 years, emerging markets have tended to grow at a slower pace, on average, during periods of extended dollar appreciation. In Latin America, this pattern appears stronger than in other emerging market regions, particularly for South America's commodity exporters (Figure 2.2.1).

Event analysis (Figure 2.2.2) shows that during periods of extended dollar appreciation, lower growth in Latin America has been associated with higher U.S. real interest rates, weaker dynamics in commodity markets, and hence less favorable terms of trade.

Interestingly, U.S. growth outturns have not differed much on average between appreciation and depreciation episodes. This suggests that differences in Latin America's growth rates between dollar appreciation and depreciation episodes mainly reflect factors other than U.S. growth. Moreover, Latin American currencies have appreciated, on average, somewhat less during periods of dollar strength, though apparently without providing sufficient support to overall demand through better net exports.[1]

U.S. dollar appreciation can arise from different underlying shocks, with distinct spillovers to Latin America. Monetary tightening and/or strong growth have usually driven the appreciation. But other factors, such as a global flight to quality and coordinated foreign exchange interventions, have also contributed in the past, reflecting the dollar's central role in the international monetary system. With that in mind, what are possible transmission channels that could

Figure 2.2.1

Dollar Strength and South America's Growth
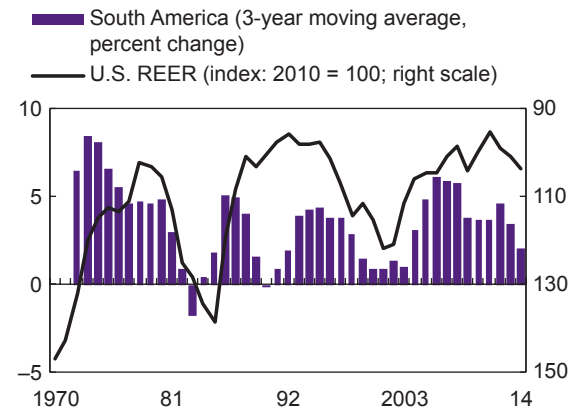
Sources: Federal Reserve Economic Data; IMF, *International Financial Statistics*; IMF, World Economic Outlook database; and IMF staff calculations.
Note: REER = real effective exchange rate. Higher value = appreciation.

Figure 2.2.2

Appreciation and Depreciation Cycles
(Percent)
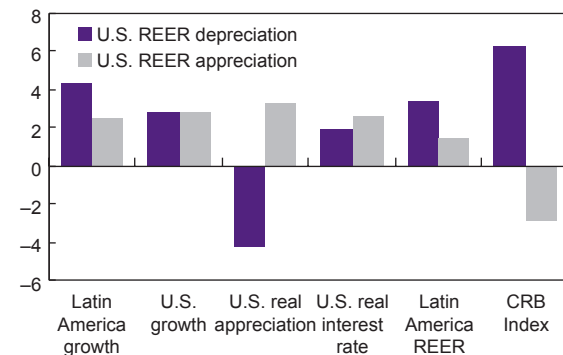
Sources: IMF, *International Financial Statistics*; IMF, World Economic Outlook database; and IMF staff calculations.
Note: CRB = Commodity Research Bureau (commodity price index); REER = real effective exchange rate. U.S. real interest rates are 10-year treasury rates deflated by observed annual inflation. Appreciation and depreciation cycles defined by peak-to-trough long-term trend changes in U.S. real effective exchange rate. Depreciation cycles: 1970–78, 1986–92, and 2002–11. Appreciation cycles: 1979–85, 1996–2001, and 2011–13. Bars show average percent change per annum. See Druck and Magud (forthcoming) for details.

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Note: This box was prepared by Pablo Druck and Nicolas Magud, with excellent research assistance from Rodrigo Mariscal; based on a forthcoming paper by Druck and Magud.
[1] A stronger U.S. dollar in multilateral terms need not improve competitiveness of any country vis-à-vis other exporters to the United States, in particular for countries with little export share to the United States.

Box 2.2 *(continued)*

explain the link between a stronger U.S. dollar and lower activity in Latin America? Empirical analysis in Druck and Magud (forthcoming) points to the following channels:

- *Financial channel:* After controlling for U.S. growth, higher U.S. real interest rates make external financing more costly and restrictive for emerging market borrowers, negatively affecting investment and consumption. These effects have been further compounded in past episodes of sustained dollar appreciation by currency mismatches in private and public sector balance sheets.

- *Income/substitution effects:* A stronger U.S. dollar implies weaker domestic currencies and commodity prices, reducing the dollar-purchasing power of agents in emerging markets. Expressing purchasing power in commodity terms of trade, this effect is even more pronounced (Figure 2.2.3), amplifying the weakness in aggregate domestic demand.[2] This argument is particularly relevant for South America's large net commodity exporters, though less so for Central America and Mexico. In principle, the resulting weakness in domestic output should be outweighed by positive expenditure switching effects (that is, demand shifting toward domestic goods, as foreign goods become more expensive due to the depreciation). However, many Latin American economies rely on foreign final, intermediate, and capital goods that cannot be easily replaced with domestic goods, given limited economic diversification. The implied low rate of substitution between imported and domestic goods would lend credence to the argument that the income effect dominates the expenditure switching effect of exchange rate changes.

