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## Latam Weekly: Chile's Central Bank Next to Bat; Global Markets Await US CPI

## ECONOMIC OVERVIEW

- Chile's BCCh to roll out another 25 or 50bps hike at its policy decision next week amid elevated inflation.
- Markets will monitor frictions between Colombia's Petro and BanRep after the president's comments on foreign exchange controls.
- The US release of CPI figures on Thursday will catch the market's eye during a short trading week in the US and Canada.

## PACIFIC ALLIANCE COUNTRY UPDATES

- We assess key insights from the last week, with highlights on the main issues to watch over the coming fortnight in the Pacific Alliance countries: Chile, Colombia, Mexico, and Peru.

## MARKET EVENTS &amp; INDICATORS

- A comprehensive risk calendar with selected highlights for the period October 8–21 across the Pacific Alliance countries and Brazil.

## Economic Overview: Chile's Central Bank Next to Bat; Global Markets Await US CPI

- **Chile's BCCh to roll out another 25 or 50bps hike at its policy decision next week amid elevated inflation.**
- **Markets will monitor frictions between Colombia's Petro and BanRep after the president's comments on foreign exchange controls.**
- **The US release of CPI figures on Thursday will catch the market's eye during a short trading week in the US and Canada.**

It was a volatile week for global markets with OPEC+ rolling out a larger than expected supply cut, the US reporting another strong gain in employment, and each of the Pacific Alliance countries releasing inflation figures for September that, in the case of Colombia and Chile, may have made central bankers somewhat uncomfortable.

**Peru's BCRP hiked by a widely expected 25bps at its policy decision on Thursday while leaving the door open to small tightening steps** while it maintains a data-dependent approach (see [Latam Daily](#)). Economic activity data due next week may worsen the bank's dilemma in fighting elevated inflation against weakening growth.

**In Colombia, Thursday's CPI data surprised economists and likely BanRep members—who sounded more confident at their recent meeting that inflation would slow in September.** BanRep anticipates that the Colombian economy will respond more significantly to the current hiking cycle next year, given the monetary policy lag, and additional large hikes may be unnecessary. However, the limited signs that inflation is decelerating are challenging their recent downshift in the pace of hiking.

**President Petro's comments on the negative impact on the economy of rising rates and his floating of a temporary tax (or capital controls) on 'hot money flows' responding to BanRep's rate settings have put markets on alert.** BanRep Governor Villar said today that foreign exchange controls can have 'perverse' effects. Close attention will likely be paid to friction between the executive and the central bank over coming days alongside the release of August retail sales, industrial production, and economic activity data next week.

**On Wednesday, we anticipate that Chile's central bank will hike its policy rate by 25 or 50bps after Friday's CPI release showed a still uncomfortably high rate of inflation—particularly when the most volatile components are excluded. Discussions over the guidelines for drafting a new constitution next year will also take place** as parties coalesce around limiting the powers of the assembly tasked with its authorship. **Chilean markets are closed on Monday.**

**The Mexican data and events calendar is relatively empty aside from Banxico's meeting minutes and industrial production figures for August.** The bank hiked by 75bps at its most recent meeting and is expected to continue to keep pace with the Federal Reserve while they express concerns about higher for longer core inflation in Mexico. **In this week's report, our team looks at the political risks ahead in Mexico including USMCA negotiations and the possible end of Esquivel's term at the Banxico Board in December.**

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**The final thing to monitor in the region is the evolution of second-round polls in Brazil.** Former President Lula is still leading the incumbent Bolsonaro, but the latter could see some votes flow his way in coming weeks, with a televised debate scheduled for October 16. **Brazil also publishes September CPI figures on Tuesday, where the median economist is projecting a 7.14% y/y increase in prices—slowing from August’s 8.73% and contracting m/m for a third consecutive month.**

**Global markets will, however, remain laser-focused on Thursday’s US CPI release that should reinforce expectations for continued aggressive hikes from the Federal Reserve—and see continued downward pressure on global markets and risk-sensitive currencies. With US markets closed on Monday, low participation may result in sharp gyrations in markets that affect the appeal of Latin American assets.**

## Pacific Alliance Country Updates

### Chile—Wide Political Agreement for a New Constitution in Progress, with Less Space for Extreme Proposals

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On Wednesday, October 12, the central bank (BCCh) will announce its monetary policy decision, where we expect a 50bps increase, in line with the latest Financial Traders Survey but in contrast to most recent Economic Expectations Survey that sees a 25bps hike. After the reference rate reaches its maximum level at the October meeting, we think the BCCh will be forced to cut the rate quickly and aggressively upon the first signs of disinflation amid a negative output gap and an economy heading towards a full recession. We anticipate cuts of “no less” than 100bps during Q1-2023, compared to the BCCh’s base scenario of 25bps (September [Monetary Policy Report](#)).

Political parties that have representation in Congress are negotiating a broad political agreement that defines the guidelines for drafting a new constitution next year. With the rejection of the assembly proposal, the political parties have agreed on the idea of putting up ‘walls’ or ‘limits’ on the work of the new assembly, which would be elected by popular vote during the second quarter of 2023 and would be advised by a group of experts. In general, the political parties widely agree that, prior to the work of the new assembly, it must be established that the constitution ensures: a unitary State, autonomy of the powers of the State, and respect international agreements and rights. Regarding the composition of the assembly, the political parties proposed: the participation of Indigenous people in relation to their share of the population, independents as part of the lists of established political parties, and gender equality. Other matters that the political parties want to enshrine before the work of the assembly are the autonomy of the central bank and the existence of the Senate. In our view, all of the above would give greater certainty that extreme proposals can be avoided, such as those present in the recently rejected constitutional proposal.

