REPORT ON THE LATIN AMERICAN ECONOMY

Latin America in the new era of geopolitical and trade tensions

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Editorial

Geopolitical and trade tensions have emerged as the primary risk factor for the Latin American economy. This owes not only to significant uncertainty about how the region will be affected by the new US Administration's policy agenda on trade, migration and regulation, but also how other global actors might respond. Thus, the region may be affected in terms of its trade and people flows, currency values, financing conditions, capital flows and banking sector resilience, and therefore the outlook for economic activity and inflation rates.

Against this highly uncertain backdrop, economic activity in the region is expected to slow in 2025 towards its potential growth rate, with cross-country heterogeneity. Despite the persistence of upside risks (some of them specific to certain countries), inflation is expected to resume its broad-based downward trajectory in the coming quarters, having held stable in the second half of 2024. A degree of monetary policy divergence has been observed, with rate hikes in Brazil, incipient pauses in Chile, Colombia and Peru and cuts in Mexico. Generally speaking, the policy rate changes have been consistent with the actual and expected developments in activity and inflation across the various countries. The monetary policy stance will remain tight, while financial markets are pricing in few further policy rate cuts in the region and fresh hikes in Brazil, greatly influenced by developments in the United States.

The depreciation pressures of recent quarters driven by heightened global risk and by US monetary policy and its macroeconomic outlook have been partly offset by domestic factors and policies. Meanwhile, the rise in local currency long-term bond yields has essentially been determined by domestic factors. In addition, portfolio capital flows into the region continued, despite lower carry trade returns.

Regarding international trade, Mexico has far closer ties with the United States – in terms of trade volume, value chain integration and product concentration – than other countries in the region, and therefore could be harder hit by more restrictive US trade policy, with especially adverse repercussions for manufacturing sector exports. This is also true, albeit to a far lesser extent, for Colombia. In the near term, the European Union (EU) could be an alternative destination for these two countries' exports, given their established presence in the market for certain products, albeit with a limited market share. Brazil, Peru, Argentina and Chile are far less dependent on trade with the United States, since China, other countries in the region and/or the EU account for larger shares of their export markets.

In terms of the new US Administration's regulatory agenda, its energy and environmental policies are key for Latin America given its reliance on commodity exports. In the near term, a Chinese economic slowdown due to a hypothetical escalation in trade tensions would cause commodity prices to fall, whereas, conversely, the appreciation of the US dollar would drive prices up. In the medium term a less ambitious energy transition could prompt a decline in global demand for major

Latin American exports such as copper, lithium or zinc. The value of the region's oil, gas and coal exports could be affected if the United States makes it easier for companies to extract these products. But the impact on these commodity prices is not clear, since an increase in US supply would bring them down, while global demand for these commodities could potentially increase (as could the region's production) in a setting of easing environmental standards. For now, the stock prices of companies linked to these sectors are trading at a premium, also in Latin America.

More stringent immigration policies in the United States could have an impact on the region's labour supply (increasing it) and remittances (reducing them). This potentially permanent reduction over the medium term could have adverse effects, given that remittances from the United States play a key role for most countries in the region – especially in Central America and the Caribbean –, driving consumption and investment and helping to balance the current and fiscal accounts.

A more restrictive US monetary policy stance than anticipated by the financial markets would have a negative impact on bank lending in Latin America, particularly for banks that are more active on international markets and have more dollarised portfolios. In any event, lending remains robust in the region, which could mitigate the impact of any potential turmoil. Non-performing loans are declining and the vulnerability indicators of the banking sector remain contained. The main risks to financial stability reported by central banks in the region, shown in Figure 2 of this report, are geopolitical and trade tensions, climate and natural disaster risks, vulnerable public finances, increased credit risk and abrupt changes in asset values.

In addition, given the geopolitical uncertainty, there are growing concerns about the limited fiscal policy space and public debt sustainability in the region, especially in Brazil and Colombia.

Turning to the Argentine economy, the adjustment plan has managed to steadily reduce inflation, while economic activity started to pick up in the second half of 2024. Argentina is undertaking a host of structural reforms, and the financial markets continue to perform very positively, although challenges remain in the foreign exchange market.

Two boxes and two articles accompany the report. Box 1 sets out the content and ratification process of the EU-Mercosur agreement, and analyses the possible economic effects on the two regions, while Box 2 examines the impact of domestic and foreign monetary policies on bank lending in Central America and the Dominican Republic. As for the articles, the first describes the main features of foreign direct investment between Spain and Latin America, and the second provides an overview of remittances from Spain to Latin America.

Report

Contents

1 Economic activity in the region is expected to slow to around its potential growth rate, with cross-country heterogeneity and amid much uncertainty

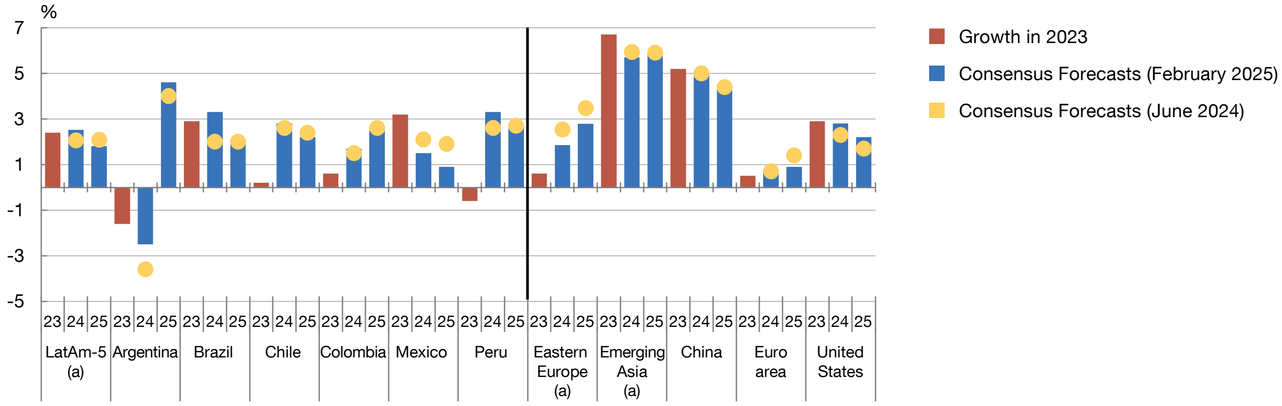
— Broadly speaking, Latin American economies saw growth quicken in 2024 (Chart 1.a). The exceptions were Mexico, with a marked slowdown, and Argentina, with a sharp decline in activity in 2024 H1 but a recovery in H2. Growth is being driven by a resilient labour market, with unemployment rates below the historical average (Chart 1.b), and the less restrictive monetary policy stance.

— For 2025, the analysts' consensus points to growth remaining moderate and close to its potential in most of the region's economies (Chart 1.a).

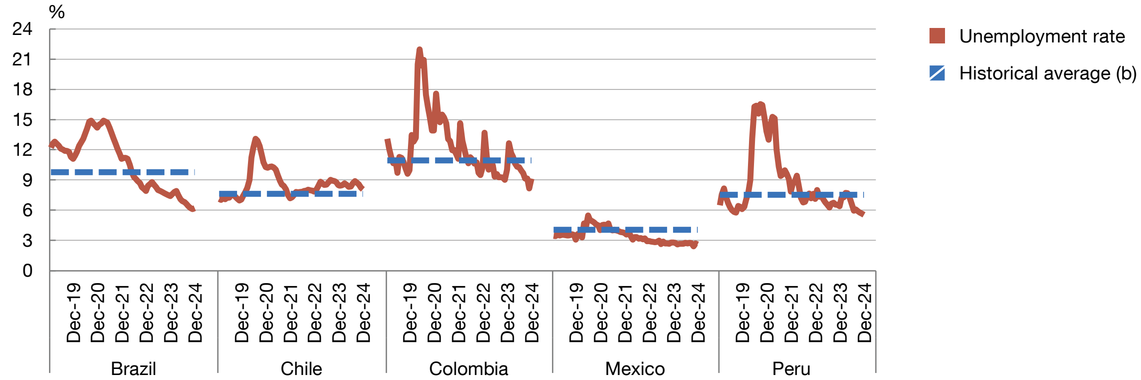
— That outlook is subject to external and internal risks. Notable among the former are the economic policies that might be adopted in the United States, while the latter include uncertainty about the future course of economic policies and concerns over the limited fiscal policy space in some countries.

Chart 1

1.a GDP growth forecasts



1.b Unemployment rates



SOURCES: Banco de España, LSEG Datastream, Consensus Forecasts and national statistics.

a LatAm-5: Brazil, Chile, Colombia, Mexico and Peru. Eastern Europe: Bulgaria, Czech Republic, Hungary, Poland and Romania. Emerging Asia: India, Indonesia, Malaysia, Philippines and Thailand. All aggregates weighted by purchasing power parity-adjusted GDP.
b Historical average: January 2010 - December 2024.

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2 Although upside risks persist, inflation is expected to resume a downward trajectory this year, having held stable in 2024 H2

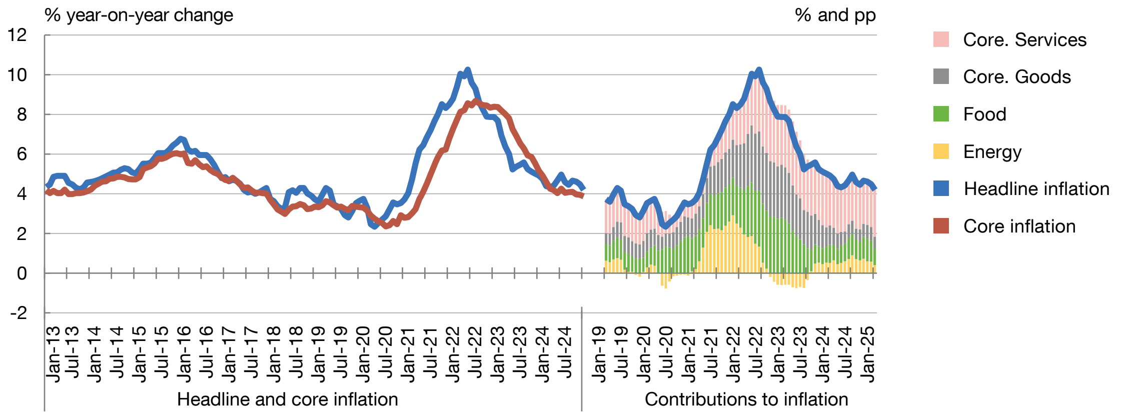
— Inflation for the aggregate of the five largest inflation-targeting economies held stable in 2024 H2 (at around 4.5% year-on-year for headline inflation and 4% for core inflation), curbing the disinflation process seen in previous quarters (Chart 2.a). Indeed, inflation in Brazil and Chile moved unexpectedly upward. In line with other regions, there was significant persistence in the services component.

— Surveys conducted by the region's central banks suggest that inflation will gradually decrease in 2025, ending the year in the upper half of the target range across all countries except Brazil (inflation in Peru has been within the target range since April 2024) (Chart 2.b).

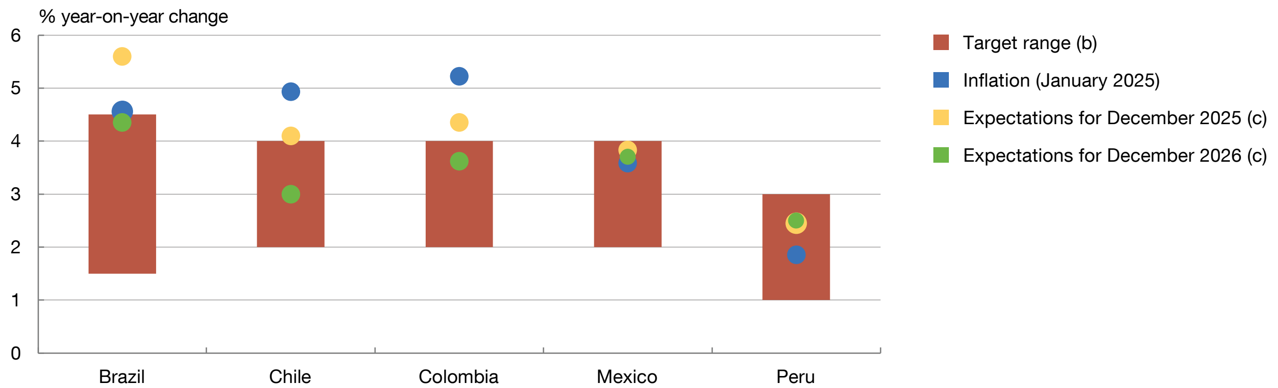
— In their reports, most central banks indicate that upside risks predominate: a deanchoring of medium-term inflation expectations in some countries, persistent services inflation, expansionary fiscal stances, climate events and, in particular, the effects of trade and other policies in the United States, how they will impact US monetary policy conduct and the potential for all this to drive further exchange rate depreciation.

Chart 2

2.a Inflation in Latin America and contributions (a)



2.b Inflation, inflation targets and inflation expectations



SOURCES: LSEG Datastream and national statistics.

a Aggregate of Brazil, Chile, Colombia, Mexico and Peru.
b The inflation target is 3% for the central banks of Brazil, Chile, Colombia and Mexico and 2% for the central bank of Peru.
c Inflation expectations for 2025 and 2026 taken from the central banks' surveys.

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3 A degree of monetary policy divergence has been observed, with rate hikes in Brazil, pauses in Chile, Colombia and Peru and cuts recently in Mexico

- The most recent developments for the region's main central banks include deeper rate cuts in Mexico and pauses in Chile, Colombia and Peru (Table 1). By contrast, Brazil has been raising its policy rate since September 2024, given the positive output gap and expectations about the country's public finances, which have led to a deanchoring of medium-term inflation expectations and a depreciation of the Brazilian real.
- The policy rate cuts made in 2024 were larger than the financial markets had anticipated at the beginning of the year (Chart 3.a). The surprising exception was Brazil, which ended 2024 with an even higher policy rate than at the start of the year. The US Federal Reserve and the ECB eased monetary policy somewhat less than markets had expected at the start of the year.

Table 1

Monthly changes in policy interest rates (bp) (a)

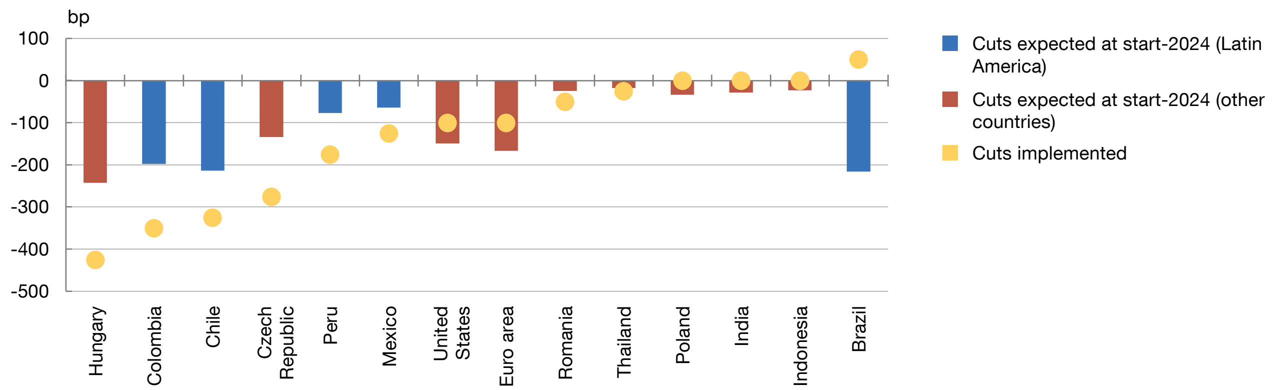
	2023							2024												2025		Policy rate (%)
Brazil			-50	-50		-50	-50	-50		-50		-25				+25		+50	+100	+100		13.25
Chile		-100		-75	-50		-75		-100		-75	-50	-25			-25	-25		-25			5.00
Colombia							-25		-25	-50	-50		-50	-50		-50	-50		-25			9.50
Mexico										-25					-25	-25		-25	-25		-50	9.50
Peru				-25	-25	-25	-25	-25	-25		-25	-25			-25	-25		-25		-25		4.75
Hungary					-75	-75	-75	-75	-100	-75	-50	-50	-25	-25		-25						6.50
Poland				-75	-25																	5.75
India																					-25	6.25
Indonesia					+25						+25					-25				-25		5.75
Euro area	+25		+25	+25									-25			-25	-25		-25	-25		2.75
United States		+25														-50		-25	-25			4.25-4.50

SOURCE: LSEG Datastream.

a Red (blue) denotes monetary policy tightening (easing), while the intensity of the colour reflects the magnitude of the change.

Chart 3

3.a Policy interest rate cuts in 2024: start-of-year expectations vs actual (a)



SOURCES: J.P. Morgan, LSEG Datastream and national statistics.

a Start-of-year expectations for end-2024 policy rates, according to futures or interest rate swaps.