Figure 2.2.3
South America and Mexico: Real Effective Exchange Rates
(Index: 2005 = 100)
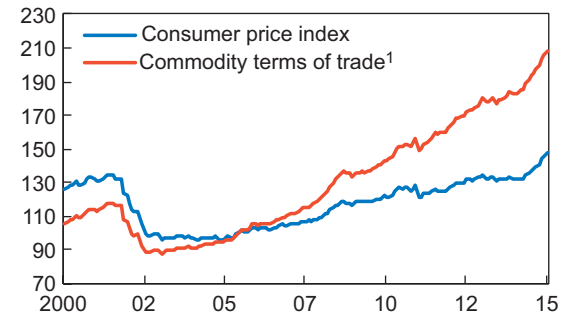
Sources: IMF, *Information Notice System*; and IMF staff calculations.
Note: South America = Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay, and Venezuela.
[1] Calculated using net commodity terms of trade data based on Gruss (2014) (instead of domestic consumer price indices) for the partner countries.

For countries that are highly integrated with the U.S. economy, the effects just mentioned need to be considered alongside *positive* demand spillovers if the strength of the U.S. dollar is driven by faster U.S. growth. Such positive spillover effects are relevant in particular for Central America and Mexico, thanks to large trade and remittance flows, but less so for South America.

Overall, the prospect for a persistently strong U.S. dollar on the back of the expected lift-off in U.S. interest rates could pose risks to growth in Latin America, particularly to commodity exporters and those exposed to currency mismatches. That said, to the extent that individual countries have implemented macroeconomic reforms since the late 1990s—by strengthening monetary policy regimes, allowing greater exchange rate flexibility, and reducing the dollarization of liabilities—they should be better placed than in the past to navigate a period of U.S. dollar strength.

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[2] This results from substituting the country-specific commodity terms-of-trade index for the basket of trading partners' price indices to compute the "commodity-terms-of-trade" real effective exchange rate.

Box 2.3

How Does the Oil Price Decline Affect Countries in Central America and the Caribbean?

Oil prices have recently witnessed the largest decline since the global financial crisis. As of March 2015, spot crude oil prices were down 50 percent from one year earlier. This sharp drop represents a large positive terms-of-trade shock for net oil importers in LAC, in particular those in Central America and the Caribbean (CAC—Figure 2.3.1). Provided the decline is passed through to end users (the application of current pricing mechanisms would imply complete or almost complete pass-through in most CAC countries by end-2015), the first-round effect of lower oil prices should be decreases in transportation and electricity costs (in particular for countries with power generation reliant on fossil fuels). This should boost households' disposable income, strengthen firm profitability, and decrease fiscal deficits in countries that subsidize energy products.

Figure 2.3.1

Improvement in Oil Trade Deficit, 2015
(Percent of GDP)

Sources: IMF, World Economic Outlook database; and IMF staff calculations.
Note: For country name abbreviations, see page 79.

However, many countries in CAC will also see a decline in financing from Venezuela-sponsored Petrocaribe. Since 2005, this initiative has allowed a number of governments in CAC to obtain long-term debt at below-market rates as their countries purchased oil from Venezuela.[1] At high oil prices, oil bills were large and so was Petrocaribe financing, representing 2.5 percent of GDP for the average member country in 2014 (Figure 2.3.2). The current low oil prices mean that Petrocaribe members should see their oil bills decline—by an average 3.3 percent of GDP in 2015. This significant gain will be somewhat offset by lower access to financing (by about 1 percent GDP for the average recipient country), as the size of Petrocaribe loans declines, while loan terms become less generous with lower oil prices (Figure 2.3.3 and Table 2.3.1).

Figure 2.3.2

Petrocaribe Financing, 2014[1]
(Percent of GDP)
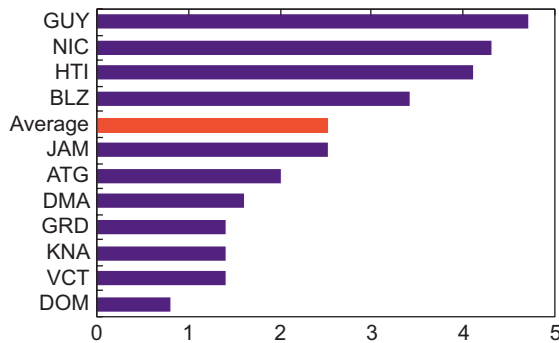
Sources: National authorities; and IMF staff calculations.
Note: For country name abbreviations, see page 79.
[1] St. Lucia and Suriname are Petrocaribe members but they have not taken any financing under the initiative.

Figure 2.3.3

Decline in Petrocaribe Financing Flows, 2015
(Percent of GDP)
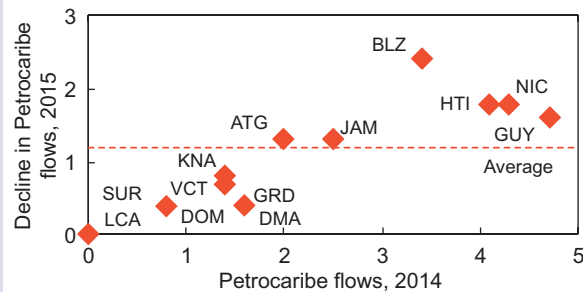
Sources: National authorities; and IMF staff calculations.
Note: For country name abbreviations, see page 79.

Note: This box was prepared by Gabriel Di Bella.
[1] In addition to Venezuela, current members include Antigua and Barbuda, Bahamas, Belize, Cuba, Dominica, Dominican Republic, El Salvador, Grenada, Guyana, Haiti, Honduras, Jamaica, Nicaragua, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Suriname. Debt terms include long repayment periods (17–25 years) and low interest rates (1–2 percent). St. Lucia and Suriname have not so far imported oil under the arrangement and thus have not accumulated Petrocaribe debt.