### Colombia—Why is Economic Growth Gaining Ground in BanRep’s Discussion? And What Can We Expect from the Tax Reform?

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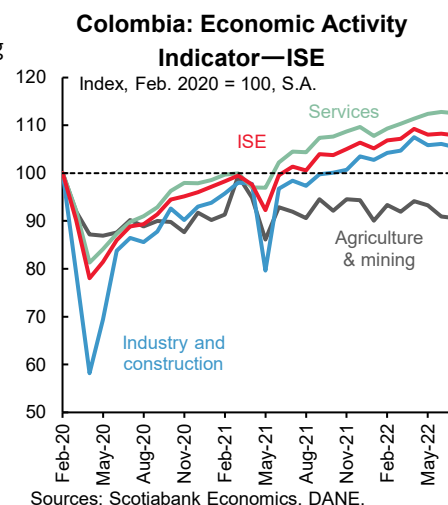
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A few days ago, BanRep surprised the market with a dovish move of a 100bps hike in a conciliatory split vote with 6 members voting for 100bps and one member voting for 50bps. The meeting’s minutes confirmed that concerns about an economic deceleration are increasing within the Board. However, what is economic activity showing? And what would confirm that BanRep is ready for a rate hikes pause?

In the year to July, the Colombian economy grew by 8.9%, but it is showing mixed signals with strong private consumption against weaker investment. On the supply side of the economy, previous imbalances have translated into a solid services sector compared to weaker primary and secondary sectors (chart 1). The current context in which headwinds such as challenging supply chains, potential tax increases, potential high increases in the minimum wage, etc. are leading to moderating business optimism, where higher rates are also hurting investment decisions in the medium term. On the demand side, despite consumer credit lending rates surpassing 36%, households maintain a stable but high demand for loans (consumer credit growing above 23% y/y), which is expected to moderate in the future.

That said, our central bank anticipates that in 2023 the economy would show the impact of the current hiking cycle and that’s why BanRep was more cautious regarding the size of the most recent hike. Leading indicators such as confidence surveys but also high-frequency data are becoming more relevant as they would confirm or challenge BanRep’s expectations. For now, we expect more moderate activity. We now also expect that at the October meeting, BanRep will likely continue to increase rates at a slower rate, probably signaling that the end of the hiking cycle is close.

Chart 1



In terms of inflation, despite September's surprise, it is expected that fading high statistical base effects will contribute to a cooling of inflation from around ~12% to something closer to ~6%, which is a win for the central bank. But as inflation is not expected to reach 3%, we don't anticipate that inflation will ease enough to allow large cuts in the monetary policy rate soon. Instead, **BanRep could be conditioned by tightening international financing conditions and by the fact that inflation will again deviate from the target range.** All in all, activity data out next week could confirm that BanRep was correct to take cautious path.

**Fiscal policy is also in the spotlight after the fiscal reform was presented this week.** The government moderated its expectation for additional revenue from COP25tn (1.7% of GDP) to COP22tn (~1.5% of GDP). The main contributors to additional fiscal revenue will be individuals (approx. 33%), while companies will also contribute with ~20%+ of the additional revenue. **The main approach of the MoF was to eliminate exemptions and implement surcharges to certain sectors such as the oil and coal sector (10% in the first year, 7.5% in the second, and 5% in the third year of implementation), the financial sector (5%), and hydroelectric companies (3%). Our take on the tax reform is that it would be credit-neutral as credit agencies are perceiving that the debt to GDP ratio will continue to deviate from the investment grade peers (chart 2).**

That said, Colombia is nearing a wait-and-see mode in terms of fiscal but also monetary policy. Higher rates and higher taxes could impact the economic performance in 2023. For now, it is too early to discuss rate cuts as uncertainty around inflation remains. Markets, for now, are pricing a structurally weaker dollar, but with some stabilization on average in the yield curve.

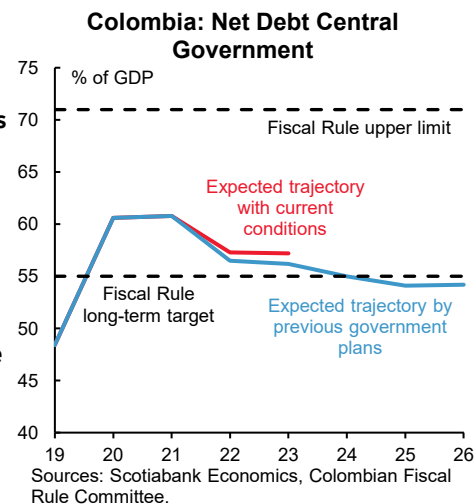
## Mexico—Political Calendar Update, and Possible Implications for MXN

