May 31, 2021

Latam Daily: PMIs and May Inflation; Banxico *QIR*; Peru Presidential Race Tightens

- **Central banks & macro: PMIs and May inflation; Banxico *QIR***
- **Peru: Presidential race tightens again**

CENTRAL BANKS & MACRO: PMIs AND MAY INFLATION; BANXICO *QIR*

PMIs in Brazil, Colombia, and Mexico dominate data releases this week, with Peru leading the first appearance of May inflation numbers and Colombia following at the end of the week. Central banks are scheduled to be quiet, with the exception of the publication of Banxico's June *Quarterly Inflation Report (QIR)* on Wednesday, June 2.

Argentina. Press reports on Sunday, May 30, indicated that the Ministry of Economy had confirmed that the country will not pay USD 2.4 bn in maturities falling due today, Monday, May 31, to Paris Club creditors.

- **The authorities are expecting to benefit from a possible 60-day grace period, though approval of this dispensation would normally require a comfort letter from the IMF, a fresh Article IV consultation, and ongoing monitoring.** Approval of the grace period is also complicated by a recent USD 400 mn debt-service payment to China, which is not a member of the Paris Club. The transfer raised questions about Argentina's respect for principles of equality of treatment in its relations with creditors.

- **Negotiations with the IMF on a new lending program to roll over USD 44 bn in outstanding borrowing, once expected to conclude in May, are now unlikely to be finalized until after scheduled mid-term elections in October 2021.** This is likely to delay until late-2021 any action by the BCRA to stabilize price pressures that have pushed sequential inflation consistently north of 4% m/m sa.

Brazil. April fiscal numbers, out on Monday, May 31, and Q1 GDP data, due Tuesday, June 1, should show further strengthening in the economy despite still high levels of COVID-19 community infection and efforts announced Friday, May 28, to tighten restrictions on foreigners' entry into the country.

- The **primary budget surplus** is expected by consensus to widen from BRL 5 bn in March to BRL 17.7 bn in April following the conclusion of some emergency spending programs. This would put the rolling 12-month primary deficit around -7% of GDP.

- The fiscal picture is being helped by **consolidating economic activity**, with Q1 sequential growth expected to slow from 3.2% q/q sa in Q4-2020 to 0.8% q/q sa in Q1-2021. This would bring annual growth up from -1.1% y/y at end-2020 to 0.7% y/y in Q1-2021, but still leave total activity slightly below pre-pandemic levels on a rolling four-quarter basis.

- May **manufacturing and services PMIs**, due for release on Tuesday, June 1, and Friday, June 4, respectively, could show some marginal gains on the back of strong external demand and Q1's growth performance (chart 1).

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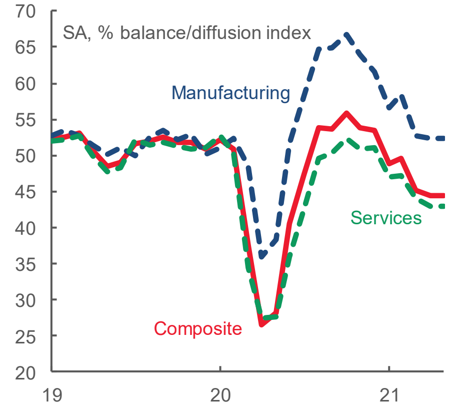
Chart 1

Brazil: Monthly PMIs Set to Stabilize

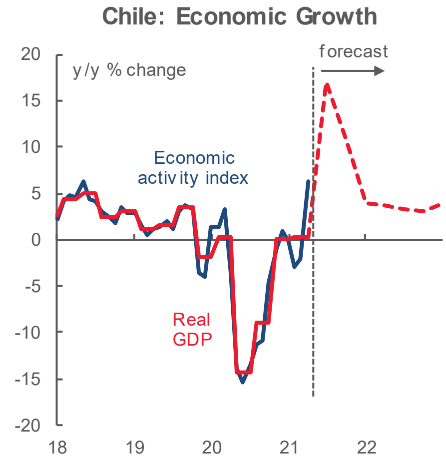


Sources: Scotiabank Economics, Markit.

Chile. A suite of activity numbers out on Monday, May 31, are likely to point to softer sequential growth in April's IMACEC monthly GDP proxy, which would still represent a strong improvement over last year's lockdowns.