Box 2.3 *(continued)*

While on balance the oil price decline will leave Petrocaribe members better off (as the gain from the lower oil bill will outweigh the expected decline in inflows), lower financing could nonetheless create problems. In this regard, the impact of lower financing will be different between the public and private sectors. While the private sector should see disposable income and profits increase, the reduction (or stop) of Petrocaribe financing will leave some governments cash-strapped. If resources are not recycled from the private to the public sector (for example, through reductions in energy subsidies), some governments may be faced with the choice to either find budgetary financing for Petrocaribe-related social or investment programs, or discontinue them. Nicaragua and Haiti, lacking market access, ample reserves, and deep domestic financial markets, may need to adjust the most (Table 2.3.2). Guyana and St. Kitts (and to a lesser extent Jamaica) have built buffers to offset the impact. Moreover, in the case of a total stop of Petrocaribe flows, fiscal deficits may increase in Antigua, Dominica, Grenada, Haiti, Jamaica, and Nicaragua, to the extent that governments take over (currently off-budget) social programs or infrastructure projects. A few countries with energy subsidies, notably Haiti, plan to offset the additional cost by recovering foregone revenue on the taxation of fuel.

Table 2.3.1. Net Benefit from Decrease in Oil Prices
(Percent of GDP)

	Continues			Stops
Petrocaribe:	Decrease in Oil Trade Deficit (A)	Decrease in Petrocaribe Financing (B)	Improvement in External Position (A − B)	Improvement in External Position
Antigua and Barbuda	3.8	1.3	2.5	1.8
Belize	2.1	2.4	−0.3	−1.3
Dominica	2.2	0.4	1.8	0.6
Dominican Republic	2.2	0.4	1.8	1.4
Grenada	3.6	0.8	2.8	2.2
Guyana	8.3	1.6	6.7	3.6
Haiti	4.9	1.8	3.1	0.8
Jamaica	3.2	1.3	1.9	0.7
Nicaragua	3.7	1.8	1.9	−0.6
St. Kitts and Nevis	1.8	0.7	1.1	0.4
St. Lucia	0.6	0.0	0.6	0.6
St. Vincent and the Grenadines	2.2	0.7	1.5	0.8
Suriname	3.9	0.0	3.9	3.9
Average	**3.3**	**1.0**	**2.3**	**1.2**

Sources: IMF, World Economic Outlook database; national authorities; and IMF staff calculations.

Table 2.3.2. Contingent Fiscal Effort, 2015
(Percent of GDP)

	Petrocaribe Flows	
	Continue	Stop
Antigua and Barbuda	0.1	0.5
Dominica	0.0	0.1
Grenada	0.2	1.0
Haiti	1.4	4.6
Jamaica	1.3	2.5
Nicaragua	1.7	4.0
Average	**0.8**	**2.1**

Source: IMF staff calculations.

A possible discontinuation of Petrocaribe flows may nonetheless be more manageable now than in the past. The budgetary cost of the oil price drop for Venezuela raises questions about whether Petrocaribe support will continue. If it were to cease, the impact would differ across Petrocaribe members. Governments receiving large flows and without alternative financing sources (like in Nicaragua and Haiti) would be most affected—although less so than they would have been in a world of higher oil prices. Governments that have built buffers (like Guyana), or that have alternative financing sources (like the Dominican Republic and Jamaica), should be affected less.[2] Belize would be particularly affected as lower oil prices also reduce the value of its own exports of crude oil.

The decline in Petrocaribe flows should not affect growth significantly. The effect on GDP growth and on the current account depends on the size of the oil trade deficit and the extent to which the increases in disposable income and profits are saved or absorbed. Taking these elements into consideration, it appears that only Haiti and Nicaragua, where fiscal adjustment will be required to compensate for the loss of financing, could face declines in growth. For other countries, lower oil prices and a potential widening of fiscal deficits should offset the effect on growth of lower Petrocaribe flows.

[2] In January 2015, the Dominican Republic cancelled all its Petrocaribe debt through a buy-back operation.

Annex 2.1. Data Disclaimer

GDP data for Argentina are officially reported data as revised in May 2014. On February 1, 2013, the IMF issued a declaration of censure, and in December 2013 called on Argentina to implement specified actions to address the quality of its official GDP data according to a specified timetable. On December 15, 2014, the Executive Board recognized the implementation of the specified actions it had called for by end-September 2014 and the steps taken by the Argentine authorities to remedy the inaccurate provision of data. The Executive Board will review this issue again as per the calendar specified in December 2013 and in line with the procedures set forth in the IMF's legal framework.

Consumer price data from December 2013 onwards reflect the new national consumer price index (CPI; IPCNu), which differs substantively from the preceding CPI (the CPI for the Greater Buenos Aires Area, CPI-GBA). Because of the differences in geographical coverage, weights, sampling, and methodology, the IPCNu data cannot be directly compared to the earlier CPI-GBA data. Because of this structural break in the data, the average CPI inflation for 2014 is not reported in the April 2015 *Regional Economic Outlook*. Following a declaration of censure by the IMF on February 1, 2013, the public release of a new national CPI by end-March 2014 was one of the specified actions in the IMF Executive Board's December 2013 decision calling on Argentina to address the quality of its official CPI data. On December 15, 2014, the Executive Board recognized the implementation of the specified actions it had called for by end-September 2014 and the steps taken by the Argentine authorities to remedy the inaccurate provision of data. The Executive Board will review this issue again as per the calendar specified in December 2013 and in line with the procedures set forth in the IMF's legal framework.