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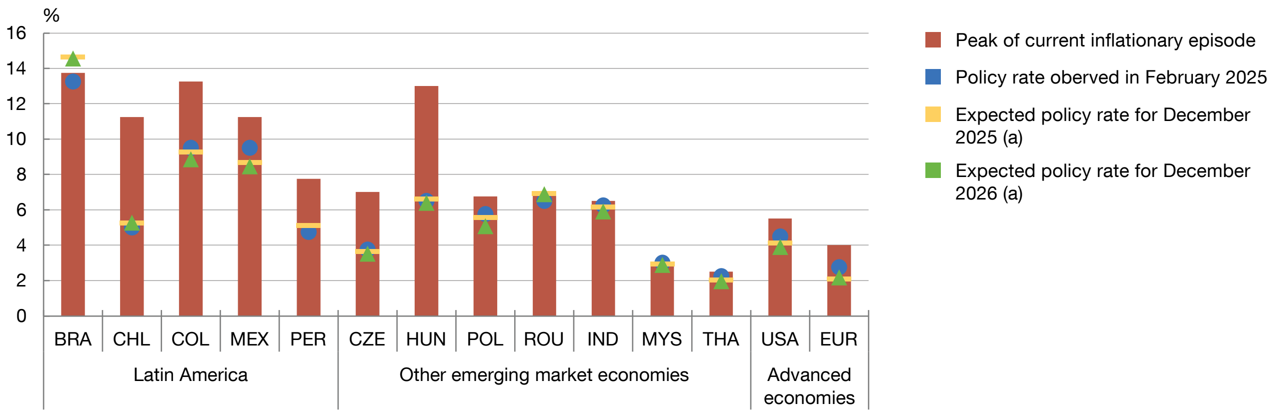
4 The financial markets, greatly influenced by developments in the United States, are pricing in few further policy rate cuts, along with further hikes in Brazil

— The financial markets are factoring in some policy rate cuts over the course of 2025 in Colombia and Mexico (around 100 bp and 50 bp, respectively), but none in Chile and Peru. The hikes in Brazil are expected to continue, with rates projected to rise by some 200 bp in 2025 (Chart 4.a). These dynamics partly reflect the smaller Federal Reserve rate cuts anticipated by the markets since September 2024.

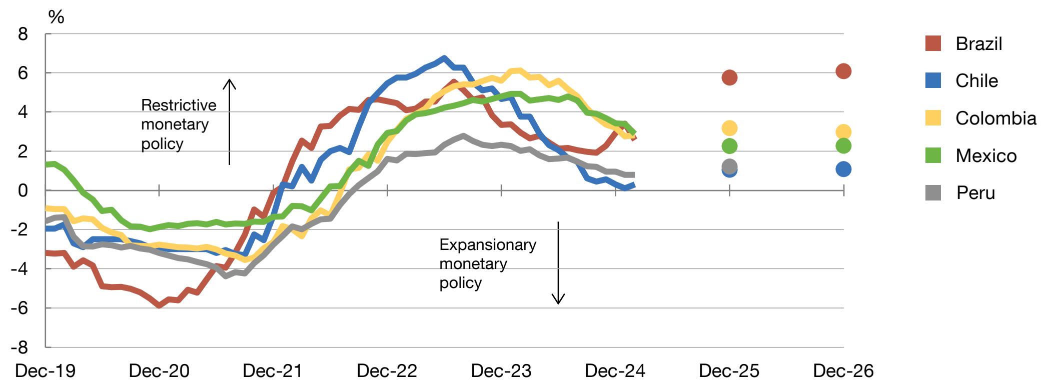
— The monetary policy stance remains tight, as reflected by the positive gap between the real policy rate and the neutral interest rate[1] estimated by central banks. This stance is expected to remain tight in the coming quarters (Chart 4.b).[2]

Chart 4

4.a Policy interest rates



4.b Real policy interest rates less equilibrium interest rates (b)



SOURCES: LSEG Datastream, J.P. Morgan, Latin Focus and national statistics.

a Priced in by financial markets (calculated as the average for the five days to 21 February 2025).
b Real policy interest rates calculated as the difference between policy interest rates and one-year-ahead inflation expectations, drawn from central bank surveys (except for December 2025 and December 2026, which are the policy rates according to futures or interest rate swaps less the inflation expected for end-2026 and end-2027, respectively, according to the LatinFocus February 2025 forecast). The equilibrium interest rates are calculated drawing on estimates by the region's various central banks.

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1 The neutral or natural interest rate is that which prevails when economic activity holds at its potential level and inflation holds stable at the monetary authority's target level. Estimates of the neutral interest rate are subject to a high level of uncertainty

2 Thus, the terminal rates expected in this easing cycle would be higher than those of previous cycles. Some research suggests that neutral interest rates have risen, although there is a great deal of uncertainty surrounding their estimation (see Diego Calderón, Sandesh Dhungana and Daniel Wales. (2025). "Natural Interest Rates in Inflation Targeting Emerging Markets". IMF, forthcoming).

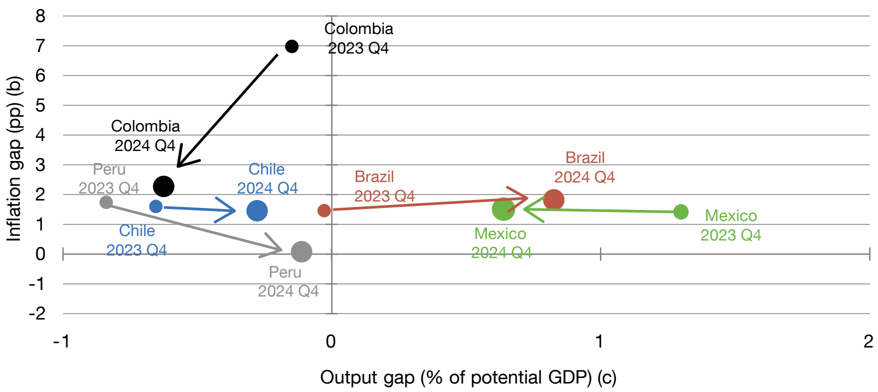
5 Generally speaking, the policy rate changes appear consistent with actual and expected developments in activity and inflation

— In most of the region's countries policy rate developments are broadly consistent with the business cycle (output gap) and the actual course of inflation relative to the target (inflation gap). Brazil and Mexico maintain positive output gaps, although they are moving in opposite directions (widening in Brazil and narrowing in Mexico). Chile, Colombia and Peru continue to have negative output gaps, but only in Colombia has the gap widened (Chart 5.a). The inflation gaps remain positive, with the gap closing only in Peru.

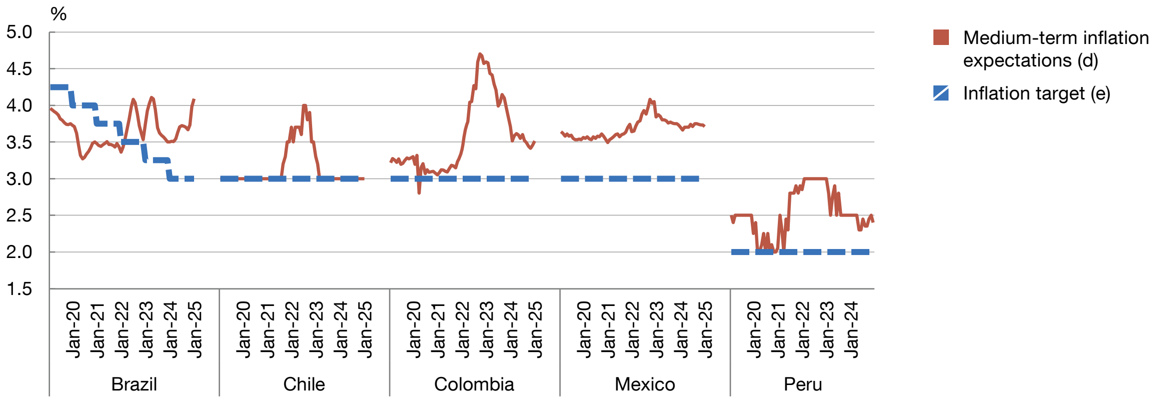
— According to the central banks' surveys, medium-term inflation expectations stand in the upper half of the inflation target ranges, except in Chile (Chart 5.b). Brazil is the notable exception, partly linked to developments in and the outlook for its public finances.

Chart 5

5.a Output and inflation gaps in Latin America (a)



5.b Medium-term inflation expectations



SOURCES: LSEG Datastream, central banks, J.P. Morgan and national statistics.

a The projections for inflation and GDP growth from LatinFocus January 2025 are used for 2024 Q4.
b Difference between inflation in the relevant quarter and the inflation target.
c The GDP trends in the economies are calculated using a two-sided Hodrick-Prescott filter with a smoothing parameter of 1,600 and using GDP forecasts up to 2025 Q4.
d Inflation expectations are two years ahead for Brazil, Chile, Colombia and Peru and over the one to four-year ahead horizon for Mexico. The surveys are those conducted by the central banks.
e Unlike the region's other countries, where the inflation targets have remained constant, in Brazil the targets are set on an annual basis in December of the preceding year, and approved by the National Monetary Council (CMN).

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6 The shift in US economic policies could affect the region through numerous channels

— Since taking office, President Trump has announced major changes to US economic policies, notably on trade (higher tariffs and other barriers), migration (tighter border controls and deportations), regulations (streamlining and deregulation) and fiscal policy (more expansionary).

— These new economic policies are expected to have an impact on the US economy. The financial markets are pricing in a scenario where US policy rates are higher than they were before the November election.

— These developments in the US economy have global effects, including in Latin America. The potential impact channels of the policies announced are summarised in Figure 1. Pages 11 to 14 present the developments observed in the region's financial variables and capital flows, while pages 15 to 22 examine Latin America's exposures to the announced US policies relating to trade, migration and energy regulation, and their potential impacts on economic activity and inflation. The impact of a tightening of the Federal Reserve's monetary policy on the volume of lending extended by the region's banks is simulated on page 23.

Figure 1

US economic policies	Main impact channels for Latin American economies			
	GDP	**Inflation**	**Commodity prices**	**Local currency / dollar**
Trade policy (protectionism) — Higher tariffs — Non-tariff barriers — Increased uncertainty on trade policy (which has become a tool to exert pressure)	— (but mitigated by potential trade diversion)	+ (if there is retaliation)	— (decreased global activity)	**Depreciation**
Migration policy (tightening) — Deportations — Tighter border controls — Tax on remittances	+ increased labour supply; improved human capital; competition in local labour market — (decrease in remitances)	— increased labour supply; improved human capital; competition in local labour market — (decrease in remitances)		**Depreciation** (decrease in incoming remittances)
Fiscal policy (more expansionary) — Extension of tax cuts — Corporate tax reduction — Tax exemptions — Cuts to "inefficient" government spending	+ (increased external demand)	+ (increased external demand)	+ (increased external demand)	**Depreciation** (more restrictive US monetary policy)
Regulatory policy (easing) — Energy production — Financial system	+ (increased external demand)	+ (increased external demand)	? (fossil fuels) — (renewables)	**Depreciation** (more restrictive US monetary policy)

SOURCE: Banco de España.

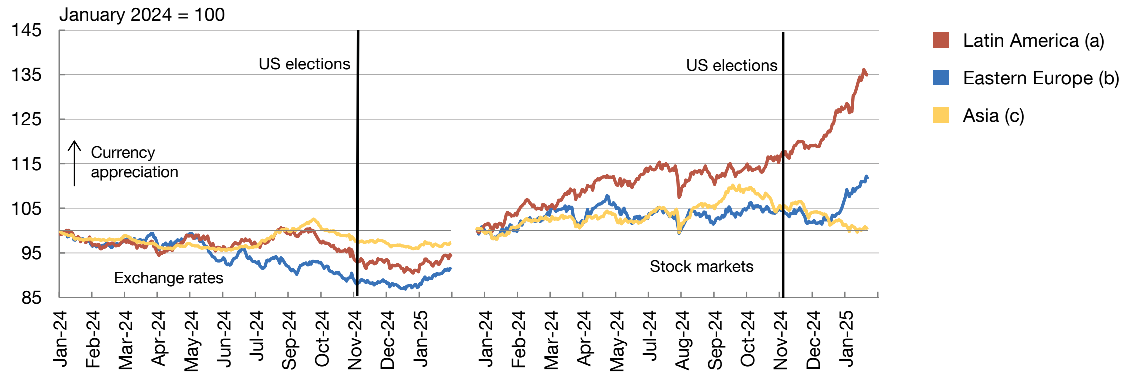
7 Financial conditions in the region had been deteriorating before the US elections, although they have eased slightly since early 2025

— Financial conditions in Latin America began to tighten from October 2024, driven by widening sovereign spreads, marked increases in long-term yields for local currency government bonds and, to a lesser extent, weaker stock market valuations (Charts 7.a and 7.b). The broad-based currency depreciation also continued (Chart 7.b). These trends carried on into the final stretch of 2024, after the US legislative and presidential elections.

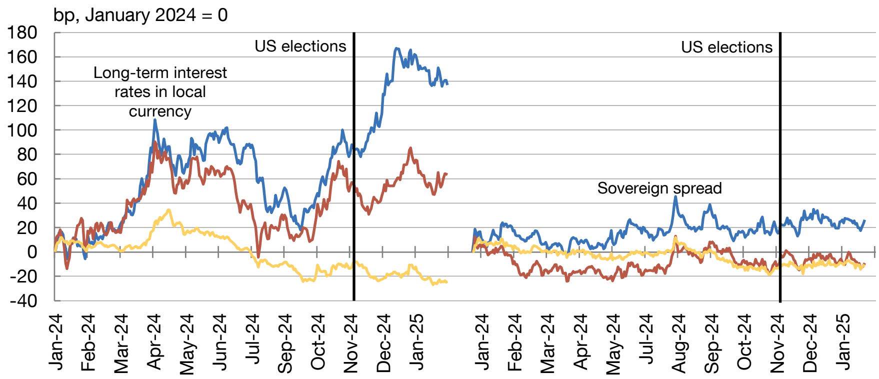
— However, the region's financial markets generally recovered from January, especially the stock market indices. This has helped ease financial conditions somewhat, while the currencies of several of the largest economies (Brazil, Chile and Colombia) have appreciated against the US dollar so far this year (Chart 7.a).

Chart 7

7.a Exchange rates and stock market indices



7.b Local currency long-term government bond yields and sovereign spreads



SOURCES: Banco de España, LSEG Datastream and national statistics.

a Simple average for Brazil, Chile, Colombia, Mexico and Peru.
b Simple average for Czech Republic, Poland and Hungary.
c Simple average for China, South Korea, Philippines, India, Indonesia, Malaysia and Thailand.

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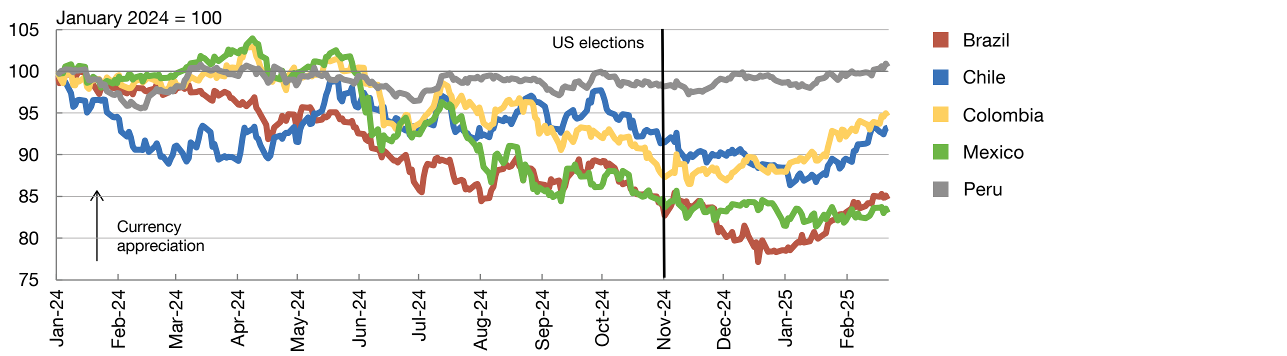
8 The depreciation pressures stemming from heightened global risk and conditions in the United States have been partly offset by domestic factors

— Most Latin American currencies weakened sharply over 2024 H2, particularly in Mexico and Colombia (Chart 8.a). Prior to the US elections the currency depreciation was mainly driven by idiosyncratic factors (local risk), falling commodity prices and the policy rate cutting cycle (except in Brazil) (Chart 8.b).

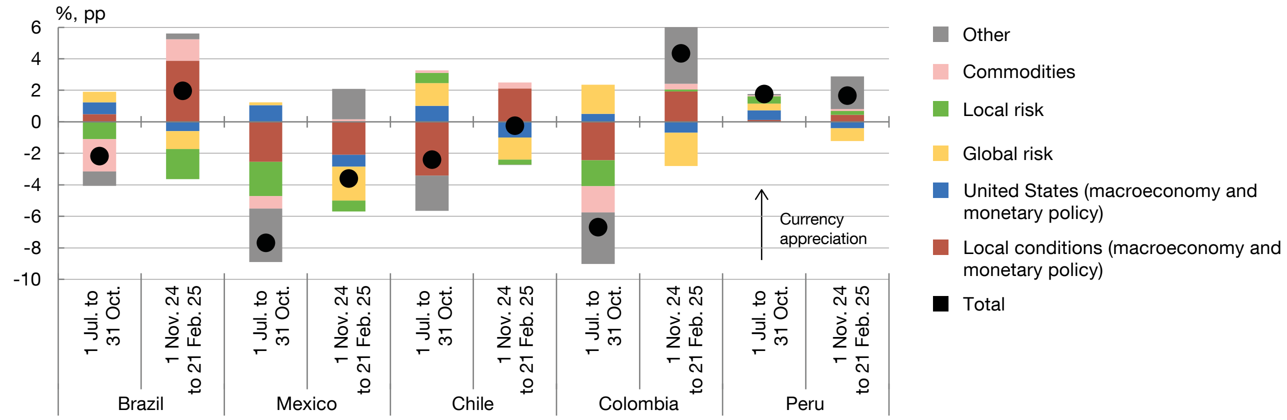
— Although depreciation pressures have intensified since the US elections, due to a heightening of global risk, the currencies of Brazil, Colombia, Chile and, to a lesser extent, Peru have appreciated since early 2025. Broadly speaking, in Brazil, Colombia and Chile the aforementioned effects were largely offset by, among other factors, the relative shift in domestic monetary policy and the countries' economic performance[3] (Chart 8.b).