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**Despite global financial market turbulence, the MXN remains anchored by limited positioning** (foreign holdings of m-bonos halved over the past 4 years, and portfolios flows into both equities and bonds had almost 4 years of consistent drops), **as well as cautious monetary policy execution by Banxico.** Although the tilt of the Banxico Board is arguably more dovish today than at any point in the last 15 years, it remains a very prudent institution. This has led MXN to sit as the third best performing major FX on a year-to-date basis. There are some metrics by which the MXN starts to look a little expensive, however, including underperforming market share gains in US imports (Mexico is trailing both Vietnam and Canada), and, more technically, its real effective exchange rate. **However, with a high carry and weak positioning, it could take a political event to trigger a correction for MXN. There are several important events to keep track of over the coming weeks, both on the domestic and external agendas.**

- **On the legislative front, there is speculation that with the process of extending the [presence of the military on the streets to combat crime now behind us, the next item for reform will be the electoral institute.](#) There have been [previous attempts](#) to push a reform of the electoral system, but those failed. **We don't see either of these issues being a major market driver.****
- **Banxico deputy governor Esquivel's term is set to end in December. [By law](#), a member of the Board of Banxico cannot be older than 65 at the start of his/her term so, at 56, he could be asked to serve a full term. However, **Esquivel has had some [public disagreements with President Lopez Obrador over the autonomy of Banxico. Esquivel has proven to be a strong and independent voice within the Board. However, he is also arguably the most dovish member of the Board](#)**, so unless he is replaced by someone who is both dovish, and non-independent, **we don't see a change at the Board of Banxico as a major driver for MXN weakness** (but a hawk on the other hand could prove a support for MXN).**
- **The 2023 electoral calendar is light, but includes Governor elections in Coahuila and the State of Mexico, the latter being the most important state in the country by population and economic relevance.** The State of Mexico election will provide important guidance for how strong Morena is heading into the 2024 presidential election (The PRI has never lost the governorship there), but should have little impact beyond that.

Chart 2



- **As we head into the end of 2023, the 2024 elections in both the US and Mexico will come into focus.** In recent elections, the most relevant electoral theme for MXN has been when US candidates question NAFTA / USMCA (Clinton, Obama, and Trump all did), but **at this point this does not seem positioned to be an electoral topic. Accordingly, this is a risk to monitor, but at this point in time, it does not seem like a major MXN risk.**
- **The [Consultations](#) under USMCA over Mexico's energy policies that were started by Canada and the USA were extended past the 75-day window specified in the treaty.** However, if an agreement is not reached the next step will be the start of arbitration procedures. On this front, Mexico's Economy Minister Tatiana Clouthier announced on October 6 that she is leaving her post. We don't know at this time whether her announced departure is linked to the evolution of this procedure. On Friday, the president announced Raquel Buenrostro, the current Head of the country's tax authority, will take over the role.

Taking all of the above into consideration, we don't anticipate political dynamics to have too much impact on the peso, at least until late-2023. Hence, we anticipate that global risk appetite, Banxico's willingness to continue to maintain a 600bps spread over US rates, as well as macro flows (remittances, net exports, etc.) will remain the primary drivers for the peso, meaning we continue to see a relatively stable MXN over the coming 6–12 months, consistent with the current pricing of USD/MXN swaps.

## Peru—The BCRP's Emerging Conundrum: Inflation versus Growth

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**August GDP data to be released next weekend will be key to determine whether the sharp slowdown to 1.4% y/y in July was an exception, or, as we believe, the onset of a low-growth period for Peru.** Given preliminary figures, we are expecting about 2% y/y GDP growth for August, a tad better than July, but well below the 3.5% of the first half of 2022.

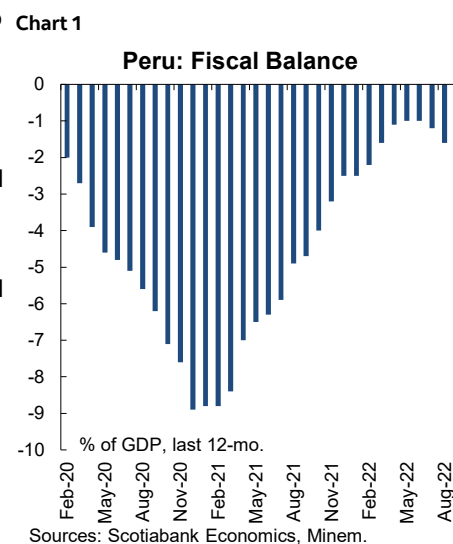
**Slowing growth puts the BCRP in a bit of a bind, as inflation (8.5% y/y in September) is still high. So far, high inflation has been carrying a greater weight on the BCRP's balance of concerns, but with the reference rate at an uncomfortably high 7.0% after the decision on October 6, the BCRP may be considering that it's almost time to stop raising rates. We still expect one more 25bps increase in November, but even this is not a sure thing.** The BCRP, in its monetary program announcement, seemed to be hedging its bets.

**Another concern that the BCRP is juggling is the FX rate.** FX volatility has not been all that high, all things considered, but that may simply reflect a market that recognizes that the BCRP has been acting as a stabilizer of last resort. Recently, the USDPEN pressed against the 4.00 mark, which many in the market consider may be as high as the BCRP wishes it to go—for now.

