



Citi Global Wealth Investments

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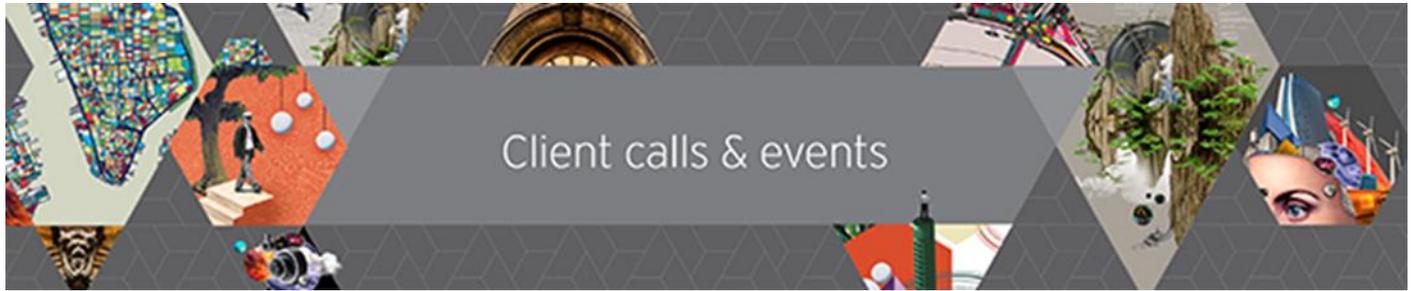
Latin America Strategy Bulletin

Colombia's Presidential 1st Round Election: Populism Wins...

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Summary:

- Colombians went to the polls Sunday to cast their votes on the first round of Presidential elections. The results mean that voters will have to cast their votes again, on a second round on June 19.
- As expected, Gustavo Petro took the lead with slightly more than 40% of the votes. The surprise, however, was the runner up, Rodolfo Hernandez with around 28%. Federico "Fico" Gutierrez, who was widely expected to face off against Petro in the run-off, was third with around 24%.
- Hernandez is considered an outsider who had been making gains in the polls recently but was not necessarily expected to pull off second place in Sunday's election. Hernandez is a 77-year-old businessman from Bucaramanga (he was its mayor from 2016-2019) who had little to no support from the established political system. He is an outspoken populist with conservative views who financed his own campaign but who has given few hints in terms of policies or cabinet choices. His mostly digital/online campaign focused on fighting corruption and has been compared, to some degree, to former US President Donald Trump.
- Hernandez's position going into the run-off is a strong one. He has received uncompromising support from Fico, and if he is able to effectively gather his votes (amassing 11mm votes vs Petro's 8.5mm), he presents a strong challenge to the first-round winner.
- Markets are likely to welcome a right-wing conservative populist over a left-wing ex-guerrilla one. Nevertheless, the results confirm the trend of extreme polarization in Latin America, as well as the high degree of rejection for traditional political candidates and structures. The extent to which populations all over the region are willing to gamble their votes with unproven or highly polarizing candidates in the most recent presidential elections has been notable.
- Investors should take caution, however. While the knee-jerk reaction of a potential Petro defeat could be perceived as a green light for assets to recover from their very depressed levels (something we believe would happen have happened even if Petro won the run-off), the medium-term prospects for the economy remain challenging. For one, little is known about what type of economic policies, or the cabinets to implement them might look like; we hope to learn more over the next 3 weeks. Fiscal stimulus remains constrained. Monetary policy is contractionary given high inflation. Levers to pull over the near term are limited. Structural reforms and the right incentives for long-term investment could help achieve potential growth. Hernandez would not enjoy legislative support, not initially or not without having to build coalitions. This means both upside and downside surprises are limited.
- As investors wait for a June 19 run-off, the near-term could see a recovery in financial markets. The currency, COP, is trading near 3900, not far from the 2020 lows of 4110. The Colombia MSCI is up nearly 20% YTD, sharing the top performer spot with Brazil. High oil prices support exports – nearly 40% of total exports. Corporate (MSCI) earnings are expected to grow 15% in 2022 and 6% in 2023, compared with 5.8% and -6% for the Latam composite consensus expectations, and '23 forward PE multiples below 8x are almost 2 standard deviations below the mean. Meanwhile, corporate profitability and margins are near commodity super cycle peaks. There is a valuation and technical positioning argument for Colombian assets to perform – a Hernandez run-off victory could prove to be the needed catalyst, at least for a temporary rebound.



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