

INTERNATIONAL MONETARY FUND

REGIONAL ECONOMIC OUTLOOK

WESTERN HEMISPHERE

Turning Tailwinds into Lasting
Gains

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The report includes two chapters and one online annex. Chapter 1, “Turning Tailwinds into Lasting Gains,” was prepared by Germán Villegas Bauer (co-lead), Yuanchen Yang (co-lead), and Genevieve Lindow. Contributions for boxes were provided by Enrico Di Gregorio, Justin Matz, and Jongsoon Shin, with data support from Junghwan Mok, Spencer Siegel, and Frank Tao (Box 1.1); Alina Carare and Juan Pablo Celis, with research analysis from Manuel Escobar and Radostin Ivanov, and useful edits and suggestions from Metodij Hadzi-Vaskov and Central America 4 country teams (Box 1.2); and Francisco Arizala and Camila Casas (Box 1.3). Chapter 2, “The Missing Link: From Foreign Direct Investment to Trade and Productivity Gains,” was prepared by Robin Koepke (lead), Olusegun A. Akanbi, Eric Huang, and Nicolás Gómez Parra, with thanks to colleagues across IMF departments, the US International Trade Commission, and the World Bank for helpful comments and input.

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Country Groupings

Country Groups

Caribbean: Commodity Exporters (CARCE)	Caribbean: Non-Tourism Dependent (CARNT)	Caribbean: Tourism Dependent (CARTD)	Central America, Panama, and the Dominican Republic (CAPDR)	Central America 4	Eastern Caribbean Currency Union (ECCU)	Latin America 5 (LA5)	Latin America 7 (LA7)	Latin America 8 (LA8)	South America (SA)
Guyana Suriname Trinidad and Tobago	Guyana Haiti Suriname Trinidad and Tobago	Antigua and Barbuda Aruba The Bahamas Barbados Belize Dominica Grenada Jamaica St. Kitts and Nevis St. Lucia St. Vincent and the Grenadines	Costa Rica Dominican Republic El Salvador Guatemala Honduras Nicaragua Panama	El Salvador Guatemala Honduras Nicaragua	Anguilla Antigua and Barbuda Dominica Grenada Montserrat St. Kitts and Nevis St. Lucia St. Vincent and the Grenadines	Brazil Chile Colombia Mexico Peru	Brazil Chile Colombia Mexico Paraguay Peru Uruguay	Argentina Brazil Chile Colombia Mexico Paraguay Peru Uruguay	Argentina Bolivia Brazil Chile Colombia Ecuador Paraguay Peru Uruguay Venezuela

List of Country Abbreviations

ATG	Antigua and Barbuda	GUY	Guyana
ARG	Argentina	HTI	Haiti
ABW	Aruba	HND	Honduras
BHS	The Bahamas	JAM	Jamaica
BRB	Barbados	MEX	Mexico
BLZ	Belize	NIC	Nicaragua
BOL	Bolivia	PAN	Panama
BRA	Brazil	PRY	Paraguay
CAN	Canada	PER	Peru
CHL	Chile	PRI	Puerto Rico
COL	Colombia	KNA	St. Kitts and Nevis
CRI	Costa Rica	LCA	St. Lucia
DMA	Dominica	VCT	St. Vincent and the Grenadines
DOM	Dominican Republic	SUR	Suriname
ECU	Ecuador	TTO	Trinidad and Tobago
SLV	El Salvador	USA	United States
GRD	Grenada	URY	Uruguay
GTM	Guatemala	VEN	Venezuela

1. Turning Tailwinds into Lasting Gains¹

Growth and job creation have continued at a steady pace across the Western Hemisphere despite a series of global shocks. External tailwinds—including strong US demand, high commodity prices, supportive financial conditions, and robust tourism and remittances—have helped sustain activity across much of the region, offsetting drags from tariffs, trade uncertainty, and changes in immigration policies. These tailwinds are supporting the near-term outlook, but they are not able to resolve the region’s fundamental challenges of high public debt and weak productivity growth.

In the United States, robust household consumption and an upswing in technology-related investment are boosting both near-term demand and labor productivity, creating positive outward spillovers to trading partners. In Canada and Mexico, however, uncertainty about future prospects—most notably, potential changes to the trading relationship with the United States—is weighing on corporate investment, amplifying the effects of long-standing structural constraints and domestic policy uncertainties, respectively. Despite these trade uncertainties, Mexico is benefiting from the upswing in demand for electronics in the United States.

In most of South America, favorable energy, mineral, and grain prices, the reshaping of global trade relationships, and the region’s limited exposure to geopolitical conflicts are supporting inward investment and activity. In some countries, these positive dynamics are interacting with improving policy frameworks to further boost growth and lessen vulnerabilities. Much of the Caribbean is benefiting from strong tourism demand, which is fortuitously helping to offset the negative effects of higher fuel and food import costs. In Central America, robust domestic demand, energized by high levels of remittance inflows and a reduction in violent crime in some countries, is allowing growth rates to remain strong.

Looking forward, continued high commodity prices, relatively supportive financial conditions, still-elevated remittance inflows, and solid global demand—including for tourism—are expected to sustain favorable near-term dynamics in the region. However, these supportive conditions should be viewed as a window of opportunity rather than a source of permanently higher growth. Growth in the region is expected to pick up slightly in 2027–28, with risks tilted to the downside. The region’s comparative advantage in energy, food, and other commodities, together with its relatively limited exposure to global geopolitical risks, should continue to attract international capital and support investment. At the same time, shifts in global trade patterns could increasingly expose domestic manufacturing to greater competition from imported goods.

Fiscal and monetary policy settings are expected to be broadly neutral in the near term in most countries, and inflation is generally expected to return to target by the end of 2027 as supply shocks—largely from tariffs and energy prices—dissipate. The strength and credibility of monetary institutions across the region will continue to be an asset in anchoring inflation expectations and mitigating the impact of external shocks, the latter also being supported by the demonstrated willingness to allow exchange rates to adjust. However, the limited progress in decisively lowering public debt in many countries—including in some of the largest economies—will curtail the policy space that may be needed to react to a more challenging global backdrop. Mitigating this vulnerability will require concerted efforts and difficult trade-offs among tax and spending priorities. In addition, there is important scope to strengthen fiscal institutions in the region, which would help guide policy and enhance the credibility of efforts to reduce public debt.

Taking advantage of the current supportive conjuncture will also require tackling the region’s persistent weakness in productivity. As demographic shifts lead to slower labor force growth and rising dependency ratios, productivity will become increasingly important for sustaining improvements in living standards. At the same time, continued strong US productivity growth—spurred by new technologies diffusing through the economy—risks widening the region’s relative income and productivity gaps. Raising potential growth will require decisive efforts to remove supply-side constraints and create a more favorable environment for investment, formal employment, innovation, and the adoption of new technologies.

¹ Prepared by Germán Villegas Bauer (co-lead), Yuanchen Yang (co-lead), and Genevieve Lindow.

Key Features of the Conjuncture

Activity in the Western Hemisphere Has Remained Resilient in the Face of Global Shocks

Growth across the Western Hemisphere has generally held up well over the past couple of years (Figure 1.1, panel 1). Despite having to confront major shocks from policy uncertainty, tariffs, and swings in commodity prices, the region was able to grow at 2.4 percent in 2025, somewhat slower than in 2024, largely because of a slowdown in the United States and Brazil. The region is expected to grow at 2.2 percent in 2026.

In Latin America and the Caribbean (LAC), growth has been relatively steady at 2.5 percent in 2025 and projected at 2.3 percent in 2026, with a notable rebound in Argentina and Ecuador in 2025, as the fruits of important reform efforts are starting to become more visible, offsetting some moderation in other countries. It is notable that the current dispersion in growth outcomes in LAC is at historically low levels (Figure 1.1, panel 2). This suggests that common factors—such as supportive global financial conditions, favorable terms of trade, strong global demand (Box 1.1), and relatively limited exposure to US tariff increases and global supply-chain disruptions—have been instrumental in shaping activity outcomes across most of the region.

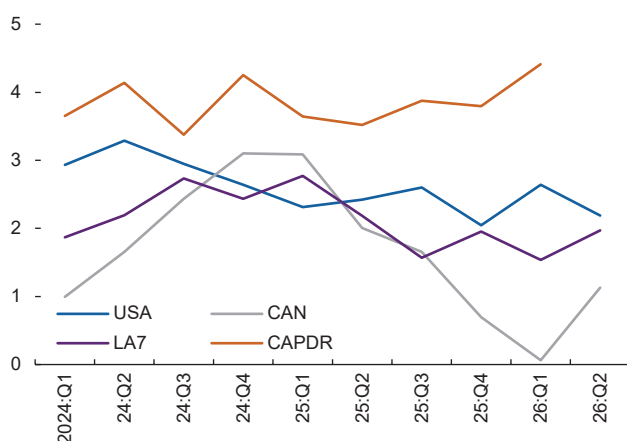
Figure 1.1. Activity

Growth has remained resilient across most of the region.

... with growth rates converging despite heterogeneous shocks, suggesting an important role for common external factors.

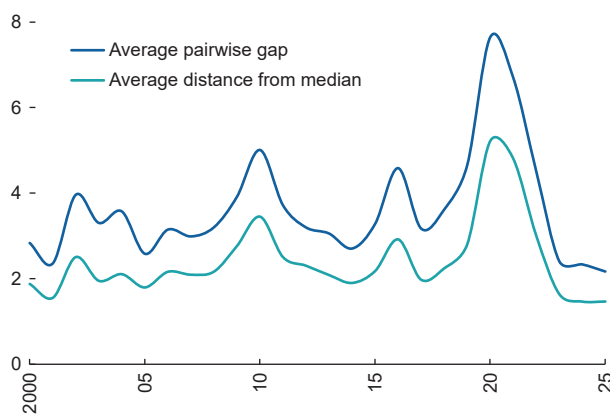
1. Real GDP Growth

(Year-over-year percent change)



2. LAC: Growth Dispersion¹

(Percentage points)



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

Note: Aggregates are purchasing-power-parity GDP-weighted averages. Data labels in the figure use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; LAC = Latin America and the Caribbean; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹ Average pairwise gap is the average absolute difference in growth rates across all country pairs. Average distance from median is the average absolute deviation of each country's growth rate from the regional median. Sample excludes Guyana.

Global Factors: Supportive Financial Conditions and Terms-of-Trade Gains

Even though the war in the Middle East has raised expectations of further monetary tightening in the United States and concerns about the fiscal outlook have pushed up term premiums across advanced economies, financial conditions across the Western Hemisphere continue to ease, providing an important impulse to growth (Figure 1.2, panel 1).

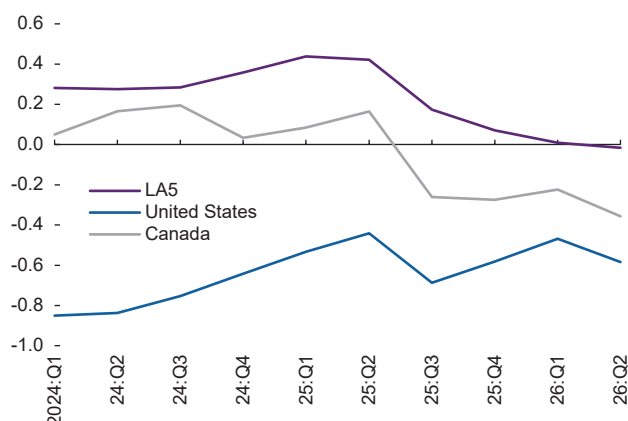
In LAC, the effect of higher global risk-free rates has been partly offset by a narrowing of sovereign spreads. The global appetite for LAC assets has remained strong (Figure 1.2, panel 2), and sovereign and corporate international bond issuance by LAC borrowers is at close-to-record levels (Figure 1.2, panel 3). This increase in investor

Figure 1.2. Financial Conditions

Financial conditions are easing.

1. Financial Conditions Index¹

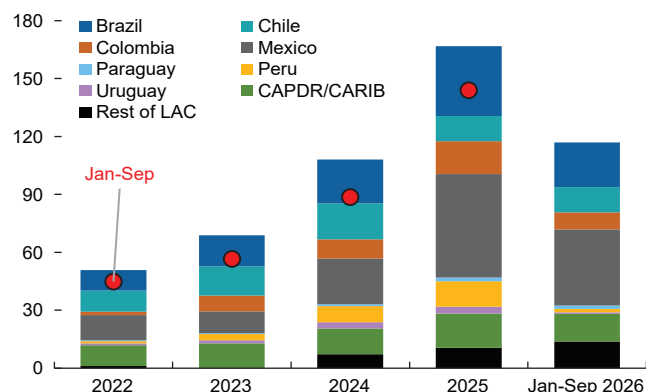
(0 = neutral; +/- = tight/loose)



International corporate and sovereign bond issuance has been robust, ...

3. LAC: International Bond Issuance³

(Billions of US dollars)



Sources: Bloomberg Finance L.P.; Bond Radar; and IMF staff calculations.

Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; EM = emerging markets; EM Asia = India, Indonesia, Malaysia, Philippines, Thailand; EM Europe = Hungary, Poland, Romania, Serbia; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay); LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

¹For methodology and variables included in the financial conditions index, refer to the online annex of the October 2018 *Global Financial Stability Report*. LA5 is purchasing-power-parity GDP-weighted averages.

²Aggregates are medians. Sovereign spread refers to EMBIG spread.

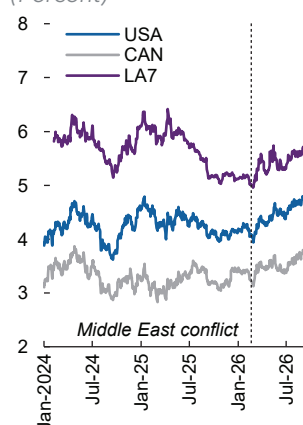
³Includes sovereign and corporate/financial bond issuances.

Declining sovereign spreads have partly offset higher term premiums in advanced economies.

2. Yields and Spreads²

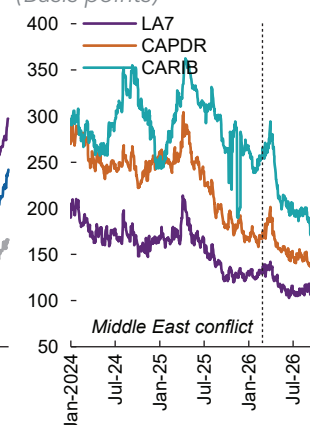
Ten-year Bond Yields

(Percent)



Sovereign Spreads

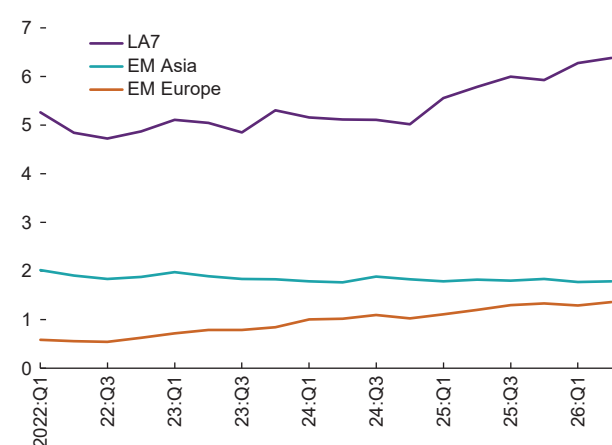
(Basis points)



... and LA7 bonds are accounting for a growing share of foreign portfolios.

4. US Holdings of Foreign Bonds

(Percent share of total world holdings)



interest (Figure 1.2, panel 4) is supported by the region's relatively limited exposure to geopolitical risks, especially when compared with other emerging markets.

In the United States, equity markets have been hovering around all-time highs and corporate spreads are close to all-time lows, driven by improvements in corporate profitability, especially for technology firms (April 2026 *Global Financial Stability Report*). Canadian equities have also risen, led by financials, basic materials, and energy, and Latin American equities have strengthened amid improved global risk appetite, favorable commodity prices,

and solid corporate earnings. These equity market gains are supporting both investment and consumption in the United States and Canada, although they likely have more negligible effects in Latin America (OECD 2019).

Terms of trade have been particularly supportive across most of the region over the past few years (Figure 1.3, panel 1). Prices have risen for several key exports, including copper, gold, soybeans, and oil. Gains were especially large for Chile and Peru. The rise in oil prices that followed the war in the Middle East (Figure 1.3, panel 2) has meant that terms-of-trade gains are rotating toward energy producers, notably Canada and Colombia (Figure 1.3, panel 3). These higher energy prices have, though, put pressure on oil importers, especially in the Caribbean and Central America.

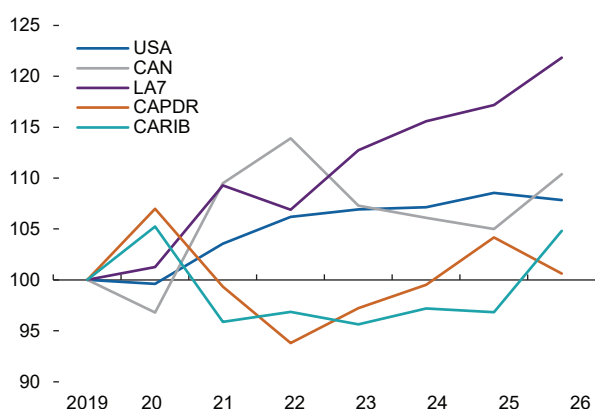
The combination of the positive terms-of-trade shock and loosening of financial conditions is expected to add about 0.6 percentage point to the region's GDP growth in 2026 relative to 2025, after controlling for other factors, including country- and time-specific effects and US and Chinese growth and inflation. However, this positive

Figure 1.3. Global Factors

Terms of trade have been improving, especially in LA7. The oil price surged after the onset of the conflict...

1. Terms of Trade

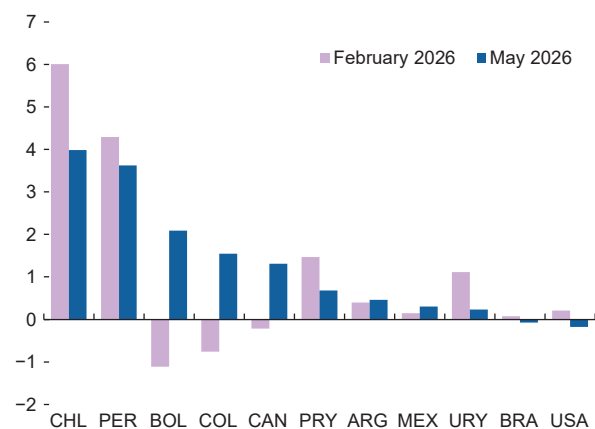
(Index: 2019 = 100)



... which redistributed terms-of-trade gains in favor of the region's net oil exporters.

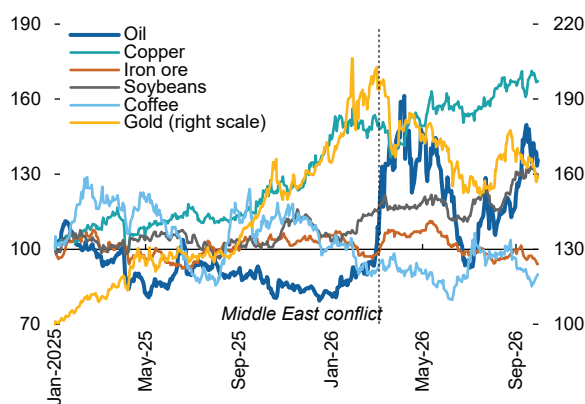
3. Change in Commodity Terms of Trade¹

(Percent change relative to January 2025)



2. Commodity Prices

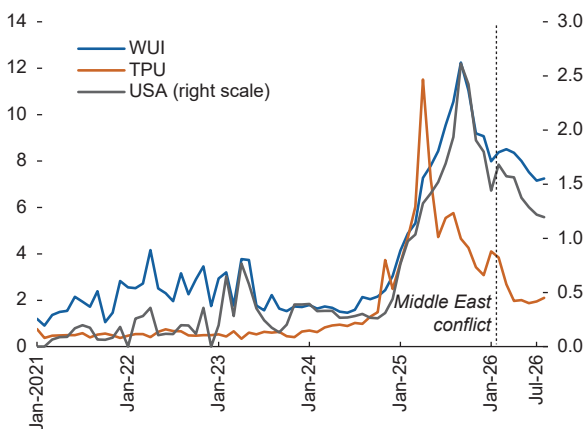
(Index: January 1, 2025 = 100)



Measures of uncertainty spiked in 2025 and have subsequently partly receded.

4. Overall and Trade Policy Uncertainties²

(Index)



Sources: Ahir, Bloom, and Furceri 2022; Bloomberg Finance L.P.; Caldara and others 2020; Haver Analytics; IMF, Commodity Terms of Trade database; and IMF staff calculations.

Note: Aggregates are purchasing-power-parity GDP-weighted averages. Data labels in the figure use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹ Commodity net export price index (individual commodities weighted by the ratio of net exports to GDP).

² The uncertainty measures are news- and media outlets-based indices that quantify media attention to global news related to the overall uncertainty (WUI) and trade policy uncertainty (TPU). Uncertainty index shown for the United States is from the WUI.

impulse is expected to be partly offset by the impact of higher global uncertainty from tariffs and geopolitical developments which may delay investment decisions and increase caution among firms and households (Figure 1.3, panel 4; Figure 1.4).