**On October 13, the BCRP will release public finances data for September. We expect the fiscal deficit to come in just above the 1.6% of GDP figure that was released for the twelve months to August (chart 1).** This means that the deficit will remain comfortably under 2% of GDP (also for now). The fiscal deficit had fallen to a low of 1.0% in May–June, just after the April–May tax season ended, but such a low level—to the extent that it reflected seasonal factors—was never expected to last. **Going forward, structural issues should carry a greater weight on the deficit, namely, a slowing economy and lower metal prices.**

**Tax revenue growth is slowing quickly.** On the face of it, the 5% y/y growth already released for September does not seem all that bad, except that it was a far cry from the nearly 19% pace in the year-to-August. Tax revenue growth is likely to continue to weaken reflecting lower copper prices and a slowing economy, and **we expect the fiscal deficit to surpass 2% of GDP in a matter of months.**

**Peru recently held regional and local elections, for governors and mayors. The most notable result of the elections was the victory of ultra-conservative candidate Rafael López Aliaga in Lima.** Moreover, the three leading candidates in Lima were right-wing, and garnered around 70% of votes between them. **López Aliaga, in particular, has been very vocal in his opposition to President Castillo.** Also significantly, the government party Perú Libre, leftist parties in general, and the fujimorista party Fuerza Popular, all had extremely poor



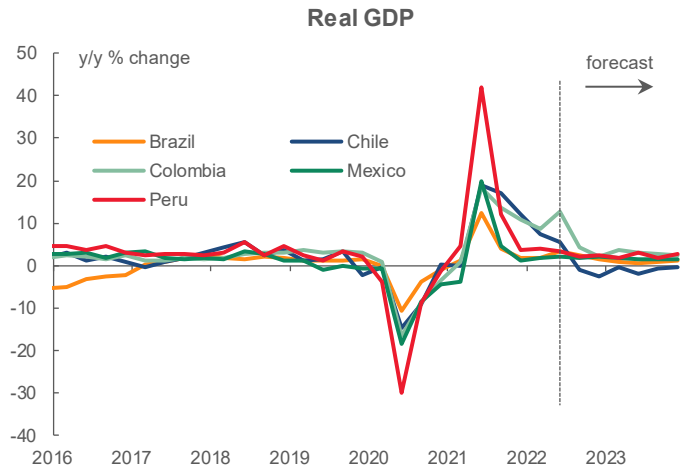
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October 7, 2022

showings. **Outside of Lima, regional movements dominated**, as has been the case for quite some time now. **Lima has now turned into a more polarized place, politically.** This has not been the case for the rest of the country, however. Setting politics aside, the problem with regional and local movements is they have proven in the past to be very poor state managers. This, I'm afraid, seems unlikely to change under the new authorities.

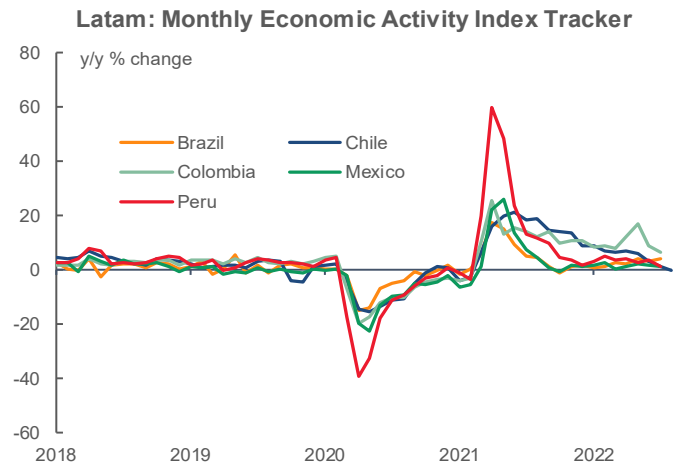
Key Economic Charts

Chart 1



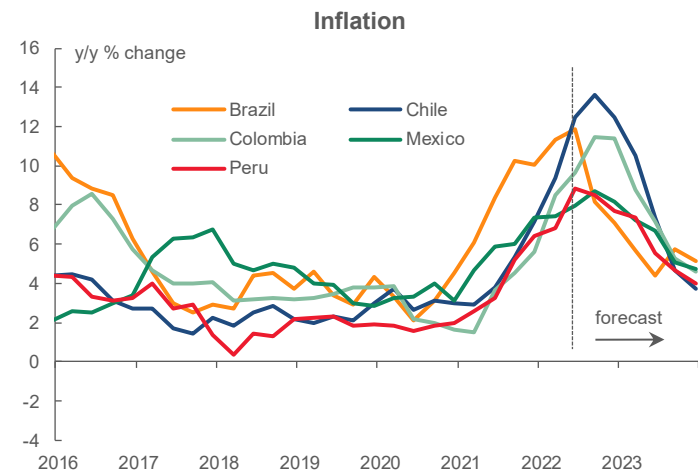
Sources: Scotiabank Economics, Haver Analytics.

Chart 2



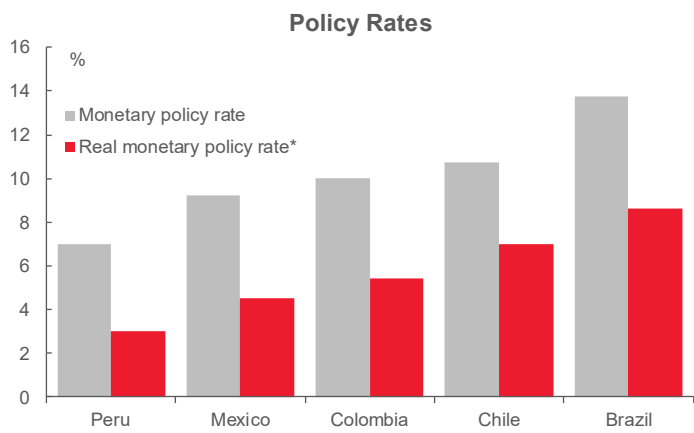
Sources: Scotiabank Economics, Haver Analytics.

