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Facing Latin America's Leftward Shift: Implications and Recommendations

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As Latin America welcomes left-leaning political regimes, the region's regulatory landscape undertakes an increasingly uncertain state for foreign investors. In terms of cross-border investment dynamics, Latin America's history has demonstrated that its embrace or lack thereof is shaped by cycles of political and economic regimes. Thus, a wave of direct or indirect expropriations, regulatory overreaches, resource nationalism, potential contract revisions, and the implementation of taxes and tariffs, is at the heart of investors' uneasiness in light of the leftward political transition.

In fact, this ideological change in governance is already triggering new trends, challenges, and opportunities for investment and trade in the region. It is now up to the system players, especially investors, to adapt and prepare to face the challenges.

In this context, this post explores the recent changes in policy in the region and their possible repercussions on foreign investments **(I.)**, as well as the available remedies to counteract the legal and economic uncertainty compounded by the rise of left-wing governments **(II.)**. We conclude that, despite the political risks, Latin America remains a fertile ground for foreign direct investment ("**FDI**"). **(III.)**

I. Latin America's Regulatory Landscape

In recent years, Latin America's political configuration has drastically skewed to the left. The former and current electoral super-cycles brought left-wing governments into the office of the region's six largest economies and most populated countries, coloring 80% of the region with a "new pink tide." However, aside from a standardized political orientation that reminisces the 2000s political climate, it is relevant to note that various ideologies and the particularities of each jurisdiction are tiling a complex mosaic of different shades of the left that must be analyzed on a case-by-case basis.

a. Mexico

Latin America's leftward shift began in 2018 with Andres Manuel Lopez Obrador's ("**AMLO**") election. In four years of administration, AMLO's unfriendly ideology towards foreign investment has already annulled the 2013 pre-existing energy reform, prioritized state-owned energy and fossil fuel generation companies, canceled incentives for renewable energy projects, and nationalized Mexico's lithium industry, amongst other stringent government interventions.

Going forward, an upsurge in arbitral proceedings is expected, especially regarding the affected sectors. Which, it is important to note, could be swollen by the North American Free Trade Agreement ("**NAFTA**") legacy claims to be filed under the still active three-year Sunset Period.

b. Argentina

The election of Alberto Fernandez returned the leftist Peronist office to power in October 2019. After fostering investors' trust for months during his campaign, he decided to expropriate one of the country's largest agri-food companies less than a year after being elected. This, alongside the political instability owed to the President and Vice President's infighting, the forecasted lack of economic viability, and the FDI plummets over the past few years, raised concerns within the investors' community, which will acutely scrutinize the upcoming October presidential elections.

c. Bolivia

With the appointment of Luis Arce, former minister of economy, Bolivian voters returned Evo Morales Movement Towards Socialism ("**MAS**", for its acronym in Spanish) to power in October 2020. Despite deciding on the continuance of the Morales administration's populist economic model, which maintains the nationalization of natural resources, Arce has demonstrated that he also understands the importance of FDI for the development of the country. His pro-FDI approach, among other things, has tapped into Bolivia's lithium reserves. In fact, as of this year, Arce secured China as Bolivia's strategic partner for the exploitation of its mineral deposits, hoping to bring in as much as US$ 1 billion by the end of his five-year term. It, therefore, seems reasonable to expect that, even if Arce's administration pursues the high social expenditure seen under Evo Morales, there will be a deepening of FDI.

d. Perú

Conservative Peru shifted to the left when Pedro Castillo assumed office in July 2021. His campaign and short mandate generated great uncertainty due to the 180-degree transformation he pledged to implement in Peru's economic policy. However, before his program could be executed, Castillo's December 2022 impeachment made Diana Boularte Peru's sixth president in the last six years.

Under these circumstances, the fact that, between 2020 and 2023, Peru has been one of the most sued countries in the world is symptomatic of fundamental administration problems. Unlike other countries in the region, Peru's arbitration crisis is due to the lack of governance since 2018 rather than specific populist policies. This upholds Peru as one of the region's most complex markets and jurisdictions for FDI.

e. Chile

In May 2021, Chile voted the former student activist Gabriel Boric as the new president. His history of protest led to concerns about his government's direction in balancing the economic and social agenda. Even if Boric has adopted a restrained attitude and encouraged FDI since assuming office, the tax hike and environmental regulation on the country's key mining sector are weighing on the economy and promoting FDI flight. Amid this political uncertainty, investors have recently pulled more than US$ 50 billion out of Chile.

Moreover, there has been a constant debate on free trade agreements, especially on investor-State dispute settlement ("**ISDS**") mechanisms. In this regard, not only did the 2022 constitutional reform aimed to prohibit the recourse to investment arbitration (Article 332), but also the signing of the Comprehensive and Progressive Agreement on Trans-Pacific Partnership ("**CPTPP**") has been pushed off by the desire to renegotiate the exclusion of ISDS.

f. Honduras

Xiomara Castro's victory brought the Honduran left back to power in January 2022. Since her campaign, concerns have been voiced regarding a plummet in Honduras' attractiveness to FDI. The abrogation of the special economic zones ("**ZEDES**" by their initials in Spanish), the promise to re-nationalize privatized assets and review concession contracts, the threat of expropriation in a May 2022 energy law, and the tendency to pass major laws swiftly have contributed to the uncertainty and instability of the investment climate.

g. Colombia

In June 2022, Colombian voters elected former guerrilla member Gustavo Petro as the first-ever left-wing president. Apprehensive that his politics would be as extreme left as they were when he started the M-19 guerrilla movement, investors anticipated that his pro-sovereignty discourse could translate into understanding investment arbitration as a limitation.