Domestic Drivers: A Mixed Picture

Private consumption has remained an important engine of growth across the region. In the United States, a strong equity market and gains in housing values have boosted household wealth, feeding into private consumption. In Canada, accumulated household savings have allowed for consumption smoothing despite weaker employment growth and smaller immigration inflows. In much of Latin America, tight labor markets and solid income growth continue to underpin household spending, and in Central America, strong remittances—including through some front-loading of transfers in anticipation of tighter US immigration enforcement (Box 1.2)—are boosting consumer demand.

By contrast, investment has been uneven across countries. In the United States, the contribution of total nonresidential investment to growth has been broadly similar in 2025–26 as in the past, although the composition has changed dramatically in favor of technology spending. High commodity prices have boosted investment in Paraguay and Peru, which, in turn, has resulted in increased imports of capital goods. In much of the rest of South America, investment has softened. Tariff uncertainty and supply-chain disruptions have weighed on investment in Canada and Mexico, while uncertainty regarding domestic policies has been a headwind in Mexico. This heterogeneous picture of capital formation has also been reflected in productivity outcomes: labor productivity growth has been exceptionally strong and broad based in the United States but weaker in Canada, Mexico, and much of South America (Figure 1.5, panel 1).

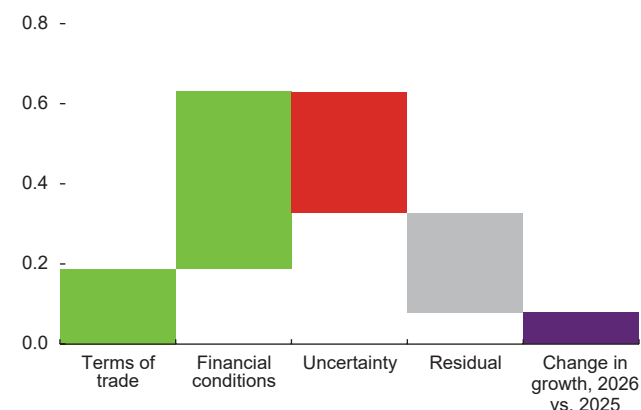
Across the region, export demand has been robust, albeit moderating in some parts of South America in 2026 (Figure 1.5, panel 2). Strong US demand has generated positive spillovers through merchandise trade, Caribbean tourism, and remittances to Central America. In Canada, repeated shifts in US tariffs have, though, disrupted the tightly integrated North American supply chains and weighed on exports. In contrast, Mexico has benefited from the accelerating US demand for electronics.

Disinflation Interrupted

The rise in global energy and food prices after the outbreak of the Middle East conflict has interrupted the disinflation that was underway across much of the hemisphere in 2025 and early 2026 (Figure 1.6, panel 1). Headline inflation has increased in several economies, although the magnitude of the increase has been cushioned by the region's high share of renewable electricity generation. The pass-through of higher energy prices to core inflation has, so far, been contained, with little evidence of second-round effects through wages and inflation expectations. Most countries have introduced fiscal measures to cushion households and firms from the effect of higher global energy costs (Figure 1.6, panel 2). However, some countries (including Argentina, Bolivia, and Ecuador) have taken bold steps to scale back subsidies and allow for global prices to be better reflected in domestic prices.

Figure 1.4. LA5: Drivers of Change in Growth, 2026
(Percentage points)

Supportive financial conditions and favorable terms of trade are being partly offset by the negative effects of uncertainty on growth.

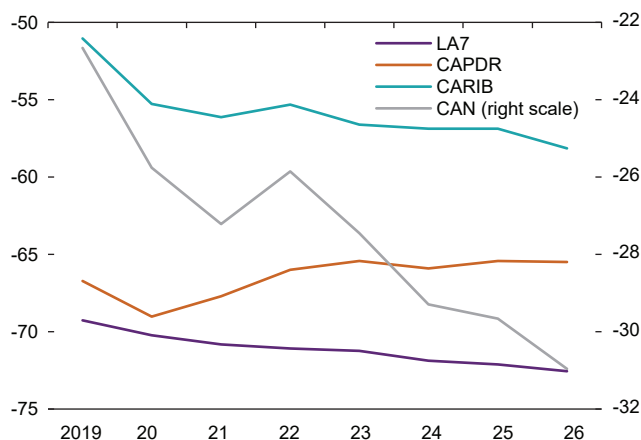


Sources: Ahir, Bloom, and Furceri 2022; Haver Analytics, IMF, World Economic Outlook database; and IMF staff calculations. Note: Aggregate is purchasing-power-parity GDP-weighted average. Estimates are obtained from a local projection regression of growth on terms of trade, financial conditions, and uncertainty, controlling for US and China growth and inflation, and country- and year- fixed effects. For methodology and variables included in the financial conditions index, refer to the online annex of the October 2018 *Global Financial Stability Report*. LA5 = Latin America 5 (Brazil, Chile, Colombia, Mexico, Peru).

Figure 1.5. Productivity and Exports

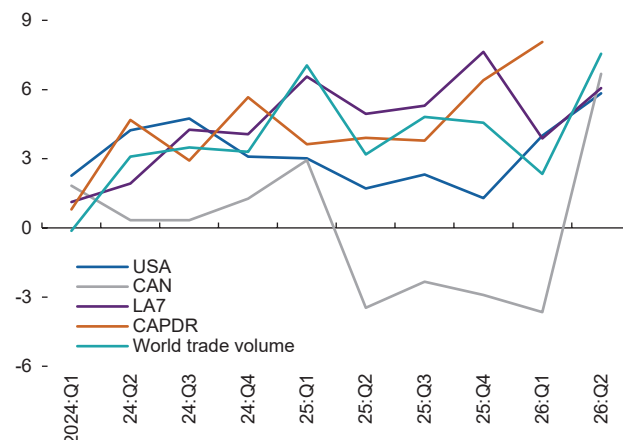
Productivity gains in the region remain uneven, with a growing gap relative to the United States.

1. Labor Productivity Gap versus the United States¹ (Percent of US labor productivity)



Export growth has been robust in most countries.

2. Real Exports Growth (Year-over-year percent change)



Sources: CPB Netherlands Bureau for Economic Policy Analysis; Haver Analytics; IMF, World Economic Outlook database; national authorities; and IMF staff calculations.

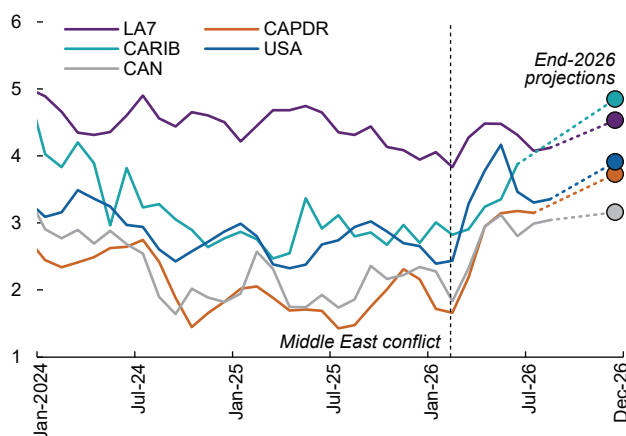
Note: Aggregates are purchasing-power-parity GDP-weighted averages. Data labels in the figure use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹Labor productivity is measured as real GDP in purchasing-power-parity international dollars divided by total employment. The gap is measured as the percent difference between labor productivity and the US level.

Figure 1.6. Inflation

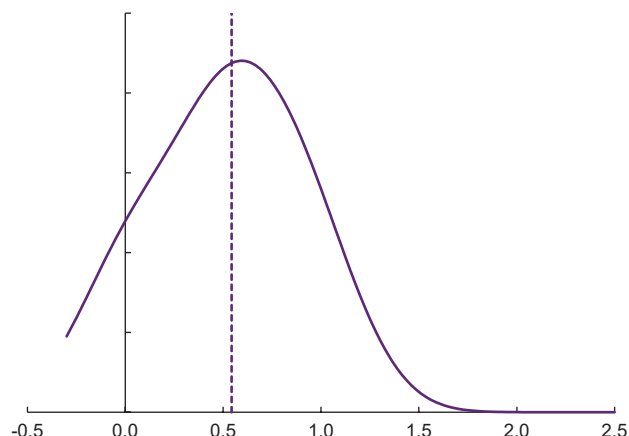
Inflation is picking up again after the energy-price shock...

1. Headline Consumer Price Inflation¹ (Year-over-year percent change)



... even though fuel-price pass-through has been only partial.

2. LAC: Oil Price Pass-through² (Ratio)



Sources: Global Petrol Price Database; Haver Analytics; IMF, World Economic Outlook database; national authorities; US Energy Information Administration; and IMF staff calculations.

Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; LAC = Latin America and the Caribbean; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹Aggregates are purchasing-power-parity GDP-weighted averages.

²The vertical dashed line refers to the median of the region. Pass-through is calculated as the percentage change in domestic dollar retail diesel prices over the percentage change in international diesel prices (both measured in US dollars) from the end of January to the end of June 2026. Pass-through is trimmed at the 1 percent level.

Outlook and Risks

An Ongoing Steady Expansion

Growth across the Western Hemisphere is projected to pick up slightly to 2.3 percent in 2027–28 (Figure 1.7, panel 1). The improved outlook for 2027 is expected to be broad based, supported by recoveries in Canada and Mexico, stronger activity in parts of South America and Central America, renewed momentum in Venezuela, and Jamaica's recovery from Hurricane Melissa.

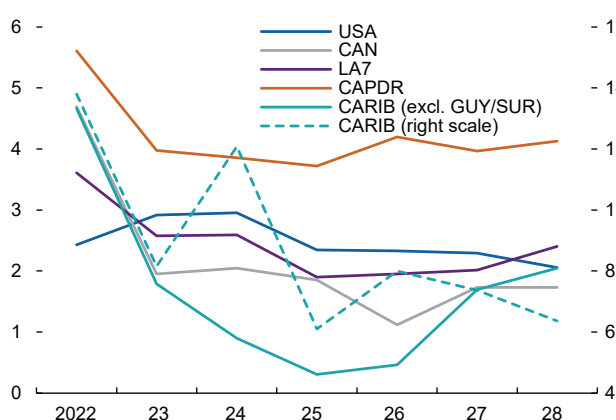
Figure 1.7. Outlook and Risks

Growth is projected to strengthen slightly in 2027...

... though with downside risks emanating from potential negative supply shocks.

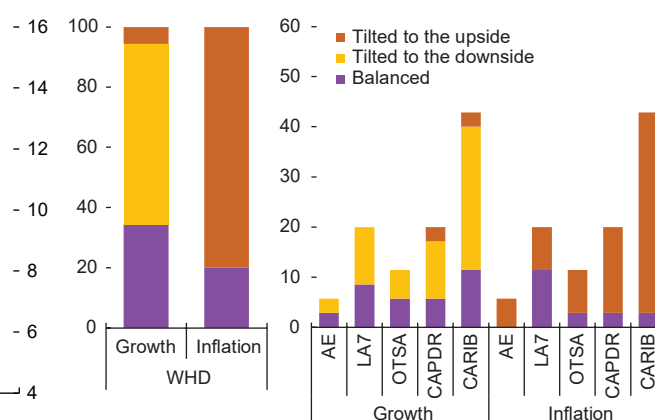
1. Real GDP Growth¹

(Year-over-year percent change)



2. Western Hemisphere: Growth and Inflation Risks

(Percent share of the total number of Western Hemisphere countries)



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

Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. AE = advanced economies; CAPDR = Central America, Panama, and the Dominican Republic; CARIB = Caribbean; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay); OTSA = other South America.

¹Aggregates are purchasing-power-parity GDP-weighted averages.

Three main forces are expected to shape the near-term outlook: commodity markets, robust domestic demand, and the reshaping of global trade.

Commodities

High commodity prices are expected to continue supporting activity across the Western Hemisphere, particularly benefiting energy exporters (including the United States, Canada, Argentina, Brazil, Colombia, Ecuador, Guyana, Trinidad and Tobago, and Venezuela). However, the increase in energy prices will be a headwind to oil-importing economies, particularly in the Caribbean. In much of South America, favorable metal and agricultural prices are expected to continue supporting exports (particularly in Chile and Peru).

Domestic Demand

US private domestic demand is projected to remain robust in 2027, with a modest decline in private investment being offset by solid momentum in private consumption. In Canada, both investment and consumption are expected to be weighed down by slower immigration inflows and trade uncertainties, although some fiscal support and a neutral monetary stance are expected to provide some offset. Brazil, Colombia, and Peru should continue to benefit from firm domestic demand, although tight monetary conditions in Brazil and the planned fiscal consolidation in Colombia will be a countervailing force. Activity in Argentina is projected to firm up in 2027, with investment and private consumption being supported by falling inflation and ongoing reform efforts.

Trade

Trade uncertainty is weighing most heavily on the highly integrated economies in North America. Canada faces a particularly challenging outlook from higher tariffs and continued trade policy uncertainty. In Mexico, export industries are expected to continue growing. However, uncertainty regarding domestic policies will weigh on corporate investment (Box 1.3). Elsewhere in LAC, the impact of US tariffs is relatively low, and some are benefiting from a shift in global demand (notably from China) away from US products. At the same time, some countries in the region are expected to face tougher competition from imports of Asian-produced intermediate and consumer goods, potentially weighing on domestic manufacturing output. Solid global tourism demand is expected to continue to support activity in much of the Caribbean in 2027.

Persistent Inflationary Pressures

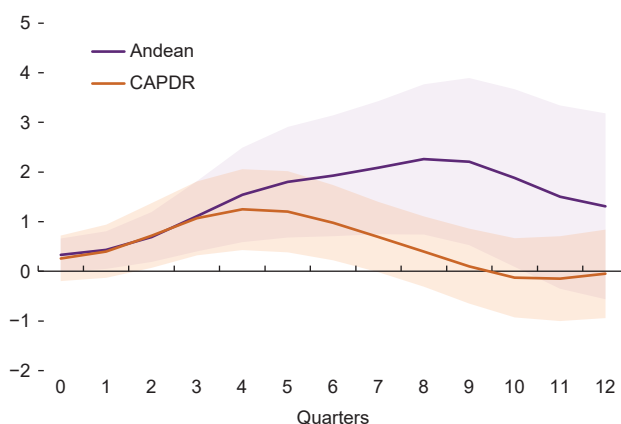
The inflation outlook has become more challenging across much of the hemisphere. Higher global energy and food prices are delaying convergence to central bank targets, although the extent of the effect varies with country characteristics and domestic policies. Fuel-tax reductions and administered price measures have limited the near-term pass-through in some countries, but inflationary pressures may persist, especially where domestic demand remains strong. Still, the boost to inflation from shifts in global commodity prices is expected to wane over time, and inflation should return to target in most countries by the end of 2027, supported by effective monetary frameworks.

Downside Risks to Growth, Upside Risks to Inflation

Negative risks to growth and upside risks to inflation dominate much of the region, consistent with an expected negative skew to future supply shocks (Figure 1.7, panel 2). A more prolonged period of high energy prices would add to inflation across the region and weigh on energy- and fertilizer-importing economies through higher production costs, reduced household purchasing power, and adverse effects on agriculture. However, such a scenario would benefit both activity and the fiscal positions for the region's oil exporters. A higher path for the US policy rate, higher global term premiums, or a decompression of sovereign spreads could raise borrowing costs and reduce capital flows to LAC. Those with significant external financing needs and high debt would be particularly hard hit. A weakening of the global technology cycle could dampen AI-related investment and lead to negative wealth effects through a downward revaluation of global equity and corporate bond prices. Such a shift in advanced economy market valuations could have broader spillovers to financial market sentiment, capital flows, commodity prices, exchange rates, and investor confidence. Trade tensions remain a continuing source of uncertainty, particularly for economies closely integrated with the United States. Finally, the historically strong El Niño could generate significant adverse weather events that would be particularly problematic for agriculture and infrastructure in some countries, potentially adding further to inflationary pressures. Although the effects of El Niño vary substantially across subregions, empirical analysis shows that the Andean region (Colombia, Ecuador, and Peru) and Central America, Panama, and the Dominican Republic (CAPDR) are likely to experience the largest losses in output (Online Annex 2 of the October 2023 *Regional Economic Outlook: Western Hemisphere*). A material increase in inflation is likely to be experienced across most of the region (Figure 1.8).

Figure 1.8. Impact of El Niño on Inflation
(Percent; cumulative impact)

A strong El Niño is expected to lead to higher inflation, particularly in Andean and CAPDR economies.



Source: Beltran Saavedra and Hadzi-Vaskov, forthcoming.
Note: The figure shows the estimated impact of El Niño events on inflation using the local projection method in a cross-country panel. Shaded areas correspond to 10th/90th percentile confidence intervals. Andean = Colombia, Ecuador, Peru; CAPDR = Central America, Panama, and the Dominican Republic.

On the positive side, if inflation in the United States were to dissipate more quickly, this could facilitate a lower path for the federal funds rate, a further compression of sovereign spreads, and stronger global demand. Similarly, the benefits of ongoing technology investments could translate into stronger productivity and growth, with positive spillovers across the hemisphere. Finally, an easing of geopolitical tensions would have a positive impact on global demand, although with a heterogeneous effect across the region depending on whether countries are net energy exporters or importers.

Medium-Term Growth Remains Subdued

Despite solid near-term growth numbers, medium-term prospects are more challenging. For much of the region, population and labor force growth will continue to slow in the coming years (October 2024 *Regional Economic Outlook: Western Hemisphere*). As a result, improvements in labor productivity will need to play a larger role in sustaining growth and raising living standards. However, the track record of productivity gains in the region other than the United States has been chronically disappointing (Figure 1.9), reflecting, among other factors, insufficient investment in human and physical capital, limited innovation and technology adoption, widespread informality, and weak business dynamism and governance (October 2023 *Regional Economic Outlook: Western Hemisphere*; October 2024 *Regional Economic Outlook: Western Hemisphere*). Digitalization, artificial intelligence, rising global demand for critical minerals and clean energy, and the ongoing reconfiguration of global supply chains represent important opportunities for the region. Nevertheless, realizing these opportunities will require addressing long-standing supply-side bottlenecks.

In the United States, output is projected to grow at close to 1.9 percent annually during 2027–31, with continued technological innovation and adoption expected to support gains in productivity even as employment growth slows. Gains in GDP per capita are projected to average 1.7 percent annually over the next five years.

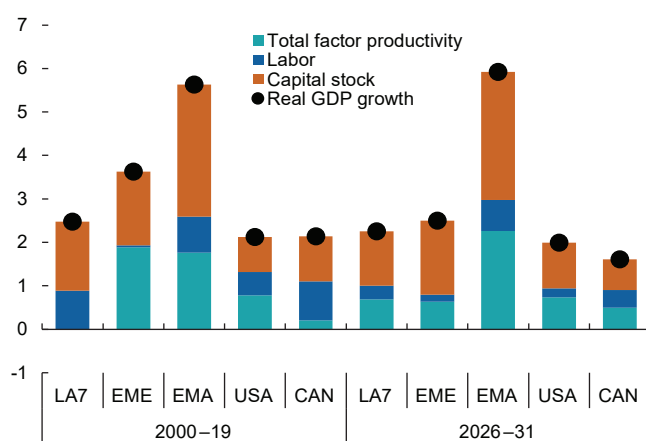
Figure 1.9. Medium-Term Outlook

In contrast to recent history, TFP is expected to contribute positively to LAC growth in the coming years...

... but even this improvement is not sufficient to close the productivity gap with the United States.

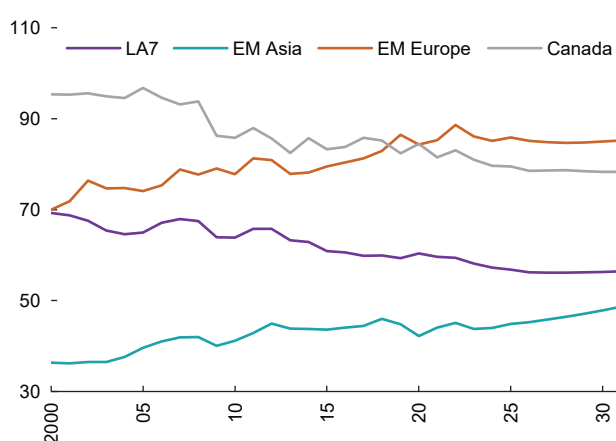
1. Contributions to Real GDP Growth

(Year-over-year percent change)



2. Total Factor Productivity Relative to the United States¹

(Percent)



Sources: IMF, World Economic Outlook database; Penn World Table 11.0 database; and IMF staff calculations.

Note: Aggregates are purchasing-power-parity GDP-weighted averages. Data labels in the figure use International Organization for Standardization (ISO) country codes. EM = emerging markets; EMA = EM Asia (India, Indonesia, Malaysia, Philippines, Thailand); EME = EM Europe (Bosnia and Herzegovina, Hungary, Poland, Romania, Serbia); LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay), TFP = total factor productivity.

¹EM Europe excludes Bosnia and Herzegovina because of data limitations.