Chart 3



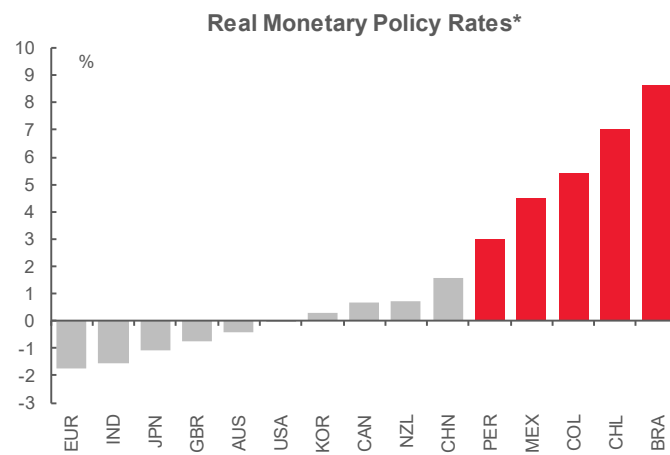
Sources: Scotiabank Economics, Haver Analytics.

Chart 4



\* Real monetary policy rate = current policy rate - BNS expected inflation, end-Q4-2023, % y/y. Sources: Scotiabank Economics, Haver Analytics.

Chart 5



\* Real monetary policy rate = current policy rate - BNS expected inflation, end-Q4-2023, % y/y. Sources: Scotiabank Economics, Bloomberg.



Key Market Charts

Chart 1

Latam Currencies Performance

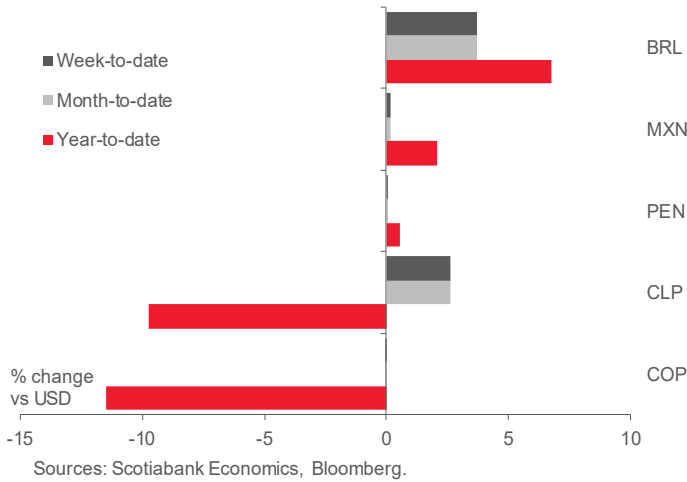


Chart 2

Latam Equities Performance

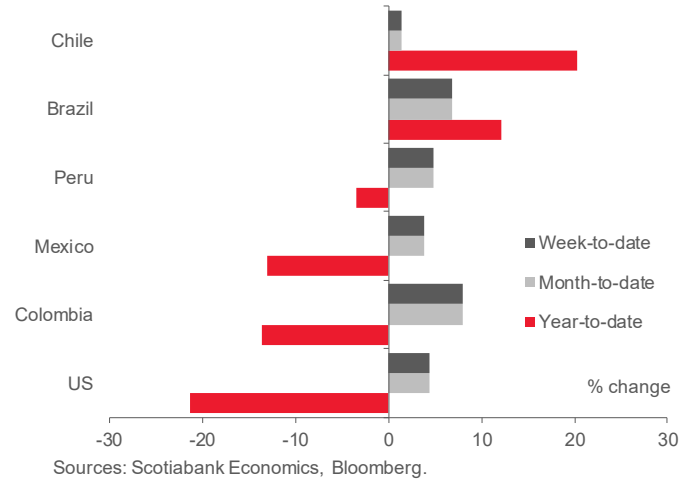


Chart 3

USD vs Latam Currencies

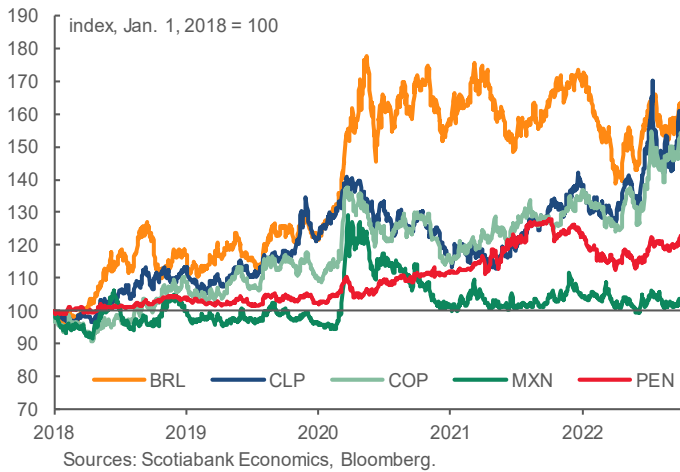
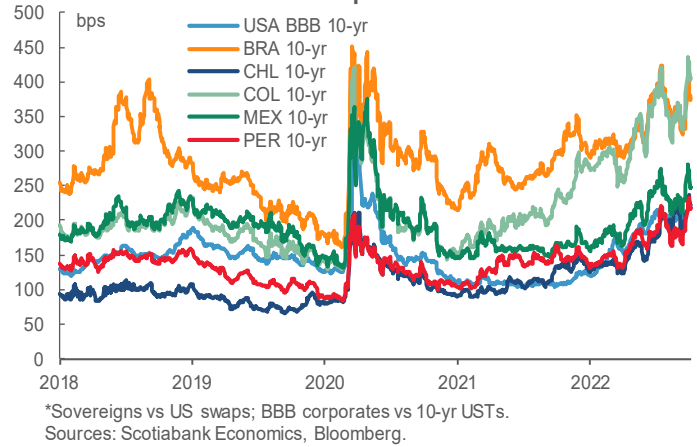


