Latam Daily: Mexico Inflation Stable, Activity Weak at End-2020; Peru to Open Up

- **Mexico: Inflation came in as expected in the first half of February; weak commercial activity at end-2020; energy bill passed in the Lower House**
- **Peru: Government relaxes mobility restrictions**

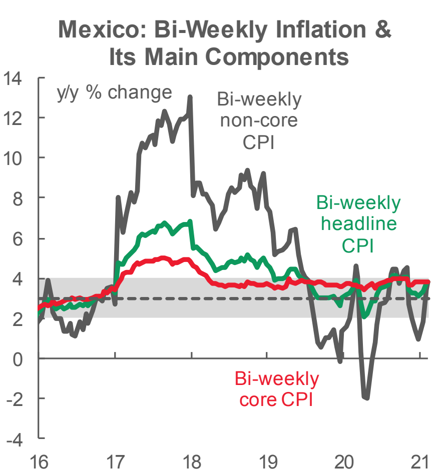
MEXICO: INFLATION CAME IN AS EXPECTED IN THE FIRST HALF OF FEBRUARY; 2020 ENDS WITH WEAK COMMERCIAL ACTIVITY; ENERGY BILL PASSED IN THE LOWER HOUSE

I. Inflation came in as expected in the first half of February

INEGI released inflation for the first half of February, which printed at 3.84% y/y (chart 1), slightly below the 3.85% y/y consensus. Non-core had the largest contribution, with the energy sub-component being the major driver of inflation. Headline inflation rose 0.23% on a bi-weekly basis, in line with expectations. By components, non-core inflation advanced 0.26% bi-weekly relative to the previous two-week period. Importantly, the energy subcomponent grew 1.28% on a bi-weekly basis, driven by increases in gasoline and domestic gas prices; while, food prices decreased -0.69% bi-weekly (versus 0.55% bi-weekly previously). Meanwhile, core inflation, advanced a more modest 0.22% on a bi-weekly basis, also in line with expectations. Core inflation components retained their differentiated performance between merchandise (+0.30% bi-weekly) and services prices (+0.13% bi-weekly) but we expect that as major cities begin to unwind social-distancing, the gap will close (chart 2).

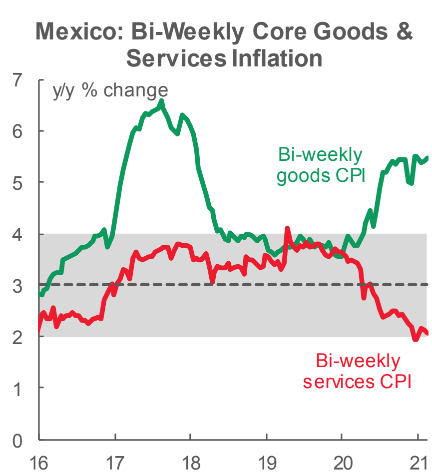
On an annual basis, inflation of 3.84% y/y rose the most since October 2020. By components, core inflation remained stable at 3.84% y/y. On the other hand, merchandise prices edged up 5.48% y/y while service prices softened from 2.12% y/y to 2.06% y/y. Finally, the non-core component rose 3.85% y/y (versus 3.03% y/y a year ago and 3.42% y/y previously). Annual Inflation remains within

Chart 1



Sources: Scotiabank Economics, INEGI.

Chart 2



Sources: Scotiabank Economics, INEGI.

CONTACTS

Brett House, VP & Deputy Chief Economist
416.863.7463
Scotiabank Economics
brett.house@scotiabank.com

Guillermo Arbe
51.1.211.6052 (Peru)
Scotiabank Peru
guillermo.arbe@scotiabank.com.pe

Sergio Olarte
57.1.745.6300 (Colombia)
Scotiabank Colombia
sergio.olarte@scotiabankcolpatria.com

Jorge Selaive
56.2.2619.5435 (Chile)
Scotiabank Chile
jorge.selaive@scotiabank.cl

Eduardo Suárez
52.55.9179.5174 (Mexico)
Scotiabank Mexico
esuarezm@scotiabank.com.mx

TODAY'S CONTRIBUTORS:

Miguel Saldaña
52.55.5123.0000 Ext. 36760 (Mexico)
Scotiabank Mexico
msaldanab@scotiabank.com.mx

the variability range of the target set by Banxico. In the short term headline inflation could exceed the 4.0% threshold, which explains why we believe there is limited scope for additional monetary easing until at least the end of the second quarter of the year. We don't see this print as a material shock, and it should not alter Banxico's policy outlook. However, we do think that the upwards pressure on US rates, and the increased amount of priced in hikes in other major EM yield curves could eventually become a factor to watch for the Board.