- Our team in Santiago expects the **unemployment rate** to edge up from 10.4% in March to 10.6% in April. The move would be explained by rising labour-market participation rates while employment remained below pre-pandemic numbers.
- **Retail sales growth** is expected to slow in sequential terms in April as consumer confidence declined, but this would still result in an annual surge from 23.8% y/y in March to 43.0% y/y in April owing to base effects from last year's closures.
- **Industrial production growth** could slow in both sequential and annual terms in April, declining from 2.9% y/y in March to 2.6% y/y in April as business confidence waned.
- As a result, Scotiabank Economics expects **monthly economic activity growth** to rise from 6.4% y/y in March to 7.5% y/y in April (chart 2), which would be consistent with a deeper sequential contraction from the -1.6% m/m sa recorded in March. Core inflation should remain below 3% y/y as there is still substantial slack in the Chilean economy.

Chart 2



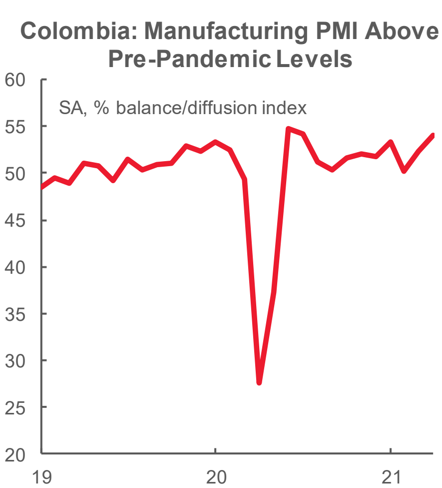
Sources: Scotiabank Economics, BCCh.

Colombia. May **manufacturing PMI** numbers, due Tuesday, June 1, are likely to show a temporary decline from recent highs (chart 3). Meanwhile, May **inflation**, set for release on Saturday, June 5, is likely to show an acceleration in sequential terms from 0.59% m/m sa in April and a base-effect-driven jump in annual terms from April's 1.95% y/y to converge toward the BanRep's 3% y/y target (chart 4).

Mexico. Amidst a revival in domestic demand, May PMIs and Banxico's June *QIR* are both set to provide slightly brighter pictures of the Mexican economy.

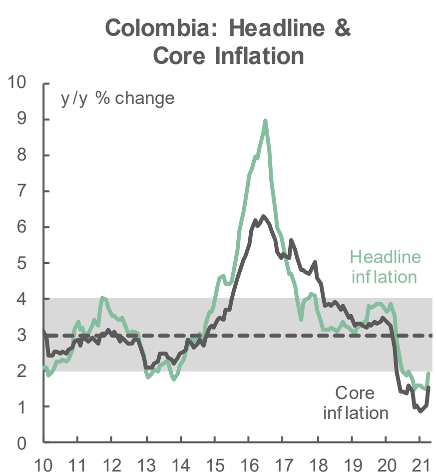
- **Manufacturing and services PMIs**, which have been trending upward lately (chart 5), are likely to continue firming in May data due on Tuesday, June 1.
- **Banxico's June *QIR***, due to be published on Wednesday, June 2, shall likely feature upgraded growth forecasts for 2021 and 2022, but also higher inflation risks, both of which were acknowledged in the minutes from the Board's May 13 policy-rate decision. Still, the central bank's assessments are likely to still be aligned with our CDMX team's expectation that the benchmark policy rate will be held unchanged at 4.00% until the beginning of 2022.

Chart 3



Sources: Scotiabank Economics, Markit.

Chart 4



Sources: Scotiabank Economics, DANE.

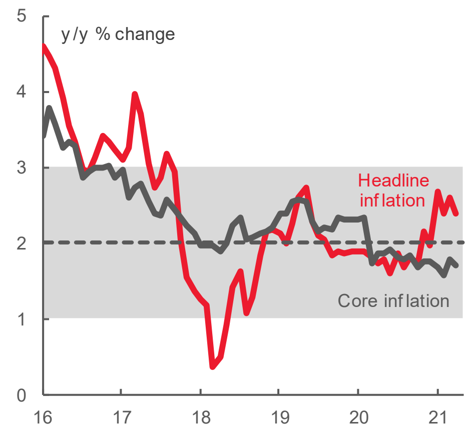
Chart 5

Sources: Scotiabank Economics, IMEF.

Peru. **The country leads the May inflation prints with its benchmark Lima price numbers out on Tuesday, June 1, where the outcomes are likely to move sideways from April.** Our Peru team expects May headline inflation to be unchanged from April at 2.4% y/y with core holding at 1.7% y/y (chart 6), though FX pass-through and non-core price pressures would push sequential inflation up from -0.1% m/m sa in April to 0.3% m/m sa in May. Headline inflation has averaged 2.5% y/y (0.34% m/m sa) in the first four months of 2021, while core averaged 1.7% y/y (0.20% m/m sa). The BCRP is unlikely to feel urgency to begin tightening its monetary -policy stance with headline inflation still well-behaved despite unfavourable base effects from last year's lockdowns. Core inflation persistently below the BCRP's 2% y/y headline target since March 2020 reflects ongoing slack in the Peruvian economy.