Chart 8

8.a Exchange rates against the US dollar



8.b Decomposition of the exchange rate variation against the US dollar (a) (b)



SOURCES: Banco de España and LSEG Datastream.

a Decomposition of the exchange rate movements against the dollar estimated drawing on a Bayesian VAR model and using short and long-term interest rates, the local and US stock markets, the long-term interest rate spread vis-à-vis the United States, the exchange rate and commodity prices as an exogenous variable. Identification is via the sign-restriction approach. A distinction is drawn between global and local risk: the latter impacts the local stock market but not the US stock market.
b Two bars are shown for each country, showing the change between (i) 1 July 2024 (the data cut-off date for the last half-yearly report) and 31 October 2024, and (ii) 1 November 2024 and 21 February 2025.

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3 Between the first week of November and early January the Brazilian real depreciated by over 8%. Since then the depreciation has corrected substantially, following the announcement of a fiscal adjustment by the Brazilian Government (around 2.5% of GDP) and the central bank's intervention in the foreign exchange markets (selling some $5 billion).

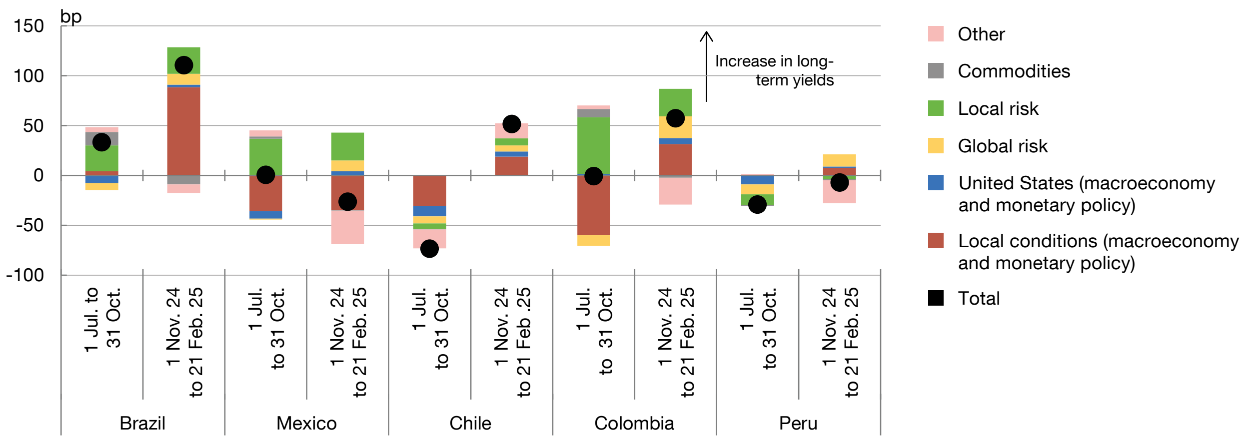
9 The rise in local currency long-term bond yields has essentially been shaped by internal factors ...

— Long-term bond yields in the region began to rise from September 2024. This is particularly true in Brazil, mainly attributable to macroeconomic developments and domestic monetary policy. In Mexico yields remained stable as the upside factors (local and global risks) were offset by the economic slowdown and prospects of monetary easing (Chart 9.a).

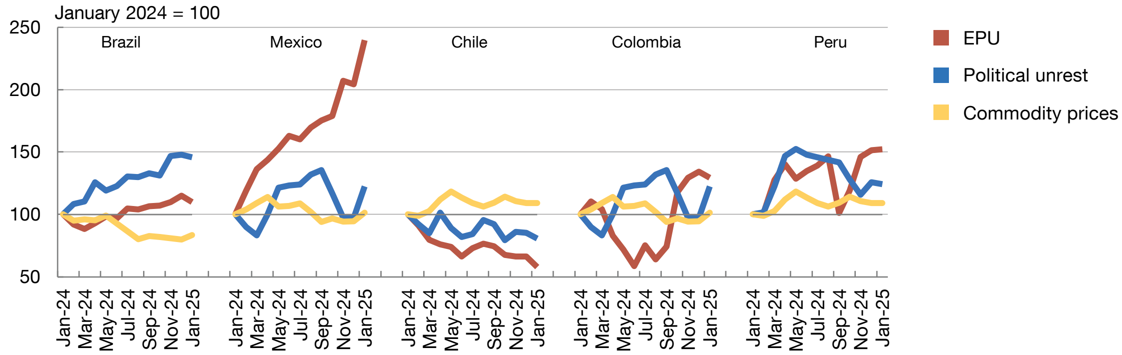
— In Brazil, Colombia and Mexico the local risks resulted in increased economic policy uncertainty (Chart 9.b), partly reflecting concerns about the health of their public finances and other reforms implemented. Political unrest also grew, albeit to a lesser extent.

Chart 9

9.a Decomposition of the change in local currency long-term government bond yields (a) (b)



9.b Determinants of local risk and commodity prices (c)



SOURCES: Banco de España, LSEG Datastream and national statistics.

a Decomposition of the movements in local currency long-term interest rates estimated drawing on a Bayesian VAR model and using each country's short and long-term interest rates, the local and US stock markets, the long-term interest rate spread vis-à-vis the United States, the exchange rate and commodity prices as an exogenous variable. Identification is via the sign-restriction approach. A distinction is drawn between global and local risk: the latter impacts the local stock market but not the US stock market.

b Two bars are shown for each country, showing the change between (i) 1 July 2024 (the data cut-off date for the last half-yearly report) and 31 October 2024, and (ii) 1 November 2024 and 21 February 2025.

c Economic policy uncertainty (EPU) is measured by an index based on words relating to economic policy uncertainty in local and international newspapers; see Erik Andres-Escayola, Corinna Ghirelli, Luis Molina, Javier J. Pérez and Elena Vidal. (2022). “Using newspapers for textual indicators: which and how many?”. Working Papers, 2235, Banco de España. Political unrest is measured by an index constructed using terms related to political confrontations in newspapers. Lastly, the commodity price shown is that for each country's main export commodity: soy (Brazil), metals (Chile and Peru) and oil (Colombia and Mexico).

10 … and portfolio capital inflows continued, despite lower carry trade returns

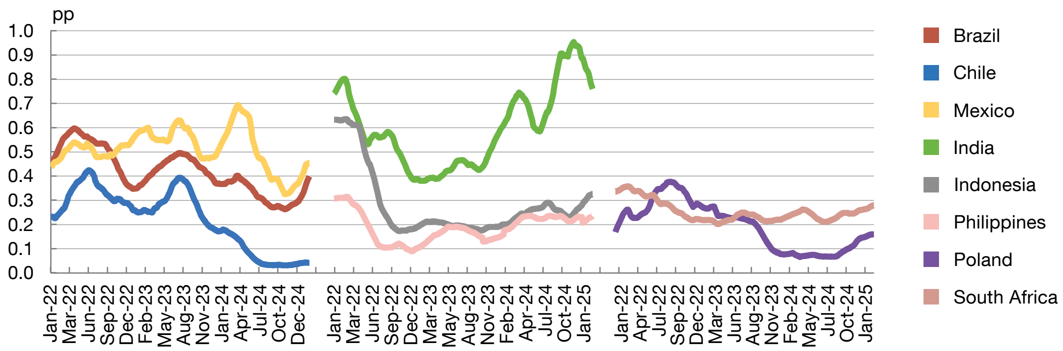
— Portfolio capital inflows held in positive territory in 2024 H2, driven particularly by bond purchases, despite the gradual decline in carry trade[4] returns in the region (Chart 10.a). Inflows over the last two years have been similar to those in other emerging regions, except for China (Chart 10.b).

— These dynamics have not changed following the US elections. However, capital flows into the region could decline under certain risk scenarios, such as if US policy rates deviate above the path currently priced in by the markets.[5]

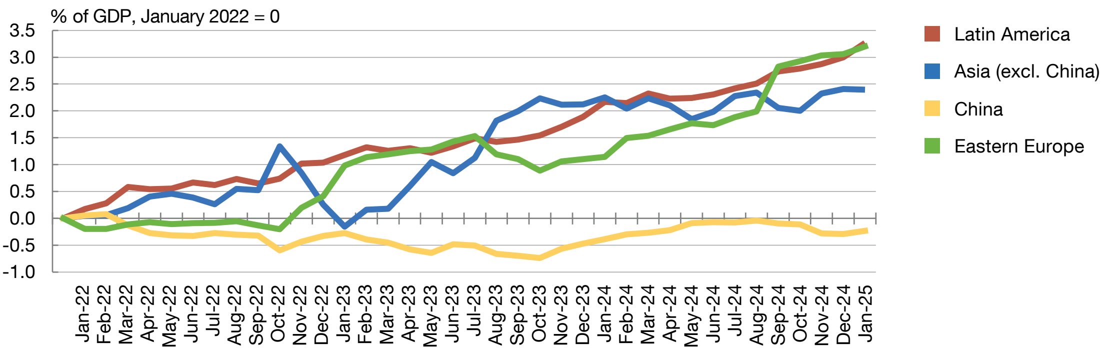
— For a description of foreign direct investment into and out of Latin America, especially vis-à-vis Spain, see Álvarez, Berganza and Martín Machuca (2025) (English version forthcoming).

Chart 10

10.a Carry trade return indicator (a)



10.b Portfolio capital flows



SOURCES: Banco de España, IIF and LSEG Datastream.

a Calculated as the ratio between the interest rate spread between 1-month deposits in the national currency and in US dollars, and the exchange rate volatility of each currency against the dollar.

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4 In a carry trade strategy, investors borrow in a low-interest rate currency to invest in another currency or asset that offers a higher rate of interest. The investor earns the difference between the two interest rates.

5 For the estimated adverse effects on portfolio capital flows into Latin America under a scenario of tighter US monetary policy, see page 18 of the *Report on the Latin American economy. First half of 2024.*

11 In terms of international trade, Mexico has far closer ties with the United States than other countries in the region ...

- Mexico is the region's most open economy to the trade in goods, with a trade openness ratio[6] of close to 70%, followed by Chile and Peru (slightly over 50%), Brazil and Colombia (around 30%) and Argentina (20%).

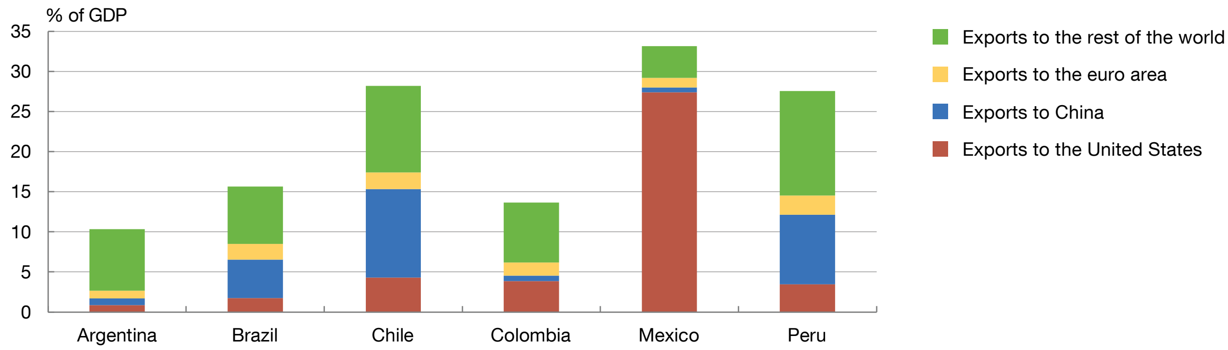
- Goods exports represent 33% of GDP in Mexico, just over 28% in Chile and Peru and only 16%, 14% and 10%, respectively, in Brazil, Colombia and Argentina (Chart 11.a).

- Mexico is by far the country most exposed to the potential disruption of trade flows with the United States, both on account of its trade openness and the fact that 83% of its exports go to the latter country (Chart 11.a). Colombia is a distant second, with slightly under 30%. These figures are significantly lower for the region's other main economies (Brazil, Chile and Peru), where trade is more diversified and more targeted towards China.

- Similarly, services exports, albeit quantitatively less significant, represent 9% of GDP in Chile and Colombia, 7% in Mexico, 6% in Brazil and 5% in Peru. The United States is the destination of 70% of Mexican services exports. This figure is 30-40% in the case of Colombia and Peru and around 10% for the remaining countries. For Brazil, Chile and Argentina, the main destination of services exports is the EU (around 20% of the total).

Chart 11

11.a Goods exports, by region, in 2023 (as a percentage of GDP)



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SOURCES: IMF (DOTS) and LSEG Datastream.

6 Exports plus imports over GDP. In this respect, Latin American economies stand at intermediate-low levels compared to other emerging economies, far from those in Eastern Europe or Malaysia (with trade openness ratios ranging from 90% to 150%), but somewhat higher, on average, than some Asian economies such as India (30%) or Indonesia (35%).

12 ... and could be harder hit by more restrictive US trade policy ...

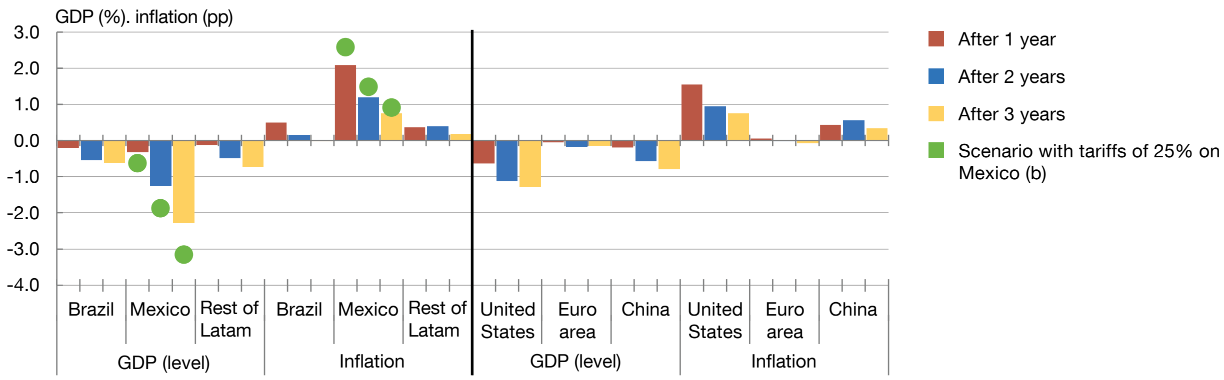
— To illustrate the potential impact on Latin America of an escalation in protectionism, a hypothetical scenario is simulated[7] in which the United States permanently raises its tariffs on Chinese imports by 50 pp and by 10 pp on imports from the rest of the world. In turn, all countries would respond with identical tariffs on US exports. Under this scenario, economic activity in Mexico, Brazil and the rest of the region would shrink, albeit more sharply in Mexico given its greater trade openness. Inflation would rise, more particularly in the first year, due to the amplifying effect of exchange rate depreciation, and would then be gradually corrected by the monetary policy response, among other factors (Chart 12.a).

— A more adverse scenario for Mexico would be the US Administration moving forward with the announced tariffs of 25% on Mexico, 25% on Canada (10% for electricity and energy) and 10% on China.[8] Under this scenario, if the affected countries were to take symmetric retaliation measures, economic activity in Mexico would contract by as much as 3.1% after three years, and inflation would rise by 2.6 pp in the first year (0.9 pp in the third year).

— The simulations are subject to high uncertainty, because of their reliance on the models used and because not all the possible impact channels are explored. In particular, the estimated effects would be amplified if uncertainty over the future course of trade policies were to increase, and in the event of global value chain disruptions.

Chart 12

12.a Impact on GDP and inflation of a more restrictive trade policy scenario worldwide (a)



SOURCE: Banco de España.

a A scenario is simulated in which the United States permanently raises its tariffs on imports from all countries by 10 pp, with the exception of China, for which the tariff increases by 50 pp (to 60%). The countries affected by this measure, in turn, impose a reciprocal tariff for the same amount on imports from the United States. The simulation uses the NiGEM model, which assumes that economic agents have rational expectations and that each country's monetary and fiscal policies respond endogenously.
b Tariffs of 25% on Mexico, 25% on Canada (10% electricity and energy) and 10% on China, with symmetric retaliation by the affected countries.

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7 The global NiGEM model is used, based on rational expectations and endogenous monetary policy. Documentation on the model, drawn up by the National Institute of Economic and Social Research, is available at https://niesr.ac.uk/nigem-macroeconomic-model

8 See https://www.whitehouse.gov/fact-sheets/2025/02/fact-sheet-president-donald-j-trump-imposes-tariffs-on-imports-from-canada-mexico-and-china/

13 ... with particularly adverse effects on manufacturing exports

— Under the global tariffs scenario, Mexico's exports to the United States would drop by 17% (21% in the more adverse scenario), while its overall exports would decline by 14%, showing its limited capacity to shift exports to other markets and thus mitigate the effect of more restrictive trade policy.