Table A2.1. Western Hemisphere: Main Economic Indicators[1]

	Output Growth (Percent)					Inflation[2] (End of period, percent)					External Current Account Balance (Percent of GDP)				
	2012	2013	2014 Est.	2015	2016	2012	2013	2014 Est.	2015	2016	2012	2013	2014 Est.	2015	2016
				Projections					Projections					Projections	
North America															
Canada	1.9	2.0	2.5	2.2	2.0	1.0	1.0	1.9	1.0	2.4	–3.3	–3.0	–2.2	–2.6	–2.3
Mexico	4.0	1.4	2.1	3.0	3.3	3.6	4.0	4.1	3.1	3.0	–1.3	–2.4	–2.1	–2.2	–2.2
United States	2.3	2.2	2.4	3.1	3.1	1.8	1.3	0.9	0.5	2.1	–2.9	–2.4	–2.4	–2.3	–2.4
South America															
Argentina[3]	0.8	2.9	0.5	–0.3	0.1	10.8	10.9	23.9	20.5	20.5	–0.2	–0.8	–0.9	–1.7	–1.8
Bolivia	5.2	6.8	5.4	4.3	4.3	4.5	6.5	5.2	5.0	5.0	8.3	3.3	0.7	–2.8	–4.2
Brazil	1.8	2.7	0.1	–1.0	1.0	5.8	5.9	6.4	8.0	5.4	–2.2	–3.4	–3.9	–3.7	–3.4
Chile	5.5	4.3	1.8	2.7	3.3	1.5	2.8	4.6	2.9	3.0	–3.6	–3.7	–1.2	–1.2	–2.0
Colombia	4.0	4.9	4.6	3.4	3.7	2.4	1.9	3.7	3.6	3.2	–3.2	–3.4	–5.0	–5.8	–4.9
Ecuador	5.2	4.6	3.6	1.9	3.6	4.2	2.7	3.7	3.0	3.0	–0.2	–1.0	–0.8	–3.3	–3.0
Guyana	4.8	5.2	3.8	3.8	4.4	3.5	0.9	1.2	1.2	3.9	–11.6	–13.3	–15.9	–16.4	–21.9
Paraguay	–1.2	14.2	4.4	4.0	4.0	4.0	3.7	4.2	4.5	4.5	–0.9	2.2	0.1	–1.7	–2.2
Peru	6.0	5.8	2.4	3.8	5.0	2.6	2.9	3.2	2.2	2.0	–2.7	–4.4	–4.1	–4.6	–4.3
Suriname	4.8	4.1	2.9	2.7	3.8	4.4	0.6	3.9	2.1	3.0	3.4	–3.9	–7.3	–7.8	–6.9
Uruguay	3.7	4.4	3.3	2.8	2.9	7.5	8.5	8.3	7.4	7.3	–5.4	–5.2	–4.7	–3.8	–4.1
Venezuela	5.6	1.3	–4.0	–7.0	–4.0	20.1	56.2	68.5	94.9	78.4	3.7	2.4	4.3	–4.7	–0.8
Central America															
Belize	3.3	1.5	3.4	2.0	3.0	0.8	1.6	–0.4	1.5	2.3	–1.2	–4.4	–5.7	–4.5	–6.1
Costa Rica	5.2	3.4	3.5	3.8	4.4	4.6	3.7	5.1	4.0	4.0	–5.3	–5.0	–4.5	–3.6	–4.0
El Salvador	1.9	1.7	2.0	2.5	2.6	0.8	0.8	0.5	0.6	1.7	–5.4	–6.5	–5.0	–4.3	–4.9
Guatemala	3.0	3.7	4.0	4.0	3.9	3.4	4.4	2.9	3.0	3.4	–2.6	–2.5	–2.3	–1.6	–1.8
Honduras	4.1	2.8	3.1	3.3	3.4	5.4	4.9	5.8	4.7	5.2	–8.5	–9.5	–7.4	–6.5	–6.4
Nicaragua	5.0	4.4	4.5	4.6	4.3	6.6	5.7	6.5	6.0	7.0	–9.8	–8.9	–6.2	–6.8	–7.5
Panama[4]	10.7	8.4	6.2	6.1	6.4	4.6	3.7	1.0	2.4	2.0	–9.8	–12.2	–12.0	–10.4	–10.0
The Caribbean															
Antigua and Barbuda	3.6	1.8	2.4	1.9	2.3	1.8	1.1	1.3	1.0	1.6	–14.6	–14.6	–14.5	–10.7	–12.4
The Bahamas	1.0	0.7	1.3	2.3	2.8	0.7	0.8	0.2	2.3	1.6	–18.3	–17.7	–21.6	–12.4	–8.2
Barbados	0.0	0.0	–0.3	0.8	1.4	2.4	1.1	2.3	0.9	1.9	–9.3	–9.3	–9.1	–5.1	–5.9
Dominica	–1.4	–0.9	1.1	2.4	2.9	1.2	–0.4	–0.1	0.9	0.6	–17.7	–13.1	–13.0	–13.1	–19.4
Dominican Republic	2.6	4.8	7.3	5.1	4.5	3.9	3.9	1.6	3.0	4.0	–6.6	–4.1	–3.1	–2.4	–3.0
Grenada	–1.2	2.4	1.5	1.5	2.0	1.8	–1.2	–0.7	–1.0	2.3	–19.2	–27.0	–23.6	–17.4	–16.1
Haiti[5]	2.9	4.2	2.7	3.3	3.8	6.5	4.5	5.3	6.1	5.0	–5.7	–6.7	–5.8	–3.0	–3.7
Jamaica	–0.5	0.2	0.5	1.7	2.2	8.0	9.5	4.7	7.0	7.2	–10.7	–8.9	–6.4	–5.0	–4.6
St. Kitts and Nevis	–0.9	3.8	7.0	3.5	3.0	0.1	0.4	2.0	2.0	2.0	–9.8	–6.7	–10.7	–16.2	–16.8
St. Lucia	0.6	–0.5	–1.1	1.8	1.4	5.0	–0.7	1.7	3.1	3.1	–13.5	–12.8	–12.4	–13.4	–13.9
St. Vincent and the Grenadines	1.1	2.4	1.1	2.1	3.1	1.0	0.0	0.6	0.1	1.6	–27.5	–31.3	–29.4	–27.6	–25.4
Trinidad and Tobago	1.4	1.7	1.1	1.2	1.5	7.2	5.6	8.5	6.0	5.3	3.4	6.7	8.3	5.2	4.4
Memorandum:															
Latin America and the Caribbean (LAC)	**3.1**	**2.9**	**1.3**	**0.9**	**2.0**	**5.4**	**7.4**	**8.2**	**9.0**	**7.2**	**–1.8**	**–2.8**	**–2.8**	**–3.2**	**–3.0**
Financially integrated LAC[6]	4.2	3.9	2.4	2.4	3.2	3.9	4.3	5.0	4.5	4.0	–3.1	–3.7	–3.5	–3.5	–3.5
Other commodity exporters[7]	3.1	6.0	2.0	0.6	1.6	8.2	17.3	20.4	26.9	22.7	2.1	1.2	0.7	–2.8	–2.4
CADR[8]	4.6	4.2	4.4	4.2	4.2	4.2	3.9	3.4	3.4	3.9	–6.9	–7.0	–5.8	–5.1	–5.4
Caribbean															
Tourism-dependent[9]	0.3	1.1	1.5	2.0	2.4	2.5	1.2	1.3	1.8	2.4	–15.6	–15.7	–15.6	–13.4	–13.7
Commodity exporters[10]	3.6	3.1	2.8	2.4	3.2	4.0	2.2	3.3	2.7	3.6	–1.5	–3.7	–5.2	–5.9	–7.6
Eastern Caribbean Currency Union[11]	0.3	1.1	1.7	2.0	2.1	2.1	0.0	0.7	1.2	1.9	–17.1	–17.2	–15.8	–13.9	–14.5

Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.

[1] Regional aggregates are purchasing power parity–weighted GDP averages unless otherwise noted. Current account aggregates are U.S. dollar nominal GDP weighted averages. Consumer price index (CPI) series exclude Argentina. Consistent with the IMF's *World Economic Outlook*, the cut-off date for the data and projections in this table is April 3, 2015.
[2] End-of-period (December) rates. These will generally differ from period average inflation rates reported in the IMF's *World Economic Outlook*, although both are based on identical underlying projections.
[3] See Annex 2.1 "Data Disclaimer" for details on Argentina's data.
[4] Ratios to GDP are based on the "1996-base" GDP series.
[5] Fiscal year data.
[6] Simple average of Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.
[7] Simple average of Argentina, Bolivia, Ecuador, Paraguay, and Venezuela. CPI series exclude Argentina.
[8] Simple average of Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.
[9] Simple average of The Bahamas, Barbados, Jamaica, and Eastern Caribbean Currency Union member states.
[10] Simple average of Belize, Guyana, Suriname, and Trinidad and Tobago.
[11] Eastern Caribbean Currency Union members are Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat, which are not IMF members.

Table A2.2. Western Hemisphere: Main Fiscal Indicators[1]

	Public Sector Primary Expenditure (Percent of GDP)					Public Sector Primary Balance (Percent of GDP)					Public Sector Gross Debt (Percent of GDP)				
	2012	2013	2014 Est.	2015 Projections	2016 Projections	2012	2013	2014 Est.	2015 Projections	2016 Projections	2012	2013	2014 Est.	2015 Projections	2016 Projections
North America															
Canada	37.7	37.5	36.3	36.6	36.3	−2.6	−2.4	−1.4	−1.4	−0.9	87.9	87.7	86.5	87.0	85.0
Mexico[2]	25.0	25.5	25.4	23.4	22.4	−1.1	−1.3	−2.0	−1.4	−0.6	43.2	46.3	50.1	51.4	51.7
United States[3]	35.0	34.0	34.1	33.6	33.2	−6.3	−3.6	−3.2	−2.2	−1.8	102.4	103.4	104.8	105.1	104.9
South America															
Argentina[4]	32.0	34.1	36.7	37.3	36.6	−0.5	−0.7	−1.0	−1.6	−1.4	37.3	40.2	48.6	49.5	50.5
Bolivia[5]	35.0	37.5	40.8	38.5	38.0	2.8	1.6	−2.3	−3.6	−4.6	33.4	32.6	32.4	36.3	40.2
Brazil[6]	31.5	32.5	33.9	32.1	31.4	2.0	1.8	−0.6	1.2	2.0	63.5	62.2	65.2	66.2	66.2
Chile	23.1	23.1	23.6	24.8	25.5	0.8	−0.4	−1.4	−1.9	−1.5	12.0	12.8	13.9	16.3	17.9
Colombia[7]	25.6	26.6	26.8	26.3	25.7	1.6	1.2	0.9	−0.5	0.0	32.0	35.8	38.0	40.6	40.1
Ecuador	39.6	43.0	42.8	38.1	37.7	−0.2	−3.6	−4.0	−4.1	−3.6	21.3	24.2	29.8	34.3	36.6
Guyana[8]	30.2	29.2	33.0	32.4	29.9	−3.9	−3.5	−4.4	−3.7	−2.9	62.5	57.3	65.8	70.6	71.1
Paraguay	24.7	22.8	23.4	24.5	24.4	−1.1	−0.7	0.3	−0.1	0.1	16.0	16.8	21.4	22.8	23.3
Peru	19.3	20.5	21.4	21.7	21.5	2.8	1.7	0.8	−0.8	−0.4	21.2	20.3	20.7	21.5	22.3
Suriname[9]	28.9	30.1	26.7	25.2	24.6	−3.0	−5.5	−4.1	−4.8	−3.7	22.2	30.7	34.1	38.3	41.8
