

## Latam Economic Update

- **Brazil:** Presentation of post COVID-19 stimulus and social measures delayed; BCB sees marginal room for easing
- **Chile:** Moody's changes the outlook on Chile's ratings to "negative"
- **Mexico** received considerably less foreign direct investment in the 2<sup>nd</sup> quarter of 2020
- **Peru:** Congress continues with controversial measures

### BRAZIL: PRESENTATION OF POST COVID-19 STIMULUS AND SOCIAL MEASURES DELAYED; BCB SEES MARGINAL ROOM FOR EASING

The expected announcement of post COVID-19 social and stimulus measures expected on Tuesday was postponed. The announcement was expected to include a new social program—Renda Brazil, as well as an infrastructure boosting plan. The government reportedly (Bloomberg) decided to seek a broader political consensus before announcing the package. We would not be shocked if the surprise veto by the Senate in Brazil last week which provided Bolsonaro with an unexpected political blow (Bolsonaro had vetoed the civil servant salary freeze overturning, which the Senate vetoed but Congress ultimately upheld), had something to do with this decision to play it safe. No date has yet been set on when the measures will be announced.

On the monetary policy front, BCB Governor Campos Neto said the economy still needs an inordinate amount of stimulus, but that any additional room for Selic rate cuts would be marginal (our house call is that there will be one more -25 bps cut), but continued to highlight that fiscal consolidation risks are the biggest risk for low rates. He also said he expects the bill to strengthen BCB autonomy, will be voted on in the next few weeks (this could strengthen the odds of lower rates being possible). On the data front, we got IPCA inflation for the first 15 days of August (IPCA-15), which printed at 2.28% y/y (chart 1), right below consensus of 2.30% and our call for 2.4%. The loss of upward momentum in inflation, should reinforce the odds of the final -25 bps cut we anticipate, particularly given it sits materially below the mid-point of the BCB's 3.5% inflation target, while this week's BCB survey of economists has 2021 year-end inflation at 3.0%, further leaving room for policy loosening.

—Eduardo Suárez

### CHILE: MOODY'S CHANGES THE OUTLOOK ON CHILE'S RATINGS TO "NEGATIVE"

On Tuesday August 25, "Moody's" changed the outlook to "negative" from "stable" on the Government of Chile. The negative outlook reflects increasing risks to Chile's fiscal strength. Even though the country entered the COVID-19 crisis with fiscal buffers and low debt relative to A-rated peers, debt-to-GDP had been rapidly rising in recent years, a trend that is being accelerated by the pandemic shock. Moody's expects debt to almost double relative to GDP in a five-year period, reaching 39% in 2021.

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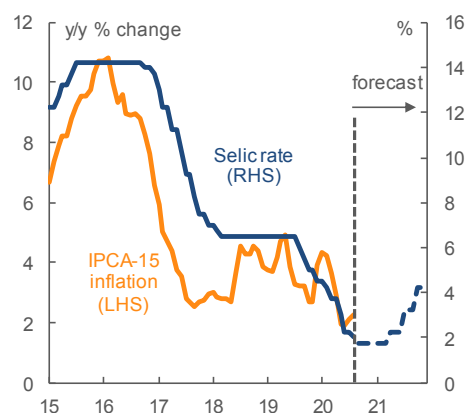
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#### Chart 1

**Brazil: IPCA-15 Inflation & Selic Rate**



Sources: Scotiabank Economics, IBGE, BCB.

Subpar medium-term growth prospects and rising social demands suggest that it will be difficult from a political economy perspective to prioritize fiscal consolidation against other competing policy priorities, which risks leading to a continued rise in debt ratios, beyond what we already expect in our baseline scenario, let alone debt reversal.

The COVID-19 outbreak, deteriorating global economic outlook and financial market turmoil are creating a severe economic and financial shock. According to Moody's, for Chile, the shock transmits mainly through weaker economic growth and increased demands for social programs that could translate into a larger spending base relative to government's revenue over time. Shifts in policy priorities due to social tensions may also erode policy effectiveness, a source of credit strength historically.

However, the agency affirmed the "A1" rating for long-term local and foreign currency issuer and senior unsecured ratings, and the (P)A1 foreign currency senior unsecured shelf ratings. Chile's "A1" rating is supported by the government's still relatively strong, albeit deteriorating, fiscal and debt metrics when compared to A-rated peers and the presence of important but narrowing fiscal buffers that help mitigate the impact of shocks. The "A1" rating also reflects solid, although pressured, institutions and a track record of policymaking that also reflects a commitment to fiscal prudence, supports macroeconomic stability and contains the country's susceptibility to event risk.

All in all, we reaffirm our GDP projection of -6.0% y/y for 2020, which we maintain with an upward bias given the latest economic data that point to a recovery in many sectors. The re-opening of the economy along with the impulse on consumption from the withdrawal of pension funds would be backing this recovery.

—Carlos Muñoz

## MEXICO RECEIVED CONSIDERABLY LESS FOREIGN DIRECT INVESTMENT IN THE 2<sup>ND</sup> QUARTER OF 2020

According to Q2 figures published on August 25 by Mexico's central bank, the current account was in a surplus of USD 5 mn (0.0% of GDP), contrary to expectations of a deficit of USD 1.9 bn. This follows a surplus of 1.4% in the second quarter of 2019. The central bank signalled that the international environment that Mexico faced during the second quarter of 2020 stands out for the profound impact that the COVID-19 pandemic had and the measures adopted to prevent its spread on global economic activity. The annual reduction in the current account balance in the second quarter of 2020 was mainly the result of a decrease in the surplus of the non-oil merchandise balance and a widening of the deficit of the services balance, which was partially offset by a reduction in the deficits of the primary income balance and the oil trade balance.

- A deficit of USD 5 mn was recorded in the capital account.
- The financial account, reported a surplus of USD 661 bn, well below the previous USD 8.516 bn and USD 4.352 bn a year earlier.
- Foreign direct investment (FDI) stood at USD 6.596 bn, significantly less than the USD 11.374 bn in the previous quarter and USD 6.431 bn a year earlier. In the first half of the year, FDI amounted to USD 17.969 bn (chart 2), compared with USD 20.802 bn in the first half of 2019, representing a -13.6% y/y decrease.

Chart 2

Mexico: Foreign Direct Investment



Sources: Scotiabank Economics, Banxico.

Looking forward, global uncertainty regarding the pandemic will remain high, and uncertainty over domestic factors could continue to hold business sentiment back. These factors could remain a drag on FDI for some time.

—Paulina Villanueva

## PERU: CONGRESS CONTINUES WITH CONTROVERSIAL MEASURES

On August 24, Congress approved a payment of up to PEN 4,300 to affiliates of the public pension system. The press reports government spokesperson estimating that the outlays would amount to over PEN 13 bn (USD 3.6 bn) or approximately 2%

of GDP. The Minister of Justice was quoted as saying that the government would veto the law and, if the veto is overridden, the law would be taken to the Constitutional Court on grounds of being unconstitutional. According to the Constitution, Congress cannot approve laws that require government spending. Unlike the law passed by Congress giving affiliates to the private pension fund system (AFPs) access to their private funds, the current law would need to be financed through public resources.

**Congress, has also required the presence of the Minister of Finance, María Alva, on two separate sessions, on September 4 and on the 7, to absolve questions on fiscal policy being implemented to confront the impact of COVID-19.** This should normally not be of significant consequence. However, this form of questioning (“interpelar”) does open the legal door for the potential removal of Minister Alva, should Congress choose to do so. Given how unpredictable this Congress has been, this option is a moderate risk.

—Guillermo Arbe

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