II. Weak end to commercial activity in 2020

Domestic demand indicators continue to point to a still somewhat lackluster rebound, with INEGI's release showing retail sales decelerating in December to -2.4% m/m, from 3.3% m/m sa in November (chart 3). Similarly, wholesale sales cooled from 1.7% m/m to 0.7% m/m sa. On an annual basis, retail sales remained in negative territory for the tenth consecutive month, declining to -5.9% y/y in real terms. Wholesale trade softened their fall, to -0.3% y/y, maintaining the negative trend of the last two years. In 2020, retail and wholesale sales fell by -9.3% y/y and -8.9% y/y respectively, compared to 2.1% y/y and -2.5% y/y, respectively in 2019. The continued weakness in retail sales, combined with the large trade surplus the country has posted suggest that when we get the details of Q4 GDP on February 25, we'll see an economy propped up by external demand.

Chart 3

Sources: Scotiabank Economics, INEGI.

III. Energy bill passed by Lower House, raising concerns in the private sector

As was expected given Morena's strong legislative presence, the Lower House approved AMLO's Power Sector Reform Bill. The main elements of the Bill are to eliminate the legal requirement that the sector operate under free competition, and instead sets a tiering of which sources of power will be distributed first: (1) CFE generated renewable power, (2) CFE generated non-renewable energy, (3) privately generated wind & solar, (4) private combined cycle generation power. The President, in his morning conferences this week, acknowledged that there are a number of litigation efforts already underway to impede the Bill's implementation, with estimates of foreign investment in the sector being close to USD 40 bn. The initiative is designated a priority initiative, which means that each House gets 31 days to vote on it, with the Senate expected to pass it over the next couple of weeks—although it is worth highlighting that the Lower Houses' approval came about 5 days later than initially expected.

In a similar direction, President Lopez Obrador mentioned on his press conference on February 24, that he expects the Bill to limit the use of outsourcing will also be approved in the current legislative period. The Bill will limit the use of outsourcing by private companies to non-core activities. Estimates suggest that at this point, about 20% of formal workers operate in this regime, which save employers somewhere in the neighborhood of 15% of employer costs.

—Eduardo Suárez & Miguel Saldaña

PERU: THE GOVERNMENT RELAXES MOBILITY RESTRICTIONS

President Sagasti announced during a press conference on Wednesday evening, the government's decision to relax the mobility restrictions that exist in large parts of the country beginning on March 1. The restrictions in place in February affected only 5% of the production of goods and services. The modifications reduce the impact on the economy even further. All but very marginal activities are allowed to operate, albeit at reduced capacity. Peru operates under four levels of alert. The most significant relaxation of restrictions was for the Extreme Alert level, which encompasses Lima and approximately two-thirds of the economy. The government relaxed the restrictions despite the fact the second wave of COVID-19 continues. Although there are incipient signs that the wave is peaking, the government decision was probably more influenced by increasing concern about the impact of the restrictions on the economy and on welfare.

The following table shows some of the highlights of the changes for those parts of the country under extreme alert.

Table 1
Peru: Extreme Alert Restrictions March 1 to 14

	Previous	Now
Prohibition on private vehicle use	All week	Sundays
Curfew	6pm to 6am	9pm to 4am
Malls, department stores	closed	20% capacity
Restaurants	only delivery	30% capacity
Beauty parlors, spas, hair salons	closed	40% capacity
Libraries, museums, galleries	closed	30% capacity
Banks, supermarkets, durgstores, continue operating at 40% capacity.		
The activities that remain closed include: casino, gyms, theaters, temples, social and sport clubs, beaches.		
All other productions activities are free to operate.		
In high alert regions, restrictions are softer, with non-significant economic impact.		

Sources: Scotiabank Economics, Presidencia del Consejo de Ministros, local press.

—Guillermo Arbe