Canada's medium-term outlook combines modest growth with a gradual recovery in investment. Real GDP growth is projected to average 1.7 percent a year over 2027–31, with the output gap closing by 2030, and per capita GDP is expected to expand, on average, by only 1.2 percent. Indeed, over the past decade, Canada's real GDP per capita has fallen by about 12 percent relative to that of the United States, largely because of smaller gains in labor productivity. This divergence is expected to continue over the medium term.

In Latin America, with income levels substantially lower than in the United States, there is significant scope for per capita real output to converge with that of the United States. However, even with a projected pickup in total factor productivity growth in some countries, medium-term growth is expected to average only 2.7 percent. As a result, and in contrast to emerging market economies in Asia and Europe, IMF staff forecasts that few countries in Latin America will bring their living standards closer to advanced economy levels over the next several years.

In some parts of the region, medium-term growth prospects are more positive. In CAPDR, output is projected to expand on average by about 4 percent per year, with the per capita GDP gap relative to the United States steadily narrowing. Commodity-exporting Caribbean economies are expected to experience high growth rates as new energy projects come online. However, the tourism-dependent Caribbean economies are projected to be less dynamic, with growth averaging less than 2 percent over the next five years as persistent supply-side constraints offset strong tourism demand.

Policy Priorities

The central policy challenge ahead for the region is to capitalize on the current relatively supportive global conditions to address high levels of public debt and to remove supply-side constraints that stand in the way of achieving higher productivity.

Lowering Public Debt

Fiscal space remains limited across much of the region, reflecting high levels of public debt and high financing costs (Figure 1.10, panel 1; Background Paper 2 of the October 2024 *Regional Economic Outlook: Western Hemisphere*). After delays in planned fiscal adjustment (October 2025 *Regional Economic Outlook: Western Hemisphere*), countries in Latin America finally implemented consolidation measures in 2025, reversing the expansionary stance that was in place since 2022. However, overall, the resulting fiscal adjustment has been smaller than previously envisaged and, for many, that adjustment has stalled in 2026 (Figure 1.10, panel 2). Some countries (including Brazil, Canada, and many Caribbean economies) have put in place measures to cushion the impact of higher energy prices, which will run counter to fiscal consolidation. However, Argentina and Ecuador provide a contrasting picture where efforts to strengthen debt sustainability have been ambitious, supported by IMF resources. An important fiscal adjustment is also underway in Bolivia after the change in government in late 2025, supported by a new IMF program.

In designing the budgets for 2027, renewed efforts will be needed across much of the region to reduce deficits and debt, especially given mounting pressures from increases in global interest rates. These efforts should be anchored in medium-term plans and stronger fiscal frameworks (Khachatryan and others 2026) designed to credibly put debt-to-GDP ratio on a downward path. Smaller deficits would help reduce debt vulnerabilities and, where relevant, rebalance the policy mix, easing the burden on monetary policy in bringing inflation back to target (Figure 1.11, panels 1 and 2). Lower debt would also help strengthen monetary policy effectiveness (Online Annex 3 of the October 2025 *Regional Economic Outlook: Western Hemisphere*).

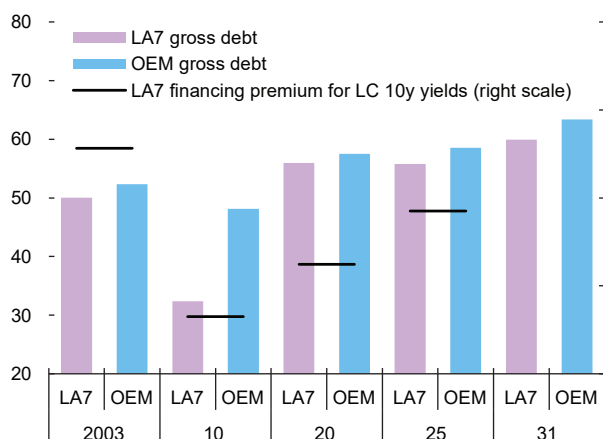
Figure 1.10. Fiscal Space

Public debt continues to rise in many countries in the region...

... and fiscal consolidation in the coming years is expected to be, at best, gradual (after a recent history of less-than-expected reductions in the deficit).

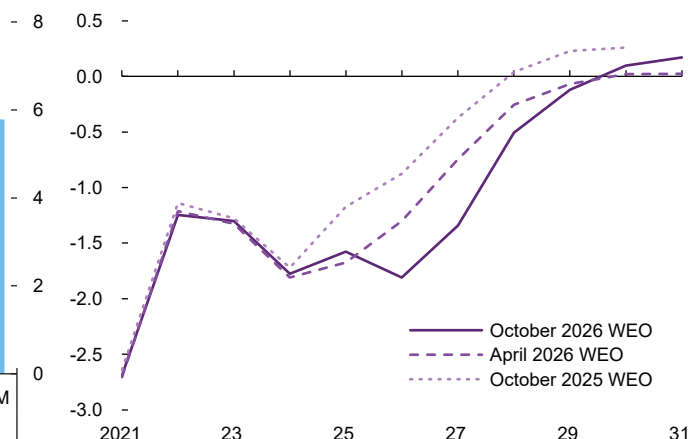
1. General Government Gross Debt and Financing Cost¹

(Percent of GDP; unless noted otherwise)



2. LA7: General Government Structural Primary Balance²

(Percent of potential GDP)



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

Note: Aggregates are simple averages. CAPDR = Central America, Panama, and the Dominican Republic; LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay); LC = local currency; OEM = other emerging markets (Bosnia and Herzegovina, Hungary, India, Indonesia, Malaysia, Philippines, Poland, Romania, Serbia, Thailand); WEO = *World Economic Outlook*.

¹Financing cost in percentage points is the difference between LA7 and OEM's nominal 10-year local currency bond yields.

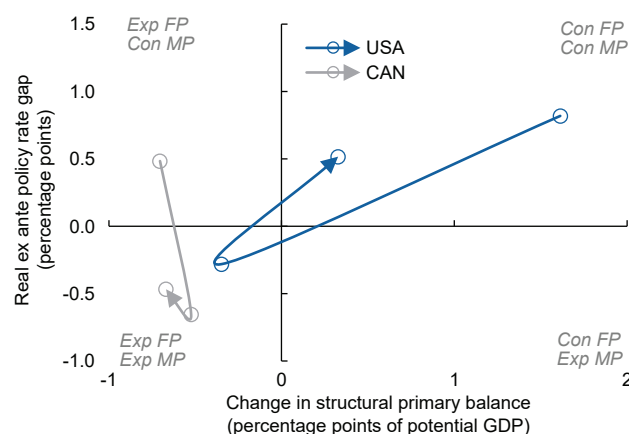
²Chile refers to the central government's structural non-mining primary balance. Colombia refers to the consolidated public sector's structural non-oil primary balance. Peru refers to the nonfinancial public sector's structural primary balance.

Figure 1.11. Monetary and Fiscal Policy, 2024-26

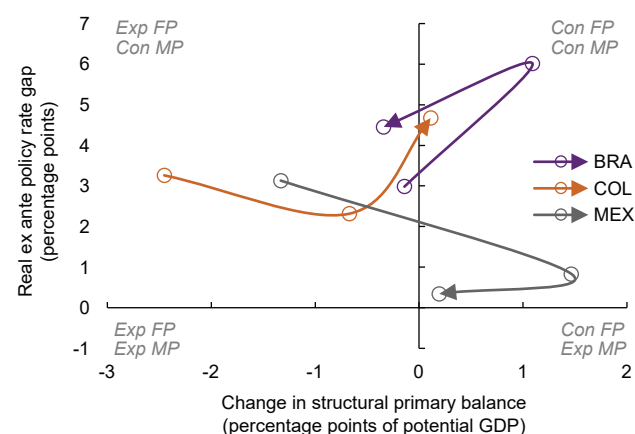
Policies have become less restrictive in the United States and somewhat expansionary in Canada...

... while in LAC, policy settings are diverging, with Brazil and Colombia standing out with relatively restrictive monetary stances.

1. United States and Canada



2. Brazil, Colombia, and Mexico



Sources: Consensus Economics; Haver Analytics; IMF, World Economic Outlook database; and IMF staff calculations.

Note: The real ex ante policy rate gap is the difference between the real ex ante policy rate and the real neutral rate. The real ex ante policy rate is the difference between the nominal policy rate and the one-year ahead inflation expectations. Data labels in the figure use International Organization for Standardization (ISO) country codes. Con = contractionary; Exp = expansionary; FP = fiscal policy; MP = monetary policy.

A successful consolidation will require improved revenue mobilization that is firmly focused on removing distortionary tax exemptions, bringing a greater share of households into the personal income tax net, and increasing progressivity. Increased revenues, potentially aided by further digitalization, will allow governments to protect spending on health, education, social assistance, and growth-enhancing public investment projects. Over time, there is also a need to tackle the relatively high corporate tax rates in the region, particularly given that tax policies in the United States have significantly reduced the effective tax rate on corporate profits, which will incentivize multinational firms to redirect investment toward the United States.

Commodity exporters should regard revenue gains from higher global prices as temporary and, as such, should save a significant share of additional revenues. This is all the more important in cases where debt is high, foreign exchange reserves are low, and gross financing needs are large. Institutional improvements, such as through fiscal rules, stabilization funds, sovereign wealth funds, and coherent medium-term fiscal frameworks, can help in making the case to save the upswing in commodity revenues and prevent a procyclical fiscal policy.

At the same time, favorable financial conditions provide an opportunity for governments to prefinance near-term fiscal needs and issue longer-duration debt, which will help to strengthen public sector balance sheets and reduce fiscal vulnerabilities.

Securing Price Stability

Monetary policy should remain focused on safeguarding price stability. Stronger central bank independence and improved monetary policy frameworks have, over time, helped anchor inflation expectations more firmly across much of the region. Evidence shows that well-anchored expectations, in turn, limit the pass-through of terms-of-trade and exchange rate shocks to inflation, reducing the risk that temporary energy price increases become persistent, and lowering the output costs of bringing inflation back to target (Figure 1.12, panel 1).

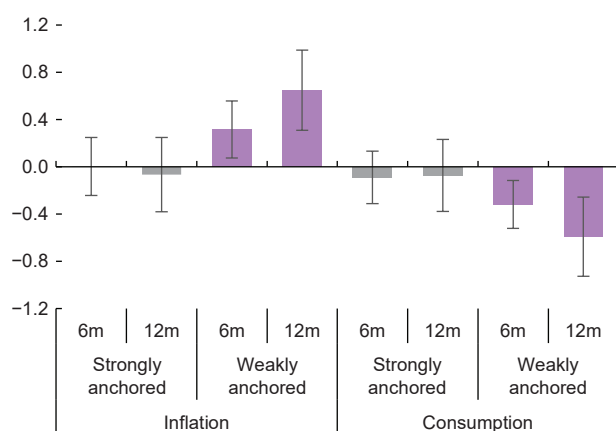
Figure 1.12. Monetary Policy

Better anchoring of inflation expectations has reduced the pass-through of terms-of-trade shocks in the region.

Inflation expectations have remained broadly stable in the face of the energy-price shock.

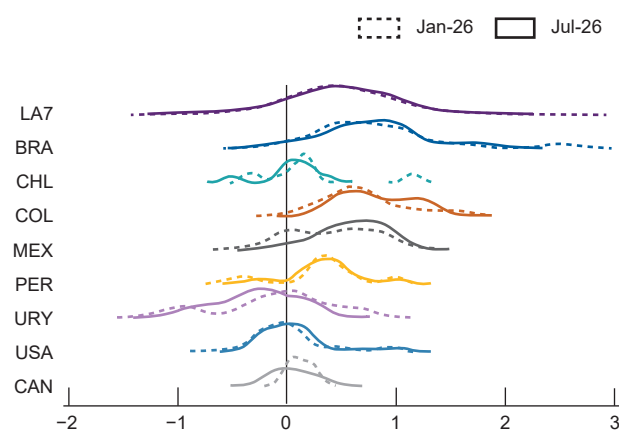
1. Response to Terms-of-Trade Shocks by Anchoring Level¹

(Percentage points)



2. Distribution of Inflation Expectations by Forecasters, 2028²

(Percentage points; deviation from target)



Sources: Barrett and others 2026; Bems and others 2021; Consensus Economics; IMF, Commodity Terms of Trade database; and IMF staff calculations.

Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. LA7 = Latin America 7 (Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹Cumulative response to month-over-month percentage change in the commodity terms-of-trade index. Each country-year is classified as strongly (weakly) anchored when it is in the top (bottom) 25 percent of the observations of the anchoring index. Error bars denote 90 percent confidence intervals.

²Density plots of one-year-ahead (December-over-December for LA7; 12 months for USA/CAN) inflation forecast deviation from inflation targets by Consensus Forecasts vintage. LA7 excludes Paraguay because of data limitations.

The region's monetary policy frameworks have been tested in recent years and proven successful in controlling inflation with a relatively modest output cost (October 2025 *World Economic Outlook*). Now, the region's central banks face a new test from a sizable energy-price shock and El Niño effects. Generally, central banks have appropriately let exchange rates adjust to absorb the shock and, in some cases, raised interest rates to demonstrate their commitment to price stability. For most countries, market participants have revised upward their expected future path of policy rates. Near-term inflation expectations have edged higher, as energy prices are reflected in headline inflation and fiscal measures to cushion the impact are allowed to expire. Currently, inflation expectations remain stable at a two- to three-year horizon (Figure 1.12, panel 2), consistent with confidence that institutional credibility will prevent second-round effects from taking hold.

Despite the actions of most central banks in the region, inflation is expected to converge slowly back to target. Monetary policy is expected to be broadly neutral across most of the region. In this environment, any material easing of monetary conditions should proceed very cautiously and only once it is clear that the current inflationary impulse is firmly in the rearview mirror. Despite central banks' demonstrated commitment to price stability, inflation has remained above target in many economies for a prolonged period, leaving little room to look through the current energy-price shock or assume that second-round effects will be limited or temporary. For some, this means that monetary policy will need to tighten, particularly where inflation has been persistently above target and fiscal policy is not working to restrain demand.

Protecting the Vulnerable and Boosting Human Capital

Many governments introduced measures in 2026 to cushion the impact of higher energy prices on households and firms, including through fuel subsidies, tax reductions, credit guarantees, and other interventions (Figure 1.13). These measures provided prompt relief, but the untargeted interventions introduced distortions and suppressed price signals that would have otherwise reduced energy demand.

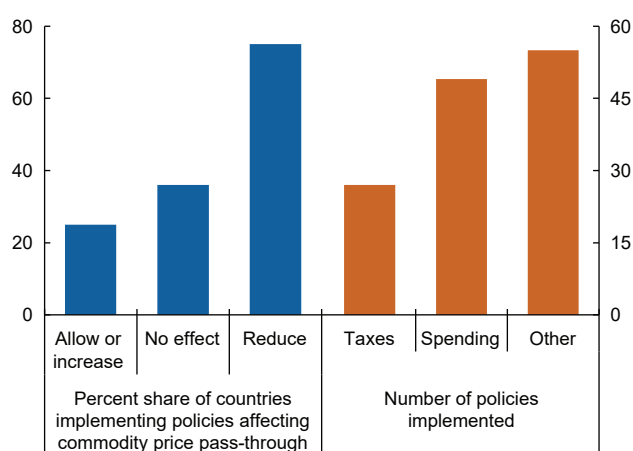
There is a need to recast these interventions to improve their effectiveness. The hard-won progress made in several countries (including Argentina, Bolivia, and Ecuador) in reducing or eliminating energy subsidies should be preserved. Instead, governments should strengthen systems to deliver well-targeted direct transfers to low-income households (Chapter 2 of the October 2026 *World Economic Outlook*). Beyond this, prioritizing investment in health and education will help boost human capital and strengthen income security, especially for lower-income families. This would reduce the need for broad-based fiscal support when future supply shocks occur.

Capitalizing on the Terms-of-Trade Gains to Catalyze Export-Led Growth

The current commodity boom differs from previous episodes in ways that may allow the region to derive more lasting growth benefits from higher commodity prices. The commodity boom of the 2000s was not accompanied by a commensurate increase in export revenues as much of the rise in dollar export prices was offset by a real appreciation of the currency which weakened competitiveness in both commodity and non-commodity exports (Bakker 2026; Druck,

Figure 1.13. Policy Responses to the Oil Shock

The region has implemented a broad range of measures to dampen the impact of the oil price shock.



Sources: IMF, Global Policy Tracker database; and IMF staff calculations.

Note: Examples of policies that increase commodity price pass-through include reductions of fuel-tax recoveries, fuel subsidy removals (Spending), removals of the fuel-price controls, and increases in domestically controlled fuel prices (Other). Examples of policies that reduce commodity price pass-through include fuel, electricity, and food subsidies (Spending), and reductions in fuel taxes (Taxes). "Other" also includes credit guarantees, export taxes, relaxation of fuel standards, release of strategic reserves, work-from-home mandates, and public sector energy conservation.

Magud, and Mariscal 2018; April 2015 *Regional Economic Outlook: Western Hemisphere*). In addition, the real appreciation boosted domestic purchasing power by pushing down the cost of imports, while procyclical fiscal policies further stimulated domestic demand (October 2011 *Regional Economic Outlook: Western Hemisphere*; Lopez Murphy, Villafuerte, and Ossowski 2010). As a result, for many countries, the commodity windfall fed into strong domestic consumption and prevented export-led growth from taking hold.

During the current commodity boom, the region has experienced less real appreciation, and exporters have responded with a significant increase in export volumes. Fiscal policies have been more contained, with public sector balances broadly stable (Figure 1.14, panel 1). As a result, during 2023–26, exports have generally grown faster than consumption (Figure 1.14, panel 2), and current account positions have improved. Looking forward, continued efforts to reduce fiscal deficits and a relatively neutral monetary stance should help contain appreciation pressures and strengthen the foundations for a more sustained export contribution to growth.

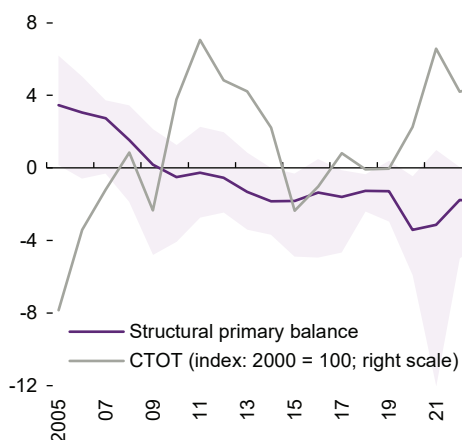
Figure 1.14. Commodity Price Booms

The commodity price boom during 2005–12 was characterized by procyclical fiscal policy...

... and the high commodity prices during that episode contributed to higher consumption rather than export growth.

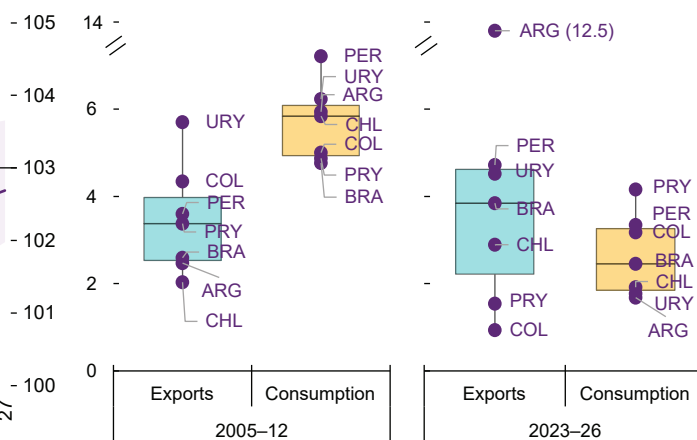
1. LA8 excluding Mexico: Structural Primary Balance and Commodity Terms of Trade¹

(Percent of GDP; unless noted otherwise)



2. Real Export and Real Private Consumption Growth

(Average annual growth; percent)



Sources: IMF, Commodity Terms of Trade database; IMF, World Economic Outlook database; and IMF staff calculations.

Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. CTOT = commodity terms of trade; LA8 = Latin America 8 (Argentina, Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay).

¹Structural primary balance is simple average. Shaded area refers to the min-max range. Chile refers to the central government's structural non-mining primary balance. Colombia refers to the consolidated public sector's structural non-oil primary balance. Peru refers to the nonfinancial public sector's structural primary balance. CTOT refers to the commodity net export price index (individual commodities weighted by the ratio of net exports to GDP); aggregate is purchasing-power-parity GDP-weighted average.

Deepening Trade with Asian Supply Chains

Latin America's trade with China has deepened markedly over the past decade. China has emerged as a major supplier of manufactured goods to Latin America and an increasingly important destination for the region's commodity exports.

