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GLOBAL ECONOMICS

LATAM DAILY

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Latam Daily: New Day, New Peruvian President

- **Chile: Inflation does not wane and becomes particularly volatile**
- **Colombia: Confidence continues to deteriorate amid persistent inflation pressures**
- **Peru: BCRP hikes 25bps as expected, leaves the door open to more**

Markets are trading mixed with only Hong Kong posting solid gains on a relaxation of Covid measures, with little of note overnight and on today's calendar. The USD is also split between gains and losses against the majors, though in +/-0.2% ranges for the most part. Commodity prices are gaining ground ahead of North American trading, both crude oil and iron ore are stronger.

It is a quiet day ahead in the region (from a calendar perspective, at least) with Chile, Colombia, and Peru closed for business for Immaculate Conception Day.

Mexican inflation softens; Esquivel to stay at Banxico?

Mexico published full-month November inflation data this morning, with headline prices rising 7.80% y/y and 0.58% m/m, falling short of respective median forecasts of 7.94% and 0.68% (and from 8.41% and 0.57%). Core prices missed expectations by a greater margin, at 8.51% y/y and 0.45% m/m versus economists seeing 8.58% and 0.53%, respectively, compared to 8.42% and 0.63% in October.

Today's report showed that prices actually contracted in the second half of November, as had maybe been teed up by Banxico's Heath at the time of the H1-Nov release (due to Mexico's Black Friday equivalent). On a bi-weekly basis, headline CPI fell 0.11% while core marginally softened 0.04%.

Overall, it still is very likely that Mexico's central bank will roll out another 50bps hike next week, though today's softer month-on-month print and December CPI data could see them hike by a smaller amount than the Fed early next year. The MXN strengthened very slightly following the data release, though simply following a bout of dollar weakness at the time.

According to a report by Bloomberg, Banxico dove Esquivel has a "fair chance" of staying in the board for an additional eight-year term instead of leaving at the expiry of his current spell this month. At the margin, this increases the odds of an earlier Banxico decoupling, although we would expect that were Esquivel to be replaced AMLO would select someone aligned with him on the dovish-hawkish scale.

Castillo-out, Boluarte-in

Yesterday, Peru's (now former) President Castillo scored a huge own-goal after calling for the dissolution of Congress ahead of an incoming impeachment vote against him. Key cabinet officials quit and alongside the military quickly denounced the President's push, and **he was detained just a few hours after his announcement.**

VP Boluarte was sworn in as Peru's head of state and we now await details on the composition of her cabinet—at the margin, she would be closer to center, but still on the left. She has become estranged from the radical leadership of the Perú Libre party since being elected and is viewed as a moderate leftist. See our full ***Latam Flash*** report on yesterday's developments. Our Peru Chief Economist Guillermo Arbe will also give his thoughts on the political outlook in a webcast scheduled for 9ET (register ***here***).

Lula's spending cap exclusion clears Senate; BCB holds, warns of possible hikes restart

In Brazil, the Senate approved the 'transition bill' that allows for a BRL145bn carve out from the fiscal cap for social spending for the next two years, also including language on the creation of a new fiscal rule next year—which means the fiscal risks can has only been kicked down the road. The lower house will today vote on the text.

The BCB held its policy rate unchanged yesterday, as expected, but sent a clear message that additional public spending may require a resumption of the tightening cycle. Without clear details on Lula's fiscal plans, the BCB cannot yet make a clear assessment on the need for more hikes, currently.

—Juan Manuel Herrera

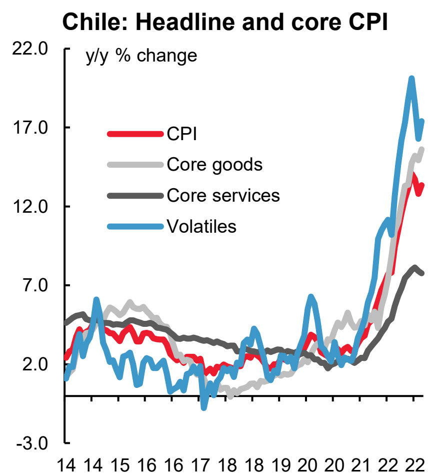
CHILE: INFLATION DOES NOT WANE AND BECOMES PARTICULARLY VOLATILE

On Wednesday, the statistical agency (INE) released November CPI data showing an increase of 1% m/m (13.3% y/y, chart 1) **notably above our expectation, the consensus expectation and the one implied by asset prices**.