—Brett House

Chart 6



Sources: Scotiabank Economics, BCRP, INEI.

PERU: PRESIDENTIAL RACE TIGHTENS AGAIN

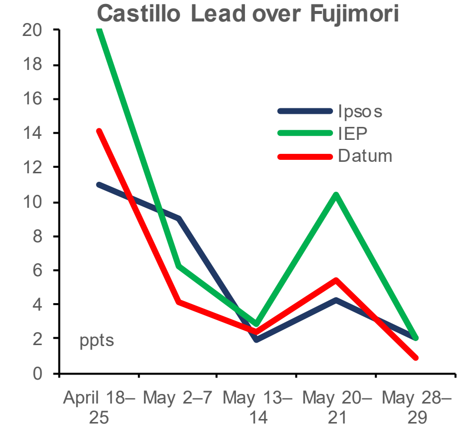
Three polls published in recent days showed Peru's presidential race tightening further ahead of Sunday night's candidates' debate and only a week prior to the June 6 run-off vote (chart 7).

- **In a voting simulation conducted by Ipsos on Friday, May 28, Pedro Castillo would garner 51.1% of votes cast with 48.9% for Keiko Fujimori according to results released on Sunday, May 30.** With 20% of participants still undecided and voting mandatory, these polling shares would translate into 40.9% and 39.1%, respectively, which means that the exercise implies that the race is now a toss-up and currently undecided voters could determine the outcome on June 6.

- **A separate survey conducted by phone during May 27–28 by the Instituto de Estudios Peruanos (IEP) and published on Sunday, May 30, produced similar results.** Compared with the previous iteration of the poll from May 23, support for Castillo fell from 44.8% to 40.3%, while voting intentions for Fujimori rose from 34.4% to 38.3%, with only 6.3% of voters undecided, 13.0% intending to spoil their ballots, and 2.0% failing to provide a response.

- **On Friday, May 28, a poll by Datum also showed Castillo registering only a slight lead of 42.6% to 41.7% over Fujimori, with 15.7% voting blank or void.**

Chart 7



Sources: Scotibank Economics, Ipsos, IEP, Datum.

Castillo's lead over Fujimori had been closing in early-March and late-April, but then had widened last week; the tightening in the gap returned this week. This renewed competitiveness in the race has occurred for a number of reasons. More than points won by Fujimori, this seemed to be a week in which points were lost by Castillo. According to some analysts, last week's debate between members of the two candidate's respective government planning teams revealed how weak the Castillo side is. However, other factors may have had equal or greater weight.

- **During the week Castillo came under fire for suggesting that the private pension-fund system would be replaced by a state-sponsored Workers Bank.** This led to concern over what would happen to individual assets, a worry which Castillo's spokespeople, instead of allaying, managed to intensify by giving rather confusing and contradictory messages. This is a sensitive point for nearly eight million people who are part of the private pension-fund system.

- **The volatility in the USDPEN rate in recent days is also likely to have triggered a risk-adverse reaction. The country continues to have a relatively high level of dollarization.** Finally, on May 23 a terrorist attack in the Peruvian selva (rainforest) in which 16 civilians were killed by a group linked to the Sendero Luminoso may have hurt Castillo due to the group's identification with the left, and helped Fujimori, as her father's government is identified by many as having been successful in defeating Sendero.

With one week left before the elections, the question is whether this tightening of the gap has run its course or whether it is part of an ongoing trend.

Much might depend on the last presidential debate which took place last night, Sunday, May 30. Fujimori had the benefit of greater experience in debate situations and came prepared to answer the criticisms Castillo sent her way, albeit without forsaking a broad and interesting presentation of her proposals. Castillo also came better prepared than in the past, and spoke calmly and reasonably, but was much more controversial, and less able to lay out the specifics of his proposals. Initially, Castillo appeared to want to send the message that there would be nothing to fear from his government, and that, in particular, his government would not put private family savings and business resources at risk. But, as the debate progressed, Castillo's messages became more mixed. He stated, for example, that the State should control markets. Even as he contended that assets in the private pension-fund system would not be touched by a Castillo administration, almost in the same breath he also said that his government would do away with "the abuses of the AFPs". In general, Castillo continued proposing an expanded role for the State, the "recovery" of the oil and gas sector, and the renegotiation of mining company contracts.

With the race so tight, the debate may make a difference on the margin.

—Brett House & Guillermo Arbe