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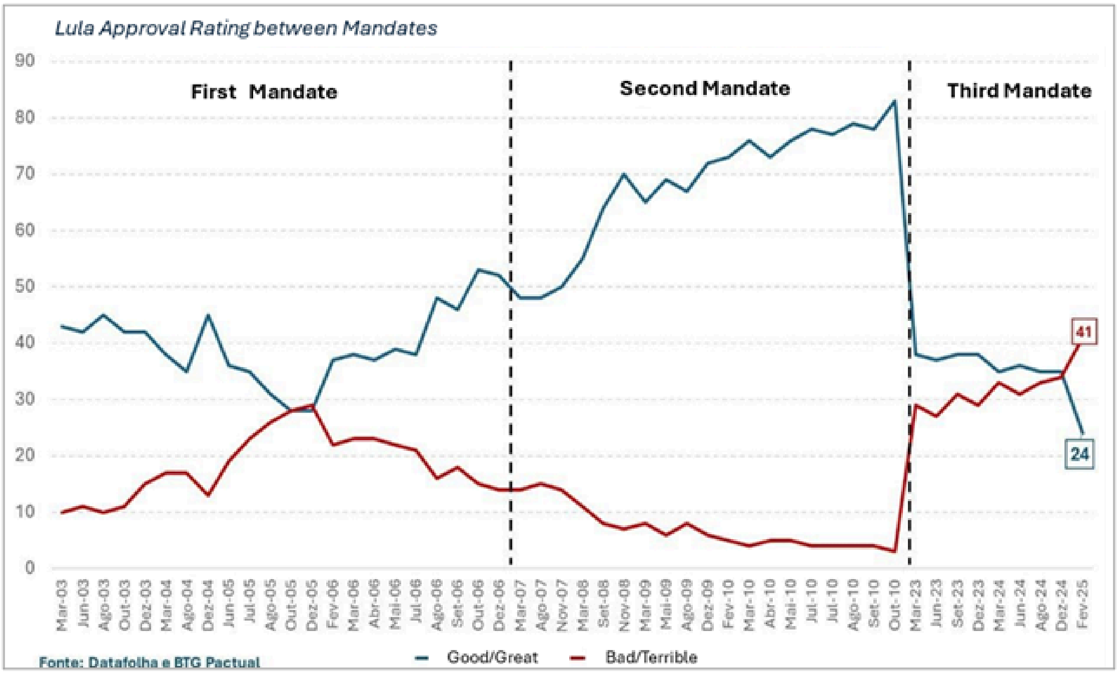
Election cycle in South America: A potential boost for local markets

March 2025

The year 2024 was significant for global democracy with over 50 nations holding elections, representing approximately half the world's population.[1] Now, South America stands at a similarly relevant moment with potential political shifts as it approaches the 2025-26 presidential elections.

The 2024 political landscape in wealthy nations was marked by voter discontent driven by geopolitical conflicts and economic instability, with leaders constrained by sluggish growth and mounting deficits, requiring unpopular measures like tax hikes and spending cuts. In Europe, France faced its first government collapse since 1962 when Macron's administration fell over budget disputes, leading to the resignation of Prime Minister Gabriel Attal. In Germany, Chancellor Olaf Scholz's coalition government disintegrated over economic policy disagreements, ultimately leading to his defeat and early elections being scheduled for 2025. In Canada, political turmoil escalated as declining support, internal Liberal Party conflicts, and external pressures culminated in Justin Trudeau's resignation after nearly a decade in power. Meanwhile, in the United States, Donald Trump secured a decisive victory in the presidential elections. In parallel, South American leftist governments struggled with economic uncertainty and declining popular support.[2] However, Argentina's right-wing leader, Javier Milei, emerged as an outlier, as his market-friendly reforms offered an alternative pathway that could shape the political trajectory of neighbouring countries.