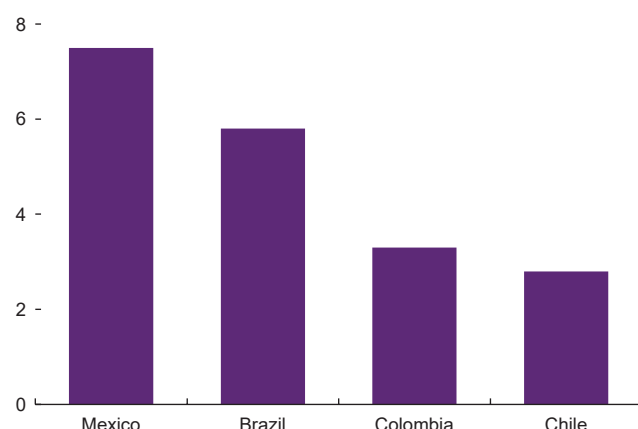
In recent years, Chinese purchases of energy, agricultural products, and other commodities have shifted away from US suppliers, resulting in a fall in the US share of China's goods imports from about 7 percent in 2021 to 4.8 percent as of the middle of 2026. This has provided an opportunity for Latin American producers to increase their market share in Asian imports. Ongoing trade frictions between China and the United States, alongside high demand for the main exports of Latin America, could further increase the region's penetration into Asian markets and attract new investment into natural resource sectors across Latin America.

An important dynamic in trade with Asia is also underway on the import side. As Chinese manufactured goods are being diverted away from the United States, China's steady increase in its share of the Latin American market has accelerated, including in sectors where domestic production is well established. At an aggregate level, US tariffs imposed on China in 2025 are estimated to have raised Chinese exports to major Latin American economies by 4–5 percent (Figure 1.15, panel 1), with larger effects for some products. Motor vehicles are a particularly striking example (Figure 1.15, panel 2), but similar pressures are visible in steel, machinery, textiles, and both consumer and intermediate manufactured goods. Lower-cost imports from Asia benefit the region's consumers and firms that rely on imported capital goods and other manufactured inputs. However, rising imports from Asian supply chains also create competitive pressures on domestic producers which, in turn, can weigh on investment in industries most exposed to that import competition. This places an important premium on domestic manufacturers being able to raise productivity to reduce the risk of their output being substituted by Asian imports. At the same time, policies that reduce supply-side distortions, help facilitate greater domestic value added in the region's commodity exports, and support a diversification of the export base beyond commodities, will become increasingly important.

Figure 1.15. Trade

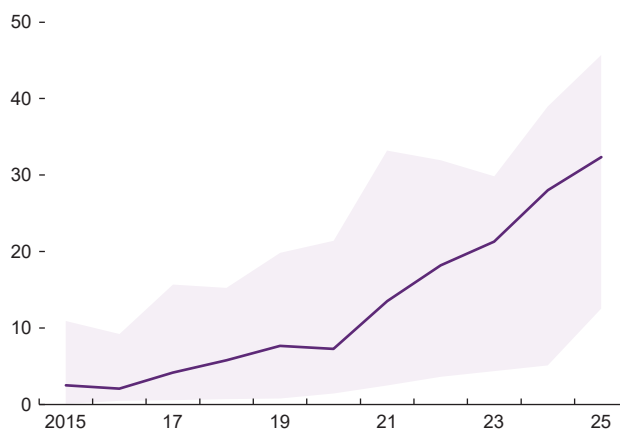
US tariffs on China are redirecting Chinese goods toward much of the region...

1. Effect of 2025 US Tariffs Faced by China on LAC Imports from China
(Predicted change in imports from China; percent)



... with China increasing its market share in LAC in various sectors.

2. China's Share of Latin American Passenger Car Imports¹
(Percent share)



Sources: Arizala, Grittayaphong, and Schauer, forthcoming; UN Comtrade; World Bank, World Integrated Trade Solution; and IMF staff calculations.

¹Includes motor cars and other motor vehicles (HS 8703). Shaded area refers to the min-max range.

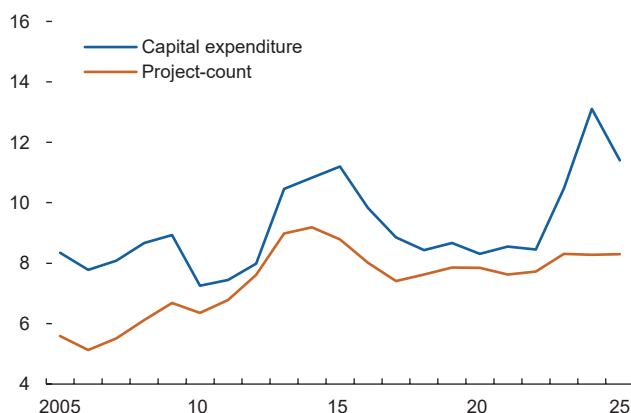
Using the New Global Trade Environment to Attract Foreign Direct Investment

The reshaping of global trade and supply chains may also serve to redirect corporate investment toward LAC, especially given the close links between trade and foreign direct investment (FDI). Multinational investment in tradable sectors can expand export capacity, deepen participation in global value chains, and facilitate technology transfer (Chapter 2).

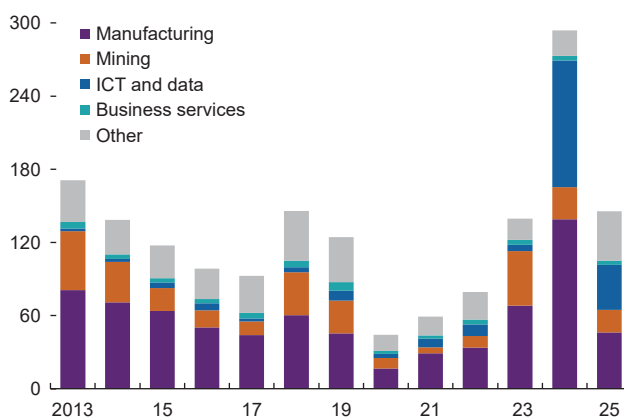
There are signs that the region is already benefiting, with Latin America's share of global greenfield FDI increasing in recent years (Figure 1.16, panel 1), particularly in mining and manufacturing (Figure 1.16, panel 2). In Mexico, these investment inflows reflect supply-chain diversification and increased US demand for information and communications technology. In other countries, FDI has been linked to efforts to secure access to critical minerals and other strategic commodities. Finally, high global commodity prices are attracting foreign capital to expand export capacity and take advantage of the region's abundant natural resources. FDI into

Figure 1.16. Foreign Direct Investment*Global FDI flows to Latin America have increased...*

1. LAC: Share of Global Greenfield FDI¹
 (Percent of world total; three-year trailing moving average)

*... particularly in manufacturing, mining, and ICT.*

2. LAC: Composition of FDI Capital Expenditure²
 (Billions of US dollars; annual levels)



Sources: Orbis Crossborder Investment database; and IMF staff calculations.

Note: Latest available data as of September 2, 2026. FDI = foreign direct investments; ICT = information and communications technology and data; LAC = Latin America and the Caribbean.

¹Shares are computed on announcement years relative to all destination economies in the database and cover announced and completed projects.

²Years are announcement years and cover announced and completed projects.

commodity-related sectors has been broad based, but manufacturing investment has been relatively concentrated in a limited number of economies (notably, Brazil, CAPDR, and Mexico). This FDI has predominantly originated from EU-based multinational corporations and, in the case of Mexico, from the United States.

Latin America is well positioned to attract investments linked to critical minerals and energy. The comparative advantage in energy may also facilitate investments in digital infrastructure such as energy-intensive data centers. The proximity to the US market should prove advantageous to producers in both Mexico and CAPDR as companies put in place more diversified supply chains. Furthermore, geopolitical factors—including “geopolitical distance” (measured using foreign policy voting patterns and other indicators of strategic alignment)—can play an important role in supporting investment inflows to the region (Alvarado, Ding, and Zhou, forthcoming). Maximizing these investment inflows and their associated benefits (such as transfer of technology and know-how and access to new markets) will require a range of reforms to make the region a more attractive destination for foreign capital.

Accelerating Supply-Side Reforms

Many of the policy priorities, including shifting to a more export-led growth model, increasing the region’s share in Asia’s imports, making the region a larger part of global supply chains, and attracting FDI, will require a structural shift to make the region’s economies more flexible, with greater reliance on human capital and innovation, fewer barriers to entry, a more competitive business environment, greater legal certainty and improved governance, more reliable infrastructure, and a more attractive tax regime (October 2024 *Regional Economic Outlook: Western Hemisphere*). Needed reforms that are common across countries include the following:

- Reducing the administrative burden on businesses, streamlining licensing procedures, strengthening contract enforcement, and eliminating tax distortions.
- Strengthening the rule of law, reducing corruption, improving regulatory quality, protecting property rights, and tackling crime.

- Increasing competition by lowering barriers to entry and reducing product market and size-dependent regulations (Online Annex 2 of the October 2025 *Regional Economic Outlook: Western Hemisphere*).
- Investing in infrastructure, including digital infrastructure and logistics, reducing trade barriers, facilitating trade integration by lowering tariff and nontariff barriers, simplifying customs procedures, and expanding trade agreements and regional integration (Background Paper 2 of the October 2023 *Regional Economic Outlook: Western Hemisphere*).
- Strengthening education quality, workforce skills, research and development, and technology adoption.
- Making labor markets more flexible, dynamic, and inclusive by facilitating formal employment, worker mobility, flexible work schedules, and women's labor force participation (Background Paper 1 of the October 2024 *Regional Economic Outlook: Western Hemisphere*).

Box 1.1. The Caribbean: Coping Well with Higher Global Energy Prices

Despite higher airfares and some disruptions to global air travel after the Middle East war, tourism has performed well this year, partly offsetting the negative growth impact of higher oil prices. As one indication, stayover arrivals in the Caribbean have risen by 6 percent in the first half of 2026.¹ This strength reflects steady US demand (which accounts for one-half to two-thirds of visitors, depending on the country) and has been accompanied by some expansion of countries' capacity to absorb those visitors (Figure 1.1.1). Tourism-related investments—that aim to further increase capacity—have also supported domestic demand (even though such projects tend to have a relatively high import content).

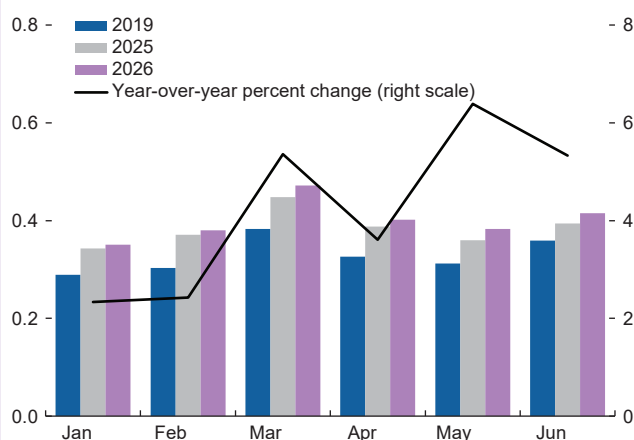
Airfares have risen, and strong demand has fed into rising accommodation costs. These price factors may become more visible as the region heads into peak tourist season. Strong consumer balance sheets and a solid labor market in source countries will likely continue to support robust tourism demand. However, some caution is warranted since surveys of tourism companies point to a slowdown of tourist inflows in the remainder of 2026.

The Caribbean has thus far experienced relatively muted inflation outturns despite the recent oil price increase. However, the full impact of these global price changes may have been delayed rather than forestalled (Figure 1.1.2). The smaller pass-through of higher global energy costs during this episode reflects several factors:

- Many economies already have in place price-smoothing mechanisms to manage volatility in global prices.
- Some have taken fiscal measures (such as fuel-tax relief, subsidies, and price caps) to insulate the population from the higher global prices.
- The energy mix for many has become less oil intensive, with renewables accounting for 11 percent of electricity generation in 2024 (3 percent higher than a decade earlier).

The region still faces large external and fiscal imbalances. The higher fuel import bill and the cost of new fiscal support measures are exacerbating these pressures which increases the urgency to undertake steps to further shift toward renewables, strengthen fiscal policy frameworks and bring down debt, improve the mechanisms that provide targeted support to poor households, and allow domestic prices to reflect international costs.

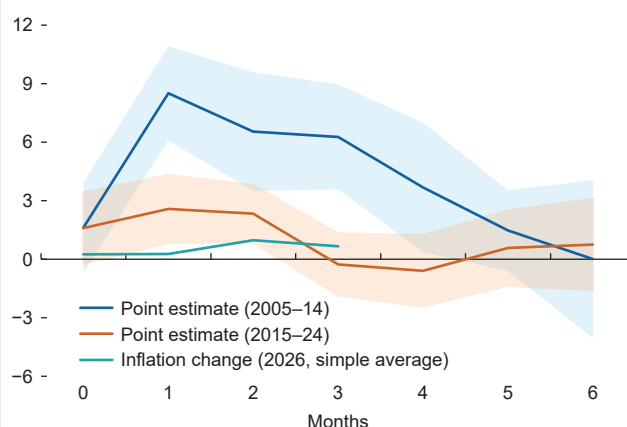
Figure 1.1.1. US Departures to the Caribbean
(Millions; unless noted otherwise)



Sources: US International Trade Administration; and IMF staff calculations.

Note: Data include 15 countries and exclude Jamaica.

Figure 1.1.2. Caribbean Inflation Response to the Oil Price Shocks
(Percentage points difference since shock month)



Source: IMF staff calculations.

Note: The oil price shock corresponds to about a 40 percent increase in oil prices, as materialized in March relative to the January–February 2026 average. The inflation response is annualized. Shaded bands represent 90 percent Driscoll–Kraay confidence intervals.

The authors of this box are Enrico Di Gregorio, Justin Matz, and Jongsoon Shin, with data support from Junghwan Mok, Spencer Siegel, and Frank Tao.

¹ Simple average of arrival growth (January–May 2026 or latest available) across tourism-dependent economies, excluding Jamaica because of the effects from Hurricane Melissa (including Jamaica, growth would be 3 percent). Source: Caribbean Tourism Organization.

Box 1.2. Remittances to Central America and US Immigration Enforcement

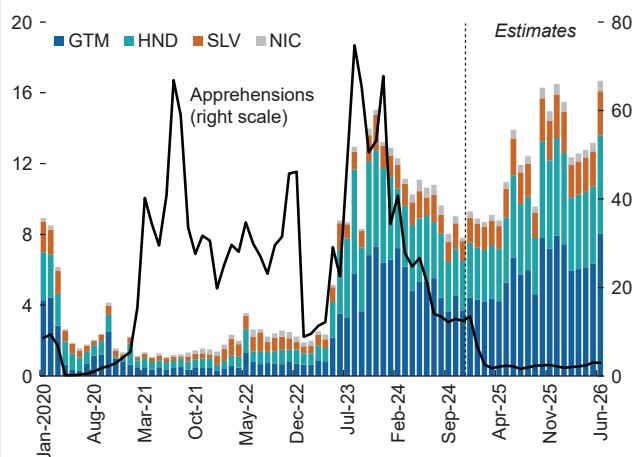
El Salvador, Guatemala, Honduras, and Nicaragua (Central America 4, CA4) received more than 20 percent of GDP in remittances in 2025. This was double the amount these countries had received on average over the past decade. These additional remittances largely originated from the United States and appear to reflect the precautionary behavior of migrants sending resources home as immigration enforcement has tightened in the United States (Figure 1.2.1).

In the first five months of 2026, remittances remain at high levels although the growth rate has slowed somewhat (Figure 1.2.2), as labor market conditions for migrant workers in the United States have softened and the level of community arrests is again rising.

Empirical analysis shows that remittance growth rises in anticipation of increased enforcement in the United States (Carare and others, forthcoming). This effect is robust even after controlling for macroeconomic conditions (Babii and others 2022; Figure 1.2.3).

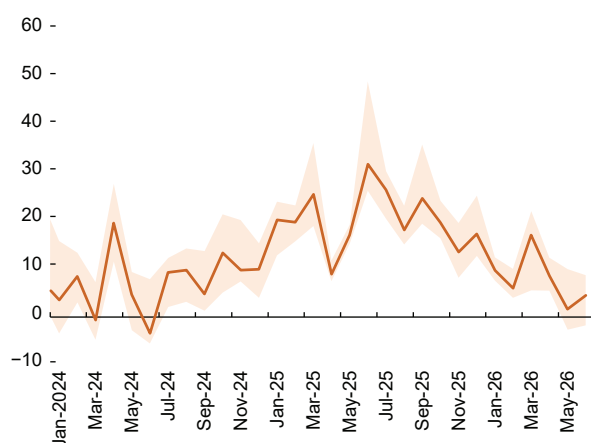
In 2027, remittance growth across the CA4 is expected to slow as precautionary transfers diminish and the number of migrant removals rises. This could weigh on the current account position, private consumption, and growth in CA4.

Figure 1.2.1. Repatriations and Border Apprehensions
(Thousands)



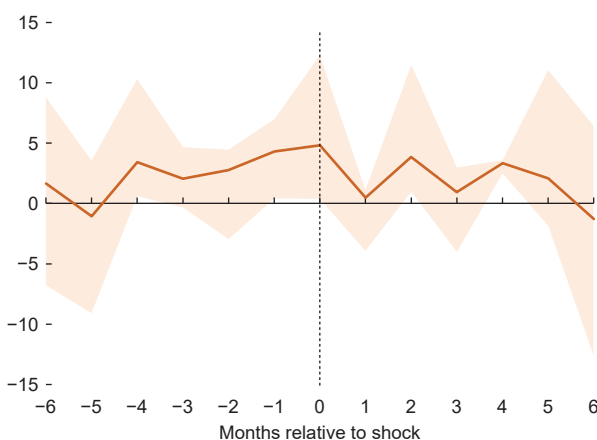
Sources: US Customs and Border Protection; US Department of Homeland Security; US Immigration and Customs Enforcement (ICE); and IMF staff estimates.

Figure 1.2.2. Remittances to CA4 Countries
(Year-over-year percent change)



Sources: Haver Analytics; national authorities; and IMF staff calculations.
Note: Nicaragua's 2025-26:H1 data are IMF staff estimates.

Figure 1.2.3. CA4: Enforcement Impact on Remittance Growth
(Percentage points)



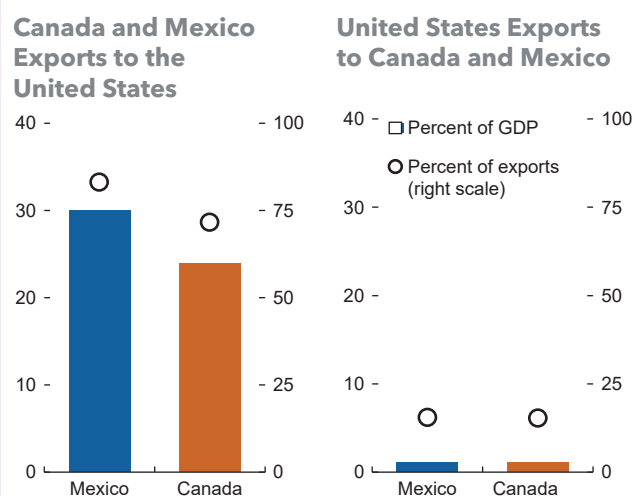
Source: IMF staff calculations.
Note: Estimated response of remittance growth to a one-unit increase in the community arrest index, equivalent to about 1,400 additional arrests in a month, based on panel local projections (Carare and others, forthcoming). Regressions include country- and time-fixed effects and macroeconomic controls. Shaded area denotes 90 percent wild cluster bootstrap confidence intervals.

Box 1.3. Preserving North American Supply-Chain Integration

The United States-Mexico-Canada Agreement (USMCA), in force since July 2020, anchors preferential trade and nontariff provisions among the United States, Mexico, and Canada. Under Article 34.7, without unanimous confirmation of a 16-year extension, the agreement remains in force and is subject to annual reviews. These annual reviews were triggered in July 2026 and will likely serve to create greater uncertainty, shorten planning horizons, delay investment and supply-chain decisions in trade-exposed sectors, and, over time, weaken North American integration.

In addition to the annual reviews of the USMCA, the United States has imposed tariffs outside of the USMCA agreement, and Canada has recently responded with its own tariffs on US products.

Figure 1.3.1. North America: Exports of Goods



Sources: Haver Analytics; national authorities; and IMF staff calculations.

Canada and Mexico depend heavily on the US market. The United States has lower aggregate exposure to Canada and Mexico but still has important linkages to the two economies through vertically integrated supply chains and sizable intra-firm trade (Figure 1.3.1). Up until the middle of 2026, about 76 percent of US imports from Canada and 77 percent from Mexico have remained duty free since the goods are compliant with the USMCA. This has kept effective US tariff rates on Canadian and Mexican goods low (at 4.8 and 3.4 percent, respectively). Mexico is particularly benefiting from strong sales of computer components and electronic equipment tied to the US technology boom.

Although average tariffs have been low, sectoral and country-specific US tariffs imposed outside of the USMCA are having important impacts. Section 232 tariffs on steel and aluminum and Section 338 tariffs on selected Canadian goods do not carry an exemption for USMCA-compliant goods. These tariffs together affect about 6 percent of Canadian goods exports to the United States, which has undermined Canadian export performance.

The current annual review of the USMCA is likely to focus on preferential access rules and related trade costs, rules of origin, external tariffs, sectoral measures, and compliance costs. Arizala and others (forthcoming) show that if the negotiated outcome were to be an increase in regional or US content requirements by 10 percentage points, this could reduce Mexico and Canada's long-term output by about 0.5–1.0 percent (with limited net impact on the United States). In this estimation, the largest sectoral losses would be in automobiles and automobile parts, as well as electronics.

