



## Why Canadians Should Be Concerned by Latin America's Latest Crisis

### Description

A series of political crises have rocked Latin America in recent months with civil unrest breaking out in Ecuador, Chile, and Colombia. While much of it appears driven by minor grievances, there are signs that unrest is far from over and will have a major impact on what is historically an unstable region.

You would be excused for asking why these latest events are relevant for Canadian investors. The answer is relatively simple: much of the foreign investment in the region has been made by Canadian companies including **Bank of Nova Scotia** ([TSX:BNS](#))([NYSE:BNS](#)), which is a top-10 ranked financial institution in Mexico, Chile, Peru, and Colombia.

Dollar store operator **Dollarama** ([TSX:DOL](#)) has also invested in Latin America, acquiring a 51% interest in Latin American retailer Dollarcity, which has 45 stores in El Salvador, 56 in Guatemala, and 91 in Colombia. This makes them susceptible to the impact of civil unrest and rising geopolitical risk on the economies of the affected nations.

### Economic impact

Scotiabank and Dollarama are among the most exposed because they are dependent on strong economic growth, solid business confidence, and rising consumption to grow earnings from their Latin American operations. Scotiabank is particularly vulnerable because it is the third-largest privately-owned bank in Chile, where the finance minister has cautioned that the protests could shave up to 0.6% from annual GDP growth for 2019. That would lead to lower demand for credit because there is a correlation between it and economic growth. Chile was responsible for 15% of the net income earned by Scotiabank's international division for the fourth quarter 2019.

The impact of lower regional growth will be magnified by weaker commodity prices, particularly for copper, which, according to the World Bank, is responsible for half of Chile's export earnings. Copper is caught in a multi-year slump and has lost 7% over the last year despite greater optimism surrounding the global economic outlook. The threat posed by Trump's trade war, which he recently expanded to Brazil and Argentina by slapping tariffs on aluminum and steel shipments, poses a dire threat to Chile's economy. This is because the world's single largest consumer of copper is China,

which will experience a sharp downturn in manufacturing activity if further U.S. tariffs are placed on imports.

A similar threat is posed to the Scotiabank's earnings in Colombia, which was responsible for around 5% of Scotiabank's international businesses' reported net income.

Dollarama's investment in Dollarcity means that it has considerable exposure to Colombia's emerging economic crisis because the latter retailer has almost half of its 192 stores in the Andean nation. While thrift retailers are typically considered recession-resistant, it isn't the case for Dollarcity in Colombia. A combination of extremely low wages – the minimum salary is around \$315 per month – fierce local competition among discount retailers, and a lack of access to credit makes it a difficult market to operate in.

The difficulties associated with operating in Colombia are being exacerbated by an emerging economic crisis, reduced government spending on social programs, declining security, rising geopolitical risk, and the latest round of protests.

Nonetheless, rising geopolitical risk in Latin America will have little [material impact](#) on Dollarama's earnings, unlike for Scotiabank. This is because Canada, where 1,250 of its stores are located, is responsible for most of Dollarama's earnings.

The investment in Dollarcity has provided the retailer with a second growth platform in a region that has experienced strong economic growth, which will return once the current unrest eases. The acquisition reduces Dollarama's dependence on Canada and diversifies its earnings into a region where economic performance is less correlated to developed markets, notably the U.S. and Canada. Sales could continue to grow even if there is a domestic economic downturn and U.S. recession because the impact on Latin America will be muted.

## Foolish takeaway

The latest round of unrest could certainly disrupt the Scotiabank's and Dollarama's planned growth, but it is likely it will be minimal over the long term. The cyclical nature of these types of events, and with both stocks poised to benefit from Latin America's solid long-term growth potential, means that investors shouldn't panic.

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### TICKERS GLOBAL

1. NYSE:BNS (The Bank of Nova Scotia)
2. TSX:BNS (Bank Of Nova Scotia)
3. TSX:DOL (Dollarama Inc.)

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