Consequently, we must withdraw our call for an aggressive benchmark rate cut at the January meeting despite the fact that inflationary determinants have been and will be aligned towards lower inflation. After surprisingly low October CPI across all its core measures, November CPI reverses much of the good news. The CPI for December, given the higher bases of comparison, could be yet another surprise, this time on the negative side of expectations. However, in a context of excessive inflationary volatility, it is difficult for the central bank to make a decision to cut with conviction.

Inflation of 1% m/m in November was mainly explained by a rebound in goods inflation (excluding volatiles), **especially durable goods**, after the sharp drop in the previous month. Also notable in this print are the increases in the alcoholic and beverages division, especially beer and cigarettes, where, given the volatility, a reversal is expected in coming months. For its part, the volatile CPI (1% m/m) continues to support inflation, where in addition to increases in fruits and dairy products, there are increases in non-perishable foods. **At the level of services, price increases continue but with a clear downward trend in recent months.**

Chart 1



Sources: Scotiabank Economics, INE.

Regarding the *Monetary Policy Report*, the central bank increased its forecast for GDP growth in 2022 and reduced its projection for 2023 (to 2.4 and -1.25%, respectively), in line with our scenario. At the same time, **their scenario foresees a greater inflationary persistence**, mainly due to external factors, which is why they raised their projection for end-2022 to 12.3% y/y and for end-2023 to 3.6% y/y. In line with this, the central bank continues to see only modest policy rate cuts in the coming year. **Finally, the central bank revised upwards its estimate for the neutral interest rate from 3.50% to 3.75%** and for trend GDP growth, to 2.2%.

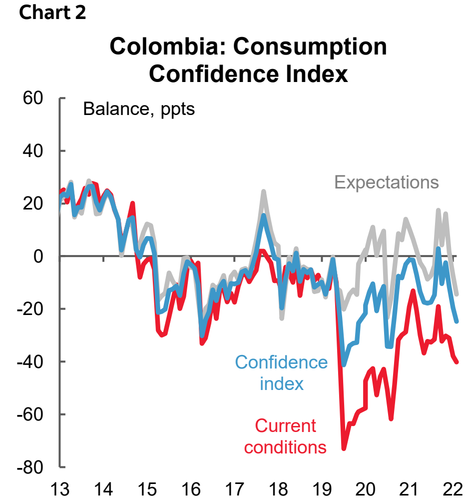
—Aníbal Alarcón, & Waldo Riveras

COLOMBIA: CONFIDENCE CONTINUES TO DETERIORATE AMID PERSISTENT INFLATION PRESSURES

Colombia's Consumer Confidence Index (CCI) in November came in at -24.8, showing a m/m decrease of 5.3 points. The drop in consumer perception is due to a decrease in the expectations component of future conditions, which fell from -7.3 to -14.5 (chart 2), and the current conditions component had a deeper drop from -37.9 to -40.2.

The expectations index is lower. Consumers think that the conditions of their households will not be as favourable in the coming year, as well as the conditions of the country. In the same line, the willingness to buy houses fell 6.1 points from the previous month (-36.6ppts to -42.7) and the willingness to buy vehicles showed a negative balance, worsening compared to the previous month decreasing 2.8 points to the level of -70.1.

Chart 2



Sources: Scotiabank Economics, Fedesarrollo.

Likewise, the willingness to buy durable goods decreased by 5.5 points versus the previous month from -47.4 to -52.9. This shows a more negative balance of households about the economic future, and uncertainty about economic activity especially price pressures, accompanied by a still complex international scenario with fears of a recession next year.

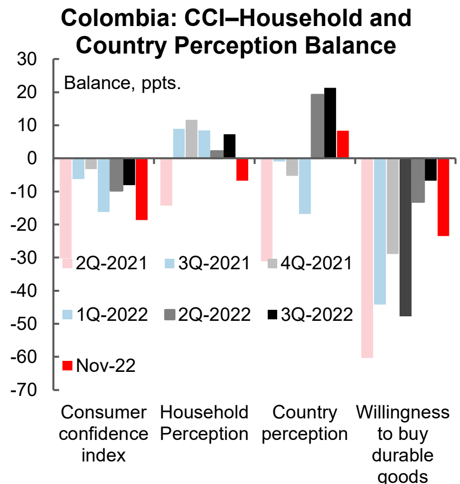
Continued growth and consumption dynamics will be relevant for year-end, given that inflation is still at its highest level in 23 years and is likely to remain pressured next year by indexation and depreciation effects. Therefore, consumer credit is expected to continue to slow amid tighter monetary policy, which proves necessary for the economy to return to healthier growth with moderating inflation pressures.