The policy priority in renegotiating the USMCA should be to achieve a durable, rules-based, trade-preserving agreement that capitalizes on the strong integration of North American supply chains.

The authors of this box are Francisco Arizala and Camila Casas.

Appendix Table 1.1. Western Hemisphere: Main Economic Indicators

	Real GDP Growth (year-over-year percent change)					Inflation ¹ (end of period; percent)					External Current Account Balance (percent of GDP)				
	2024	2025	Projections			2024	2025	Projections			2024	2025	Projections		
			2026	2027	2028			2026	2027	2028			2026	2027	2028
North America	2.7	2.1	2.2	2.2	2.0	2.8	2.8	3.8	2.3	2.1	-3.7	-3.5	-3.4	-3.4	-3.2
Canada	2.0	1.9	1.1	1.7	1.7	1.9	2.2	3.2	2.0	2.0	-0.5	-0.9	-0.1	-0.2	-0.2
Mexico	1.5	0.5	1.5	1.8	2.2	4.2	3.7	3.6	3.3	3.0	-0.9	-0.5	-0.3	-0.5	-0.7
United States	3.0	2.3	2.3	2.3	2.1	2.7	2.8	3.9	2.2	2.0	-4.1	-3.8	-3.9	-3.8	-3.6
Puerto Rico ²	3.2	0.3	-0.1	1.0	0.6	1.9	1.9	4.4	2.8	2.3	...	...	...	...	...
South America	2.4	2.9	2.1	2.4	2.8	16.7	8.0	8.4	5.9	4.5	-1.3	-1.6	-1.1	-1.2	-1.4
Argentina	-1.4	4.5	2.1	3.5	4.2	118	31.5	29.5	18.0	12.5	0.9	-1.1	0.6	0.6	0.7
Bolivia	-1.1	-1.6	-3.0	-1.5	0.5	10.0	20.4	14.2	10.7	8.7	-2.4	-1.9	1.6	1.0	0.4
Brazil	3.4	2.3	2.2	1.9	2.4	4.8	4.3	4.8	3.8	3.0	-3.0	-2.9	-2.4	-2.0	-2.1
Chile	2.8	2.5	0.6	2.6	2.4	4.5	3.4	4.2	3.0	3.0	-1.2	-1.2	-0.3	-1.5	-1.4
Colombia	1.5	2.6	2.2	2.3	2.4	5.2	5.1	6.7	4.8	3.8	-1.7	-2.4	-2.6	-3.4	-3.4
Ecuador	-1.9	3.7	2.7	2.5	2.7	0.5	1.9	2.8	1.9	1.5	5.7	5.9	4.6	4.6	4.4
Paraguay	4.7	6.6	4.5	4.0	3.8	3.8	3.1	3.1	3.5	3.5	-3.3	-2.5	-2.8	-3.0	-2.6
Peru	3.5	3.4	3.0	2.9	3.2	2.0	1.5	4.4	2.2	2.0	2.4	3.5	4.0	3.0	2.0
Uruguay	3.3	1.8	1.3	2.4	2.2	5.5	3.7	4.5	4.5	4.5	-0.8	-0.5	-0.9	-1.0	-1.2
Venezuela	8.9	9.0	5.0	7.0	...	47.9	475	337	140	...	2.3	0.6	-1.0	-3.4	...
CAPDR	3.9	3.7	4.2	4.0	4.1	1.8	2.1	3.7	3.4	3.1	-0.4	1.0	-0.3	-0.7	-0.7
Costa Rica	4.1	4.6	3.3	3.5	3.5	0.8	-1.2	0.7	2.2	2.4	-0.9	-0.6	-1.5	-1.6	-1.4
Dominican Republic	5.0	2.1	4.6	4.4	4.6	3.3	5.0	4.9	4.8	4.0	-3.0	-1.2	-1.5	-1.7	-1.6
El Salvador	2.6	3.9	4.5	4.0	3.3	0.3	0.9	3.0	2.1	1.8	-2.8	-3.5	-4.8	-3.0	-2.1
Guatemala	3.7	4.3	4.0	3.8	3.9	1.7	1.7	4.4	3.7	3.7	2.9	4.7	3.6	3.1	2.4
Honduras	3.6	3.8	3.3	3.4	4.1	3.9	5.0	6.7	4.2	4.0	-4.4	2.4	-2.0	-3.5	-3.6
Nicaragua	3.6	4.9	3.8	3.8	3.5	2.8	2.7	4.0	3.5	3.0	5.0	9.5	6.4	4.0	4.2
Panama	2.7	4.4	5.0	4.2	4.6	-0.2	0.4	2.5	1.8	2.0	0.7	-0.2	-1.5	-2.5	-2.7
Caribbean	12.1	6.1	8.0	7.4	6.4	6.1	6.2	6.1	5.4	5.0	2.0	1.6	3.9	1.3	3.2
Caribbean: Tourism Dependent	2.1	2.0	1.4	2.3	2.0	2.7	2.6	4.6	3.5	3.2	-2.7	-3.9	-6.8	-5.8	-4.9
Antigua and Barbuda	2.5	3.0	2.4	2.5	2.5	5.4	3.1	4.5	2.3	2.0	-7.5	-11.6	-12.7	-11.9	-11.2
Aruba	5.5	6.3	3.7	2.7	2.0	0.3	0.4	2.3	2.2	2.0	9.8	11.6	10.5	9.9	9.3
The Bahamas	4.2	3.8	2.5	1.9	1.8	0.0	2.3	5.2	3.2	2.2	-8.1	-8.3	-9.3	-8.7	-8.0
Barbados	3.4	2.7	1.8	2.2	2.1	0.4	1.6	3.7	2.3	2.4	-3.7	-5.9	-6.3	-6.2	-5.5
Belize	3.5	2.6	1.9	2.0	2.0	2.6	0.4	4.5	1.6	1.3	-1.6	-2.8	-5.2	-4.2	-3.2
Dominica	3.5	4.5	3.1	2.8	2.7	2.1	0.7	3.1	1.5	2.2	-37.8	-38.7	-35.7	-28.5	-21.6
Grenada	3.2	4.8	3.9	3.0	2.9	0.8	0.6	2.0	1.8	2.0	-21.2	-23.1	-22.8	-18.8	-17.9
Jamaica	-0.5	0.1	0.0	2.4	1.8	5.0	4.5	5.4	5.0	5.0	2.9	1.5	-5.1	-3.6	-2.4
St. Kitts and Nevis	1.7	1.5	1.8	2.3	2.4	1.9	0.9	3.6	3.2	2.5	-13.0	-14.4	-16.2	-15.4	-13.7
St. Lucia	4.8	-0.6	1.2	1.8	1.6	0.9	-0.2	3.8	2.3	2.3	-1.5	-5.2	-5.8	-4.9	-4.0
St. Vincent and the Grenadines	4.5	2.4	2.3	2.4	2.7	2.1	0.5	5.0	2.2	2.0	-17.1	-16.4	-17.2	-15.2	-13.8
Caribbean: Non-Tourism Dependent	17.3	8.2	11.0	9.6	8.2	7.9	8.0	6.8	6.2	5.7	5.6	5.5	10.4	5.3	7.6
Haiti ³	-4.2	-2.7	-1.7	-0.5	0.7	27.9	31.9	16.0	15.0	12.7	1.5	1.4	1.3	0.2	-0.8
Commodity Exporters	23.5	10.9	13.8	11.6	9.5	2.7	2.6	4.9	4.5	4.5	7.5	7.8	15.3	8.4	12.9
Guyana	43.8	19.3	22.3	16.8	9.2	2.9	2.5	5.7	5.2	5.4	16.5	21.4	31.6	17.5	20.6
Suriname	1.0	4.0	4.0	4.1	28.2	10.1	11.4	12.4	8.3	5.6	-13.4	-53.3	-51.0	-51.4	-8.7
Trinidad and Tobago	2.6	-0.5	0.2	2.2	3.1	0.5	0.4	1.2	1.8	2.0	2.5	5.0	5.6	8.1	7.5
<i>Memorandum</i>															
Western Hemisphere	2.7	2.4	2.2	2.3	2.3	5.5	3.9	4.8	3.1	2.6	-3.3	-3.2	-3.0	-3.1	-2.9
Latin America and the Caribbean	2.4	2.5	2.3	2.5	2.9	12.2	6.5	6.8	5.0	4.1	-1.1	-1.0	-0.7	-0.9	-1.0
LAC (simple average)	3.9	3.5	3.0	3.2	3.8	7.3	4.8	5.7	4.2	3.7	-2.9	-4.0	-4.2	-4.4	-2.6
LAC excluding Argentina and Venezuela	2.8	2.2	2.3	2.3	2.7	4.2	4.0	4.6	3.6	3.1	-1.4	-1.1	-0.8	-1.0	-1.1
Latin America 7	2.6	1.9	2.0	2.0	2.4	4.5	3.9	4.5	3.6	3.0	-1.7	-1.5	-1.1	-1.3	-1.4
Latin America 8	2.1	2.2	2.0	2.2	2.6	13.7	6.9	7.2	5.2	4.1	-1.4	-1.5	-1.0	-1.1	-1.2
Eastern Caribbean Currency Union ⁴	3.6	2.1	2.4	2.4	2.3	2.2	0.9	3.6	2.2	2.1	-8.6	-10.6	-10.9	-10.1	-8.7

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

Note: Regional output growth aggregates are purchasing-power-parity GDP-weighted averages. Consumer price index inflation aggregates exclude Venezuela and are geometric purchasing-power-parity GDP-weighted averages. Current account aggregates are US dollar nominal GDP-weighted averages. See Country Notes for details on the data. Data in this table have been compiled based on information available through September 30, 2026, but may not reflect the latest published data in all cases. For the date of the last data update for each economy, please refer to the notes provided in the online World Economic Outlook database. CAPDR = Central America, Panama, and the Dominican Republic; LAC = Latin America and the Caribbean; Latin America 7 = Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay; Latin America 8 = Latin America 7 plus Argentina.

¹These figures will generally differ from period average inflation reported in the IMF *World Economic Outlook*, although both are based on the same underlying series.

²Puerto Rico is classified as an advanced economy. It is a territory of the United States, but its statistical data are maintained on a separate and independent basis.

³Fiscal year data.

⁴Eastern Caribbean Currency Union comprises Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat (which are not IMF members).

Appendix Table 1.2. Western Hemisphere: Main Fiscal Indicators

	General Government Primary Expenditure (percent of GDP)					General Government Primary Balance (percent of GDP)					General Government Gross Debt (percent of GDP)				
	2024	2025	Projections			2024	2025	Projections			2024	2025	Projections		
			2026	2027	2028			2026	2027	2028			2026	2027	2028
North America	33.5	33.4	33.7	33.0	32.9	-4.2	-3.5	-4.4	-3.5	-3.4	117.7	120.0	121.9	123.4	126.5
Canada	40.9	40.6	41.1	40.9	40.7	-2.1	-1.9	-2.6	-2.3	-2.1	110.0	113.6	115.6	113.4	111.8
Mexico	24.2	23.2	22.8	22.8	22.2	0.2	1.2	1.7	1.8	1.9	59.0	61.7	62.1	62.9	63.4
United States	33.6	33.5	34.0	33.2	33.1	-4.6	-3.9	-4.9	-4.0	-3.9	122.3	124.4	126.8	128.7	132.3
Puerto Rico ¹	21.2	21.7	21.1	20.4	18.7	0.4	0.4	0.4	0.4	0.1	16.8	17.6	18.2	18.5	18.6
South America	32.5	32.1	33.0	32.7	32.3	-0.6	-0.7	-0.6	-0.3	0.3	78.0	82.5	80.6	81.8	81.8
Argentina	29.3	29.7	29.2	29.2	29.0	2.2	1.3	1.7	2.1	2.2	84.6	80.1	69.3	70.4	65.6
Bolivia	29.0	25.6	23.4	20.3	19.3	-6.1	-8.8	-6.5	-3.0	-0.3	83.2	83.3	100.2	95.1	93.0
Brazil	37.4	37.0	38.5	38.3	38.0	-0.3	-0.1	-0.3	-0.1	0.4	87.0	93.3	97.0	99.3	101.3
Chile	25.6	25.0	25.0	24.4	24.1	-2.1	-2.0	-1.3	-0.8	-0.7	41.8	41.5	42.8	44.5	46.0
Colombia	30.1	30.4	30.8	30.4	29.8	-2.2	-3.5	-3.4	-2.5	-1.2	61.0	59.9	59.5	62.9	65.1
Ecuador	36.0	36.0	...	...	...	-0.1	-1.7	...	...	...	54.1	54.5	...	...	...
Paraguay	18.9	17.9	19.3	19.3	17.1	-0.1	0.2	-1.4	-1.4	0.8	44.6	38.2	36.6	37.9	37.1
Peru	20.7	19.9	19.4	19.4	19.2	-2.2	-1.0	0.0	-0.2	-0.2	32.1	30.1	28.6	29.0	29.4
Uruguay	28.4	29.4	29.8	29.8	29.7	-1.0	-1.3	-2.1	-1.2	-0.6	67.6	65.6	67.7	68.7	69.7
Venezuela	20.1	21.1	...	...	...	-5.0	-4.5	...	...	...	...	...	...	...	...
CAPDR	17.0	16.6	16.8	16.6	16.4	0.0	0.3	0.2	0.3	0.5	51.4	51.1	51.2	51.0	50.5
Costa Rica	13.8	13.5	13.3	13.0	12.7	1.0	0.9	0.9	0.8	0.9	58.9	60.4	61.8	62.8	63.3
Dominican Republic	16.1	15.9	16.0	15.7	15.4	0.3	-0.1	-0.1	0.1	0.4	58.8	59.0	57.2	55.3	54.3
El Salvador	27.2	25.9	25.5	24.8	24.7	0.0	1.9	2.9	3.6	3.7	87.7	87.6	85.0	89.2	87.3
Guatemala	11.8	12.9	13.4	14.0	13.7	0.7	-0.3	-1.0	-1.3	-1.1	26.3	26.7	27.5	28.4	29.2
Honduras	23.5	22.8	22.9	23.2	23.3	-0.4	-0.3	-0.2	-0.4	-0.3	42.2	40.3	44.0	42.3	41.3
Nicaragua	24.4	24.0	25.1	24.8	24.8	4.0	4.7	3.5	3.6	3.6	37.9	34.6	31.7	28.8	28.4
Panama	20.2	17.9	18.5	17.8	17.4	-3.3	-0.7	-0.4	0.0	0.4	57.8	56.6	56.4	55.9	54.9
Caribbean	20.8	20.8	19.9	19.3	19.0	1.2	-0.2	-0.8	0.4	0.9	55.9	55.2	50.2	47.4	45.6
Caribbean: Tourism Dependent	23.0	23.6	24.3	23.4	22.9	3.6	2.7	1.5	2.3	2.9	72.7	73.0	71.1	69.1	67.6
Antigua and Barbuda	17.9	17.5	20.8	20.3	20.0	4.0	4.9	1.0	0.7	0.9	71.6	70.2	66.8	65.8	64.7
Aruba	17.7	17.3	18.4	18.7	18.8	8.2	7.7	5.8	4.8	4.6	72.5	64.8	59.6	56.1	53.3
The Bahamas	16.9	16.8	17.7	18.2	17.8	2.7	3.6	3.6	3.9	4.3	73.0	71.7	70.2	65.4	62.9
Barbados	23.2	22.7	25.1	23.3	22.6	4.0	4.2	3.5	3.5	4.1	98.9	96.2	93.8	88.4	84.3
Belize	24.2	23.6	23.9	24.0	23.8	1.0	1.3	-0.4	-0.4	0.4	64.3	66.9	64.6	65.8	66.5
Dominica	65.1	55.5	49.6	41.6	40.6	-4.3	1.8	1.6	1.3	1.6	108.2	99.9	99.7	97.1	93.4
Grenada	33.8	34.5	39.3	28.5	28.3	10.0	-1.5	-9.4	1.5	1.5	72.8	69.4	66.8	67.2	67.5
Jamaica	24.9	27.4	27.6	26.5	25.8	5.4	2.3	0.5	2.0	2.7	62.5	66.0	64.3	64.0	63.2
St. Kitts and Nevis	43.1	41.3	39.7	38.1	36.4	-10.0	-10.5	-7.8	-5.6	-3.2	58.1	58.7	65.1	69.2	71.6
St. Lucia	21.6	22.2	22.4	22.1	22.1	0.8	1.4	0.2	0.4	0.5	75.9	76.8	78.1	78.2	78.4
St. Vincent and the Grenadines	40.7	37.6	33.5	34.7	33.4	-16.0	-9.9	-5.7	-7.1	-5.8	102.8	107.7	111.6	117.1	121.8
Caribbean: Non-Tourism Dependent	19.0	18.9	17.3	16.9	16.7	-0.6	-2.3	-2.2	-0.8	-0.1	42.8	42.5	37.4	34.9	33.4
Haiti	5.0	5.1	5.3	5.3	6.0	7.2	0.0	-0.3	-0.3	-0.8	15.1	12.3	10.5	9.4	9.3
Commodity Exporters	25.5	26.5	23.7	23.9	23.6	-4.2	-3.6	-3.2	-1.0	0.3	55.6	59.4	51.8	50.2	48.7
Guyana	22.3	23.1	18.5	19.5	20.2	-7.0	-5.1	-5.6	-2.6	-1.9	24.3	28.9	25.3	26.0	27.1
Suriname	27.6	34.0	27.1	23.9	19.5	0.4	-4.6	-0.1	1.1	4.9	84.0	96.9	85.1	72.1	52.1
Trinidad and Tobago	28.3	28.7	30.8	30.8	30.2	-2.2	-1.9	-0.4	1.0	2.4	81.0	84.0	84.6	83.1	81.6
<i>Memorandum</i>															
Western Hemisphere	33.2	33.0	33.4	32.7	32.5	-3.7	-3.1	-3.8	-3.1	-2.9	112.5	114.9	115.9	117.4	120.0
Latin America and the Caribbean	28.8	28.4	28.8	28.5	28.1	-0.3	-0.1	0.0	0.3	0.8	70.4	74.1	72.9	73.7	73.6
LAC (simple average)	25.7	25.3	25.3	24.3	23.7	-0.3	-0.6	-0.7	0.1	0.8	68.5	72.6	68.8	67.4	65.5
LAC excluding Argentina and Venezuela	28.9	28.4	28.8	28.5	28.1	-0.5	-0.2	0.0	0.2	0.7	66.5	69.0	70.4	71.7	72.5
Latin America 7	30.1	29.6	30.1	29.9	29.4	-0.5	-0.1	0.0	0.2	0.7	68.4	71.4	72.9	74.6	75.8
Latin America 8	30.0	29.6	30.0	29.8	29.4	-0.2	0.0	0.2	0.4	0.8	70.1	72.4	72.5	74.2	74.8
Eastern Caribbean Currency Union ²	31.3	30.7	31.0	28.3	27.8	-0.2	-0.5	-2.0	-0.4	0.0	74.2	73.8	74.3	74.9	75.2

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

Note: Government coverage varies across countries, depending on country-specific institutional differences, including on what constitutes the appropriate coverage from a fiscal policy perspective, as defined by the IMF staff. See Country Notes for details on the data. All indicators are reported on a fiscal year basis. Regional aggregates are fiscal year US dollar nominal GDP-weighted averages. Data in this table have been compiled based on information available through September 30, 2026, but may not reflect the latest published data in all cases. For the date of the last data update for each economy, please refer to the notes provided in the online World Economic Outlook database. CAPDR = Central America, Panama, and the Dominican Republic; LAC = Latin America and the Caribbean; Latin America 7 = Brazil, Chile, Colombia, Mexico, Paraguay, Peru, Uruguay; Latin America 8 = Latin America 7 plus Argentina.

¹Puerto Rico is classified as an advanced economy. It is a territory of the United States, but its statistical data are maintained on a separate and independent basis.

²Eastern Caribbean Currency Union comprises Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat (which are not IMF members).

Country Notes

Argentina. The official national consumer price index (CPI) starts in December 2016. For earlier periods, CPI data for Argentina reflect the Greater Buenos Aires Area CPI (prior to December 2013); the national CPI (IPCNu, December 2013 to October 2015); the City of Buenos Aires CPI (November 2015 to April 2016); and the Greater Buenos Aires Area CPI (May 2016 to December 2016). Given limited comparability of these series because of differences in geographic coverage, weights, sampling, and methodology, the WEO does not report average CPI inflation for 2014–16 and end-of-period inflation for 2015–16. In addition, Argentina discontinued the publication of labor market data starting in the fourth quarter of 2015, and new series became available starting in the second quarter of 2016.

Bahamas, The. Coverage of fiscal series is central government.

Barbados. Overall and primary balances cover budgetary central government. Gross debt covers central government debt, central government guaranteed debt, and arrears.

Belize. Coverage of fiscal series is central government.

Bolivia. Nonfinancial public sector is reported excluding the operations of nationalized mixed-ownership companies in the hydrocarbon and electricity sectors.

