June 29, 2021

Latam Daily: Colombia on Hold (for Now); Mexican Trade and Peruvian Political Update

- **Colombia: BanRep keeps benchmark monetary-policy rate at 1.75% retaining a data-depended mode**
- **Mexico: Trade data continue to point towards more balanced growth**
- **Peru: Castillo suggests that Velarde could stay at the BCRP; polls favour partial changes in the Constitution rather than a complete overhaul**

COLOMBIA: BANREP KEEPS BENCHMARK MONETARY-POLICY RATE AT 1.75% RETAINING A DATA-DEPENDED MODE

On Monday, June 28, BanRep's Board kept the benchmark monetary-policy rate at 1.75% in a unanimous vote (chart 1). Staff raised its' GDP growth base case scenario from 6% y/y to 6.5% y/y for 2021, underscoring that inflation expectations remain firmly anchored. In announcing the decision, BanRep Governor Leonardo Villar emphasized that Colombia's macro conditions differ from those of other Latam countries such as Brazil or Mexico, which have already started hiking rates. He highlighted that the monetary policy stance remains very expansionary to support economic recovery, and that any change in stance would depend on incoming data. Gov. Villar also emphasized that a rejection of proposed fiscal reforms could limit the Bank's room to maintain the countercyclical monetary policy. All in, we don't see a rate hike coming out of July's Board meeting, and **we retain our call for the central bank to start a tightening cycle by September 2021**.

Key features of the decision included:

- **GDP growth forecast was revised up from 6.0% y/y to 6.5% y/y for 2021.** Despite challenges from the nationwide strike, activity surprises in Q1, and a particularly strong performance in April, led the central bank to raise its growth scenario. However, it highlighted that uncertainty remains high due to the long -third COVID-19 wave.
- **The communiqué underscored core inflation metrics are still below the 3% y/y target (1.56% for inflation ex-food and regulated prices).** As always, the communiqué stressed the Board will remain vigilant if some of the recent pressures persist and impact inflation expectations, which for now remain anchored.
- **BanRep highlighted that any change in Federal Reserve's monetary policy would change financial conditions for Colombia and that approval of fiscal reform measures is critical for monetary policy to remain supportive employment and economic recovery.**

In the press conference following the announcement, Gov. Villar used neutral language in assessing future rate hikes, stressing that BanRep would continue in a data-dependent mode. Mr Villar noted that Colombia differs from other countries in Latam facing inflationary pressures, which may have

CONTACTS

Jim Haley
416.607.0058
Scotiabank Economics
jim.haley@scotiabank.com

Adriana Vega
613.564.5204
Scotiabank Economics
adriana.vega@scotiabank.com

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

Sergio Olarte
+57.1.745.6300 Ext. 9166 (Colombia)
Scotiabank Colombia
sergio.olarte@scotiabankcolpatria.com

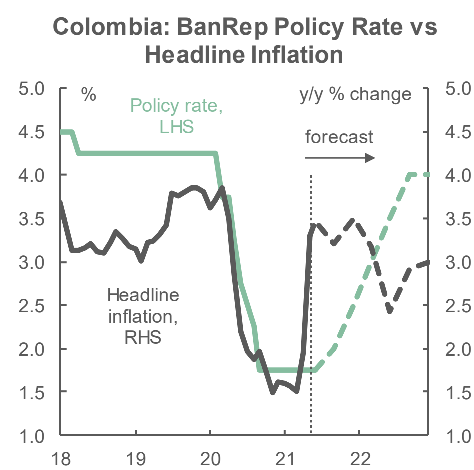
Jorge Selaive
+56.2.2619.5435 (Chile)
Scotiabank Chile
jorge.selaive@scotiabank.cl

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

TODAY'S CONTRIBUTORS:

Jackeline Piraján
+57.1.745.6300 Ext. 9400 (Colombia)
Scotiabank Colombia
jackeline.pirajan@scotiabankcolpatria.com

Chart 1



Sources: Scotiabank Economics, BanRep, DANE.

affected inflation expectations. That stance affirms our perspective that BanRep will maintain its approach giving more weight to local conditions over regional conditions in deciding about rate hikes.

We retain our call that the BanRep will remain on hold in July, with the possibility of the first rate hike in September 2021. We anticipate a lift-off in policy rates later in 2021 would be backed by further consolidation of the economic recovery, with inflation rising closer to BanRep's 3% y/y inflation target. The July Board meeting will be critical, since BanRep staff will update its macroeconomic scenario, which could signal a more hawkish tone for the future.