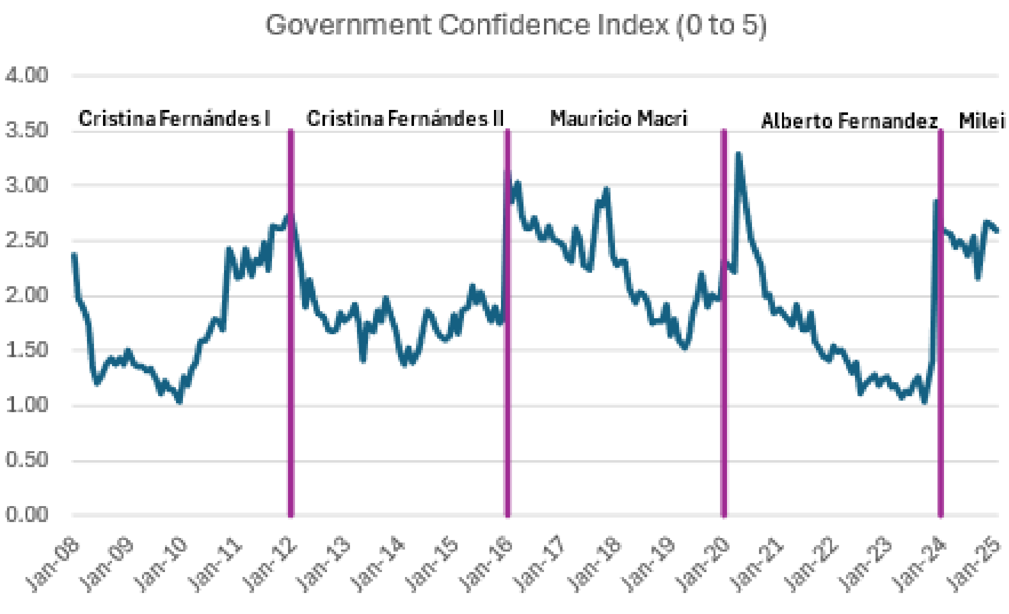
South America political climate is experiencing significant volatility, with incumbent leftist governments facing widespread decline in support. In Brazil, President Lula's administration is seeing a sharp drop in popularity, with disapproval rating (41%) significantly surpassing approval rating (24%) for the first time in his three mandates. This decline is particularly notable as disapproval grows even among his usual and historic supporters.[3] While macroeconomic factors—such as rising interest rates, unanchored inflation expectations, currency depreciation, fiscal concerns, and rising food prices—have created a challenging environment, other structural and political dynamics are also at play. An increasingly effective opposition has amplified government mistakes, making them more visible and damaging than in previous administrations. Additionally, there is growing fatigue with the government, as it struggles to introduce new agendas that resonate with the population. Communication with younger demographics remains a challenge, as they are more inclined toward discourses on entrepreneurship and a smaller state. The rise of conservative values has also made it harder for the government to connect with a significant portion of society. Finally, political uncertainty looms given Lula's age and the lack of a clear successor to take his place.



Source: Datafolha, BTG

Recent municipal elections across Brazil, Chile, and Colombia have also revealed a pattern, with centre-right opposition forces showing strong performance in all three countries, suggesting a potential regional shift away from the current leftist governments. This trend aligns with the broader decline in incumbent support - Chile's President Boric struggles with just 31% approval against 62% disapproval[4] following failed constitutional reforms and rising security concerns, while Colombia's political landscape presents perhaps the most challenging picture, with President Petro's support eroded to just 28% approval versus 63% disapproval,[5] stemming from a combination of security issues, stalled reforms, and increasing judicial tensions.

On the other hand, despite the significant macroeconomic adjustments implemented by his government, Milei's popularity in Argentina remains high, with high levels of confidence levels, while overall government confidence sitting at high levels.[6]



Source: Universidad Toucuato Di Tella

Hence, the upcoming election cycle could bring transformative political changes. Chile will hold its presidential election in Nov 2025, followed by Peru in Apr 2026, Colombia in May 2026 and Brazil in Oct 2026, while Argentina's 2025 midterm elections, which will renew 1/3 of senate and half the chamber of deputies, will serve as a test of President Milei's reform agenda and could boost governability.

A challenging macro environment in the region could support a regime change. Brazil GDP growth is projected to slow down to 2.0% in 2025 and 1.7% in 2025 (Focus survey),[7] while Chile is expected to maintain steady growth at 2.2% in 2025 and 2.1% in 2026.[8] Colombia anticipates a 2.5% growth in 2025, rising to 2.8% in 2026.[9] Inflation remains a challenge across the region, requiring a strong commitment from central banks to achieve the last mile of disinflation and reach monetary policy targets. Brazil's inflation is forecast to increase to 5.6% (above 4.5% target ceiling) in 2025 before slowing to 4.3% in 2026 (Focus Survey). Chile's inflation is projected to rise to 4.1% in 2025 and slow down to 3.0% in 2026, while Colombia expects a drop to 4.3% and to 3.6% over the same period.[10]

Brazil also faces persistent challenges through primary deficits (0.6% in 2025, 0.5% in 2026) and substantial nominal deficits (8.5% for 2025, 7.6% in 2026)[11] leading to a concerning debt trajectory reaching 97.6% of GDP by 2029 (IMF Fiscal Monitor). Chile forecasts deficits of 1.7% in 2024 and 0.8% in 2025, keeping debt stable at 41.8%. Colombia expects a 0.1% deficit in 2024, turning to a 0.2% surplus in 2025, with debt peaking at 56.6% in 2027 before declining.[12] In Brazil specifically, fiscal challenges remain a key concern for investors, driving volatility in market prices and FX throughout 2024, due to deteriorating fiscal sentiment and a disappointing fiscal package. In response, the central bank raised the Selic rate to 13.25% and signalled more hikes, yet uncertainty and investor pessimism persist, weighing heavily on market sentiment in Latin America's largest economy.