In November, consumer confidence continued to show that consumer expectations for the economy have worsened, households remain afflicted by the effects of rising inflation and the perception of a slowdown in economic activity (chart 3). In addition, the fact that rates are already at elevated levels and are likely to continue to rise and last longer at these levels given the deterioration in inflation keep deterioration consumer confidence.

In spite of this, given that we do not yet see inflation peaking, we reaffirm our expectation for the December monetary policy meeting of 100bps to 12.00%, and we cannot discard another 50bps at the January meeting if December inflation continue with an upward trend.

—Sergio Olarte, María (Tatiana) Mejía & Jackeline Piraján

Chart 3

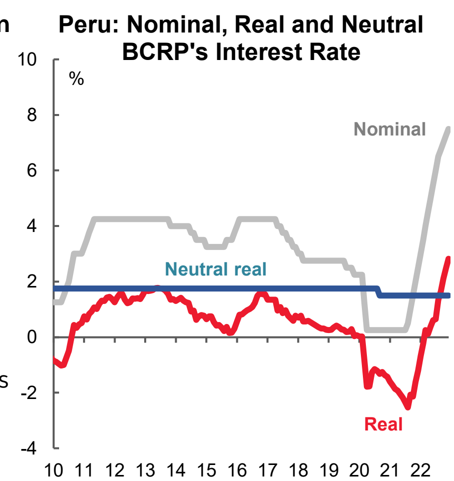


Sources: Scotiabank Economics, Fedesarrollo.

PERU: BCRP HIKES 25BPS AS EXPECTED, LEAVES THE DOOR OPEN TO MORE

The board of Peru's central bank (BCRP) raised its key interest rate by 25bps to 7.50% on Wednesday, in line with our expectations and the market consensus. This is the fourth consecutive time that the BCRP raises its key interest rate by 25bps, after 50bps increases in each of the previous twelve decisions (chart 4).

Chart 4

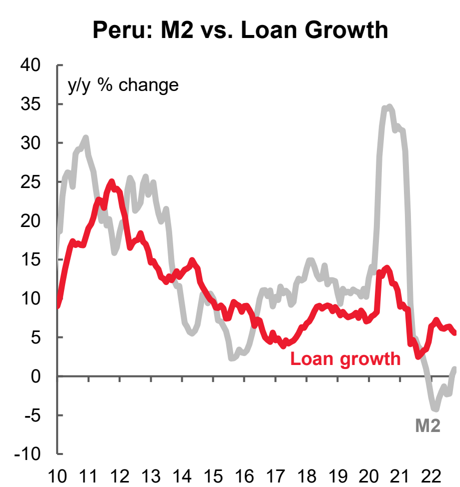


Sources: Scotiabank Economics, BCRP.

In its statement, BCRP kept the same tone as in previous decisions, leaving the door open to the possibility of additional hikes. We maintain that the end of the inflation cycle and cresting is close, but we do not see yet see convincing signs of a pronounced deceleration.

The key remains the speed with which inflation expectations weaken. This is occurring, but at a slow pace, going from 4.78% in October to 4.68% in November in their reading for the next 12 months, while for 2023 they remained at 4.4%, in both cases above the upper limit of the target band. Inflation rose in November to 8.45% y/y, from 8.28% y/y in October, while inflation excluding food and energy dropped marginally, from 5.72% in October to 5.71% in November. Other price indices, such as wholesale prices and those linked to construction materials and machinery, continue to slow. On a regional basis, 3 out of the 26 largest cities in the country posted a year-on-year inflation above 10%. This represents a reduction compared to the 6 cities at 10%+ in October.

Chart 5



Sources: Scotiabank Economics, BCRP.

The real interest rate rose from 2.47% to 2.82%, placing itself above its neutral level (1.50%) for the fourth consecutive month (chart 4, again). The BCRP kept the forward guidance used in previous releases, which left open the possibility of new heights, depending on how the inflation drivers evolved. Our base scenario considers that at this level (7.50%) the terminal rate has already been reached. This statement poses upside risks to this forecast, but the deviation should not be too major.

Like us, the central bank predicts a trend towards lower interannual inflation, although it has changed its expected return to the target range from the second half of 2023 to the fourth quarter of 2023 showing that the central bank now sees a slower descent in inflation.

The statement kept its pessimistic outlook for global and local economic activity, emphasizing the effects of restrictive monetary policy on advanced economies, the impact of inflation on consumption (purchasing power), lower growth of China, and ongoing international conflicts. On the quantitative side, the growth in cash (M2) accumulated in the twelve months to October remains (0.9% y/y), while the expansion of credit held above 5% y/y for the second consecutive month (chart 5).

—Mario Guerrero