Brazil. Nonfinancial public sector is reported excluding Petrobras and Eletrobras and consolidated with the Sovereign Wealth Fund. The definition includes treasury securities on the central bank's balance sheet, including those not used under repurchase agreements (repos). The national definition of general government gross debt includes the stock of Treasury securities used for monetary policy purposes by the central bank (those pledged as security in reverse repo operations). It excludes the rest of the government securities held by the central bank.

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

Costa Rica. The central government definition was expanded as of January 1, 2021, to include 51 public entities in accordance with Law 9524. Data back to 2019 are adjusted for comparability.

Dominican Republic. The fiscal series have the following coverage: Public debt, debt service, and the cyclically adjusted/structural balances are for the consolidated public sector (which includes the central government, the rest of the nonfinancial public sector, and the central bank); the remaining fiscal series are for the central government.

Eastern Caribbean Currency Union (ECCU). For all countries, coverage for primary expenditure and primary balance is central government; public sector gross debt is reported.

Ecuador. Fiscal projections for 2026–31 are excluded from publication because of ongoing program discussions. Public sector gross debt includes liabilities under advance oil sales, which are not treated as public debt in the authorities' definition. In late 2016, the authorities changed the definition of debt to a consolidated basis; both the historical and projection numbers are now presented on a consolidated basis.

El Salvador. The coverage of fiscal data is the nonfinancial public sector. Gross debt is presented on a consolidated basis. In 2027, gross debt includes the recognition of accrued but unpaid interest to private pension funds for US\$2,329 million.

Guatemala. Coverage of fiscal series is central government.

Guyana. Coverage of fiscal series is central government, including the National Insurance Scheme for primary expenditure and primary balance.

Haiti. Coverage of fiscal series is central government.

Jamaica. Central government is reported for primary expenditure and primary balance. Public debt includes central government, guaranteed, and PetroCaribe debt.

Mexico. Fiscal series have the following coverage: central government, social security system funds, nonfinancial public corporations, and nonmonetary public financial corporations. Primary expenditure and balance include the Petróleos Mexicanos' (PEMEX) Fondo de Pago a Proveedores (FPP), in accordance with GFSM guidelines. Gross debt includes the Special Purpose Vehicle (SPV) that issued pre-capitalized notes (P-Caps) to support PEMEX and the FPP, in accordance with GFSM guidelines.

Nicaragua. Coverage for primary expenditure and primary balance is general government. Gross debt is presented on a consolidated basis.

Panama. Ratios to GDP are based on the 2018-base GDP series. Fiscal data cover the nonfinancial public sector excluding the Panama Canal Authority.

Paraguay. Coverage of fiscal series for the WEO is broader than the budgetary central government, which is used by the authorities to measure fiscal rules and targets.

Peru. Gross debt is that of the nonfinancial public sector.

Suriname. Coverage of fiscal series is central government. Primary expenditures exclude net lending.

Trinidad and Tobago. Fiscal accounts, including the primary and overall balances, cover the budgetary central government only and exclude the transactions of the social security system. Gross debt refers to public sector debt and includes central government debt and guaranteed debt of non-self-serviced state-owned enterprises and statutory authorities. It excludes short-term monetary policy liabilities matched by government deposits and temporary central bank overdraft advances. Debt data are reported on a non-consolidated basis and exclude self-serviced, non-guaranteed debt of state-owned enterprises and statutory authorities. Net debt refers to gross debt less the government's position in the Heritage and Stabilisation Fund (HSF) and deposits with the central bank.

United States. For cross-country comparability, expenditure and fiscal balances of the United States exclude the items related to the accrual-basis accounting of government employees' defined-benefit pension plans, which are counted as expenditure under the 2008 System of National Accounts (2008 SNA) adopted by the United States but not for countries that have not yet adopted the 2008 SNA. Data for the United States in Appendix Table 1.2 may thus differ from data published by the US Bureau of Economic Analysis.

Uruguay. In December 2020, the authorities began reporting national accounts data according to the SNA 2008, with base year 2016. The new series begin in 2016. Data prior to 2016 reflect the IMF staff's best effort to preserve previously reported data and avoid structural breaks.

Starting in October 2018 *Uruguay's* public pension system received transfers in the context of Law 19,590 of 2017, which compensates people affected by the creation of the country's mixed pension system. These funds are recorded as revenues, consistent with the IMF's methodology. See IMF Country Report 19/64 for further details.¹ The disclaimer about the public pension system applies only to the revenues and net lending/borrowing series.

¹ Uruguay Staff Report for the 2018 Article IV Consultation, Country Report 19/64 (Washington, DC: International Monetary Fund, February 2019).

The coverage of the fiscal data for *Uruguay* was changed from consolidated public sector to nonfinancial public sector with the October 2019 WEO. In *Uruguay*, nonfinancial public sector coverage includes the central government, local government, social security funds, nonfinancial public corporations, and Banco de Seguros del Estado. Historical data were also revised accordingly. Under this narrower fiscal perimeter—which excludes the central bank—assets and liabilities held by the nonfinancial public sector, for which the counterpart is the central bank, are not netted out in debt figures. In this context, capitalization bonds issued in the past by the government to the central bank are now part of the nonfinancial public sector debt.

Venezuela. Historical series have been revised to incorporate official data where this has been made available, particularly for the balance of payments and national accounts at the aggregate level. Nominal GDP in US dollars is derived by converting local currency GDP using staff estimates of a representative exchange rate reflecting the official and parallel market rates. Fiscal accounts are estimated by staff from 2018 onward and cover the budgetary central government, public enterprises (including Petróleos de Venezuela, S.A.), the Instituto Venezolano de los Seguros Sociales (IVSS), and the Fondo de Garantía de Depósitos y Protección Bancaria (FOGADE). Estimates of public debt are not published due to market sensitivity considerations.

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2. The Missing Link: From Foreign Direct Investment to Trade and Productivity Gains¹

This chapter analyzes why the Latin America and the Caribbean (LAC) region's sizable foreign direct investment (FDI) inflows have not translated into commensurate increases in exports and trade integration. Evidence from a gravity framework suggests that the region has a weaker trade-FDI nexus relative to peer emerging markets, with foreign investment generating smaller export gains and exports attracting less follow-on FDI. Sector-level analysis suggests that this gap reflects both the sectoral composition of FDI and weaker trade-investment synergies within sectors, particularly in manufacturing. Among the factors examined, weak innovation and technology-absorption capacity and less developed trade logistics emerge as the largest contributors to LAC's weaker export response to FDI. Reducing financial, regulatory, and trade barriers could further strengthen trade and investment performance and increase the broader productivity gains associated with FDI.

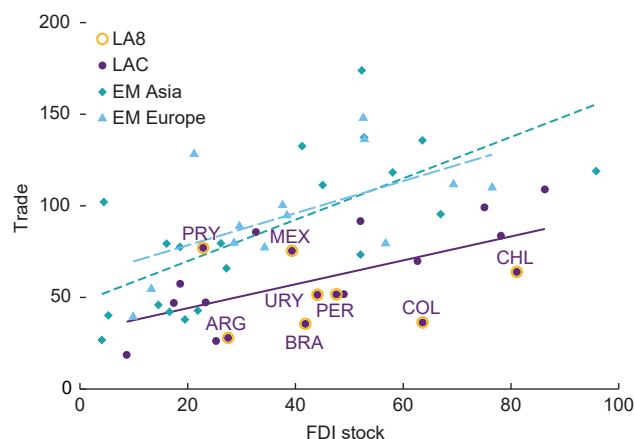
Introduction

Latin America and the Caribbean (LAC) has attracted substantial foreign direct investment (FDI) but it remains less integrated into international trade than many peer emerging market (EM) regions. The stock of inward FDI in the region was valued at about \$3 trillion in 2024, equivalent to 44 percent of LAC GDP, compared with 25 percent in Asian EMs and 21 percent in European EMs. Trade as a share of GDP, by contrast, remains well below that of peer EMs, and intraregional trade is particularly limited (Figure 2.1). This coexistence of high FDI and comparatively weak trade raises a central question: why has FDI in LAC not translated into stronger trade linkages?

This question is especially important in today's environment, where elevated trade frictions are raising the prospect of lasting shifts in global production, sourcing, and investment.

Trade and FDI often reinforce each other through direct economic linkages. The literature generally shows that inward FDI is associated with stronger host-country exports and higher export quality. Inward FDI can expand export capacity, provide access to technology and managerial know-how, boost imported inputs, and connect firms to regional and global markets. Strong export performance, in turn, can attract further FDI by signaling a competitive production base and reliable access to foreign markets.

Figure 2.1. Trade and Inward FDI Stock, 2024
(Percent of GDP)



Sources: United Nations Conference on Trade and Development; World Bank, World Development Indicators database; and IMF staff calculations.

Note: Trade is the sum of exports and imports of goods and services as a percent of GDP. Inward FDI stock is expressed as a percent of GDP. Country groups based on the *World Economic Outlook* database. Data labels use International Organization for Standardization (ISO) country codes. Economies with inward FDI stocks above 100 percent of GDP are excluded. LAC includes LA8. EM = emerging markets; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

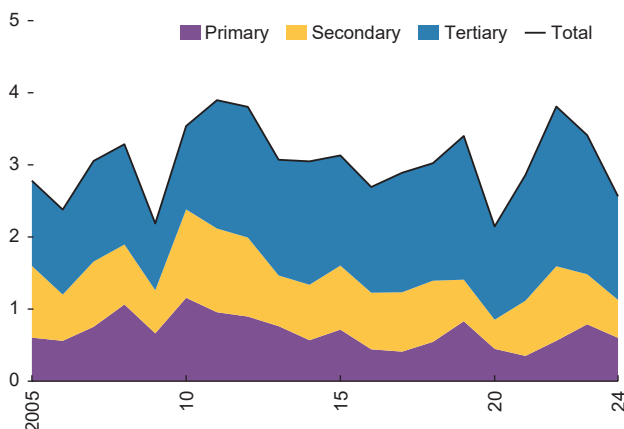
¹ Prepared by Robin Koepke (lead), Olusegun A. Akanbi, Eric Huang, and Nicolás Gómez Parra. The team thanks Samuel Pienknagura, Alfredo Alvarado, Longmei Zhang, Robert Zymek, and Monika Sztajerowska for helpful comments. Hannah Wei, Thomas Elkjaer, and Jannick Damgaard provided data and advice on FDI measurement. The team also thanks Saad Ahmad and Heather Wickramarachi (US International Trade Commission) for sharing insights. The team thanks other colleagues across IMF departments and the World Bank for helpful discussions. Camila Casas contributed to the chapter proposal, and Federico Dueñas provided research assistance.

The commonly observed positive relationship between trade and FDI comes with two important caveats. First, if FDI primarily takes place to serve domestic demand, it may substitute for imports rather than expand trade. Second, even where genuine complementarities exist, they are not automatic. The trade response to foreign investment depends on the sectors receiving investment, and the domestic environment in which they operate.

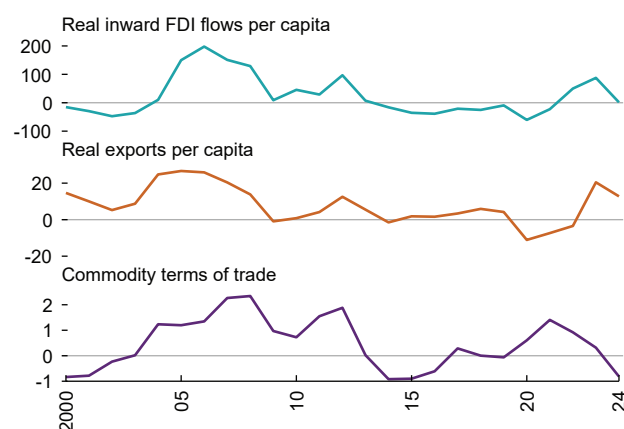
A separate empirical challenge is that trade and FDI may also move together because they share structural and cyclical drivers, rather than because one causes the other. Common structural determinants are geography, market size, comparative advantage, trade costs, institutions, and firms' production strategies, among others. Cyclical drivers are particularly relevant in LAC, where commodity price cycles can simultaneously affect commodity exports and investment in resource sectors. The commodity price downturn after 2012, for example, coincided with declines in both exports and FDI in much of the region (Figure 2.2).

Figure 2.2. Sectoral FDI Inflows and Commodity Terms of Trade in LA8*

1. Sectoral Inward FDI Flows
(Percent of GDP; annual medians)



2. Real Inward FDI Flows and Exports per Capita, and Commodity Terms of Trade
(Median percent change from three years earlier)



Sources: IMF's Commodity Terms of Trade database; national authorities; UN Trade and Development; World Bank, World Development Indicators; and IMF staff calculations.

Note: LA8* comprises Argentina, Brazil, Chile, Colombia, Paraguay, Peru, and Uruguay; Mexico is excluded. In panel 1, the sample excludes Peru because sectoral data are unavailable. Total FDI inflows are allocated among primary, secondary, and tertiary sectors using national-authority sector shares. The first and last available shares are carried backward and forward, respectively. Each stacked series is the annual median across countries, and the total line is the sum of the three sectoral medians. In panel 2, the series are medians of country-level cumulative percentage changes over three years. Real inward FDI flows and exports per capita are measured in constant 2015 US dollars. Commodity terms of trade are measured as the commodity net export price index weighted by the ratio of net commodity exports to GDP. FDI = foreign direct investment.

This chapter examines the relationship between trade and FDI in an integrated framework that recognizes the central role of multinational enterprises (MNEs) in linking foreign investment and trade. Although the analysis considers linkages in both directions, it places particular emphasis on whether inward FDI is associated with stronger export performance. Export growth is not the ultimate objective, but it is an intermediate indicator of gains in productivity, real incomes, and living standards (Frankel and Romer 1999; Javorcik 2004). Stronger exports may reflect gains from scale, technology and quality upgrading, stronger domestic supplier capabilities, and the reallocation of resources toward more efficient firms. In this sense, stronger FDI-export complementarities are consistent with foreign investment being translated more effectively into domestic productivity growth and integration into higher value-added segments of the global economy. This focus is supported by an earlier regional analysis showing that LAC's growth challenge reflects not only capital accumulation, but also

the productivity payoff from capital formation, for example, through the diffusion of technology and the efficiency of resource allocation (Background Paper 2 of the October 2023 Regional Economic Outlook: Western Hemisphere).

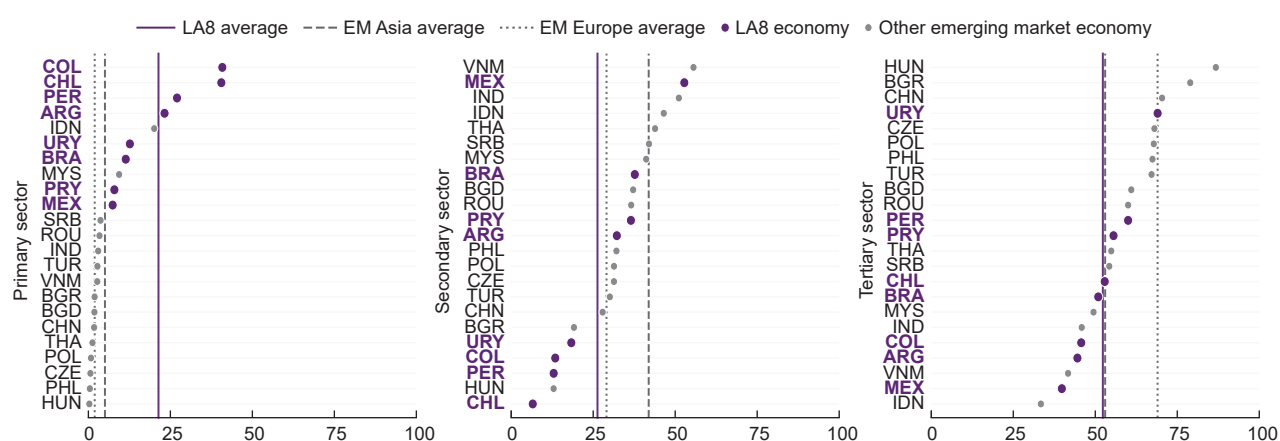
This chapter evaluates two complementary explanations for why inward FDI is less strongly associated with exports in LAC than in peer economies. First, foreign investment may be concentrated in sectors in which trade complementarities are relatively limited—a composition effect. Second, the trade-FDI relationship may be weaker even within the same sectors—a structural effect mainly reflecting differences in the broader enabling environment and multinational firms’ export orientation.

The empirical analysis proceeds in three steps. First, a gravity framework estimates the two-way relationship between bilateral trade and FDI and distinguishes the role of sectoral composition from differences in the trade-FDI relationship within sectors. Second, the analysis estimates whether domestic capabilities help explain why these complementarities are stronger in some economies than in others. Third, it assesses how barriers to trade and investment separately affect trade and FDI performance.

Explaining the Trade-FDI Disconnect in LAC

Differences in the sectoral destination of FDI provide part of the explanation of the trade-FDI disconnect in LAC. Trade-FDI complementarities tend to be strongest in manufacturing, particularly in activities that are deeply integrated into global value chains (GVCs) (Buelens and Tirpák 2017). However, FDI is concentrated relatively heavily in primary sectors in LAC, including mining, hydrocarbons, and agriculture, reflecting the region’s abundance of natural resources and the long-standing attraction of these sectors to multinational firms (Figure 2.3). This allocation broadly mirrors the region’s export structure, which remains tilted toward primary commodities, while participation in GVC-intensive manufacturing and services is more limited than that in emerging Europe and Asia.

Figure 2.3. Composition of Inward FDI Stock by Sector
(Percent of total FDI)



Sources: Banco Central do Brasil; InvestmentMap; Mexico Ministry of Economy; and IMF staff calculations.

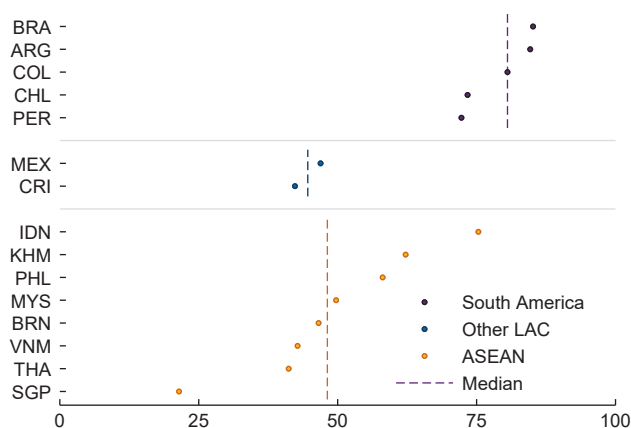
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. Proxies for the 2010–19 period.

Coverage differs by country depending on data availability. InvestmentMap harmonizes the data from national authorities. Brazil and Mexico are compiled directly from national authorities because sectoral disaggregations are not available in InvestmentMap. Stocks are preferred when available; flows are used where stock data are unavailable. Primary sector includes agriculture and extractive industries; secondary sector refers to manufacturing; and tertiary sector refers to services. Shares sum to 100 within each economy. Regional averages are simple country averages. EM = emerging markets; FDI = foreign direct investment.

Another explanation lies in the orientation of multinational activity *within* sectors. In LAC, foreign affiliates are more likely to serve domestic markets than to participate in export-oriented production networks. This difference remains pronounced even within manufacturing. In the median LAC country, domestic sales account for about 81 percent of foreign manufacturing affiliates' gross output, compared with 48 percent in ASEAN (Figure 2.4). The greater domestic-market orientation of foreign affiliates in LAC helps explain why relatively high FDI has not translated into equally strong trade linkages.

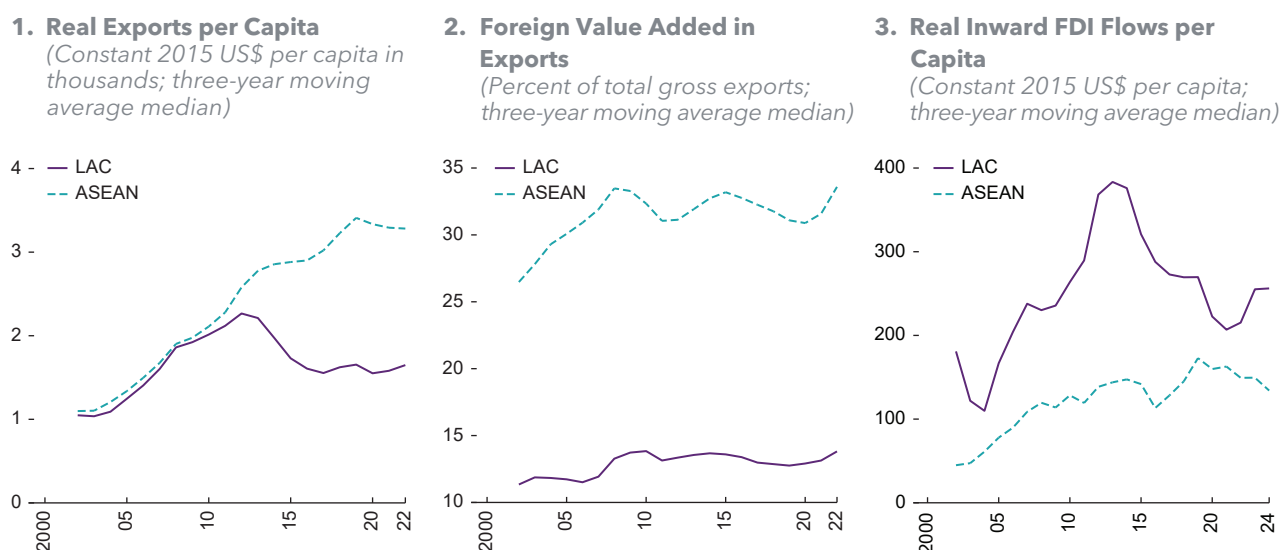
The contrast is also visible in export outcomes. Over the past 15 years, real exports per capita have grown considerably faster in ASEAN than in LAC, alongside a persistently higher share of foreign value added in ASEAN exports. This stronger export performance has occurred despite LAC receiving consistently higher inward FDI inflows per capita than ASEAN (Figure 2.5), reinforcing the point that the volume of FDI alone does not determine its contribution to trade integration.