Chart 4

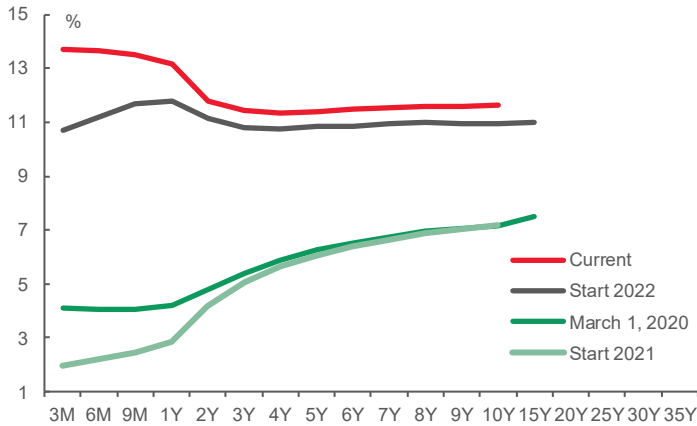
10-yr CDS Spreads: Latam Sovereigns & US BBB Corporates vs US\*



**Yield Curves**

**Chart 1**

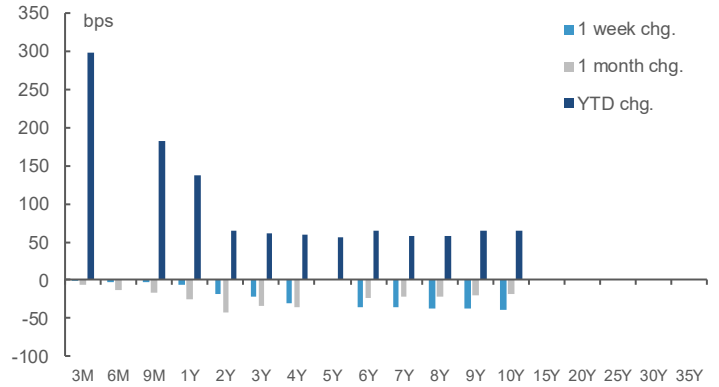
**Brazil: BM&F Pre x DI Curve**



Sources: Scotiabank Economics, Bloomberg.

**Chart 2**

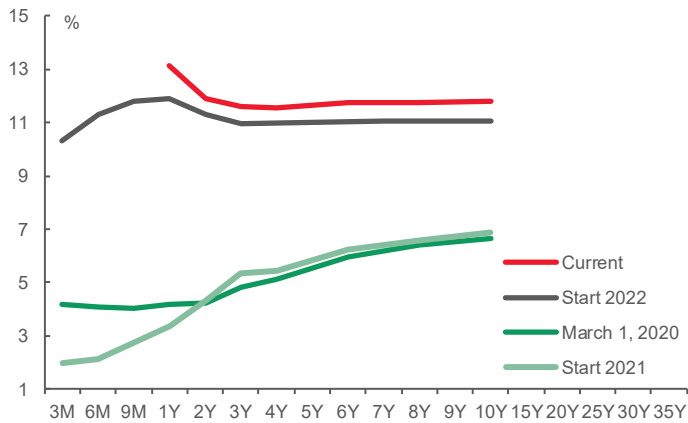
**Brazil: BM&F Pre x DI Curve Moves**



Sources: Scotiabank Economics, Bloomberg.

**Chart 3**

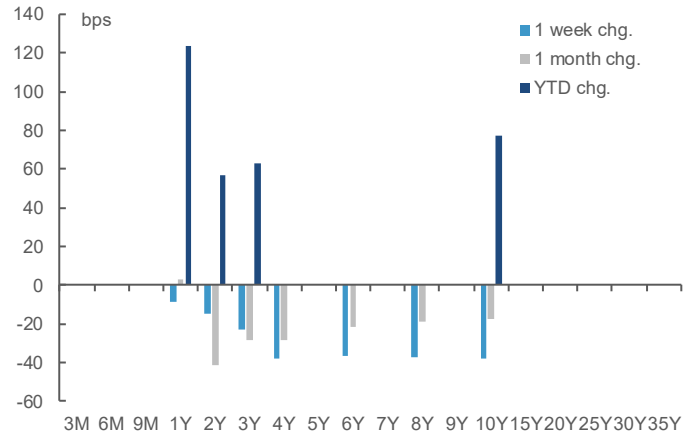
**Brazil: NTN Curve**



Sources: Scotiabank Economics, Bloomberg.

