Latin American Country Risk—An Update

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Widespread and growing trade conflicts--a world-wide development--has deflected attention away from foreign direct investment, a $1.3 trillion enterprise. Latin America is no exception. And while trade flows—imports and exports—may ebb and flow, foreign direct investment is the "long game". Recognizably, it is also an economic activity that produces these tradable products, be they manufactured goods, agricultural and natural resource products, or services.

Collecting and analyzing data on foreign direct investment and country risk, the Adam Smith Center for Economic Freedom at Florida International University recently published *The Latin America Country Risk Index and Analysis*, a comprehensive study that evaluates the political, economic, social, and international risk factors in Argentina, Brazil, Chile, Colombia, El Salvador, and Mexico. Center researchers Erich de la Fuente, Eduardo Gamarra and Sary Levy carried out a comprehensive study in which 427 respondents were asked to assess the risk level when considering whether they would recommend investing in their own country based on their assessment of the risk factors.

The study's findings reveal that while each Latin American country faces distinct challenges, there are common regional risks. The primary social risk identified is the threat of organized crime, with transnational criminal entities expanding geographically and exerting influence over government and business structures. This escalation is associated with high crime rates in most countries. Additionally, political polarization and low trust in political parties, politicians, and most institutions are the principal political risks across the region. Economic risks differ by country; however, high unemployment and inflation are common issues. Although international risk factors are lower, China's growing influence in key economic sectors raises concerns. Experts also caution that U.S.-China tensions may pose challenges for Latin American countries with strong economic ties to both superpowers.

The table below summarizes the main regional risks, in general:

Main Regional Risks

POLITICAL RISKS	ECONOMIC RISKS	SOCIAL RISKS	INTERNATIONAL RISKS
Polarization across the political landscape	High inflation	Organized crime's expansion and influence	China's influence in key economic sectors
Low trust in political parties and politicians	High unemployment	Elevated crime levels	Tensions in U.S.–China relations
Low trust in institutions/corruption	Slow economic growth/challenging investment climate	Social unrest/unions and activist groups engaging in demonstrations or strikes	Adverse effects caused by climate change

Source: Adam Smith Center for Economic Freedom

For those engaged in cross-border trade, finance and investment, assessing the region's main economic risks is paramount for decision-making. The study reports that high unemployment is perceived as a significant risk throughout the year in all countries, with impacts that can affect impact poverty rates and widen socioeconomic inequality in what is already the world's most unequal region. High inflation has been prevalent across Latin America, eroding purchasing power and creating uncertainty for businesses and consumers. In some countries, fiscal imbalances and elevated public debt have also exacerbated the situation. Slow economic growth and a challenging investment climate, in general, were identified as other risk factors.

Examining a subset of countries that account for 85% of Latin America's GDP—Argentina, Brazil, Colombia and Mexico—the findings are illuminating.

In **Argentina,** experts perceived the lowest annual level of risk when considering investing in the country compared to Brazil, Colombia and Mexico. The explanation here is that respondents are optimistic that President Javier Milei's policies could stimulate the economy and attract foreign investment. Many experts believe that economic pain in the general economy is to be expected as the country recovers from years of fiscal mismanagement, astronomical inflation, and uncontrolled government spending.

Colombia has the second-lowest level of investment risk even though overall the country has a significantly higher annual country risk level. There are great concerns regarding President Petro's economic and regulatory policies, especially within the business sector. However, initial fears about the country's political instability have subsided. With the judicial branch retaining independence and elections in less than two years, experts are cautiously optimistic about investing in the country. Nevertheless, foreign firms such as Canada's Frontera Energy expect to expand their activities throughout the country.

Results from **Mexico** are counter-intuitive, as there is heightened concern about the investment climate. As such the country manifests a high investment risk level. Foreign firms in particular have displayed a good degree of pessimism with the ruling Morena party winning reelection, state institutions losing independence, and a controversial judicial reform to elect judges by popular vote, raising doubt about legal certainties for investors.

Investment in **Brazil** is a bright spot. The Brazilian economy remained the largest in Latin America and relatively stable. Nevertheless, experts perceived President Lula da Silva's administration as lacking fiscal discipline and market friendliness, causing uncertainty among investors and weakening the currency value. Rating momentum for Brazilian corporates could turn sharply negative in 2025 if interest

rates continue to climb, according to Fitch Ratings. Be that as it may, many U.S. companies are expanding into Brazil, including Chevron, Ford, General Motors, Apple, and Megaport. Steel group ArcelorMittal announced on early February an investment of about 4 billion reais ($700 million) to launch a new product line at its Tubarão unit in Brazil's Espírito Santo state.

In sum, despite a slew of challenges in the aforementioned countries, respondents were optimistic for medium-to-long-term improvement, contingent on necessary economic reforms amid political polarization and gridlock.

In the words of Luciano Macagno, Delta Air Lines managing director for the region: *"Latin America continues to demonstrate its resilience and potential, attracting significant international investment across various sectors. It's inspiring to see major companies committing to the region, creating jobs, and driving economic growth. Beyond energy, technology, and agriculture, we are also highly optimistic about the tourism industry, which remains a powerful engine for development."*

What all can agree on is that private sector investments will be needed to spark economic growth. However, countries must enhance regulatory certainty and reform to alleviate complex bureaucratic systems and create an attractive environment for large-scale investments, especially in energy, technology, agriculture, and extractive industries.

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