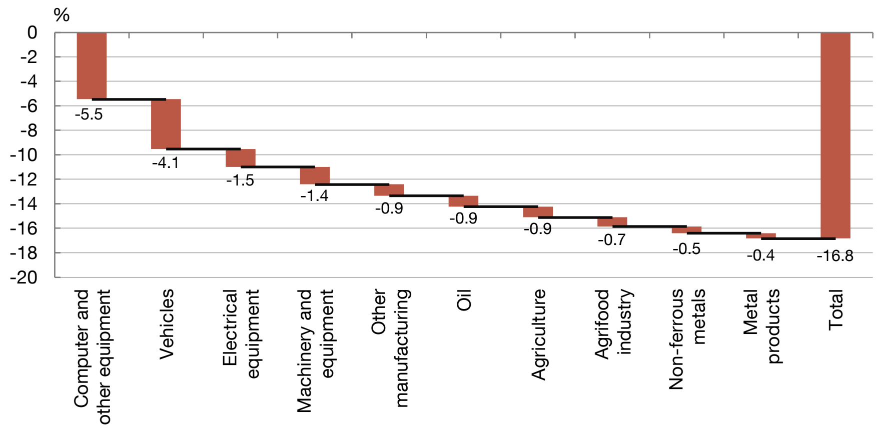
— The impact by sector can be broken down using a multi-sector general equilibrium model.[9] The results show that advanced vehicle and computer manufacturing sectors would bear the brunt of the fall in exports to the United States (Chart 13.a).

— The sectoral pattern shows Mexico's strong reliance on specific high value-added industries geared towards the United States. A possible path for diversifying Mexican exports towards other markets is the modernised Global Agreement entered into between Mexico and the EU in January 2025, replacing the Global Agreement signed in 2000, which could boost trade between the two partners.[10]

— Similarly, elsewhere in the region, Mercosur and the EU entered a partnership agreement in December 2024 to strengthen trade, political and cooperation ties (see Box 1).

Chart 13

13.a Mexico: sectoral impact on exports to the United States of a more restrictive policy scenario worldwide (a)



SOURCE: Banco de España.

a A scenario is simulated in which the United States permanently raises its tariffs on imports from all countries by 10 pp, with the exception of China, for which the tariff increases by 50 pp (to 60%). The countries affected by this measure, in turn, impose a reciprocal tariff for the same amount on imports from the United States. The simulation uses the GTAP model.

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9 The GTAP model is a computable general equilibrium model used to analyse the effect of economic policies on international trade. It is a multi-region and multi-sector model that contains information for 141 countries and 76 economic sectors, and has substitution elasticities that tend to be higher for final goods, since these are more differentiated and are less replaceable than intermediate goods or commodities. In addition, the border crossings of intermediate goods in the manufacturing stage of the value chain are included in the GTAP model in line with the customs policy between the two countries.

10 See https://ec.europa.eu/commission/presscorner/detail/en/ip_25_248 and Baker, Estevadeordal and Talvi (2025).

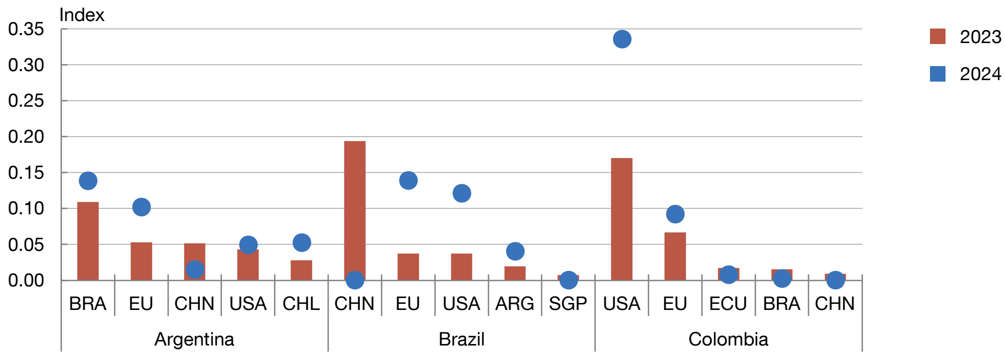
14 The United States is Mexico's main market for a great number of products. This is also true, to a far lesser extent, for Colombia

— An economy's exposure and vulnerability can also be measured by calculating, with granular bilateral trade flow data, the export market share of a particular country for the specific products it receives from that economy (bilateral concentration indices).[11] High bilateral concentration shows that the trading partner in question is an important export market for a high number of products.

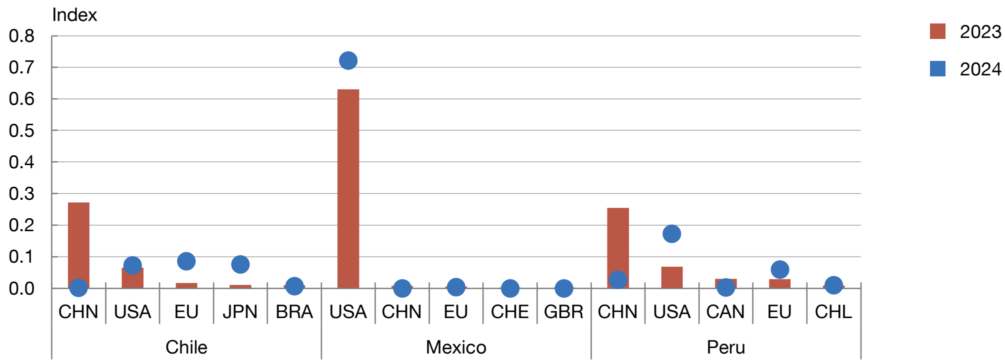
— Mexican exports are highly concentrated in the United States, far more than those of the other countries in the region vis-à-vis their main export markets (Charts 14.a and 14.b). Colombia's concentration with respect to the United States is almost three times lower than that of Mexico. Brazil, Chile and Peru have a higher concentration of exports in China, making them more vulnerable to Chinese market developments. Argentina's exports markets are more diversified.

Chart 14

14.a Bilateral concentration of goods exports (a)



14.b Bilateral concentration of goods exports (a)



SOURCE: Banco de España, drawing on CEPII-BACIdata.

a For each product, identified at the 6-digit HS level, the concentration of a country's exports is measured using the Herfindahl-Hirschman index, as the squared sum of the shares of that product in all its export markets. Higher index values denote greater export concentration. The product-level concentration indices are aggregated at the export country level, weighting the value of the exports of each product in the country's total goods exports. Lastly, each country's export concentration index is broken down in bilateral terms, assigning each product to the largest destination market. Intuitively, high bilateral concentration values denote that the trading partner in question is the largest destination market for many of the exporting country's exports. Such exports are highly concentrated in the destination market and represent a large share of the country's exports. For more details, see Irina Balteanu, Katja Schmidt and Francesca Viani. (2025). “Sourcing all the eggs from one basket: trade dependencies and import prices”, Documentos de Trabajo, 2503, Banco de España.

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11 The indices range from 0 to 1 (highest concentration).

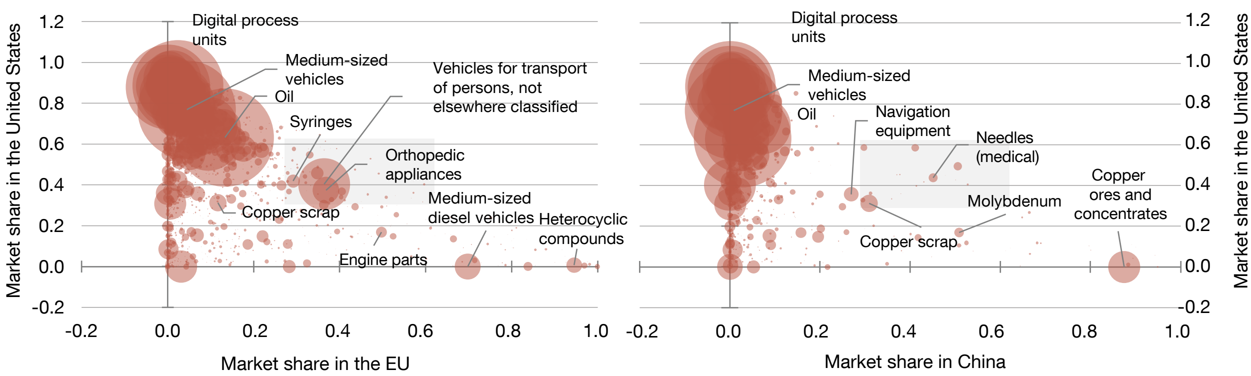
15 In the near term, the EU could be an alternative destination for some of Mexico's and Colombia's exports

— Latin American economies now have a presence in the European and Chinese markets, which may provide an indication of their potential to shift exports to these markets in the near term, should they face difficulties in accessing the US market. Such a shift would be easier towards markets where the exporter is already present.

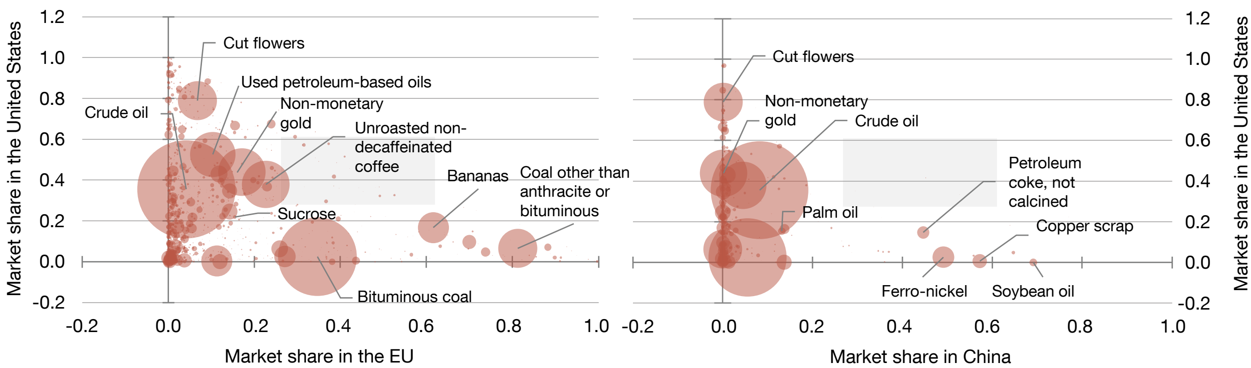
— For Mexico, the EU could be an alternative export destination for certain goods, such as crude oil, some types of vehicles, specific engine parts or medical instruments, given its established presence and strong market shares in the European market (Chart 15.a). In the short term, any shift to the Chinese market could be limited to a few products, such as medical instruments or copper (Chart 15.a). As for Colombia, its biggest export to the United States (oil) has a very low market share in the EU and China. However, other products such as coffee, gold and some oil products, which have large market shares in both the United States and the EU, could help strengthen Colombia's presence in the European market (Chart 15.b). Redirecting towards the Chinese market in the short term would be more difficult (Chart 15.b).

Chart 15

15.a Mexico: market shares in the United States, the EU and China (a)



15.b Colombia: market shares in the United States, the EU and China (a)



SOURCE: Banco de España, drawing on CEPII-BACI data.

a For each product, identified at the 6-digit HS level, the market share of exports to the United States is compared with that to the EU or China. The shaded areas denote the products for which none of the represented countries/areas are clearly predominant relative to the others.

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16 The impact of the new US Administration's energy and environmental agenda could be very significant for the region

— A large share of the exports of Latin America's main economies (excluding Mexico) is composed of agricultural commodities (particularly those from Argentina and Brazil, but also, to a lesser extent, Chile and Peru), energy commodities (Colombia) and mining commodities (Chile and Peru) (top two panels in Table 2).

— The changes in US policy could affect commodity prices in the short term. For instance, an escalation in trade tensions would dampen demand from China, the biggest buyer of commodities, and lead to a fall in prices. Conversely, the appreciation of the US dollar would drive up the prices in other currencies, since most commodities are traded in US dollars.

— A less ambitious energy transition would prompt a decline in the demand for major Latin American exports such as copper, lithium and zinc (third panel in Table 2). Oil, gas and coal prices could be affected if the United States makes it easier for companies to extract these products. But the impact on prices is not clear, and will depend on the magnitude of the possible increase in supply and global demand.

Table 2
Latin America commodity exports: breakdown by product and commodity needed for the energy transition

	Argentina	Brazil	Chile	Colombia	Mexico	Peru
Exports by sector. As a % of GDP						
Agriculture	5.9	6.6	6.0	2.2	1.2	4.2
Energy	1.2	2.0	0.0	6.9	1.9	1.5
Mining	0.7	1.7	15.6	1.7	0.5	15.9
Industrial	3.2	4.4	6.6	2.9	29.6	2.7
Total	**11.1**	**14.7**	**28.2**	**13.7**	**33.2**	**24.3**
Main export products. As a % of each country's total exports						
Food	57.2	42.4	21.1	15.7	3.7	17.5
Soy	18.5	19.8	0.0	0.2	0.0	0.0
Corn	9.2	4.0	0.1	0.1	0.0	0.0
Other foods	29.6	18.5	21.0	15.4	3.7	17.5
Energy	11.8	12.5	0.0	50.7	5.6	6.1
Oil	5.6	12.5	0.0	31.8	4.7	0.3
Coal	0.0	0.0	0.0	18.4	0.0	0.4
Other energy sources	6.3	0.0	0.0	0.5	0.9	5.4
Mining	6.9	10.7	55.3	12.3	2.5	66.1
Minerals needed for the energy transition (a)	2.2	2.8	54.0	2.5	2.5	44.2
Other minerals	4.6	7.9	1.2	9.8	0.0	21.9
Industrial	24.0	34.4	23.6	21.2	88.2	10.2
Total	**100**	**100**	**100**	**100**	**100**	**100**
Commodities needed for the energy transition. As a % of each country's total exports						
Copper	0.0	1.2	46.4	0.7	1.1	36.7
Lithium	0.7	0.0	6.8	0.0	0.2	0.0
Zinc	0.0	0.1	0.1	0.0	0.2	4.1
Other (b)	0.0	0.1	0.0	0.1	0.1	0.0
Total	**2.2**	**2.8**	**54.0**	**2.5**	**2.5**	**44.2**

SOURCES: LSEG Datastream, Comtrade and national statistics.

a Includes copper, lithium, zinc, aluminium, silver, lead, platinum, nickel, tin and cobalt.
b Platinum, nickel, tin and cobalt.

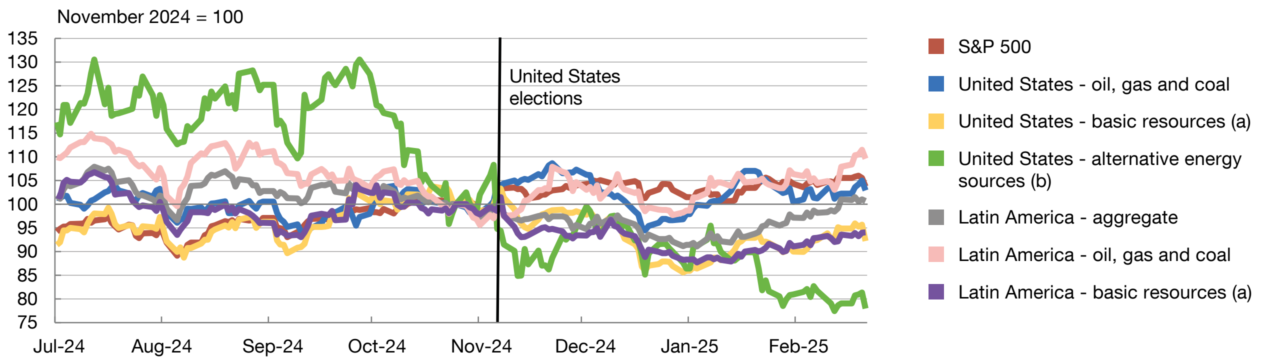
17 In any event, the markets have begun to factor in the change in the US energy policy stance, with rising stock prices for oil, gas and coal companies, including those in Latin America

— The stock prices of companies that could benefit from the changes in US energy policy (oil, gas and coal) rose significantly from mid-December 2024, especially in the United States, but also in Latin America as a whole (Chart 17.a).

— By contrast, stock prices of less polluting energy companies (for instance, solar panel firms in the United Statesor basic resources firms in Latin America, including metal mining and industrial metals) have either plummeted since 2024 Q4 or performed relatively worse than those of conventional energy firms (Chart 17.a).

Chart 17

17.a Stock market indices



SOURCE: LSEG Datastream.

a Comprises the mining, industrial metals, forestry and paper sectors.
b Comprises solar panel firms and solar energy storage firms.

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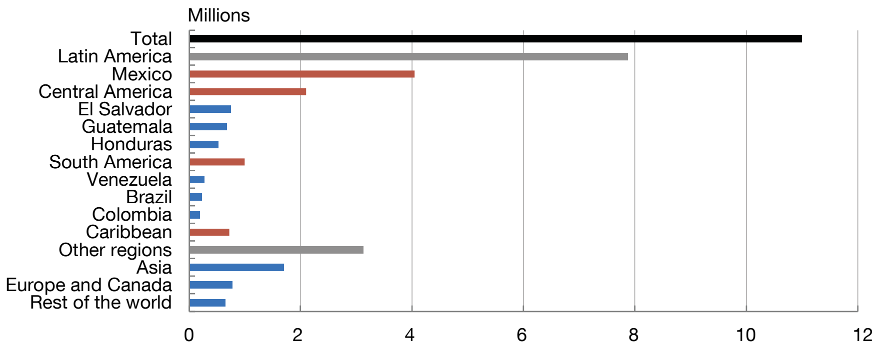
18 More stringent immigration policies in the United States could have an impact on the region’s labour supply (increasing it) and remittances (reducing them)

— Proposals to tighten border controls and increase deportations of illegal immigrants would not only have an impact on the US labour market, but also on some Latin American countries. It was estimated that there were some 11 million illegal immigrants in the United States in 2022, of which 7.9 million were Latin American, most notably from Mexico and Central America (Chart 18.a). Although such policies could increase the local labour supply in returnee’s home countries, the economic impact is uncertain, given that around 1 million people per year, on average, were already repatriated between 2021 and 2024.[12] Against this backdrop, migration flows to Spain could potentially increase.