**Chart 4**

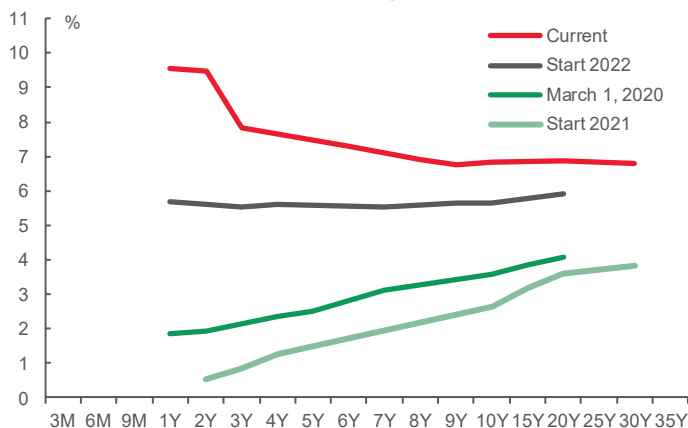
**Brazil: NTN Curve Moves**



Sources: Scotiabank Economics, Bloomberg.

**Chart 5**

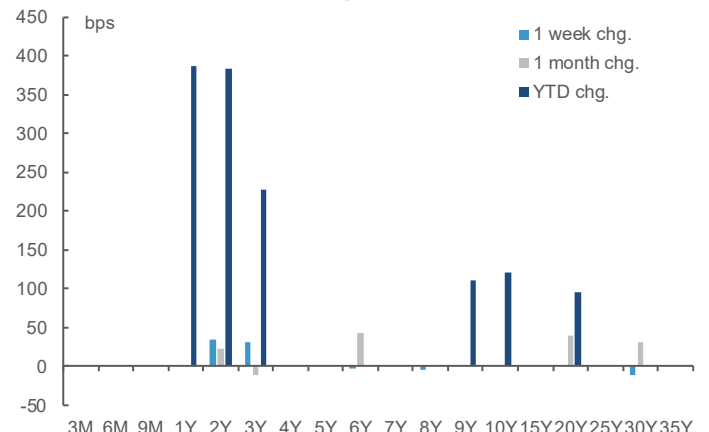
**Chile: Sovereign Curve**



Sources: Scotiabank Economics, Bloomberg.

**Chart 6**

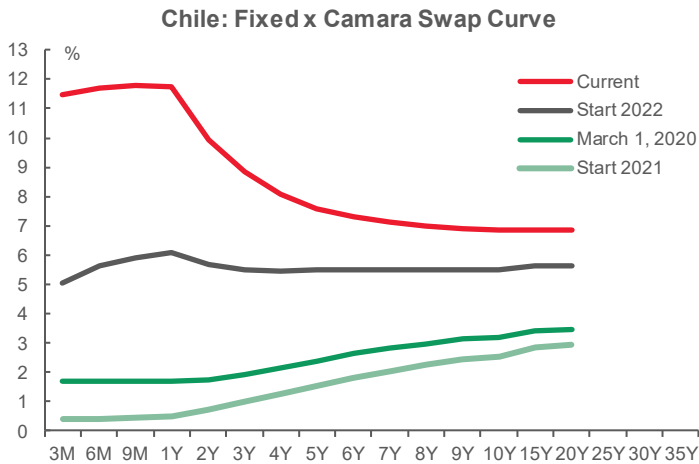
**Chile: Sovereign Curve Moves**



Sources: Scotiabank Economics, Bloomberg.

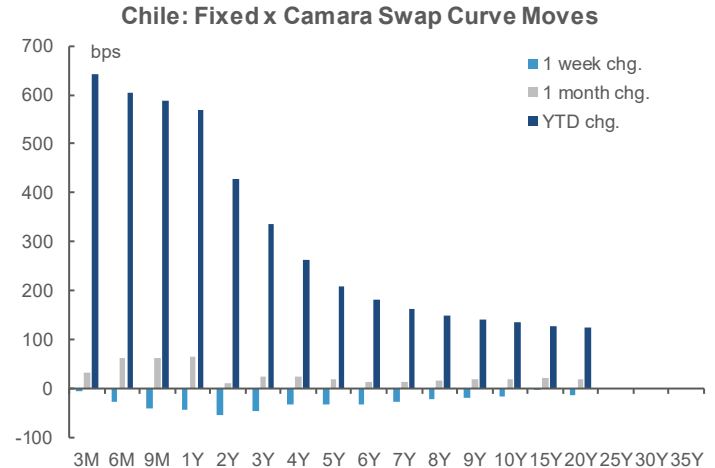
Yield Curves

Chart 7



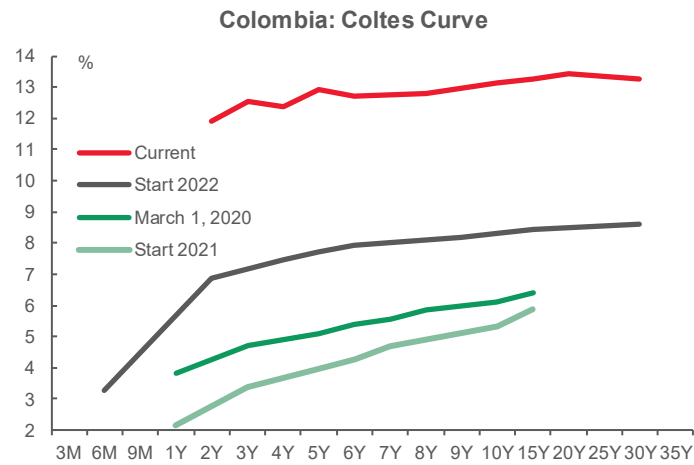
Sources: Scotiabank Economics, Bloomberg.