Figure 2.4. LAC and ASEAN: Domestic Sales of Foreign Manufacturing Affiliates
(Percent of total gross output)



Sources: OECD's Analytical Activity of Multinational Enterprises database; and IMF staff calculations.
Note: Domestic sales are calculated as gross output less exports. Country shares are calculated after summing gross output and exports over 2021-23; dashed lines show unweighted medians across countries by country group. Data labels use International Organization for Standardization (ISO) country codes. The LAC sample comprises Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, and Peru; the ASEAN sample comprises Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. ASEAN = Association of Southeast Asian Nations; LAC = Latin America and the Caribbean.

Figure 2.5. LAC and ASEAN: Exports, Foreign Value Added, and FDI Inflows



Sources: OECD TiVA 2025; UNCTAD; World Bank, World Development Indicators; and IMF staff calculations.

Note: Exports and inward FDI inflows are deflated using the U.S. GDP deflator and divided by population. Regional series are three-year moving averages of median country-year values. The harmonized sample includes Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, and Peru for LAC; and Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam for ASEAN. ASEAN = Association of Southeast Asian Nations; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

Main Gravity Analysis: The Trade-FDI Nexus

Gravity Framework

This section examines how LAC's trade-FDI nexus differs from that of peer economies and what accounts for those differences. The analysis uses a novel gravity framework that tracks bilateral trade and multinational activity across country pairs, sectors, and years (see Online Annex 2 for details), with a rich set of fixed effects to account for confounding factors such as supply and demand shocks, exchange rates, economic size, and standard gravity variables such as distance and cultural and political ties. This level of detail permits like-for-like comparisons in both directions: whether investment from a given country in a particular sector is followed by higher exports to that country in the same sector, and whether stronger export relationships subsequently attract additional investment.²

The framework also captures broader spillovers. FDI in one sector or from one partner may be associated with export gains in other sectors or markets by strengthening supplier linkages, diffusing knowledge, or creating new connections to GVCs.

Main Findings

Three main findings emerge from the gravity analysis:

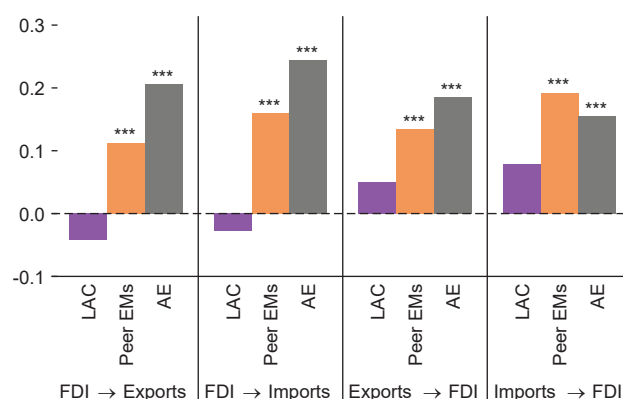
- **The trade-FDI nexus is weaker in LAC than in peer EMs and advanced economies.**

The estimates point to a positive two-way relationship between trade and FDI in peer EMs and advanced economies. Inward investment is followed by higher exports and imports, whereas stronger trade relationships are followed by stronger follow-on investment. In peer economies, a 1 percent increase in FDI is followed by a 0.1–0.2 percent increase in same-sector imports and exports with the FDI-origin country, with positive relationships of a similar magnitude from imports and exports to subsequent FDI (Figure 2.6).

By contrast, the aggregate relationship is weaker in LAC. In particular, inward FDI shows little systematic association with subsequent exports back to the country of origin. This could reflect the sectoral composition of FDI, weaker trade complementarities within sectors, or domestic conditions that limit the extent to which multinational activity supports export production.

The following sectoral analysis distinguishes between the first two explanations. A subsequent exercise examines the extent to which differences in domestic capabilities are associated with the remaining gap, particularly LAC's weaker ability to convert inward FDI into export growth.

Figure 2.6. Aggregate Trade-FDI Nexus
(Coefficients)



Sources: International Trade and Production Database for Estimation (ITPD-E) (Borchert and others 2021; Larch, Shikher, and Yotov 2025); Multinational Revenue, Employment, and Investment Database (MREID) (Ahmad and others 2025); and IMF staff calculations.

Note: Statistical significance is denoted by *, **, and *** for the 10, 5, and 1 percent levels, respectively. AE = advanced economy; EMs = emerging markets; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

² The gravity estimation relies on the Multinational Revenue, Employment, and Investment Database, built from firm-level Orbis data (Ahmad and others 2025). The literature validates Orbis against administrative records and identifies it as well suited to large and high-performing firms such as multinational enterprises, with weaker coverage limited to parts of Africa and Asia (Gopinath and others 2017; Bajgar and others 2020; Ahmad and others 2025). Evidence on announced investment activity uses Orbis Crossborder Investment, which compiles project-level greenfield and M&A announcements from news aggregators, press releases, company websites, and stock-exchange and regulatory filings rather than from firm balance sheets, linking each project to the investing firm and its global ultimate owner.

- **Relative to peer EMs, LAC exhibits weaker FDI-to-export linkages in manufacturing and weaker export-to-FDI linkages in primary sectors.**

At the sector level, LAC's trade-FDI nexus differs from that of peer EMs in both directions (Figure 2.7).

From FDI to subsequent exports. Two patterns stand out in goods-producing sectors:³

- In manufacturing, inward FDI is less strongly associated with subsequent exports in LAC than in peer EMs.
- In primary sectors, the linkage between inward FDI and subsequent exports is broadly comparable across the two groups.

From exports to subsequent FDI. LAC is broadly aligned with peer EMs in most sectors. The main exception is the primary sector, where exports are less strongly associated with subsequent inward FDI.

Taken together, these results show that LAC's weaker aggregate trade-FDI nexus reflects not only sectoral composition but also weaker linkages within sectors.

On the FDI-to-export side, the gap is concentrated in manufacturing, the sector most closely associated with export-intensive participation in GVCs. On the export-to-FDI side, the gap is concentrated in primary sectors, where LAC receives a comparatively large share of foreign investment.

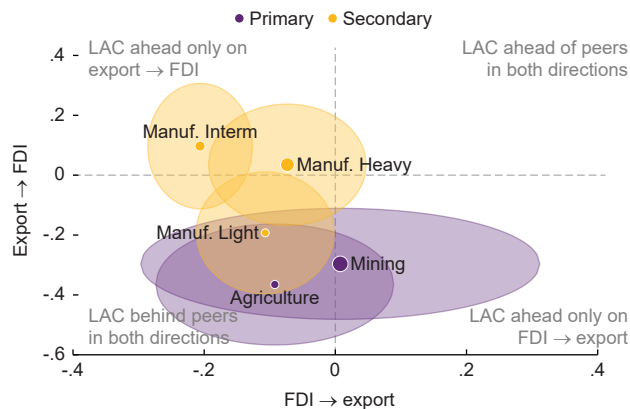
One possible explanation for the weaker export-to-FDI linkage in LAC's primary sectors is that the large existing stock of foreign-invested production capacity allows exports to expand without requiring substantial new investment. Investment decisions may also depend on factors such as resource endowments and commodity price cycles that are only weakly related to recent export performance. In addition, a substantial portion of LAC's resource exploitation is undertaken by domestic firms, which tends to weaken the link between FDI and commodity exports. The gravity estimates do not distinguish between these mechanisms.

- **LAC's exports could be substantially higher if they responded to inward FDI as strongly as in peer EMs.**

FDI may affect exports beyond the sector receiving the investment and the FDI-origin country, including through supplier linkages, knowledge diffusion, and connections to GVCs. To illustrate the economic significance of LAC's weaker FDI-export nexus, the analysis considers a counterfactual in which LAC retains its current level and sectoral allocation of FDI but matches peer EMs' sector-specific export elasticities to FDI, including both direct export responses to the FDI-origin country in the receiving sector and indirect export spillovers across other destination markets and sectors. The exercise is intended as an illustrative benchmark rather than a forecast. Figure 2.8 shows the implied change in exports by sector and in aggregate.

The counterfactual results show that LAC's weaker FDI-export nexus remains even after accounting for the indirect export spillovers. In this counterfactual scenario, LAC's aggregate exports would be more than 20 percent higher, mostly because of stronger direct export responses to FDI. The largest gains occur in intermediate manufacturing, where exports rise by about 54 percent, followed by heavy manufacturing. These are also the sectors in which

Figure 2.7. LAC-EM Gap in the Export-FDI Nexus by Sector (Coefficients)



Sources: International Trade and Production Database for Estimation (ITPD-E) (Borchert and others 2021; Larch, Shikher, and Yotov 2025); Multinational Revenue, Employment, and Investment Database (MREID) (Ahmad and others 2025); and IMF staff calculations.

Note: Shaded region represents the 90 percent confidence intervals along each axis. Marker size indicates the export volume in LAC. Tertiary sectors are included in the estimation but omitted in the figure. EMs = emerging markets; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

³ This chapter focuses on goods-producing sectors because (1) merchandise exports are measured more consistently and accurately than services exports, and (2) international service delivery often occurs through foreign affiliates rather than cross-border exports, making exports and FDI conceptually less distinct in services industries.

LAC shows the largest gap relative to peers in the relationship between foreign investment and exports.

The implied gains in primary sectors are more limited, despite the relatively large share of FDI they receive in LAC, as FDI is only weakly associated with export gains in those sectors. This reinforces the broader conclusion that attracting foreign investment is not sufficient by itself: the export benefits depend on the strength of the link between investment and tradable production.

These estimates should be interpreted cautiously. The exercise holds the level and allocation of FDI fixed and abstracts from changes in prices, resource allocation, capacity constraints, and other general equilibrium responses. Such adjustments could moderate the implied gains. The exercise also assumes that LAC could attain the elasticity of exports to inward FDI observed in peer EMs. Doing so would likely require wide-ranging improvements in the domestic conditions that support export-oriented multinational activity.

The next exercise examines whether differences in domestic conditions help explain LAC's weaker export response to inward FDI.

Strengthening the FDI Ecosystem to Unlock Export Gains

If inward FDI is less strongly associated with subsequent exports in LAC relative to peer economies, an important question is what domestic conditions may help explain this pattern. One way to assess these conditions is through a set of indicators of absorptive capacity. Absorptive capacity refers to a country's ability to translate multinational activity into domestic production, supplier linkages, knowledge diffusion, and cross-border trade (Borensztein, De Gregorio and Lee 1998).

Strong linkages between MNE affiliates and domestic firms depend on reliable supplier networks, efficient logistics, adequate skills, access to finance, and effective contract enforcement. Weaknesses in these areas will limit the extent to which foreign investment translates into stronger exports.

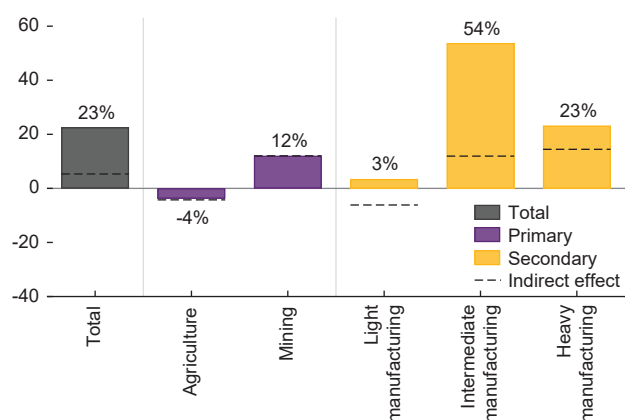
Therefore, the analysis examines how the relationship between inward FDI and subsequent exports varies with several dimensions of absorptive capacity, and then combines these estimates with observed gaps between LAC and peer EMs. This provides an indication of how much LAC's export response to FDI could strengthen if domestic capabilities moved closer to peer levels.

Because these dimensions are correlated, the estimates should not be interpreted as additive contributions or as identifying the causal effect of each individual factor.

The analysis considers five indicators on which LAC, on average, lags peer EMs (Figure 2.9):

- **Innovation and technology absorption:** the capacity to adopt and adapt technologies introduced by multinational firms, thus allowing local production to expand around foreign affiliates.
- **Infrastructure and trade logistics:** the cost, speed, and reliability of moving goods across borders and through the domestic economy.

Figure 2.8. LAC's Export Gain from Closing the Nexus Gap (Percent)



Sources: International Trade and Production Database for Estimation (ITPD-E) (Borchert and others 2021; Larch, Shikher, and Yotov 2025); Multinational Revenue, Employment, and Investment Database (MREID) (Ahmad and others 2025); and IMF staff calculations.

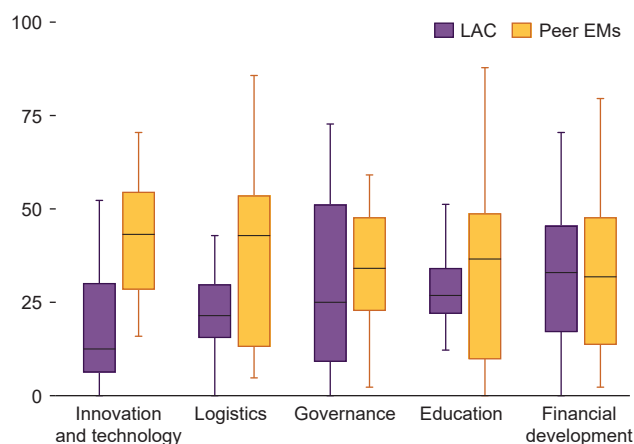
Note: The bars show each sector's export gain or loss in a counterfactual scenario where LAC matches peer EMs' FDI-export elasticities from the direct and indirect spillover specifications. The indirect effect captures export responses in destination countries and sectors other than the FDI-origin country and the sector receiving the investment. Each sector's FDI spillover to exports in other sectors is allocated according to those sectors' baseline export shares. Each bar is the sum of the direct and indirect effects. Tertiary sectors are included in the estimation but omitted in the figure. EMs = emerging markets; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

- **Institutional quality and governance:** contract enforcement, regulatory quality, and the rule of law, which affect affiliates' ability to rely on local suppliers, distributors, and legal institutions.
- **Education and human capital:** workforce capabilities, which influence the sophistication of activities undertaken locally and the types of FDI a country can attract.
- **Financial development:** the ability of domestic firms to finance the investment and working capital required to participate in multinational supply chains as suppliers or distributors.

The two largest contributors to the LAC-peer EM gap in the responsiveness of exports to inward FDI are innovation and technology absorption and infrastructure and trade logistics, accounting for 30 and 23 percent of the gap, respectively (Figure 2.10). The first result is consistent with the idea that FDI generates larger export gains when domestic firms can learn from, adopt and adapt the technologies and business practices introduced by multinational firms. The importance of logistics points to a complementary channel: even when firms have the capacity to produce for external markets, high transport costs, customs delays, and unreliable infrastructure can weaken their ability to participate in regional and GVCs. Together, these results show that the strength of the trade-FDI nexus depends not only on where foreign investment has been made, but also on whether domestic capabilities allow that investment to translate into broader export gains.

Figure 2.9. LAC versus Peer EMs: Absorptive Capacity Indicators

(Percentile; latest since 2020)

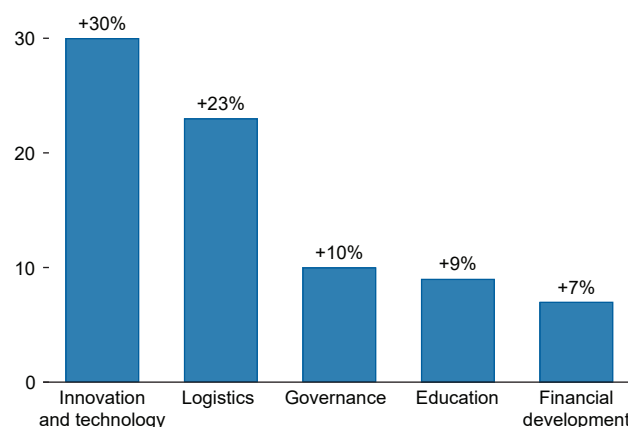


Sources: IMF, Financial Development Index database; OECD, Programme for International Student Assessment; World Bank, Logistics Performance Index and Worldwide Governance Indicators; World Intellectual Property Organization; and IMF staff calculations.

Note: Values are percentile ranks, with higher values indicating stronger absorptive capacity. For each indicator, the latest available country observation from 2020 onward is used. Percentiles are calculated across LAC12, 17 selected peer EMs, and 16 advanced economies; the figure displays only LAC and peer EMs. Boxes span the 25th–75th percentiles, horizontal lines indicate medians, and whiskers show the most extreme observations. Governance is the average of the Worldwide Governance Indicators; logistics is the overall Logistics Performance Index; innovation and technology is resident patent applications per million population; education is the combined mathematics, reading, and science score (Programme for International Student Assessment); and financial development is the IMF Financial Development Index. Data labels in the figure use International Organization for Standardization (ISO) country codes. EMs = emerging markets; LAC = Latin America and the Caribbean; LAC12 = ARG, BOL, BRA, CHL, COL, CRI, ECU, MEX, PAN, PER, TTO, URY; peer EMs = ALB, ARE, BGR, GEO, HUN, IDN, KAZ, MAR, MDA, MKD, MYS, PHL, POL, QAT, SRB, THA, TUR.

Figure 2.10. Gains in LAC's Export Response to FDI from Closing Absorptive Capacity Gaps

(Percent share of LAC-peer EM elasticity gap)



Sources: International Trade and Production Database for Estimation (ITPD-E) (Borchert and others 2021; Larch, Shikher, and Yotov 2025); Multinational Revenue, Employment, and Investment Database (MREID) (Ahmad and others 2025); and IMF staff calculations.

Note: Bars show the increase in LAC's elasticity of exports with respect to inward FDI from matching peer EM absorptive capacity, as a share of the total LAC-peer EM elasticity gap. EMs = emerging markets; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

Opening the Gates to Trade and FDI

Domestic capabilities determine how effectively FDI translates into trade and productivity gains. However, policy barriers operate upstream, constraining trade and foreign investment directly before any question of conversion arises. Barriers to trade, investment, and business activity can reduce exports and FDI even where domestic capabilities are relatively strong. Therefore, reducing these barriers can raise trade and investment directly, while also creating more opportunities for the two to reinforce each other.

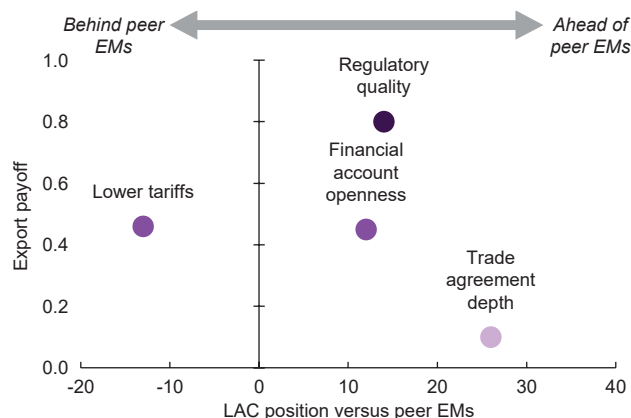
This section examines four policy dimensions—market-oriented regulation, financial account openness, tariffs, and preferential trade agreements—and asks where LAC has the greatest scope for improvement and where reforms are associated with the largest gains in exports or FDI. The analysis uses a gravity framework similar to that in Section “Main Gravity Analysis: The Trade-FDI Nexus” (see Online Annex 2).⁴ The analysis pools observations across sectors as the policies are expected to affect all sectors simultaneously.

Figure 2.11 summarizes the potential policy priorities emerging from the analysis. It combines LAC’s current position relative to comparator economies with the estimated trade or FDI payoff associated with improving each policy lever. Policies located toward the upper left indicate relatively large policy gaps and high estimated payoffs from reform. Those toward the lower right indicate stronger starting positions and smaller estimated marginal gains.