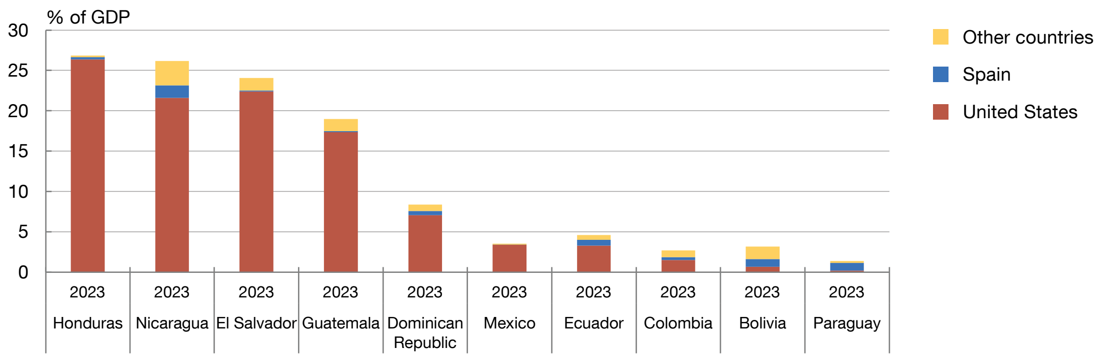
— These policies would also affect remittances, permanently reducing them over the medium term for people forced to leave the United States, and also for those who stay, if affected by the other measures that have been announced, such as a new tax on remittances.[13] These transfers from the United States play a key role for many countries, especially in Central America and the Caribbean, but also in others like Colombia or Mexico (Chart 18.b).[14]

Chart 18

18.a Illegal immigration in the United States. 2022



18.b Main countries of origin of remittance income as a percentage of GDP. Latin America, 2023



SOURCES: National statistics, World Bank and Pew Research Center.

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12 See “How many people are deported from the US each year?” and Diodato, Hausmann and Neffke (2023).

13 In his election campaign, President Trump announced the possibility of introducing such a tax.

14 See Berganza, Cobián González, García Cid and López Espinosa (2025).

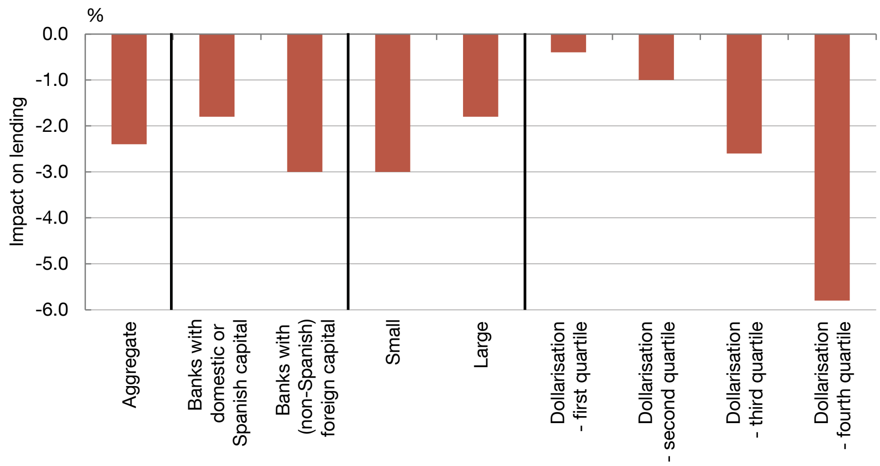
19 US monetary tightening would adversely affect bank lending in Latin America

— To measure the impact on bank lending in Latin America of a tightening of US monetary policy resulting from the new economic policies, an econometric model is estimated to determine how the pass-through of the monetary shock is influenced by different characteristics of the banks (origin of their capital, size and loan dollarisation).

— Chart 19.a shows how a 200 bp hike in the Federal Reserve's policy rates (consistent with the simulations on page 16) would affect loans granted by banks in Brazil, Chile, Mexico and Peru (see Box 2 for a similar exercise for the CADR region). On average, lending would fall by 2.4%. Lending by non-Spanish foreign banks[14] would be more affected, reflecting their increased reliance on international sources of finance and their greater exposure to the global financial cycle, as would lending by smaller banks, which have less access to alternative sources of financing than larger institutions. Bank dollarisation also amplifies the impact of the Federal Reserve's measures,[15] as banks with more dollarised portfolios are more dependent on funds in foreign currency.[16]

Chart 19

19.a Impact of monetary policy tightening by the Federal Reserve on lending by banks in Latin America (a)



SOURCE: Own estimates, drawing on data from monetary and supervisory authorities.

a The chart depicts the impact on loans granted by Latin American banks of a 2 pp hike in the Federal Reserve's policy rates under a simulated scenario such as that described on page 16, in which the United States permanently raises its tariffs on Chinese imports (by 60 pp) and imports from the rest of the world (by 10 pp) and, in turn, all countries impose identical tariffs on US exports. The model is estimated using data from individual banks in Brazil, Chile, Mexico and Peru, for the period between 2005 Q1 and 2023 Q2. The impact of Taylor residuals is estimated using the policy rates in each country as variables of interest in a dynamic panel whose dependent variable is the stock of bank loans. The panel with the breakdown by dollarisation quartile includes only banks in Peru and Chile.

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14 This classification is based on the results of Box 4 of the *Report on the Latin American economy. First half of 2024.* This box shows that domestic and Spanish banks behave similarly in the event of shocks derived from monetary policy decisions by the Federal Reserve, while there is a stronger response in lending from non-Spanish foreign banks than from other banks. This may be attributable to Spanish banks' business model, which is based on independent subsidiaries.

15 Conversely, bank dollarisation is estimated to reduce the impact of domestic monetary policy.

16 See, for example, Alfaro, Calani and Varela (2023), who document the low degree of foreign exchange hedging by firms with dollar-denominated borrowings in Chile, which has one of the most developed derivatives markets in Latin America.

20 Although heterogeneous across segments and countries, lending remains robust in the region, which could mitigate the impact of any potential turmoil ...

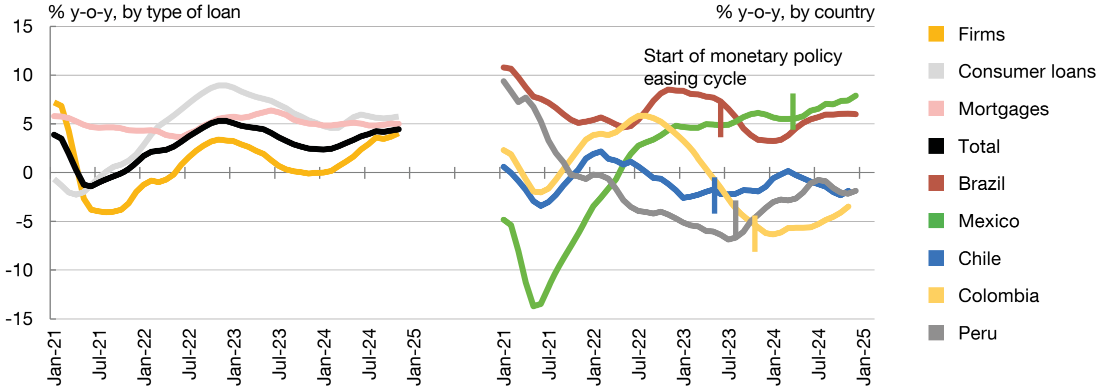
— Real credit growth increased in 2024 H2, driven by the corporate segment (Chart 20.a, left-hand panel). According to central bank surveys on credit conditions, this stemmed from a pick-up in demand and an easing of credit standards, suggesting there may be sustained credit growth in the region over the coming quarters (Chart 20.b).

— The acceleration in aggregate credit was the result of developments in Brazil and Mexico (Chart 20.a, right-hand panel). In those countries that embarked on their policy rate cutting cycle earlier, such as Chile and Peru, credit has seen a slowdown, but it has quickened in those countries that began cutting policy rates later, such as Mexico and Colombia (Chart 20.a, right-hand panel).

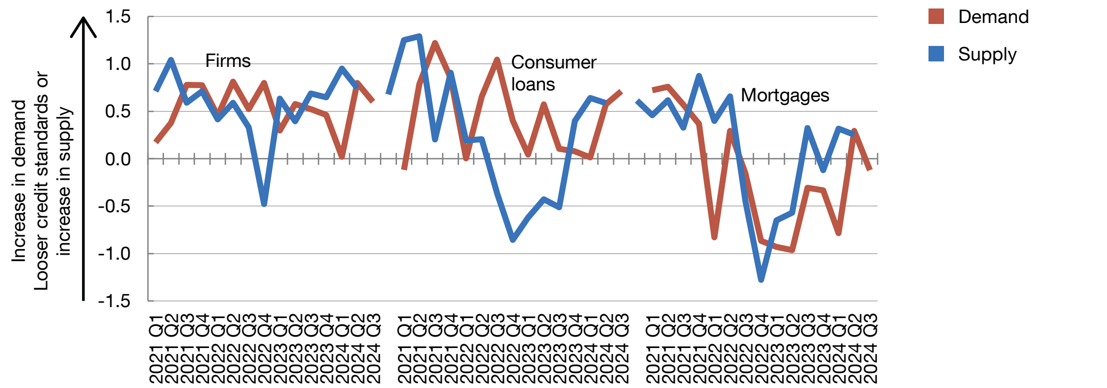
— According to a recent study by the Banco de España,[17] the pass-through of policy rates to lending rates in the current monetary policy cycle has been similar to that of previous cycles, standing at around 100%, 80% and 20% in the consumer, corporate and mortgage segments, respectively.

Chart 20

20.a Changes in credit to the non-financial private sector (real) in Latin America (a)



20.b Credit conditions index: Latin America (b)



SOURCES: Banco de España, LSEG Datastream and national statistics.

a Aggregate of Brazil, Chile, Colombia, Mexico and Peru, with GDP in purchasing power parity terms.
b Aggregates calculated using GDP weightings in purchasing power parity terms. Latest data: 2024 Q3.

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17 See Amado, Molina, Díaz and Quiñonez. (2025). "La transmisión de los movimientos de los tipos de interés oficiales (...)". Forthcoming.

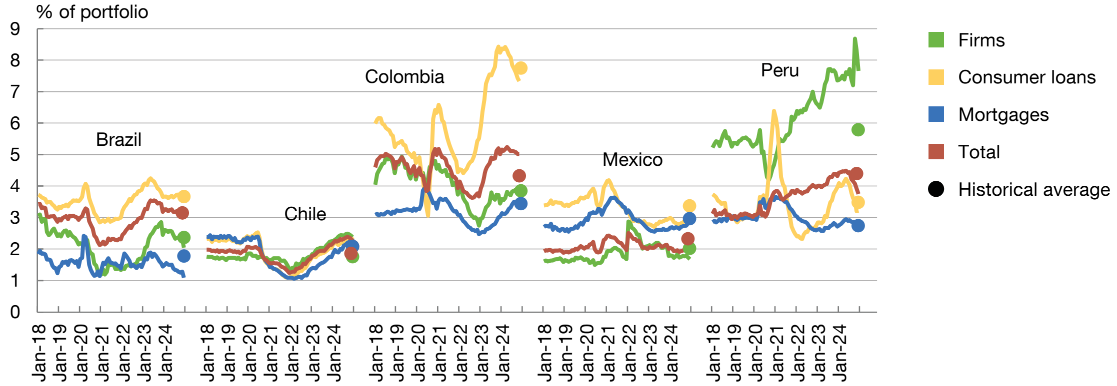
21 ... and the vulnerability indicators of the banking sector remain contained, but there are still significant risks to financial stability

— Non-performing loan ratios have begun to decline across the region, but they still exceed their historical averages in some segments (Chart 21.a). The risks to the region's banking sector remain contained, according to synthetic early warning indicators of banking crises[18] (Chart 21.b).

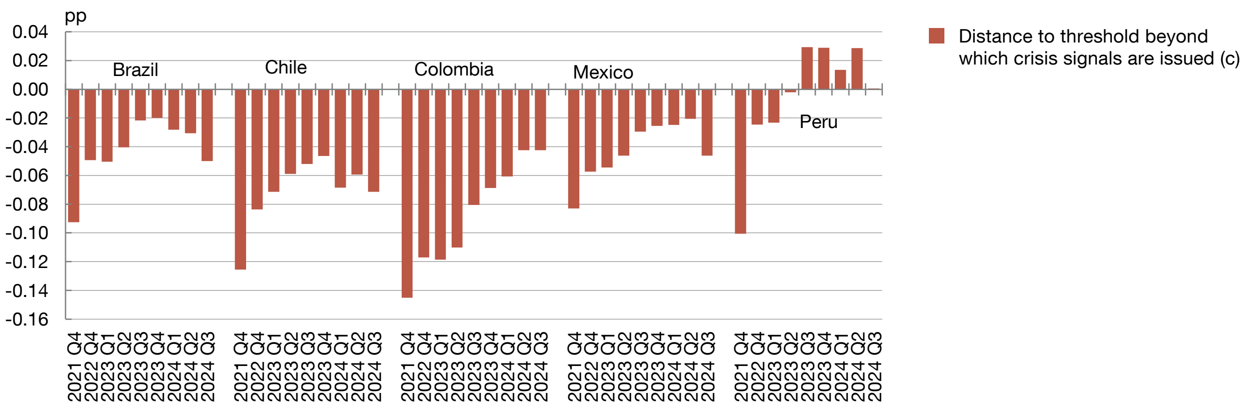
— The central banks in the region, however, report some risks to financial stability (Figure 2). The main risks are: geopolitical risks and trade tensions, due to their impact on financial conditions, capital flows and currency values; climate transition risks; high household and corporate debt; vulnerability of public finances (Brazil, Colombia); operational risks due to digitalisation; increase in credit risk; abrupt changes in asset values; and uncertainty about domestic politics and the institutional framework (Mexico).

Chart 21

21.a Non-performing loans (a)



21.b Vulnerability to a banking crisis (b)



SOURCES: Banco de España, LSEG Datastream and national statistics.

a Percentage of gross loans. The dots denote the historical average (2015-2024) for each type of loan and each country.
b Likelihood of being in a vulnerable state, estimated using a logit probability model for banking crises with pre-selected variables based on the issuance of correct signals six quarters before a crisis (ROC curve threshold).
c The threshold is defined as the percentile beyond which the synthetic index has anticipated banking crises in the past. See Irma Alonso-Álvarez and Luis Molina. (2023). "How to foresee crises? A new synthetic index of vulnerabilities for emerging economies". *Economic Modelling,* Vol. 125(106304).

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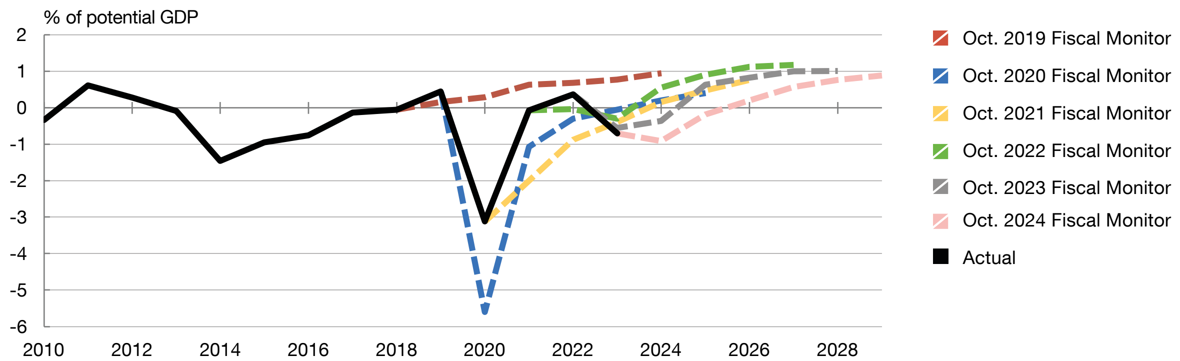
18 "Indicators of vulnerability in emerging countries which are material for the Spanish banking system. Second half of 2024".

22 Given the uncertain geopolitical situation, there are growing concerns about the limited fiscal policy space and public debt sustainability ...