Argentina's experience under President Milei's market-friendly government highlights the potential impact of regime change in the region. Since his election in November 2023, 12 month inflation has dropped significantly from 289% in April 2024 to 85% in January 2025, with monthly inflation reaching 2.2% (8.8% in April 24).[13] Looking ahead, the IMF forecasts continued improvement, projecting inflation to close 2025 at 45% and decline further to 25% in 2026.[14] Fiscal performance has also improved, with a primary surplus of 10.4 billion pesos in 2024, compared to a 5.2 billion deficit 2023, marking the first surplus over a decade.[15] While the IMF projects a 3.5% GDP contraction for Argentina in 2024, it forecasts a solid rebound of 5.0%[16] in 2025 despite the strong fiscal consolidation. Argentina was the best-performing market in Latin America in 2024, with the S&P Argentine ADR total return of 160.9% (USD), 117.1% for the MSCI Argentina (USD), and 113.7% for the S&P Merval (USD). The Argentine Peso was the strongest currency in 2024, appreciating over 40% in real terms against the USD.[17] The key catalyst was better-than-expected economic improvements, along with President Milei's resilient approval rating, which supported investor confidence, signalling a positive trajectory that could inspire a rerating of other regional markets ahead of upcoming elections.

2025 could be a turning point for South American markets. Valuations vary across the region, with Chile trading at 10.5x forward P/E (ex-mining), Brazil at 8.6x forward P/E (ex-Petrobras & Vale), and Colombia at 6.8x forward P/E, making it the most undervalued market in the region. All these markets are currently trading within 1.0x standard deviation below their historical averages, highlighting the potential for re-rating if market sentiment improves. With historically low valuations across the region and Argentina's so far successful turnaround as a backdrop, investor interest in the 2025–26 election cycle is likely to continue rising. According to recent research from Bradesco BBI, markets typically begin pricing in political changes 12–18 months ahead of major elections. The study notably highlights that Brazilian markets have historically delivered strong returns in the third year of presidential terms, particularly when there is potential for a shift from left- to right-wing leadership, though the sample size is limited. The path forward will largely depend on pre-election polling, government approval ratings, and the broader macroeconomic environment, with markets adjusting expectations based on the perceived likelihood of political change. FX volatility is also expected to remain elevated, not only due to global macro and geopolitical factors but also as fiscal and electoral debates drive fluctuations in local currencies. The big question for investors this year will be getting the timing right to capitalise on opportunities arising from the political cycle. The current combination of depressed valuations and potential political shifts presents an interesting setup for regional markets from a top-down perspective. In the meantime, the region offers a wide range of high-quality companies with significant competitive advantages and attractive long-term prospects, that are well positioned to navigate different scenarios.

As of January 2025, Utilico Emerging Markets' exposure to Latin America is around one-third of the portfolio.

Eduardo Greca
March, 2025

Source Data: ICM Limited.

[1] The year of elections – Is 2024 democracy's biggest test ever? | Elections News | Al Jazeera
[2] Image of Power | NOV – DEC 2024 – Directorio Legislativo
[3] Datafolha: Aprovação de Lula desaba para 24% e é recorde - 14/02/2025 - Poder - Folha
[4] Encuesta Plaza Pública Cadem. N°578
[5] Opinómetro
[6] ICG | Universidad Torcuato Di Tella
[7] Sistema Expectativas de Mercado – Focus Report
[8] Encuesta de Expectativas Económicas – Febrero 2025
[9] World Economic Outlook (October 2024) - Real GDP growth
[10] Encuesta Mensual de Expectativas de Analistas Económicos (EME)
[11] Sistema Expectativas de Mercado – Focus Report
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[13] Índice de Precios al Consumidor (IPC). Cobertura nacional. Enero de 2025
[14] World Economic Outlook (October 2024) - Inflation rate, end of period consumer prices
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[16] Argentina in 'transition' to growth, says top World Bank official | Buenos Aires Times
[17] Factset

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