Uruguay[10]	28.7	30.1	30.6	29.9	30.0	−0.2	0.4	−0.5	0.2	0.0	59.5	62.1	62.8	64.4	65.3
Venezuela	37.3	35.0	39.8	39.4	39.1	−13.8	−11.6	−10.9	−16.8	−18.0	46.0	55.4	45.6	39.6	30.6
Central America															
Belize[8]	25.1	28.1	27.8	27.6	27.0	1.3	0.8	0.1	0.0	0.4	75.0	75.3	76.3	75.7	95.6
Costa Rica[8]	16.0	16.6	16.6	16.3	16.5	−2.3	−2.9	−3.1	−2.5	−1.9	35.2	36.3	39.8	42.4	44.6
El Salvador[11]	19.6	19.7	19.0	19.6	19.8	−1.7	−1.2	−1.1	−1.6	−1.4	55.2	55.5	56.5	59.1	61.2
Guatemala[8]	12.5	12.2	11.7	12.0	11.9	−0.9	−0.6	−0.4	−0.9	−0.6	24.3	24.6	23.7	24.6	25.3
Honduras	25.4	28.5	26.6	25.3	24.7	−4.3	−7.1	−3.8	−1.6	−0.5	34.7	45.3	46.1	48.3	49.7
Nicaragua[11]	22.4	23.0	23.3	23.6	24.1	0.7	−0.1	−0.6	−0.3	−0.1	32.1	32.4	32.2	31.6	30.6
Panama[12]	24.5	25.1	25.4	24.2	23.9	0.0	−0.5	−2.4	−1.5	−1.2	42.6	41.7	45.6	47.3	47.2
The Caribbean															
Antigua and Barbuda[13]	18.7	20.3	20.4	28.6	16.5	1.1	−1.6	−0.2	−7.4	5.0	87.1	94.3	98.7	106.9	102.4
The Bahamas[8]	21.2	20.5	18.7	19.3	18.9	−3.3	−4.2	−1.7	−0.9	−0.1	48.4	56.4	60.4	61.6	61.4
Barbados[14]	39.6	39.6	36.6	34.8	35.2	−4.0	−7.7	−3.5	−1.6	−1.4	84.6	95.9	100.4	102.5	103.9
Dominica[13]	32.6	30.7	31.3	30.8	30.8	−3.3	−1.0	−1.6	−1.4	−1.6	69.8	73.9	76.6	78.5	80.1
Dominican Republic[11]	17.8	15.8	15.6	14.6	14.7	−4.2	−1.2	−0.5	0.2	0.1	30.5	34.6	35.1	30.7	36.2
Grenada[13]	23.3	25.0	27.4	23.7	21.0	−2.5	−4.0	−2.4	1.3	3.5	104.5	108.0	107.2	107.1	102.7
Haiti[8]	27.8	27.5	25.5	23.5	22.7	−4.4	−6.7	−5.9	−2.6	−2.3	16.6	21.5	26.7	27.6	28.6
Jamaica[13]	20.3	19.5	18.9	19.6	19.1	5.4	7.7	7.7	7.5	7.5	146.5	141.6	140.6	132.8	127.3
St. Kitts and Nevis[13]	25.4	29.7	30.0	28.6	28.0	10.8	16.3	13.1	3.6	2.4	137.3	104.7	81.0	74.5	68.3
St. Lucia[13]	30.6	27.5	27.6	27.6	27.6	−5.8	−2.1	−2.2	−2.6	−2.8	73.7	79.0	83.9	88.0	92.5
St. Vincent and the Grenadines[13]	26.4	29.3	30.3	29.6	28.3	−0.3	−4.1	−3.4	−3.3	−1.6	72.3	73.4	75.1	77.1	78.8
Trinidad and Tobago[15]	32.1	33.8	33.5	32.0	33.5	1.4	−0.4	−2.4	−2.2	−3.3	40.3	37.4	37.6	39.5	43.7
Memorandum:															
Latin America and the Caribbean (LAC)	**29.1**	**29.7**	**30.6**	**29.1**	**28.3**	**0.0**	**−0.1**	**−1.3**	**−0.9**	**−0.5**	**47.9**	**48.7**	**51.6**	**51.7**	**51.7**
Financially integrated LAC[16]	25.5	26.4	27.0	26.4	26.1	1.0	0.6	−0.5	−0.5	−0.1	38.6	39.9	41.8	43.4	43.9
Other commodity exporters[17]	33.7	34.5	36.7	35.6	35.2	−2.5	−3.0	−3.6	−5.3	−5.5	30.8	33.8	35.6	36.5	36.2
CADR[18]	19.8	20.1	19.7	19.4	19.4	−1.8	−1.9	−1.7	−1.2	−0.8	36.4	38.6	39.9	40.6	42.1
Caribbean															
Tourism-dependent[19]	26.5	26.9	26.8	26.9	25.0	−0.2	−0.1	0.6	−0.5	1.2	91.6	91.9	91.5	92.1	90.8
Commodity exporters[20]	29.1	30.3	30.3	29.3	28.8	−1.0	−2.2	−2.7	−2.7	−2.4	50.0	50.2	53.5	56.0	63.1
Eastern Caribbean Currency Union[13,21]	26.2	27.1	27.2	28.3	25.4	−0.4	0.3	0.9	−1.9	1.0	85.7	85.2	84.4	86.7	85.7

Sources: IMF, World Economic Outlook database; and IMF staff calculations and projections.