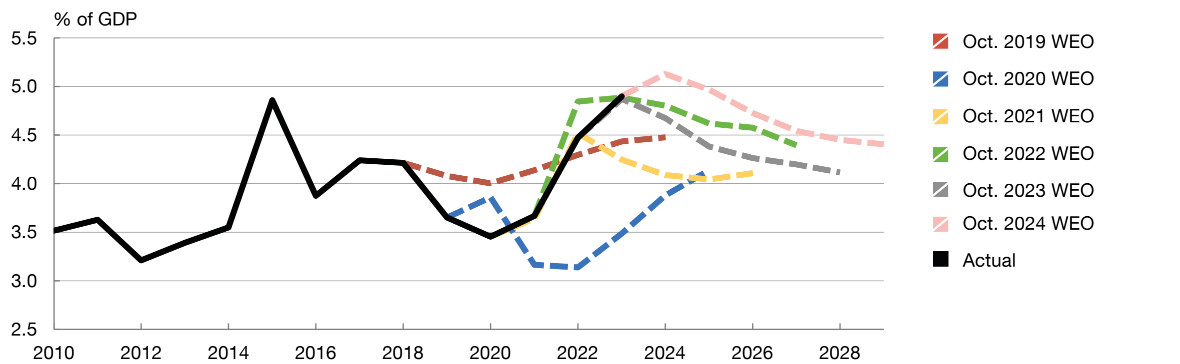
- The structural primary balances of the region's main economies deteriorated in 2024 for the second consecutive year. In part because of this, the structural fiscal outlook continued to worsen relative to previous forecasts (Chart 22.a).
- At the same time, despite the policy rate cuts made in most countries, the interest burden saw a further – and greater than expected – increase, rising to above 5% of GDP in 2024, and is projected to decline only very gradually over the coming years (Chart 22.b).
- The combined forecast of lower structural primary balances and higher interest burdens, along with low potential growth, has heightened concerns among analysts and the financial markets about public debt sustainability. In addition, tighter international financial conditions would drive up debt service, to some extent owing to the depreciation of the dollar and its impact on foreign currency-denominated debt.

Chart 22

22.a Structural primary balance. LatAm-5 (a)



22.b Interest payments. LatAm-5 (a)



SOURCE: IMF.

a Aggregate of Brazil, Chile, Colombia, Mexico and Peru, weighted by purchasing power parity-adjusted GDP.

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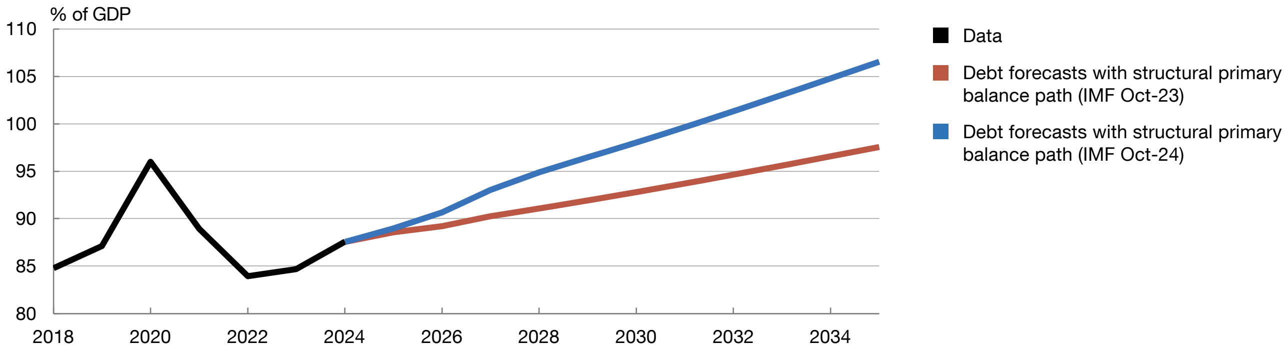
23 … particularly in Brazil and Colombia

— Although the deterioration in the fiscal outlook has been widespread across the region's main economies, it has been particularly acute in Colombia and, especially, Brazil, which faces a combination of high public debt, a persistently negative primary fiscal balance – reflecting non-compliance with the fiscal rule approved in 2023 – and high interest rates.

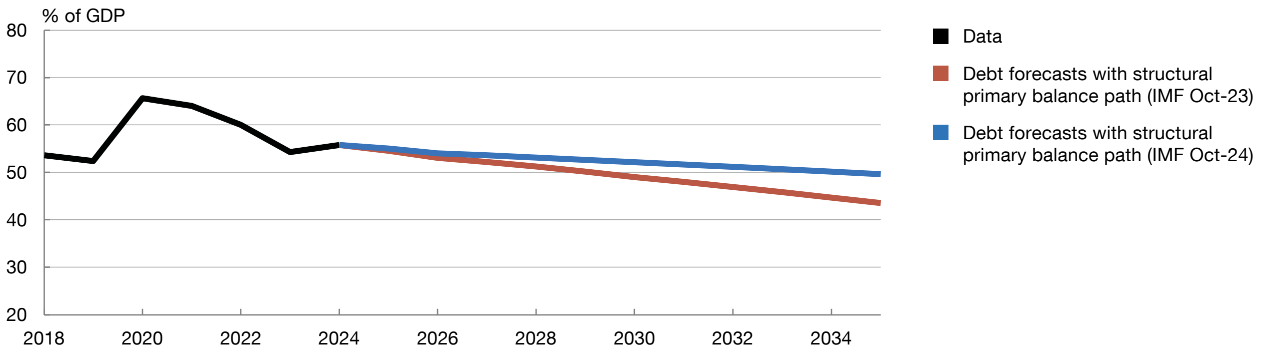
— According to some simulations of debt sustainability in the two countries, a greater than anticipated deterioration in structural fiscal balances would significantly impact public debt dynamics, with a difference of up to 10 pp over ten years in the case of Brazil (Charts 23.a and 23.b), a country which also has very high levels of public debt compared with the rest of the region and with other emerging market economies. In Colombia, however, higher potential growth relative to the other main economies in the region would counteract the negative impact of larger structural primary deficits and higher interest burden. As a result, the public debt-to-GDP ratio would not exceed – but would hold at values very similar to – its current level over the ten-year simulation horizon.

Chart 23
Projections of public debt over the next decade

23.a Brazil



23.b Colombia



SOURCES: Banco de España, LSEG Datastream, IMF and World Bank.

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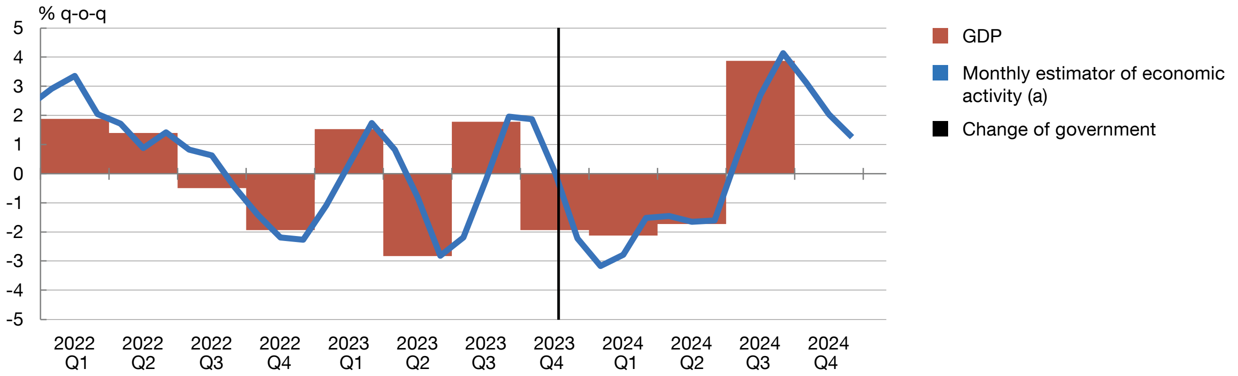
24 Turning to the Argentine economy, the government has steadily and significantly brought down monthly inflation rates under its adjustment plan, while economic activity started to pick up in 2024 H2

— Following a contraction in the first half of 2024, economic activity picked up in H2 (Chart 24.a), reflecting a recovery in private consumption and investment.

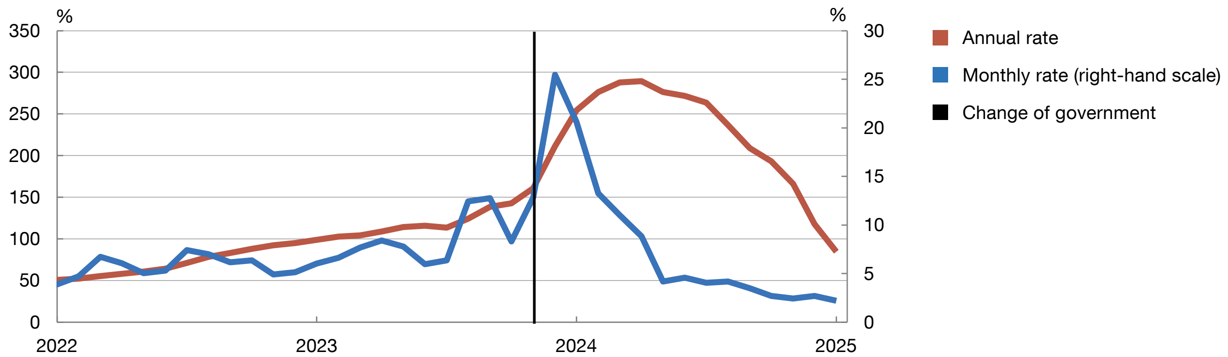
— Inflation has been quickly tamed under the government's adjustment plan (public spending cuts and a sharp devaluation of the peso), and eased from a monthly rate of 25% in December 2023 to 2.2% in January 2025 (Chart 24.b). Inflation expectations have converged to a monthly rate of 2%, matching the peso's (pre-announced) monthly devaluation rate that was in force until 31 January.[19] The convergence of inflation expectations owes to the greater credibility derived from a more sustainable fiscal policy, after fiscal equilibrium was reached in 2024. Nevertheless, maintaining and consolidating the progress made will require pressing ahead with fiscal reforms (to reduce complexity and distortions in the tax system) and improving the sustainability of public spending (mainly wages and pensions), as well as fiscal relations with provinces.[20]

Chart 24
Economic activity and inflation in Argentina

24.a Economic activity



24.b Inflation



SOURCES: LSEG Datastream and national statistics.

a The monthly estimator of economic activity (EMAE, by its Spanish initials) is an economic activity index published by Argentina's National Institute of Statistics and Censuses (INDEC), and is considered a sound leading indicator of Argentina's GDP.

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19 The devaluation rate has been 1% since 1 February.

20 IMF (2025).

25 The financial markets in Argentina continue to perform positively, driven by a host of structural reforms, but challenges remain in the foreign exchange market

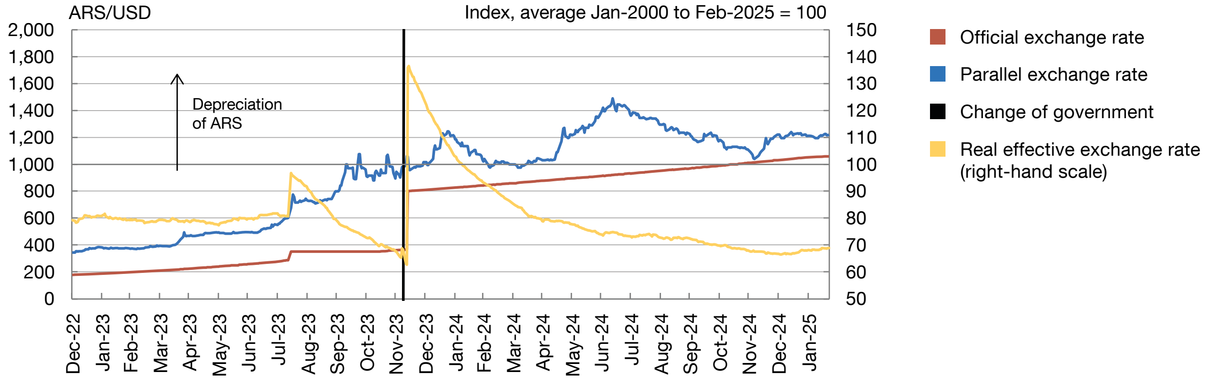
— The main measures taken last year by the government within the area of economic deregulation included liberalising the rental market, bringing greater flexibility to the labour market and partially deregulating international trade, as well as enacting a law that promotes investment in some sectors of the economy, such as mining. In addition, nationwide public sector restructuring began in 2024 H2.

— In this setting, there has also been an improvement in the financial variables. The gap between the official and parallel exchange rates has narrowed considerably (Chart 25.a) and the central bank has been able to start re-building its international reserves. Stock market indices and sovereign spreads also substantially improved in 2024 H2 (Chart 25.b).

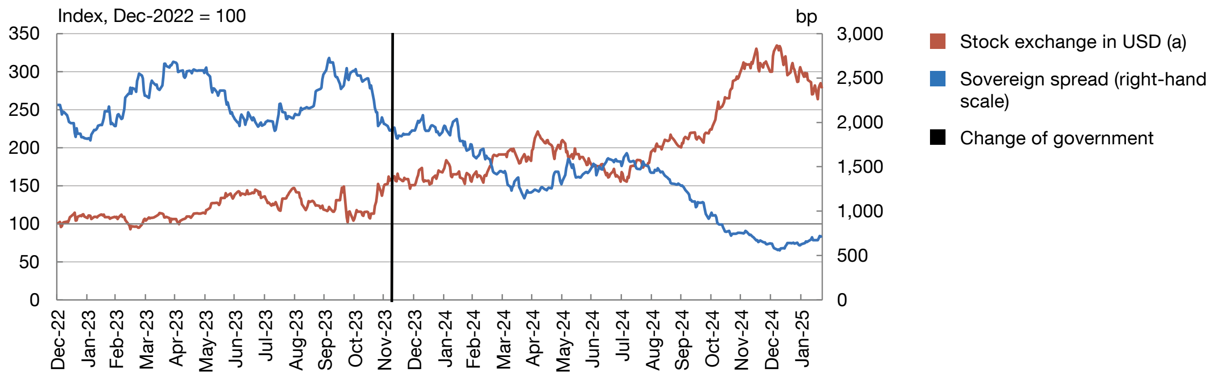
— However, capital controls remain in place and the real effective exchange rate[21] has appreciated markedly since December 2023 and stands at stronger levels than its historical average (Chart 25.a). Therefore, if the exchange rate misalignment were resolved by a large depreciation of the nominal exchange rate that deanchors inflation expectations, the adjustment programme could be jeopardised.

Chart 25
Financial markets in Argentina

25.a Exchange rates



25.b Stock exchange and sovereign spread



SOURCES: Banco Central de la República Argentina and LSEG Datastream.

a The stock exchange in USD is calculated using the parallel exchange rate.

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21 The real exchange rate is a multilateral real exchange rate index (ITCRM) calculated by the Banco Central de la República Argentina. The historical average of this index is calculated for the period from January 2000 to February 2025.

