Latam Economic Update

- **Argentina: Construction and industrial production point to an even deeper recession ahead**
- **Brazil: War Budget Bill passes; BCB surprises with 75 bps cut, signals another cut to come**
- **Chile: BCCh keeps policy rate at technical minimum, signals possible unconventional measures**
- **Colombia: A new period of State of Economic Emergency declared**

ARGENTINA: CONSTRUCTION AND INDUSTRIAL PRODUCTION POINT TO AN EVEN DEEPER RECESSION AHEAD

Construction activity and industrial production continued to contract sharply in March according to data released on May 6 (chart 1)—even though Argentina's lockdown was imposed in only the latter half of the month. Construction activity fell by -46.8% y/y, quickening its drop from February's -22.1% y/y shrinkage. Similarly, industrial production, which fell a revised -1.0% y/y in February, dropped -16.8% y/y in March. Construction carries a 3.6% weight in GDP and a 3.1% share in the monthly economic activity index, whereas industrial production accounts for a much larger 22.3% weight in GDP and 18.9% in the monthly index.

Real GDP growth in Q1-2020 is tracking significantly below the -0.9% y/y contraction that we have forecast and is now likely to come in somewhere around -2.3% y/y. This would imply, on current trends, a decline of -5.9% y/y in 2020 as a whole, rather than the -5.6% y/y contraction we have forecast.

—Brett House

BRAZIL: WAR BUDGET BILL PASSES; BCB SURPRISES WITH 75 BPS CUT, SIGNALS ANOTHER CUT TO COME

Brazil gave us two somewhat positive surprises, and two expected items of bad news on Wednesday, May 6. On the political front, the lower House ratified the War Budget Bill, which means it can now, finally, come into effect. The bill validates the stimulus package the country has been seeking to implement to the tune of over 3.5% of GDP, but how much will actually flow is debatable. Given Congress' last-minute changes to the bill in its second reading on Tuesday, May 5, which included larger state funding, we expected a final vote to be delayed—but we were proved wrong. Overall, it was a positive surprise that the polarized political system is still willing to cooperate enough to speed up responses to the COVID-19 economic shock—even if political consensus in the country, in terms of medical response, is still very split.

At the same time, the BCB surprised markets by cutting the Selic rate by 75 bps from 3.75% to 3.00%, and left the door open for further easing through a "final" cut that could be as large as the one implemented on May 6.

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Chart 1

Sources: Scotiabank Economics, INDEC.

Consensus and our own forecasts had looked for a 50 bps yesterday. The BCB showed boldness to prop up the economy with this decision: recall that the Selic was at 14% as recently as the second half of 2016. Our fear on this front, however, is that with the BRL plummeting, and with strongly toned-down expectations for political consensus on fiscal reforms, the BCB could be forced to back pedal in late-2020 or early-2021 in order to provide more "yield-support" for a BRL that now offers strongly negative real returns.

On the "bad news front", both services and composite Markit PMIs for April printed at extremely weak levels: 27.4 for services and 26.5 for the composite. These outcomes supported the view that the second quarter for Brazil looks set to break the records as the weakest print in the country's history. Nevertheless, overall, Wednesday had a relatively positive tone in what have otherwise been two rough weeks for Brazil, during which the BRL has been a global underperformer.

—Eduardo Suárez

CHILE: BCCh KEEPS POLICY RATE AT TECHNICAL MINIMUM, SIGNALS POSSIBLE UNCONVENTIONAL MEASURES

In a unanimous decision at its May 6 meeting, the Chilean central bank (BCCh) maintained its monetary policy rate at 0.5%, the level it reached following the global financial crisis and what the BCCh characterizes as its “technical minimum”. Analysts had uniformly anticipated this result. In forward guidance, the BCCh further noted that it expected the policy rate to remain at this level for an “extended period”. The bias of the statement pointed toward intensifying monetary stimulus and supporting financial stability with unconventional instruments, if required. The monetary policy committee highlighted a marked concern for SMEs, which could be the focus of any new measures.

—Carlos Muñoz

COLOMBIA: A NEW PERIOD OF STATE OF ECONOMIC EMERGENCY DECLARED

On Wednesday, May 6, President Duque declared the second period of the State of Economic Emergency in Colombia, which will last for the next 30 days (the first one was between March 17 and April 17). The State of Economic Emergency gives special powers to the President to rule by decree on issues associated with the crisis. In this vein, Finance Minister Alberto Carrasquilla announced a new payroll aid program under which the government for three months will subsidize the equivalent of 40% of the minimum wage for the employees of enterprises, regardless of size, that have had sales contractions of at least 20% and can prove that the revenue reductions are due to the COVID-19 shock. Additionally, President Duque announced that the second payment of the corporate tax will be deferred until the end of the year. More details on government support measures are expected during the course of May 7.

—Sergio Olarte & Jackeline Piraján