[1] Definitions of public sector accounts vary by country, depending on country-specific institutional differences, including on what constitutes the appropriate coverage from a fiscal policy perspective, as defined by the IMF staff. All indicators reported on fiscal year basis. Regional aggregates are purchasing power parity–weighted GDP averages, unless otherwise noted. Consistent with the IMF's *World Economic Outlook*, the cut-off date for the data and projections in this table is April 3, 2015.

[2] Includes central government, social security funds, nonfinancial public corporations, and financial public corporations.

[3] For cross-country comparability, expenditure and fiscal balances of the United States are adjusted to exclude the items related to the accrual basis accounting of government employees' defined benefit pension plans, which is counted as expenditure under the 2008 System of National Accounts recently adopted by the United States, but not so in countries that have not yet adopted the 2008 System of National Accounts. Data for the United States in this table may thus differ from data published by the U.S. Bureau of Economic Analysis.

[4] Federal government and provinces; includes interest payments on a cash basis. Primary expenditure and primary balance include the federal government and provinces. Gross debt is for the federal government only.

[5] Nonfinancial public sector, excluding the operations of nationalized mixed-ownership companies in the hydrocarbon and electricity sectors.

[6] Nonfinancial public sector, excluding Petrobras and Eletrobras, and consolidated with the sovereign wealth fund. The definition includes Treasury securities on the central bank's balance sheet, including those not used under repurchase agreements. The national definition of general government gross debt includes the stock of Treasury securities used for monetary policy purposes by the Central Bank (those pledged as security in reverse repo operations). It excludes the rest of the government securities held by the Central Bank. According to this definition, general government gross debt amounted to 58.9 percent of GDP at end-2014.

[7] Nonfinancial public sector reported for primary balances (excluding statistical discrepancies); combined public sector including Ecopetrol and excluding Banco de la República's outstanding external debt reported for gross public debt.

[8] Central government only. Gross debt for Belize includes both public and publicly guaranteed debt.

[9] Primary expenditures for Suriname exclude net lending. Debt data refer to central government and government-guaranteed public debt.

[10] Consolidated public sector.

[11] General government.

[12] Ratios to GDP are based on the "1996-base" GDP series. Fiscal data cover the nonfinancial public sector excluding the Panama Canal Authority.

[13] Central government for primary expenditure and primary balance; public sector for gross debt. For Jamaica, the public debt includes central government, guaranteed, and PetroCaribe debt.

[14] Overall and primary balances include off-budget and public-private partnership activities for Barbados and the nonfinancial public sector. Central government for gross debt (excludes NIS holdings).

[15] Central government for primary expenditure. Consolidated public sector for primary balance and gross debt.

[16] Simple average of Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.

[17] Simple average of Argentina, Bolivia, Ecuador, Paraguay, and Venezuela.

[18] Simple average of Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

[19] Simple average of The Bahamas, Barbados, Jamaica, and ECCU member states.

[20] Simple average of Belize, Guyana, Suriname, and Trinidad and Tobago.

[21] Eastern Caribbean Currency Union members are Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat, which are not IMF members.

Table A2.3. Western Hemisphere: Selected Economic and Social Indicators, 2005–14[1]