Table 3

Latin America: main economic indicators

	2007-2022 average	2023	IMF forecasts (October 2024 WEO)			2023				2024			
			2024	2025	2026	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
GDP (change on previous period) (a)													
Latin America and the Caribbean (b)	2.0	2.4	2.4	2.5	2.7	1.0	0.1	0.5	0.0	0.4	0.5	1.2	—
Argentina	1.7	-1.6	-3.5	5.0	4.7	1.5	-2.8	1.8	-1.9	-2.1	-1.7	3.9	—
Brazil	1.8	3.2	3.7	2.2	2.2	1.4	0.8	0.2	0.2	1.1	1.4	0.9	—
Mexico (c)	1.5	3.3	1.8	1.4	2.0	0.7	0.8	0.5	0.4	0.0	0.3	0.9	-0.6
Chile	3.1	0.2	2.5	2.4	2.5	0.7	-0.6	0.5	0.2	2.0	-0.6	0.7	—
Colombia (c)	3.7	0.6	1.6	2.5	2.8	0.9	-0.5	-0.1	0.3	1.1	0.4	0.3	0.6
Peru	4.3	-0.6	3.0	2.6	2.3	-0.6	-0.3	-0.1	0.8	1.2	1.4	0.4	1.3
CPI (year-on-year rate) (a)													
Latin America and the Caribbean (b)	6.0	14.8	16.8	8.5	5.7	7.5	5.9	5.5	5.1	4.7	4.5	4.7	4.6
Argentina	25.5	133.5	229.8	62.7	31.8	102.0	113.0	125.9	172.8	273.5	278.7	234.2	154.4
Brazil	5.8	4.6	4.3	3.6	3.1	5.3	3.8	4.6	4.7	4.3	4.0	4.4	4.8
Mexico	4.4	5.5	4.7	3.8	3.0	7.5	5.7	4.6	4.4	4.6	4.8	5.0	4.5
Chile	3.9	7.6	3.9	4.2	3.1	11.8	8.7	5.6	4.6	4.0	4.1	4.5	4.5
Colombia	4.4	11.7	6.7	4.5	3.1	13.3	12.4	11.4	10.0	7.8	7.2	6.3	5.3
Peru	3.3	6.3	2.5	1.9	2.0	8.6	7.4	5.5	3.7	3.1	2.2	2.0	2.1
Budget balance (% of GDP) (a) (d)													
Latin America and the Caribbean (b)	-4.1	-5.1	-4.8	-4.1	-3.6	-4.5	-4.8	-5.3	-6.0	-6.2	-6.6	-6.4	—
Argentina	-3.8	-6.0	-0.1	0.2	0.9	-4.2	-4.3	-4.2	-5.9	-3.3	-1.5	-0.9	—
Brazil (e)	-5.5	-8.9	—	—	-6.9	-6.0	-6.3	-7.5	-8.8	-9.0	-9.8	-9.2	—
Mexico (e)	-3.1	-3.8	—	—	-2.7	-3.7	-4.2	-4.4	-3.8	-5.0	-5.1	-5.3	-5.5
Chile	-1.1	-2.4	-2.3	-1.4	-0.4	0.8	-1.8	-2.3	-2.4	-3.4	-3.6	-3.7	—
Colombia	-2.9	-3.3	-4.4	-3.8	-3.4	-4.9	-3.7	-3.4	-4.2	-4.6	-6.7	-7.0	—
Peru	-0.9	-3.5	-3.2	-2.0	-1.4	-2.8	-3.7	-3.5	-3.6	-4.1	-4.1	-4.5	-3.9
Public debt (% of GDP) (a)													
Latin America and the Caribbean (b)	57.5	73.9	69.4	69.8	69.7	63.6	63.4	63.2	65.9	65.0	67.2	66.5	—
Argentina	63.2	-	91.5	78.5	68.0	69.3	65.6	69.4	85.9	70.9	72.7	70.5	—
Brazil	73.3	84.7	87.6	92.0	94.7	81.7	83.3	81.1	84.0	84.5	87.6	84.9	—
Mexico (e)	49.0	53.1	—	—	57.8	48.6	47.9	48.7	47.4	49.4	51.0	53.1	53.4
Chile	19.8	39.4	41.0	41.6	41.4	38.0	38.3	38.8	39.4	39.5	39.3	39.7	—
Colombia	46.3	54.3	55.8	56.1	56.5	57.8	55.7	55.1	54.7	55.5	58.3	58.4	59.9
Peru	27.3	33.0	34.2	35.3	35.7	32.9	32.2	32.5	32.9	32.2	32.6	32.6	32.7
Current account balance (% of GDP) (a) (d)													
Latin America and the Caribbean (b)	-1.9	-1.1	-0.9	-1.1	-1.2	-2.6	-2.4	-1.8	-1.4	-1.2	-1.1	-1.1	—
Argentina	-0.9	-3.3	0.6	0.6	0.8	-1.3	-2.1	-2.5	-3.2	-2.4	-0.8	0.4	—
Brazil	-2.4	-1.4	-1.7	-1.8	-1.8	-2.3	-2.3	-1.6	-1.3	-1.2	-1.4	-2.1	—
Mexico	-1.2	-0.3	-0.7	-0.9	-1.0	-1.7	-1.4	-0.9	-0.3	-0.4	-0.4	-0.4	-0.3
Chile	-3.2	-3.5	-2.3	-2.7	-2.8	-7.0	-5.1	-4.1	-3.5	-3.7	-3.4	-2.7	—
Colombia	-3.9	-2.7	-2.5	-2.6	-2.8	-5.4	-4.7	-3.3	-2.3	-2.0	-1.8	-1.8	—
Peru	-2.4	0.6	0.3	-0.1	-0.6	-2.9	-1.6	-0.2	0.7	1.2	1.5	2.1	2.2
External debt (% of GDP) (a)													
Latin America and the Caribbean (b)	37.5	46.8	43.2	41.9	—	34.5	33.9	33.1	32.9	33.0	32.5	33.6	—
Argentina	41.5	44.5	—	—	—	42.8	42.7	43.6	44.4	46.9	47.4	46.4	—
Brazil	29.4	33.7	—	—	—	34.8	35.0	33.9	33.4	33.2	32.8	34.4	—
Mexico	13.5	12.0	—	—	—	13.6	12.3	11.4	11.3	11.7	11.1	12.3	12.5
Chile	56.8	71.8	—	—	—	74.3	72.2	70.3	71.8	73.5	75.4	78.7	—
Colombia	34.3	54.0	—	—	—	54.8	55.5	54.6	53.3	50.4	48.0	47.6	—
Peru	34.6	39.5	—	—	—	41.3	40.7	38.9	39.2	38.6	37.9	39.0	37.5
MEMORANDUM ITEMS: Aggregate of emerging market economies excluding Latin America and China (IMF, October 2024 WEO)													
GDP (year-on-year rate)	4.2	4.4	4.2	4.3	4.5								
CPI (year-on-year rate)	7.5	11.1	10.1	7.2	5.7								
Budget balance (% of GDP)	6.4	-4.4	-4.7	-4.5	-4.3								
Public debt (% of GDP)	42.9	58.4	58.6	60.0	60.9								
Current account balance (% of GDP)	0.7	0.6	0.1	-0.2	-0.3								
External debt (% of GDP)	27.5	27.1	27.0	26.5	—								
Share of global GDP, in PPP (%)	31.8	33.2	33.5	33.9	34.3								

SOURCES: IMF, LSEG Datastream, LatinFocus and national statistics.

a Latin America and the Caribbean account for 7.3% of global GDP measured in PPP. The six economies shown account for 84% all Latin America and the Caribbean (IMF).
b Quarterly data, aggregate of the six main economies (Argentina, Brazil, Chile, Colombia, Mexico and Peru), and for inflation, aggregate excluding Argentina.
c Seasonally adjusted series.
d 4-quarter moving average.
e Annual IMF forecasts are not shown since they are not comparable with quarterly data from national sources.

Figure 2

Recent developments in the Latin American banking systems and risks to financial stability according to the region's central banks

BRAZIL

Political/geographical risk

Heightened geopolitical tensions in the Middle East could generate inflationary pressures due to oil price rises. Climate transition risks encompass multiple factors, such as regulatory changes, shifting consumption patterns and the impact on technological innovation.

Credit risk

High household indebtedness and corporate leverage reduces households' and firms' ability to pay, especially in the face of rising interest rates.
Possible reduction in the flow of funding through funds investing in corporate debt if these become less attractive. This would raise the cost of financing for firms through debt issuance.

International risk

A less favourable global environment could lead to abrupt financial asset price movements, despite recent improvements in financial conditions.

Resilience of the financial and fiscal system

High public debt (and its foreseeable upward momentum) are the main source of risk to financial stability. Deteriorating government deficits could lead to interest rate increases and exchange rate movements affecting financial institutions' balance sheets.
As financial services become more digitalised, operational risks linked to fraud and cyber attacks increase.

CHILE

Political/geographical risk

Growing geopolitical tensions due to wars and deglobalisation. Trade restrictions and supply chain disruptions could increase, putting upward pressure on global inflation and global interest rates.

Credit risk

The banking system should continue efforts to manage the rising credit risk in the loan portfolio and to prepare for full convergence to Basel III.

International risk

Possible abrupt changes in asset value. High asset prices could be subject to fluctuations in response to risk appetite changes in the international markets.
In addition, international tensions could lead to the repatriation of capital as countries face new defence spending needs amid heightened global risk aversion.
In addition, the limited depth of the financial markets by historical standards increases exposure to global developments affecting financial prices.

Resilience of the financial and fiscal system

Upward pressure from long-term interest rates, driven by high national and global indebtedness, and growing financing needs for structural expenditures such as climate transition investment.

COLOMBIA

Credit risk

Potential deterioration in banks' profitability, which have increased their provisioning level. The aim was to improve solvency in the face of higher levels of non-performing loans compared with the last five years, although these have improved since early 2024.

Resilience of the financial and fiscal system

Increased exposure to market risk due to a decline in asset value arising from greater volatility.
Fiscal uncertainty amid financial institutions' increased exposure to government debt, and international markets' greater sensitivity to a weaker economic outlook.

Foreign exchange risk

High global indebtedness and heightened uncertainty due to the change of government in the United States and the escalating wars give rise to increased volatility in asset and some commodity markets, which in the face of an appreciation of the dollar would lead to a depreciation of Latin American currencies.

SOURCE: Banco de España.

Figure 2

Recent developments in the Latin American banking systems and risks to financial stability according to the region's central banks (cont'd)

PERU

Political/geographical risk

Potential bouts of uncertainty, which could impair the growth outlook for consumption and private investment. However, the economy is showing a gradual recovery and improved business confidence indicators.

Credit risk

Credit remains sluggish owing to weak demand.
Consumer lending has declined as credit standards tightened on account of higher credit risk and households' lower financing needs following withdrawals from pension funds.
Weak lending to SMEs owing to low private investment growth and tighter lending standards, although this has been partially offset by the loans provided through the Impulso Perú (MYPERÚ) programme, which provides State guarantees for loans to SMEs.

International risk

A high level of uncertainty remains due to the new US Administration's policies and the weaker growth prospects of major economies such as China and Germany, which could lower commodity prices.

Foreign exchange risk

A looser fiscal policy by the new US Administration could moderate the Federal Reserve's interest rate cuts, generating higher volatility in the international financial markets, with potential capital outflows from emerging market economies and exchange rate depreciations.

MEXICO

Political/geographical risk

Risks related to more frequent extreme weather events, such as hurricanes, flooding and droughts.
Increased national political uncertainty, coupled with a deterioration in perceived security in the country.

Credit risk

A greater slowdown than expected in the domestic economy, which would entail greater credit risk due to debtors' lower ability to pay. Risks to consumer credit would increase owing to weaker employment growth in the United States and a concomitant fall in remittances.

International risk

Escalating international tensions and trade disputes, with an impact on non-performing loans. Trade tensions could significantly affect sectors strongly geared to exports. In turn, a more volatile macro-financial environment would entail rising financing costs.

Resilience of the financial and fiscal system

Factors conducive to a downward revision of Mexico's credit rating may emerge, such as those concerning the institutional and governance framework, limited long-term economic growth and fiscal risks related to Pemex's contingent liabilities and growing budget rigidities.

Foreign exchange risk

Economic policy changes in the United States.

SOURCE: Banco de España.

Box 1

THE EU-MERCOSUR AGREEMENT

Juan Carlos Berganza, Rodolfo G. Campos and Jacopo Timini

In December 2024, the European Union (EU) and the Mercosur countries (Argentina, Brazil, Paraguay and Uruguay) reached a partnership agreement (which is yet to be ratified) to boost trade, political and cooperation ties between the two regions. In Mercosur, the trade agreement will take effect in each member country once it is approved by its Parliament or Congress. In the EU, the process is more complex. Given the division of powers between European and national institutions, a two-tiered approval process is required for the agreement to come into force. The part of the agreement that deals with strictly trade-related issues (lower tariffs and changes to certain non-tariff barriers) needs to be ratified by the Council of the EU (with the support of at least 15 of the 27 Member States representing 65% of the EU population) and by the European Parliament. Additionally, the Member States must approve the parts of the agreement affecting national competences in areas related to fiscal, labour, environmental and foreign investment policy, as these require parliamentary ratification to ensure compliance with each country's laws and regulations.

If it comes into force, the EU-Mercosur agreement will create an integrated market of more than 770 million people with a combined GDP of €18 trillion (around 25% of world GDP).[1] The EU will thus have trade agreements with all Latin American countries except Bolivia, Cuba and Venezuela – more than the United States or China. This would give the EU preferential access to markets representing 95% of the region's GDP, significantly expanding its presence beyond that of other global players.[2]

The agreement would make trade between two areas with strong economic ties even easier. Mercosur is an important partner for a number of EU countries – including Spain – from the standpoint of both trade and financial transactions. For example, around one-third of the EU's trade with Latin America is conducted with Mercosur countries which, in turn, account for 2% of the EU's total exports and imports outside the bloc (Chart 1). However, in some sectors, such as food and commodities, Mercosur countries represent 13% and 14%, respectively, of extra-EU imports. Having Mercosur as a trading partner would also help EU countries reduce economic vulnerabilities stemming from geopolitical factors.[3] This could be achieved, for example, by further diversifying global value chains – particularly those including critical raw materials for the digital transition and the transition to a lower-emissions economy –[4] and by reducing uncertainty regarding compliance with multilateral trade rules and those of its institutions. The EU is also one of Mercosur's main trading partners, as it accounts for between one-sixth and one-fifth of its exports and imports outside the bloc (Chart 2).

Bilateral trade relations between the EU and Mercosur are currently subject to the most-favoured-nation tariff. This tariff is decided on a product-by-product basis but applied indiscriminately to all World Trade Organization members. In 2023 the average tariff levied by the EU was 5%, while that levied by Mercosur was more than double that figure (around 11%). Tariffs for specific products may be much higher. For example, Mercosur imposes tariffs of between 14% and 35% on manufacturing imports such as car parts, machinery, chemical products, pharmaceuticals, textiles and footwear. On foodstuffs, such as dairy products, chocolate and confectionery, spirits and wines, they may range between 20% and 35%.

The EU-Mercosur agreement would gradually remove tariffs on over 90% of the products traded between the two regions. For most products, trade will be liberalised over a period of up to ten years. For some more sensitive products, such as beef, poultry meat and rice, a partial liberalisation will be applied. This means that the existing

1 In this integrated market, the EU would account for 63% of the population and 86% of GDP, while Mercosur would account for 37% of the population and 14% of GDP.

2 The United States has agreements with the same countries as the EU, except the Mercosur countries, Ecuador and a number of Caribbean countries. By contrast, China only has trade agreements with five countries in the region: Chile, Costa Rica, Ecuador, Nicaragua and Peru. For a comparison of the trade agreements with Latin America concluded by the EU, the United States and China, see Juan Carlos Berganza, Rodolfo G. Campos, Antoni Estevadeordal, Ernesto Talvi and Jacopo Timini. (2025). "EU-MERCOSUR: a platform for a new era of transatlantic (and intra-regional Latin American) integration?". Real Instituto Elcano.

3 Demosthenes Ioannou and Javier J. Pérez (eds.). (2023). "The EU's Open Strategic Autonomy from a central banking perspective", Occasional Paper Series No 311, European Central Bank; and Maria Grazia Attinasi et al. (2024). "Navigating a fragmenting global trading system: insights for central banks". Occasional Paper Series No 365, European Central Bank.

4 Rodolfo G. Campos, Marta Suárez-Varela and Jacopo Timini. (2022). "The EU-Mercosur trade agreement and its impact on CO_2 emissions". *Economic Bulletin - Banco de España,* 1/2022, Analytical Articles.

Box 1
THE EU-MERCOSUR AGREEMENT (cont'd)

tariffs will be reduced, rather than removed, for a specific quota of imports, which has been set at levels close to current trade volumes. For imports exceeding this quota, the existing tariffs will still apply. Moreover, in these cases the liberalisation period may be extended to up to 15 years.

The agreement would also reduce non-tariff barriers in various key areas. These include sanitary and phytosanitary barriers, technical barriers to trade (i.e. the rules and regulations used by countries to ensure products meet certain standards),[5] restrictions on access to public tenders and limits to trade in services. Moreover, the agreement protects more than 350 European and 220 Mercosur geographical indications for foodstuffs whose qualities are specifically linked to the area of production. The aim is to strengthen trade in high-quality products of controlled origin.

This agreement is one of the most ambitious worldwide in terms of environmental sustainability and labour standards. It includes express obligations to combat climate change and deforestation, based on the Paris Agreement commitments, and ensures respect for labour rights following the International Labour Organisation's recommendations and good practices.

Chart 1
Composition of extra-EU trade, 2023

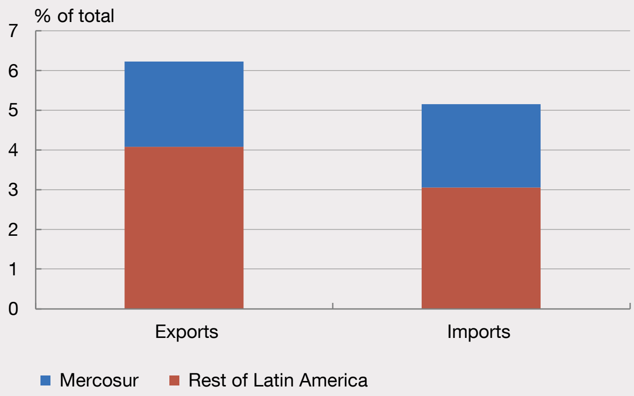


Chart 2
Composition of extra-Mercosur trade, 2023

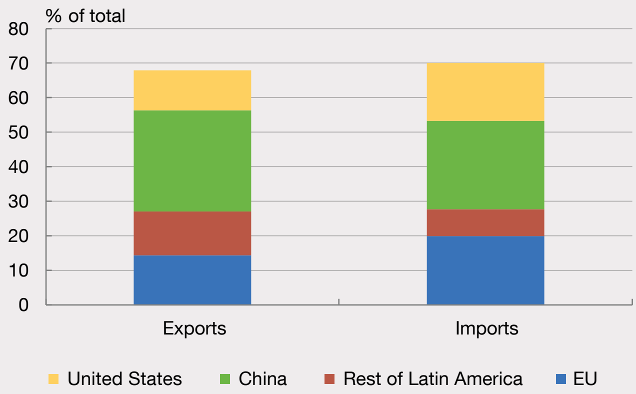


Chart 3
Impact of the agreement on Mercosur trade

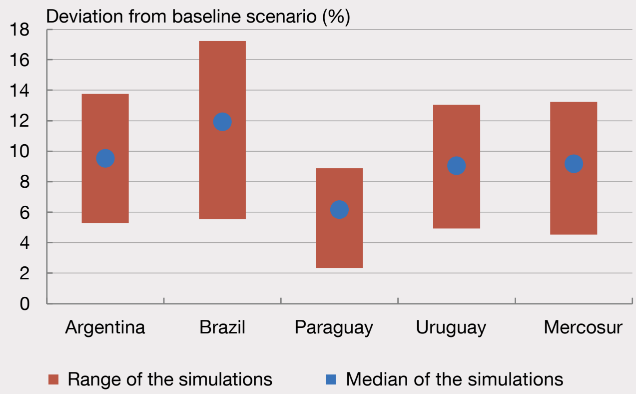
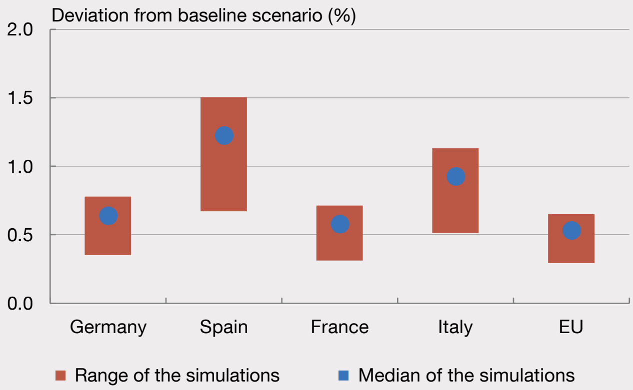


Chart 4
Impact of the agreement on EU trade



SOURCES: UN Comtrade and Banco de España.
NOTES: The range and median of the simulations have been calculated drawing on the results in Jacopo Timini and Francesca Viani. (2022). "A highway across the Atlantic? Trade and welfare effects of the EU-Mercosur agreement". *International Economics*, 169, pp. 291-308;. The averages for the two regions, labelled "Mercosur" and "EU", are the simple averages of the effects calculated for each country in each region. See also Juan Carlos Berganza, Rodolfo G. Campos, Antoni Estevadeordal, Ernesto Talvi and Jacopo Timini, "EU-MERCOSUR: a platform for a new era of transatlantic (and intra-regional Latin American) integration?". Real Instituto Elcano.

