Editorial

In 2023, economic activity in Latin America slowed to a growth rate of around 2% (from 3.6% in 2022), with marked cross-country heterogeneity. This lower growth owed mainly to weaker domestic demand (due to the cumulative effects of tight monetary policy and households losing purchasing power amid high inflation) and a less favourable external environment. Slower growth is expected in 2024 (just under 1.5%), with the notable exception of Argentina, where a sharp economic contraction is anticipated. Some downside risks to economic growth persist, most of them external: the possibility of a tighter than anticipated US monetary policy stance and the economic slowdown in China proving sharper than expected. In the medium term, the outlook for Latin America's potential growth rate remains around 2%, less than forecast for other emerging regions.

Inflation has steadily declined across the region in recent quarters and is expected to continue to ease, albeit very gradually, to stand within the central banks' target intervals in 2024. Going forward, the pace of disinflation will primarily depend on how quickly inflationary pressures ease in services (which have displayed some general downward price stickiness) and in food (the prices of which have risen far more sharply than other consumer basket prices and also face upside risks associated with the El Niño climate phenomenon) and on countries adopting a fiscal stance more consistent with the tight monetary policy stance.

Against this economic backdrop, the region's main inflation-targeting central banks (with the exception of the Banco de México) began lowering their policy interest rates in the second half of 2023. In the near term, central banks face the challenge of calibrating the monetary easing cycle in response to movements in inflation, with the external conditioning factor of policy rate decisions adopted in other jurisdictions, particularly in the United States.

In line with the policy rate cuts, financial conditions have begun to ease in the region and financial markets continue to perform better than those in other emerging regions. In the banking sector, credit growth moderated virtually across the board in 2023, owing to weak demand and tighter lending standards. There was also an increase in non-performing loans, particularly in the corporate segment. On balance, however, the indicators available suggest that banking system risks remain very much contained.

Notably, public finances have generally been rendered more vulnerable by relatively high levels of public debt and large structural deficits compared with recent decades. Making matters worse are the expected unfavourable interest burden dynamics, low growth rates (both observed and expected) and uncertainty over the actual enforcement of the fiscal rules.

Compliance with these fiscal rules and the introduction of structural measures to boost potential growth are two of the key challenges facing the region. With some exceptions, substantive reforms aimed at addressing the main structural challenges, such as demographics and climate change, have not been forthcoming. The indicators available point to some easing of social and political unrest, which could pave the way for these reforms in the near term. Moreover, some countries could benefit from the complex global geopolitical situation if the incipient trend – observed in some qualitative data – of productive activity being relocated to nearby countries (nearshoring) takes hold. The benefits of this would mainly be through greater foreign direct investment.

This report includes three boxes. Box 1 offers a synopsis of recent developments in the Argentine economy following the presidential elections in late 2023, and the measures proposed by the new Government to tackle the country's economic imbalances. Box 2 provides an overview of the Latin American insurance sector, pointing out the scope for the industry to grow and develop in the region, in particular driven by new insurance needs stemming from climate change (as also seen elsewhere in the world) and an increasing number of natural disasters (to which the region is particularly prone). Lastly, Box 3 discusses immigration to Spain from Central America, Panama and the Dominican Republic. Such immigration has grown markedly in recent years, owing, among other factors, to improved economic conditions in Spain (pull factors) and episodes of social and political unrest in the countries of origin (push factors).