—Sergio Olarte & Jackeline Piraján

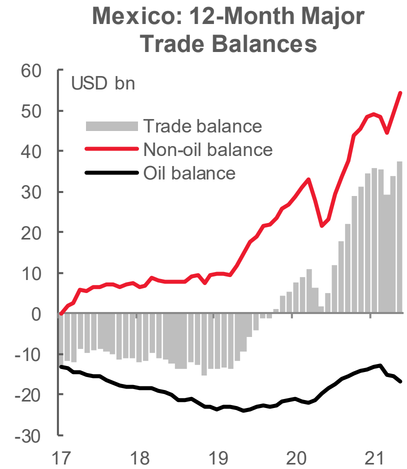
MEXICO: TRADE DATA CONTINUE TO POINT TOWARDS MORE BALANCED GROWTH

Data on Mexico's trade balance for May, released June 28, 2021, showed a more modest surplus than consensus anticipated, coming in at USD 340 mn versus an expected USD 1.2 bn surplus (chart 2). Non-oil exports totaled USD 38.5 bn, while oil exports continued to benefit from stronger oil prices, reaching USD 4.0 bn (having bottomed out at USD 1.4 bn during the crisis).

Part of the reason for the milder than anticipated surplus is the rebound in imports, which are increasingly showing a more balanced growth profile for the Mexican economy, as domestic demand continues to recover from the pandemic shock (chart 3). Capital goods imports continue to grow at around half the pace of consumer and intermediate goods, but they are nonetheless finally showing signs of life, which suggests some improvement in business confidence. The rebound in domestic demand has now mostly eliminated the record trade surpluses recorded at the peak of the pandemic crisis and could be one of the factors that has led to reduced appreciation pressures for MXN.

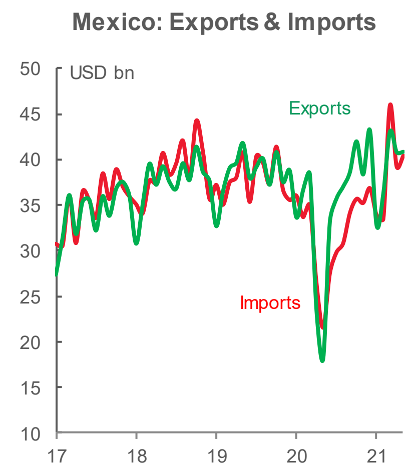
—Eduardo Suárez

Chart 2



Sources: Scotiabank Economics, INEGI.

Chart 3



Sources: Scotiabank Economics, INEGI.

PERU: CASTILLO SUGGESTS THAT VELARDE COULD STAY AT THE BCRP; POLLS FAVOUR PARTIAL CHANGES IN THE CONSTITUTION RATHER THAN A COMPLETE OVERHAUL

Over the weekend Pedro Castillo stated in a speech to his followers that he would like to see central bank Governor Julio Velarde "work permanently" at the helm of the BCRP. This message in favour of Velarde staying on was later ratified in social media. In his speech, Castillo also mentioned the need for "governability", "economic calm", and "opening the doors to investment". The market reacted to these more friendly comments with the expected optimism; the FX rate opened at USDPEN 3.96 on Monday and closed at USDPEN 3.89. The fact that Castillo has reiterated his message of moderation even though the elections are over, makes his statements more convincing. However, we will feel more comfortable with this assessment once a cabinet that is consistent with a moderate platform is named. While it is widely known that Velarde has been contemplating his retirement, Pedro Francke—Castillo's economic advisor—stated on Monday that Velarde was studying the possibility of staying.

The local polling firm, Ipsos, released a poll that included a question on constitutional change. According to the poll, only 32% of the population would prefer a completely new Constitution to be drawn up by a constitutional assembly. The plurality, 39%, prefer only partial changes to the current constitution, to be implemented by the current Congress through mechanisms already established by the Constitution. Finally, 22% would prefer no changes in the Constitution. These results could be taken as meaning that a clear majority (71%) want changes in the Constitution, but also that a sizeable majority (61%) do not want a complete overhaul of the Constitution, or the convening of a Constitutional Assembly. But the poll results also mean that whatever approach that the next government adopts is likely to have its detractors.

—Guillermo Arbe