5 World Trade Organisation. (2024). Agreement on Technical Barriers to Trade.

Box 1
THE EU-MERCOSUR AGREEMENT (cont'd)

Entry into force of the EU-Mercosur agreement would increase trade between the two areas by over a third in the long run, according to Banco de España studies.[6] Given that the EU accounts for a greater share of Mercosur trade, the effects would be more significant for the latter: total trade is expected to increase by between 5% and 13% for Mercosur (Chart 3) and by between 0.3% and 0.7% for the EU. Trade flow gains for Spain could be twice the EU average (Chart 4), reflecting the higher weight of Mercosur in Spain's trade flows compared with those of the rest of the EU.[7] These estimates do not consider other potential benefits, such as access to advanced technologies, stronger global value chains and increased investment. Nor have potential short-term adverse effects (such as job losses in some of the sectors most exposed to greater international competition) been taken into account.[8]

6 Jacopo Timini and Francesca Viani. (2020). "The EU-Mercosur free trade agreement: main features and economic impact". *Economic Bulletin - Banco de España,* 1/2020, Analytical Articles; Jacopo Timini and Francesca Viani. (2022). "A highway across the Atlantic? Trade and welfare effects of the EU-Mercosur agreement". *International Economics,* 169, pp. 291-308; Juan Carlos Berganza, Rodolfo G. Campos, Antoni Estevadeordal, Ernesto Talvi and Jacopo Timini. (2025). "EU-MERCOSUR: a platform for a new era of transatlantic (and intra-regional Latin American) integration?". Real Instituto Elcano. These studies analyse the 2019 agreement, which was updated in 2024. However, most of the changes are concentrated in areas that should not affect the long-term estimates presented in this box. The changes relate to environmental issues (the Paris Agreement), institutional issues (the existence of a dispute settlement mechanism) and the calendar for tariff reductions.

7 For more information about the trade flows between the EU, Spain and the main Mercosur countries, see the macro-financial indicators for Argentina and Brazil.

8 In the type of models considered, labour supply is inelastic.

Box 2

EFFECTS OF DOMESTIC AND FOREIGN MONETARY POLICIES ON BANK LENDING IN CENTRAL AMERICA AND THE DOMINICAN REPUBLIC

María Alejandra Amado, Juan Carlos Berganza and Luis Ortiz Cevallos[1]

This box analyses the impact of domestic and foreign monetary policies on bank lending in Central America and the Dominican Republic (CADR). According to the economic literature,[2] the monetary policy of the US Federal Reserve and other reference economies can have a direct impact on lending by banks in other economies, especially when these are small, open and highly integrated with the US economy, as is the case of the CADR countries.

The magnitude of this effect is influenced by the shift in bank ownership in Central America. Foreign capital banks,[3] notably those from Colombia and, to a lesser extent, Central America (in particular from Honduras and Nicaragua), have increased their presence in the region, chiefly through subsidiaries and branches,[4] since the 2008 financial crisis. These banks have progressively acquired US financial institutions and consolidated their role in the Central American credit market. As Chart 1 shows, Colombian banks have a share of over 50% of the credit market in El Salvador, while their share in other Central American countries ranges between 17% and 29%. Moreover, foreign (non-Colombian) capital banks, particularly Honduran banks, have a significant share of loans in El Salvador and Nicaragua.

In this setting, a dynamic panel data model[5] is used to estimate the impact of domestic and foreign monetary policies on lending in the region. In this model, the volume of credit granted by a bank in a given quarter that operates in one of the six CADR countries is explained by lending in the previous period and by monetary policy shocks. At international level, lending by banks in the region is affected by monetary policies in the United States and Colombia,[6] which are proxied through Taylor rules. Meanwhile, at domestic level, the regime set out in the monetary policy reports of each country in the region is used: in the case of Costa Rica, Guatemala and the Dominican Republic, the central banks indicate having an inflation-targeting regime, and consequently the shocks of their policies are also proxied through a Taylor rule. By contrast, in the case of Honduras, its central bank indicates that it has a managed devaluation regime, and therefore its monetary policy shocks are inferred by drawing on the residuals of an estimation of an exchange rate rule.[7] Lastly, no variables for monetary policy are included in the model in the case of El Salvador and Nicaragua.[8]

The main results of this exercise, shown in Chart 2, are set out below.

— An increase of 1 percentage point (pp) in the Federal Reserve's policy rate reduces the volume of lending on average by 0.3 pp, with a similar decline being observed across all banks, irrespective of the origin of their capital.

— An increase in Colombia's policy rate would have a positive impact on lending by Colombian bank subsidiaries and branches in the region. This may be attributable to the geographical diversification of their

1 Luis Ortiz Cevallos belongs to the Executive Secretariat of the Central American Monetary Council (SECMCA).

2 Falk Bräuning and Victoria Ivashina. (2020). "U.S. monetary policy and emerging market credit cycles". *Journal of Monetary Economics,* Vol. 112, pp. 57-76. Also, Bernardo Morais, José-Luis Peydró, Jessica Roldán-Peña and Claudia Ruiz-Ortega. (2019). "The International Bank Lending Channel of Monetary Policy Rates and QE: Credit Supply, Reach-for-Yield, and Real Effects". *The Journal of Finance,* Vol. 74(1), pp. 55-90.

3 See the macro-financial indicators, where the banking structure of these countries is described in more detail.

4 A bank is classified as a subsidiary or a branch depending on its relationship with the parent entity. The branch model is often used by banks with a more centralised structure, where decisions are taken at the parent. Subsidiaries are present in more decentralised models, in which the banks are aligned with the local environment, from both a business and a regulatory perspective. Centralised models are generally associated with banks that have a strong weight in investment banking, where wholesale funding predominates and there are significant intragroup positions (i.e. the parent directly funds a large portion of local activities). Decentralised models are typically used by banks with retail business, which are funded by deposits and have few intragroup positions (i.e. local activities are funded with local resources).

5 This model is similar to that used to calculate this same effect on the main inflation-targeting Latin American economies. See Banco de España. (2024). "Box 4. Impact on bank lending of monetary policies in the region and worldwide". *Report on the Latin American economy. First half of 2024.* pp. 39-42.

6 The econometric model considers the effects of Colombia's monetary policy only on lending by Colombian bank subsidiaries and branches. This is because Colombia is a small economy and CADR exchange rate regimes are not related to its currency. In addition, the Colombian currency does not play the same role in the international monetary system as the dollar.

7 This rule entails defining the change in the exchange rate based on exchange rate lags, the inflation differential and output. Such a rule is used by the International Monetary Fund in its Article IV Report for Honduras.

8 El Salvador is a dollarised economy, and Nicaragua has a high dollarisation of credit, exceeding 95% of bank lending.

Box 2

EFFECTS OF DOMESTIC AND FOREIGN MONETARY POLICIES ON BANK LENDING IN CENTRAL AMERICA AND THE DOMINICAN REPUBLIC (cont'd)

business model. Indeed, when a contractionary monetary policy in their country of origin reduces lending, and this adjustment is not linked to global or regional financial conditions, these banks offset the decrease in lending by increasing their loans in Central America as a way to stabilise profitability. As a result, Colombian banks have a high exposure to Central America, which is why in a recent Article IV report on Colombia the International Monetary Fund urges continuing the monitoring of cross-border risk and strengthening it with regional stress-testing exercises and information sharing with regional supervisors.[9]

— As regards the effect of a 1 pp hike in the policy rate in inflation-targeting CADR countries, the central estimate indicates that lending would contract by roughly 0.1 pp, but this is not statistically significant. However, in the specific case of Colombian banks, there is an additional contraction of 1.1 pp, which may be explained by the characteristics of Costa Rica's banking market, where the credit portfolio of Colombian banks, unlike those of other foreign capital banks, is less concentrated in consumer loans (whose interest rates do not appear to be affected by the policy rate).[10] Furthermore, in Costa Rica the

Chart 1
Composition of loans by home country of bank

Chart 1.a
Costa Rica

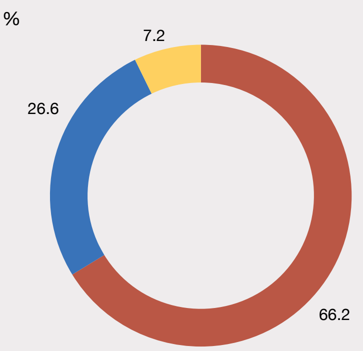


Chart 1.b
El Salvador

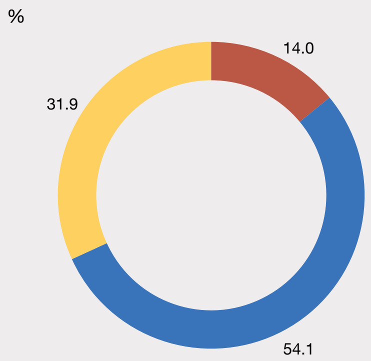


Chart 1.c
Guatemala

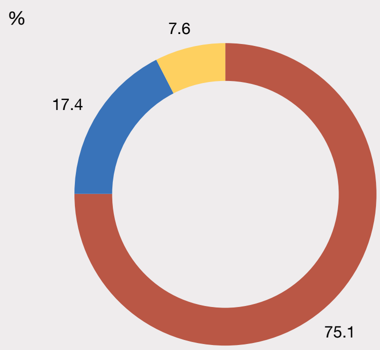


Chart 1.d
Honduras

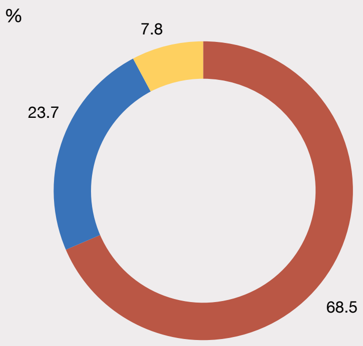


Chart 1.e
Nicaragua

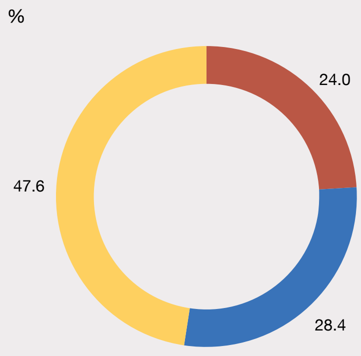
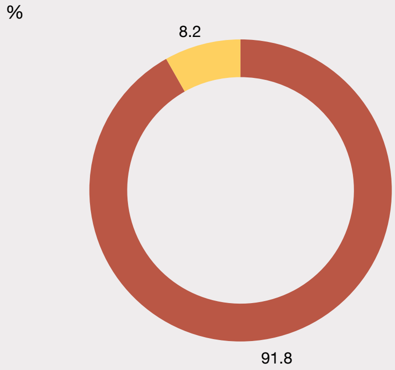


Chart 1.f
Dominican Republic



Local banks Colombian banks Other foreign capital private banks

SOURCE: Monetary and supervisory authorities in Central America and the Dominican Republic.

9 Banco de la República. (2024). *Reporte de Estabilidad Financiera. I semestre de 2024*.

10 Banco Central de Costa Rica. (2025). "Recuadro 2. Transmisión de la tasa de política monetaria a las tasas activas en Costa Rica, 2018-2024". *Informe de Política Monetaria. Enero 2025.*

Box 2

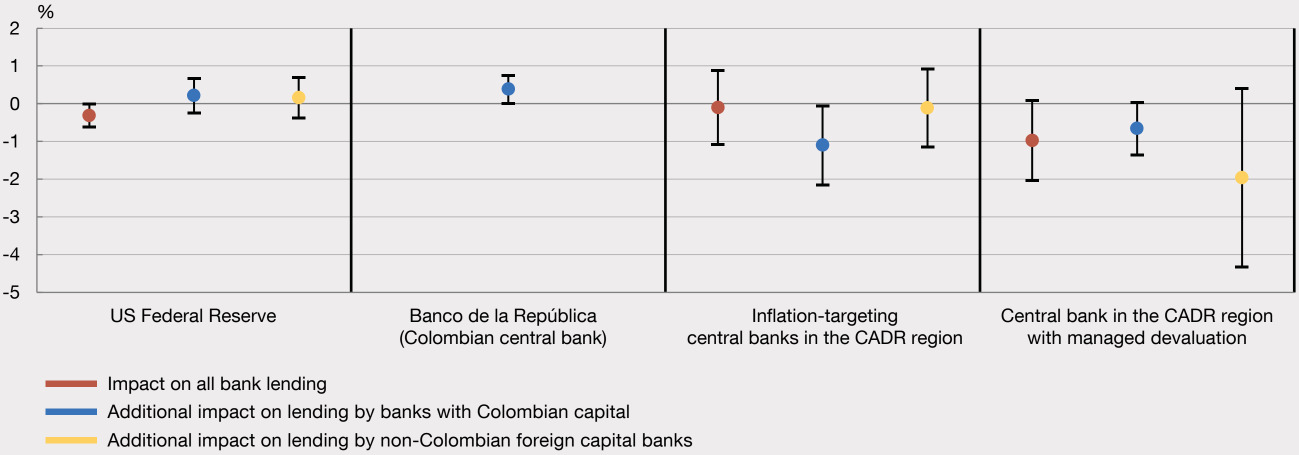
EFFECTS OF DOMESTIC AND FOREIGN MONETARY POLICIES ON BANK LENDING IN CENTRAL AMERICA AND THE DOMINICAN REPUBLIC (cont'd)

Colombian banks compete in a market dominated by State-owned banks, which are the only banks whose deposits are fully guaranteed. This means that Colombian banks have to be cautious when managing their liquidity,[11] by maintaining a sound financial position against a backdrop of tight domestic monetary conditions, which limits their ability to lend.[12]

— Lastly, in the case of Honduras, which has a managed devaluation regime, an unexpected increase (unexpected depreciation) in its exchange rate drives up the local interest rate, which reduces demand for credit. Indeed, as banks extend export credit lines, they tend to grant loans whose interest rates are indexed to exchange rates and which thus respond immediately to dollar price fluctuations.

Chart 2

Impact on the stock of bank loans of an increase of 1 pp in policy rates nationally and internationally and of a 1% depreciation in the exchange rate (a)



SOURCE: SECMCA, drawing on data from the monetary and supervisory authorities in Central America and the Dominican Republic.

a The coloured dots denote the estimated impact on bank lending in the CADR region of increases of 1 pp in the policy rates of the US Federal Reserve, the Banco de la República (Colombian central bank) and the inflation-targeting central banks in the region, such as those of Costa Rica, Guatemala and the Dominican Republic. In the case of Honduras (which has a managed devaluation regime), they denote the impact of a 1% depreciation in the exchange rate against the dollar. The lines denote a 90% confidence interval.

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11 According to the Banco Central de Costa Rica, monetary policy interest rates pass through more forcefully to interest rates on credit extended by private banks than they do to rates on credit extended by State-owned banks. See Banco Central de Costa Rica. (2025). "Recuadro 2. Transmisión de la tasa de política monetaria a las tasas activas en Costa Rica, 2018-2024". *Informe de Política Monetaria. Enero 2025.*

12 Douglas W. Diamond and Raghuram G. Rajan. (2001). "Liquidity Risk, Liquidity Creation, and Financial Fragility: A Theory of Banking". *Journal of Political Economy,* Vol. 109(2), pp. 287-327.

ACRONYMS AND ABBREVIATIONS

ARS	Argentine peso
CADR	Central American and the Dominican Republic
CEPII-BACI	International trade database of the Centre d'Études Prospectives et d'Informations Internationales
CMN	National Monetary Council (Brazil)
DOTS	Direction of Trade Statistics
ECB	European Central Bank
EMAE	Monthly estimator of economic activity
EPU	Economic policy uncertainty
EU	European Union
GDP	Gross domestic product
GTAP	Global Trade Analysis Project
HS	Harmonised system
IIF	Institute of International Finance
IMF	International Monetary Fund
LSEG	London Stock Exchange Group
Mercosur	Mercosur Mercado Común del Sur (Southern Common Market)
NiGEM	National Institute Global Econometric Model
PPP	Purchasing power parity
ROC curve	Receiver operating characteristic curve
SECMCA	Executive Secretariat of the Central American Monetary Council
UN	United Nations
USD	US dollar
VAR	Vector Autoregressive Model
WEO	World Economic Outlook

bn	Billion
bp	Basis points
pp	Percentage points
H	Half
Q	Quarter
Q-o-q	Quarter-on-quarter
Y-o-y	Year-on-year

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