While concerns regarding specific sectors are still looming, given the President-elect's environmentalist view and hostile stance towards the oil and mining industries, as experts predicted, changes to Colombia's FDI regulations were not the first items on the President's agenda. In fact, due to Colombia's strong institutions and the fact that Petro rules with a minority on a divided Congress, nationalization measures are improbable.

Nevertheless, the government's plan that seeks to halt hydrocarbon exploration licenses, stop fracking projects, and further regulate the electricity supply, are all measures that should be carefully monitored, especially in light of the surprising and unannounced recent cabinet shuffle.

h. Brazil

Luiz Inacio Lula da Silva's win over Jair Bolsonaro in Brazil's 2022 elections consolidated a "new pink tide" in Latin America. In contrast to other countries in the region, Brazil's transition to the left did everything but tarnish the country's allure to FDI. Investors recalled Lula's two previous terms in office as a time of economic prosperity fueled by a commodities boom and were further reassured by the strong, market-friendly institutions that will restrain the more populist aspirations of the incoming administration. In fact, right after Lula's election, the Brazil's Real gained another 3% as investors celebrated the assuagement of political uncertainties.

Under the Lula Administration, Brazil is expected to be even better positioned for the energy transition. Significant investment in green fuel, including renewable energy, biodiesel, sustainable mining, and green hydrogen, is foreseen.

II. How to Navigate the New Pink Tide

Facing the foregoing complexities brought on by the leftward shift, investors would be well-advised to take preemptive measures to safeguard or at least reduce potential implications to their investments. These may include:

- **Conduct a thorough analysis of existing IIA protections** to fully understand available treaty rights and how to benefit from them in the event of a dispute with the host State. This includes assessing the procedural requirements and the barriers the treaty poses, such as notices of dispute, cooling-off periods, umbrella and fork-in-the-road clauses, among other things.
- **Consider restructuring investments** to avail of investment treaty protections. For instance, investors can establish a territorial nexus with the host State before any alleged breach to gain existing treaty protection, which will be rejected if the dispute has risen or become foreseeable.
- **Be aware of the available remedies and how to action them**. For example, under some IIA, pursuing local remedies will preclude international arbitration.
- **Hire specialized legal advice** to avoid unfavorable outcomes, especially regarding concession contracts, as they often include technical language and loopholes that may allow government intervention.
- **Systematically monitor legislative and policy changes** to anticipate unwanted ones. This includes considering past court rulings that assess private concessions and the stability of political institutions.
- **Consult with the government and its political leaders** to stay informed of the national development plans and potential policy changes that might affect the investment. Maintaining an open communication channel also allows investors to express their opinions on public policies and can result in helpful leverage in eventual negotiation with authorities.
- **Collaborate with a local counterpart to better understand the political and legal system, local market, and potential risks. This can be achieved through joint ventures or alliances with local companies.**
- **Establish a document organization system** to access the evidence required to prosecute potential claims easily.
- **Notify the intention to arbitrate to discuss potential settlements with the host government without commencing formal proceedings.**
- **Institute proceedings if no agreement is reached.**

III. Conclusions

Latin America's shifting regulatory landscape has brought a sense of uncertainty to foreign investors. The recent left-wing electoral victories harken back to the region's political landscape of the 2000s, characterized by a high degree of ambiguity, volatility, and political risk. As a result, investors are apprehensive that the implemented changes could exceed the acceptable scope of legislative change. Nonetheless, upon comparing the political ideologies of the current left-leaning governments to those of the previous pink tide, the diversity in left hues becomes particularly evident.

On the one hand, contemporary left-leaning governments assumed office through narrow victories in challenging political environments, giving them little leeway to pass reforms, as seen in Argentina, Chile, Colombia, and Peru. In fact, if the rising populism fails to fulfill the promised social agenda, the political outlook for the coming years suggests a transition back to more liberal policies favorable to investment.

On the other hand, as seen in Bolivia and Brazil, the leftist political agenda is not exclusively marked by political risks and ambiguity but also presents new opportunities for FDI. There is now an interest in pursuing progressive investments, such as those in the green economy and other untapped industries. By considering FDI as a means of advancing their social commitments, these governments have opened up new possibilities for investors seeking to engage in socially responsible and sustainable business practices.

In this context, investors already owning or intending to invest in Latin America face a critical decision. They must weigh the risks and opportunities that come with investing in the region. While caution is advisable, it is important not to overlook that Latin America remains a fertile region for FDI. In fact, contrary to what was anticipated, this "new pink tide" presents a unique opportunity for foreign investors seeking to engage with the region in a more socially and environmentally responsible manner.

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