Figure 2.11. Opportunity Maps: Exports and FDI

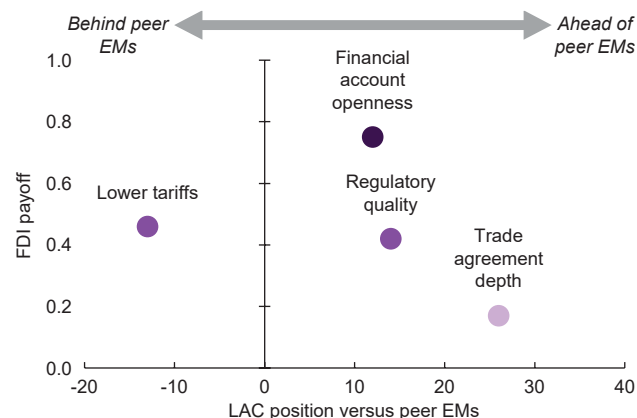
1. Policy Position versus Exports Payoff

(y-axis: elasticity; x-axis: percentile-point gap, higher = more supportive of trade and FDI compared to peer EMs)



2. Policy Position versus FDI Payoff

(y-axis: elasticity; x-axis: percentile-point gap, higher = more supportive of trade and FDI compared to peer EMs)



Sources: Chinn-Ito Index; Design of Trade Agreements (DESTA) database (Dür, Baccini, and Elsig 2014); Global Tariff Database (Teti 2024); Orbis Crossborder Investment (OCBI); World Bank Worldwide Governance Indicators; and IMF staff calculations.

Note: Each marker shows one of four policy areas. The horizontal axis shows the gap, in percentile points, between the LAC median and the median for peer EMs; positive values indicate that the LAC median is ahead of the peer EM median in the policy-supportive direction, and negative values indicate that it is behind. Tariffs are direction-adjusted, so that lower tariffs correspond to a more policy-supportive position. The vertical axis shows the estimated payoff from a more supportive policy position, for exports (panel 1) and for FDI (panel 2), expressed as elasticities. EM = emerging market; FDI = foreign direct investment; LAC = Latin America and the Caribbean.

⁴ The policy dimensions examined in this section are not the only determinants of trade and investment outcomes. Other policies can influence both the volume and characteristics of FDI, including bilateral investment treaties, double-taxation agreements, and the taxation of multinational activity. Investment-promotion policies, such as investment-promotion agencies, special economic zones, and supplier-development programs, can also affect the export orientation of foreign investment and the extent of linkages between multinational firms and domestic suppliers. Although these channels are not incorporated directly into the empirical analysis, they may complement the policy reforms discussed earlier by helping attract and retain export-oriented investment and strengthening its contribution to trade and productivity.

Quality of Market-Oriented Regulation

Market-oriented regulation captures operational aspects of openness, such as time, cost, and uncertainty involved in obtaining trade-related permits, clearing customs, and complying with standards. These aspects of regulatory quality are found to be a key enabling condition for both exports and FDI. Figure 2.11 suggests that LAC is ahead of peer EMs on this dimension, but that the estimated payoff from further improvement—especially for exports—remains relatively high. This suggests that even moderate regulatory frictions can have sizable effects on firms’ ability to trade and invest.

Therefore, reforms that simplify regulatory processes and make them more predictable and more transparent can reduce trade costs and investment uncertainty. Priorities include streamlined customs and licensing procedures, interoperable digital platforms, transparent tax administration, and strong contract enforcement. The experience of El Salvador’s border-process reform (Box 2.1) illustrates how targeted regulatory improvements can help translate formal openness into export gains.

Financial Account Openness

Financial openness is associated with stronger FDI and may also support exports indirectly. Figure 2.11 suggests that while LAC is more financially open than several peer EMs, the estimated payoff from further openness—particularly for FDI—remains relatively high. Fewer restrictions on cross-border capital flows can facilitate foreign investment, profit repatriation, and access to external financing (see Online Annex 2).

Greater financial openness can also support exports by improving access to trade finance, foreign exchange hedging, working capital, imported capital goods, and technology. These channels help domestic firms participate in multinational production networks and allow foreign affiliates to operate on a greater scale.

However, the benefits of greater financial openness depend on the broader macrofinancial environment. Credible macroeconomic policies, deeper local financial markets, sound prudential regulation, exchange rate flexibility, and predictable investment rules help channel openness toward productive FDI and export capacity while containing risks from volatile capital flows. The Dominican Republic and Chile cases discussed in Box 2.1 illustrate this distinction.

Tariffs

LAC faces comparatively high trade barriers and appears particularly sensitive to foreign tariff changes. Figure 2.11 suggests that lower tariffs are associated with moderate gains in both exports and FDI. The estimates also indicate that LAC’s exports and inward FDI are more adversely associated with higher bilateral tariffs than those of advanced economies and peer EMs (see Online Annex 2).

The tariffs captured in the estimates are those imposed by trading partners on LAC exports and therefore are not directly under the control of LAC policymakers. They nevertheless underscore the importance of market access for both trade and investment. Domestic tariff policy can complement efforts to improve market access, particularly where liberalization is reciprocal, while also lowering the cost of imported intermediate inputs, capital goods, and technology.

Therefore, policy priorities may include shoring up firms’ access to imported inputs and capital goods, particularly in an environment of global trade frictions. Peru’s experience, discussed in Box 2.1, illustrates the “imports-for-exports” channel: lower tariffs on machinery and intermediate inputs were associated with faster productivity growth and broader participation in GVCs.

Tariff reform will be most effective when accompanied by complementary regulatory and fiscal reforms that facilitate implementation, address revenue implications, and help firms translate lower trade costs into stronger export and investment outcomes.

Preferential Trade Agreements

LAC's trade agreement architecture is already relatively deep. Figure 2.11 suggests that LAC is already well ahead of peer EMs in preferential trade agreement depth, while the estimated payoff from additional deepening is smaller than for other policy levers. Deeper agreements are nevertheless associated with stronger exports and FDI, although the estimated response is weaker in LAC than in peer economies.

This suggests that the main challenge is not simply to negotiate deeper agreements, but to make existing agreements work better. Complex rules of origin, weak domestic regulatory frameworks, and limited firm capabilities can prevent firms from fully benefiting from market-access commitments. Deeper provisions on services, investment, standards, and regulatory cooperation can support export upgrading, but only if they are enforceable, transparent, and complemented by domestic reforms. The Costa Rica and Mexico cases in Box 2.1 show how deep and credible agreements can anchor export-oriented investment and regional supply chains, whereas the case of Vietnam illustrates how market-access commitments, combined with domestic investment reform, can support structural upgrading.

Policy Implications and Conclusion

LAC has been relatively successful in attracting a sizable presence of multinational firms, but less successful in converting that presence into exports and broader productivity spillovers. The analysis of the trade-FDI nexus and related policy levers points to scope for strengthening the channels through which multinational activity supports exports and broader productivity gains.

Three findings stand out. First, LAC's trade-FDI nexus is weaker than in peer EMs. Second, the gap is concentrated in manufacturing rather than primary sectors, suggesting that foreign investment is less effectively linked to export-oriented production in the sectors where trade complementarities are typically strongest. Third, innovation and technology-absorption capacity, as well as trade logistics, appear to explain the largest share of the weaker export response to inward FDI.

These findings matter particularly as nearshoring and geopolitical fragmentation may create new opportunities for LAC to attract export-oriented investment. Recent FDI announcements point to a prospective increase in multinational activity across several sectors (Figure 2.12). However, announced projects do not necessarily translate into realized investment, and realized investment does not automatically generate stronger export integration. The gains will depend both on whether investment is directed toward tradable, GVC-linked activities and on whether host economies have the domestic capabilities needed to generate linkages with local firms.

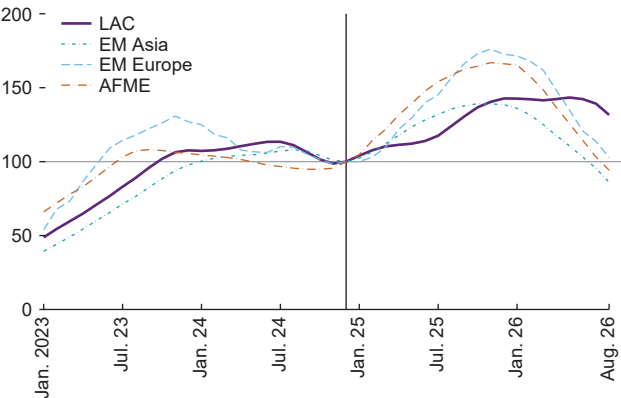
Figure 2.13 summarizes these findings with a simple analogy. FDI brings a flow of capital, technology, managerial know-how, and links to international production networks. Trade and investment openness form the gate, influencing the volume and type of investment that enters and whether foreign affiliates can import inputs and serve regional and global markets. The domestic ecosystem is the mill: it determines how effectively those opportunities are converted into local sourcing, exports, productivity, and growth. When the gate is only partly open, part of the flow does not reach productive use; when the mill is weak, the flow that does arrive is not fully converted into exports, productivity, and growth.

The empirical results point to two complementary policy priorities. The first is to reduce barriers to trade and investment. Reducing barriers to imported intermediates, making trade and investment rules more predictable, improving customs and logistics, making fuller use of trade agreements, and lowering intraregional trade costs can reduce the cost of serving regional and third markets. These reforms can also strengthen the commercial case for export-platform, vertical, and GVC-linked investment.

Figure 2.12. FDI Announcements and Trade

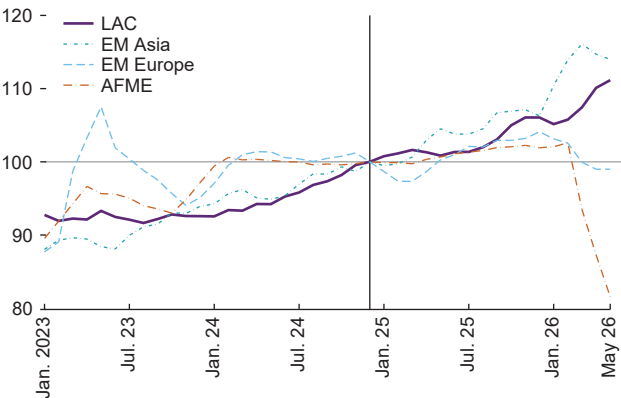
1. FDI Greenfield Announcements¹

(Index, December 2024=100; 12-month rolling sum, three-month moving average)



2. Goods Trade Volume in Emerging Markets²

(Index, December 2024=100; three-month moving average)



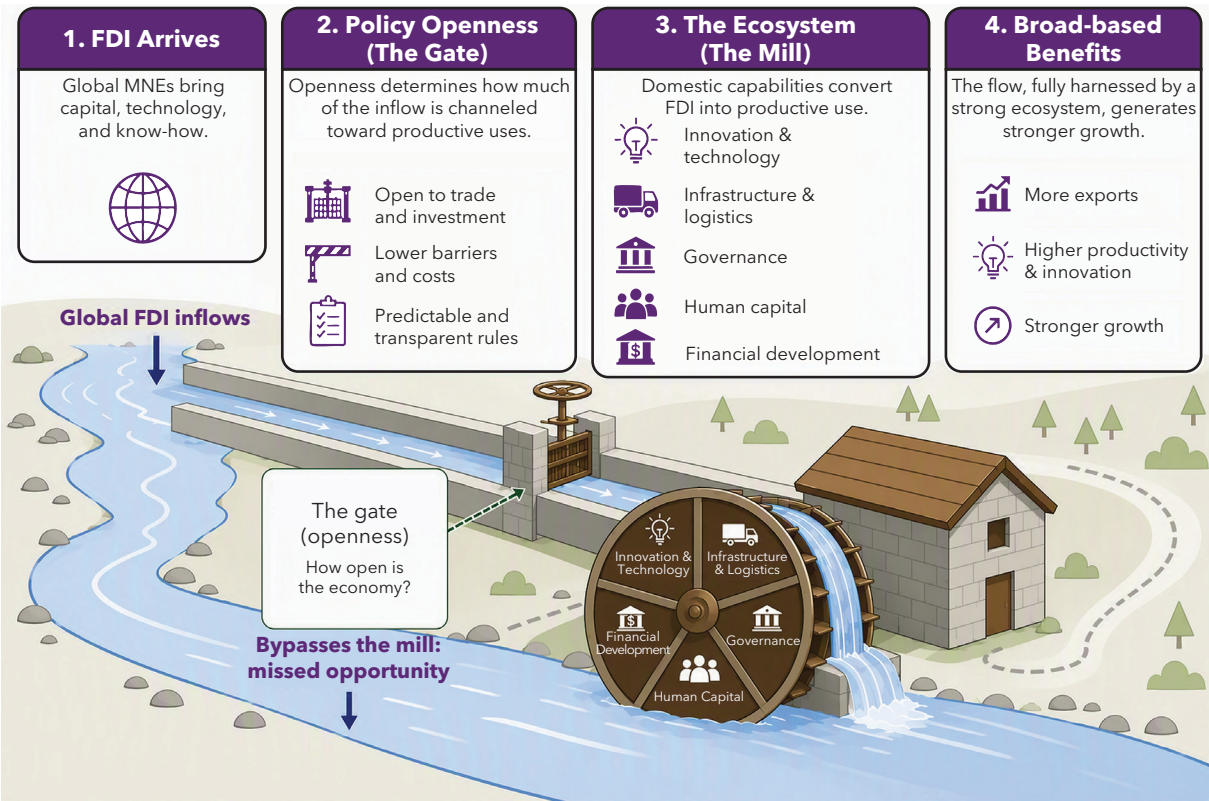
Sources: CPB Netherlands Bureau for Economic Policy Analysis, World Trade Monitor; Orbis Crossborder Investment (OCBI); and IMF staff calculations.

Note: LAC = ARG, BOL, BRA, CHL, COL, CRI, DOM, ECU, GTM, MEX, PRY, PER, and URY; EM Asia = IND, IDN, MYS, PAK, PHL, THA, and VNM (China excluded); EM Europe = BLR, KAZ, RUS, and UKR; AFME = DZA, IRN, IRQ, ISR, KEN, KWT, MAR, OMN, QAT, SAU, ZAF, TZA, ARE, and ZMB. Data labels in the figure use International Organization for Standardization (ISO) country codes. Regions follow the World Trade Monitor definitions. AFME = Africa and the Middle East; EM = emerging market; LAC = Latin America and the Caribbean.

¹ Lines show the number of announced greenfield/expansion projects, indexed to December 2024 = 100. Multi-country projects are counted once per destination country. Series are computed as a 12-month rolling sum and smoothed with a 3-month moving average.

² Lines show seasonally adjusted merchandise (goods) trade volumes by region, rebased so that December 2024 = 100 (vertical line). Regional import and export volume indices are as published in the CPB World Trade Monitor; for each region the two legs are combined using 2021 trade values as weights, and the series is smoothed with a trailing three-month moving average.

Figure 2.13. Harnessing the FDI Flow: Opening the Gate and Strengthening the Mill



Note: FDI = foreign direct investment; MNEs = multinational enterprises.

The second priority is to strengthen domestic absorptive capacity. Greater innovation and technology-absorption capacity help domestic firms learn from foreign production practices and meet multinational standards. Supplier-development programs, stronger workforce and managerial skills, and better access to trade and small and medium enterprises finance can enable local firms to invest in certification, technology, working capital, and production capacity. These measures can deepen local sourcing and strengthen the diffusion of knowledge from foreign affiliates to the wider economy.

Taken together, these reforms can help LAC derive greater domestic benefits from the sizable presence of foreign MNEs while improving the conditions for attracting additional productivity-enhancing FDI. Export growth is not the ultimate objective, but an intermediate sign that foreign investment is becoming more deeply embedded in domestic production networks and supporting higher productivity and living standards. Over time, these gains can generate a virtuous cycle in which stronger domestic capabilities deepen linkages with multinational firms, encourage further investment, and support continued upgrading. Macroeconomic stability, fiscal sustainability, and policy predictability remain essential foundations for sustaining this cycle.

Box 2.1. Lessons from Successful Trade and FDI Reforms

Implemented reforms across Latin America and the Caribbean (LAC) and comparator economies suggest that openness delivers the largest and most durable gains when market access, investment rules, macroeconomic credibility, and domestic trade facilitation reinforce one another.

Deep trade and investment agreements. Costa Rica's 2009 implementation of CAFTA-DR combined preferential market access with binding investor protection, regulatory transparency, and the opening of telecommunications and insurance. Supported by the rebound in global trade after the global financial crisis, exports to the United States rose by about 50 percent by 2012; FDI reached 5.1 percent of GDP, and FDI in the service sector increased from about 2 percent of total FDI inflows before 2004 to 39 percent in 2012 (Koehler-Geib and Sanchez 2015). Mexico provides a longer-term benchmark: The North American Free Trade Agreement locked in preferential access, national treatment, investor protections, and transfer rights, and is estimated to have raised FDI flows by roughly 60–70 percent relative to a no-agreement counterfactual scenario, thereby helping anchor export-oriented North American supply chains (Cuevas, Messmacher, and Werner 2005).¹ Vietnam's 2005 Investment Law and 2007 World Trade Organization accession similarly widened foreign entry, for example, through wholly foreign-owned firms and mergers and acquisitions and locked in phased services liberalization. High-technology products subsequently rose from 8.7 percent of manufactured exports in 2008 to 41.4 percent in 2017 (UNCTAD 2008; World Bank 2020b). These experiences indicate that agreement depth and credible implementation can matter more than tariff preferences alone by reducing policy uncertainty and supporting export-platform FDI.

Lower tariffs and the “imports-for-exports” channel. Peru's unilateral tariff reductions in the 2000s lowered the cost of imported machinery and intermediate inputs and were associated with faster firm productivity growth and the expansion and diversification of global-value-chain exports (Pierola, Fernandes, and Farole 2018; World Bank 2020a). China's World Trade Organization-era package illustrates the same complementarity at scale: the average import tariff fell from 17.2 percent in 2001 to 10.6 percent in 2005, whereas sectoral and geographic restrictions on FDI and local-content requirements were relaxed. FDI inflows increased from \$47 billion to \$72 billion over the period (Liu 2022). The common lesson is that tariff reform generates stronger export and investment payoffs when firms can access high-quality inputs and foreign investors face fewer operating restrictions.

Table 2.1.1. Selected Evidence from Eight Cases

Case / Lever	Selected Outcome
Costa Rica Trade agreement	Exports to United States increased by 50 percent; FDI reached 5.1 percent of GDP; service sector FDI increased by 37 percent of FDI.
Mexico Trade agreement	NAFTA estimated to have raised FDI about 60–70 percent versus a no-agreement counterfactual scenario.
Peru Tariff reduction	Lower input costs; faster productivity; broader GVC exports.
Dominican Republic FX openness	FDI rose from about 1.5 to 3.5 percent of GDP from the mid-1990s.
Chile Financial account openness	Opening financial account plus flexible FX and inflation targeting supported a stronger 2008–09 policy response.
El Salvador Regulation	Exports under the new regulatory system increased by 44–54 percent.
China Tariff reduction	Tariff fell from 17.2 to 10.6 percent; FDI rose from \$47 billion to \$72 billion, 2001–05.
Vietnam Investment law and WTO accession	High-tech export share of manufacturing rose from 8.7 to 41.4 percent, 2008–17.

Note: Magnitudes are study-specific and combine causal estimates with carefully interpreted before-after evidence. FDI = foreign direct investment; FX = foreign exchange; GVC = global value chain; NAFTA = North American Free Trade Agreement; WTO = World Trade Organization.

¹ The North American Free Trade Agreement (NAFTA) was replaced by the United States-Mexico-Canada Agreement (USMCA) in 2020. The evidence discussed here is based on studies that analyzed NAFTA's impact while it was in force.

Box 2.1. (continued)

Financial openness with macroeconomic safeguards. In the 1990s, the Dominican Republic embarked on a series of reforms, including reducing restrictions on trade, exchange rates, capital flows, and foreign investment. Building on these reforms, the 2002 Monetary and Financial Law further liberalized the foreign exchange regime and eased conversion and transfer restrictions. Together, these reforms contributed to a large increase in FDI, from 1.5 percent of GDP to about 3.5 percent of GDP, starting in the middle of the 1990s. Chile's post-1999 shift toward a more open capital account, flexible exchange rate, and inflation targeting illustrates the complementary macroeconomic architecture. During the 2008-09 shock, this framework permitted a stronger countercyclical response than under the tighter regime prevailing in 1997-98 (Carrière-Swallow and García-Silva 2013). The Chilean evidence is primarily about resilience rather than a clean trade- or FDI flow effect. Together, the cases support a sequenced approach: convertibility and repatriation rights improve investor confidence, but their benefits are strongest when accompanied by macroeconomic stability, exchange rate flexibility, and a credible legal framework.

Regulatory and border-process reform. El Salvador's electronic International Transit of Merchandise system replaced multiple paper forms with a single interoperable document linking customs, migration, and sanitary agencies across borders. Export flows using the system rose by approximately between 44 percent and 54 percent, with benefits of about \$14 per dollar invested (Carballo and others 2021). This shows that targeted regulatory reforms can produce large returns by lowering shipment-level fixed costs, especially when neighboring agencies and countries use compatible systems.

Overall Lessons

Openness reforms are most effective as a package. Deep agreements provide durable market access, lower tariffs improve input access, financial openness enables capital entry and repatriation, and streamlined regulation turns formal access into actual trade and investment (Table 2.1.1). Outcomes should not be mechanically compared across countries because initial barriers, macroeconomic conditions, implementation capacity, infrastructure, and export capabilities shape the payoff of reforms.

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