	2014											Latest Available		
	GDP[2] (US$ Billion)	Population (Million)	Gdp per Capita (PPP$)	Nominal Output Share of Lac Region[2] (Percent)	Real GDP Growth (Percent)	CPI Inflation[3] (Percent)	Current Account (Percent of GDP)	Domestic Saving (Percent of GDP)	Trade Openness[4] (Percent of GDP)	Gross Reserves[5] (Percent of GDP)	Unemployment Rate (Percent)	Poverty Rate[6]	Gini Coefficient[6]	Sovereign Credit Rating[7]
North America														
Canada	1,788.7	35.5	44,843	—	1.9	1.8	−1.3	22.4	64.1	4.2	6.9	—	31.3	AAA
Mexico	1,282.7	119.7	17,881	22.1	2.5	4.1	−1.3	21.4	60.6	14.9	4.8	11.4	49.1	BBB+
United States	17,418.9	319.0	54,597	—	1.6	2.1	−3.7	16.8	28.3	0.8	6.2	—	47.6	AAA
South America														
Argentina[8]	540.2	42.0	22,582	9.3	5.1	11.2	0.7	20.1	33.2	5.4	7.3	5.0	42.0	SD
Bolivia	34.4	11.2	6,221	0.6	5.0	6.2	6.1	25.0	71.9	39.4	4.0	14.4	46.5	BB−
Brazil	2,353.0	202.8	16,096	40.6	3.4	5.4	−1.4	18.7	24.0	15.3	4.8	9.4	52.3	BBB
Chile	258.0	17.8	22,971	4.4	4.3	3.6	0.1	22.8	70.8	15.7	6.4	2.0	50.8	AA−
Colombia	384.9	47.7	13,430	6.6	4.8	4.0	−2.9	20.1	35.5	12.1	9.1	15.2	53.4	BBB
Ecuador	100.8	16.0	11,244	1.7	4.4	4.2	0.7	26.7	60.4	3.5	5.0	10.5	46.2	B
Guyana	3.0	0.8	6,895	0.1	3.9	5.0	−11.8	7.1	133.0	22.3		—	—	—
Paraguay	29.7	6.9	8,449	0.5	5.0	6.2	1.2	17.1	102.1	22.5	5.5	8.3	52.6	BB
Peru	202.9	31.4	11,817	3.5	6.2	2.9	−1.4	22.4	50.7	30.2	6.0	10.0	45.3	BBB+
Suriname	5.3	0.6	16,623	0.1	4.4	7.8	3.8		104.6	10.8	8.9	—	—	BB−
Uruguay	55.1	3.4	20,556	1.0	5.4	7.5	−3.0	17.9	56.2	31.8	6.5	2.3	41.3	BBB−
Venezuela	205.8	30.5	17,695	3.5	3.7	30.9	7.4	31.1	58.1	3.4	7.0	11.5	40.4	CCC
Central America														
Belize	1.7	0.4	8,248	0.0	2.6	2.0	−5.0	12.1	124.7	28.8	12.9	—	—	B−
Costa Rica	48.1	4.8	14,864	0.8	4.6	7.6	−5.1	17.2	67.5	15.0	8.2	4.6	48.5	BB+
El Salvador	25.3	6.4	8,021	0.4	1.9	2.9	−4.7	10.3	65.1	9.6	5.5	12.7	41.8	BB−
Guatemala	60.4	15.9	7,503	1.0	3.6	5.5	−3.0	13.3	62.7	11.7		40.7	52.2	BB
Honduras	19.5	8.3	4,729	0.3	3.8	6.4	−7.3	18.9	90.5	17.6	4.5	39.6	57.2	B
Nicaragua	11.7	6.2	4,736	0.2	3.7	8.7	−10.9	15.7	94.1	19.4	4.8	29.3	45.7	B−
Panama	43.8	3.9	19,455	0.8	8.5	4.1	−8.9	16.7	75.4	9.2	4.1	9.9	51.9	BBB
The Caribbean														
The Bahamas	8.7	0.4	25,049	0.1	0.6	2.0	−14.2	13.1	95.7	10.1	15.0	—	—	BBB
Barbados	4.3	0.3	16,183	0.1	0.8	5.1	−8.8	7.1	98.1	14.7	12.7	—	—	B
Dominican Republic	64.1	10.6	13,012	1.1	5.8	5.5	−5.3	20.2	59.1	7.6	6.4	13.9	47.4	B+
Haiti	8.7	10.5	1,750	0.2	2.1	8.2	−3.1	25.6	65.3	13.2	—	—	—	—
Jamaica	13.8	2.8	8,609	0.2	0.1	10.0	−11.0	12.4	90.2	17.6	15.3	—	—	B−
Trinidad and Tobago	28.8	1.4	32,139	0.5	2.7	8.0	17.5	32.9	98.1	41.3	4.0	—	—	A−
Eastern Caribbean Currency Union	5.6	0.6	15,359	0.1	1.4	2.7	−20.2	9.9	97.5	24.7	—	—	—	—
Antigua and Barbuda	1.2	0.1	22,573	0.0	1.5	2.2	−18.2	17.3	110.6	23.9	—	—	—	—
Dominica	0.5	0.1	10,800	0.0	1.7	1.8	−17.7	−0.6	86.2	19.3	—	—	—	—
Grenada	0.9	0.1	11,979	0.0	1.3	2.6	−25.1	3.3	81.6	19.7	—	—	—	—
St. Kitts and St. Nevis	0.8	0.1	21,091	0.0	2.2	3.5	−15.9	19.4	87.3	38.9	—	—	—	—
St. Lucia	1.4	0.2	11,594	0.0	1.0	2.8	−18.7	11.5	106.7	19.0	—	—	—	—
St. Vincent and the Grenadines	0.7	0.1	10,778	0.0	1.2	3.1	−27.7	−1.3	86.5	21.4	—	2.9	40.2	B−
Latin America and the Caribbean	**5,800.4**	**603.0**	**15,489**	**100.0**	**3.7**	**6.3**	**−0.9**	**20.6**	**43.0**	**14.3**	**—**	**11.3**	**49.6**	**—**

Sources: IMF, *International Financial Statistics*; IMF, World Economic Outlook database; Inter-American Development Bank; Socio-Economic Database for Latin America and the Caribbean (CEDLAS and The World Bank); national authorities; and IMF staff calculations.

1 Estimates may vary from those reported by national authorities on account of differences in methodology and source. Regional aggregates are purchasing power parity–weighted GDP averages, except for regional GDP in U.S. dollars and population where totals are computed. Consumer price index (CPI) series excludes Argentina. Consistent with the IMF's *World Economic Outlook*, the cut-off date for the data and projections in this table is April 3, 2015.
2 At market exchange rates.
3 End-of-period, 12-month percent change.
4 Exports plus imports of goods and services in percent of GDP.
5 Latest available data from IMF's International Financial Statistics database.
6 Data from Socio-Economic Database for Latin America and the Caribbean (SEDLAC), based on the latest country-specific household surveys. In most cases, the surveys are from 2013 or 2014, though the vintage for Nicaragua (2009) is less recent. Poverty rate is defined as the share of the population earning less than US$2.50 per day. For Venezuela, poverty rate is defined as a share of the population in extreme poverty per national definition (INE). Gini index is calculated by the World Bank using pooled data for each country. For Venezuela, Gini index is based on official statistics (INE). Data for aggregate is population–weighted average from the Inter-American Development Bank. Data for the United States are from the U.S. Census Bureau; those for Canada are from Statistics Canada.
7 Median of long-term foreign currency ratings published by Moody's, Standard & Poor's, and Fitch.
8 See Annex 2.1 "Data Disclaimer" for details on Argentina's data.