Chart 8



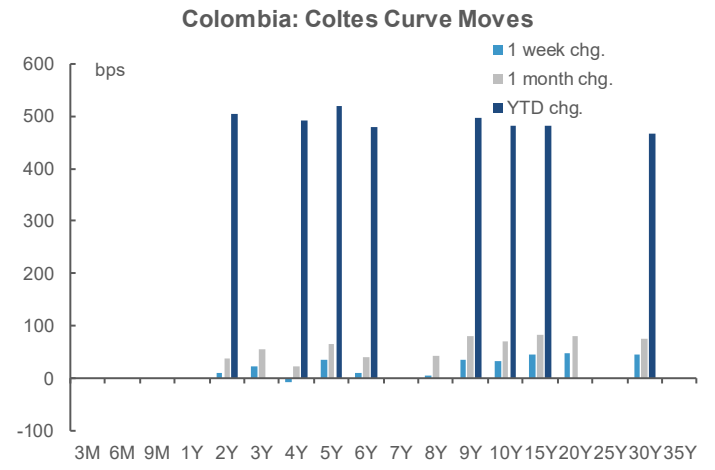
Sources: Scotiabank Economics, Bloomberg.

Chart 9



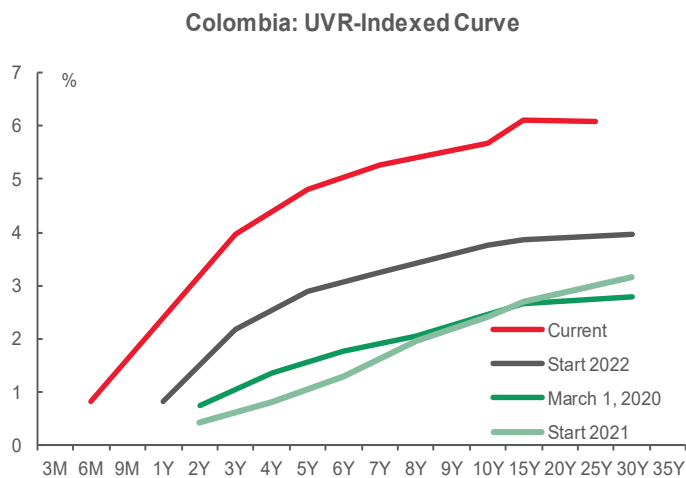
Sources: Scotiabank Economics, Bloomberg.

Chart 10



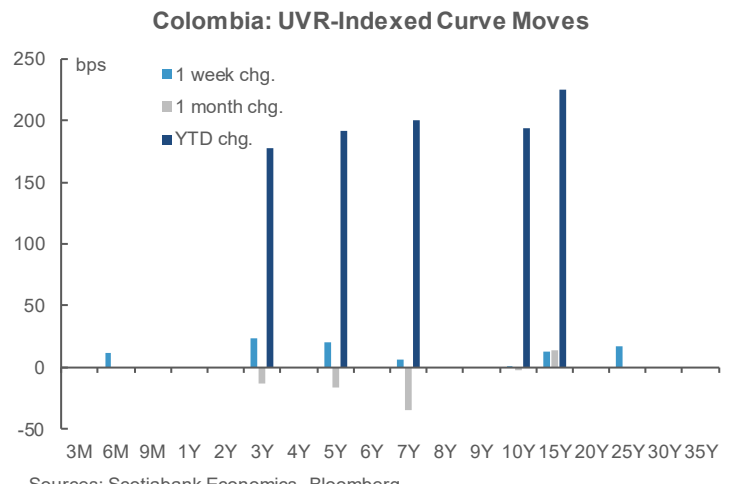
Sources: Scotiabank Economics, Bloomberg.

Chart 11



Sources: Scotiabank Economics, Bloomberg.

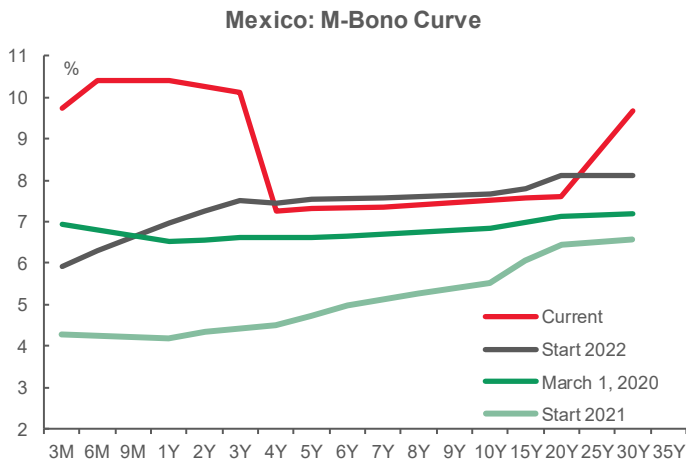
Chart 12



Sources: Scotiabank Economics, Bloomberg.

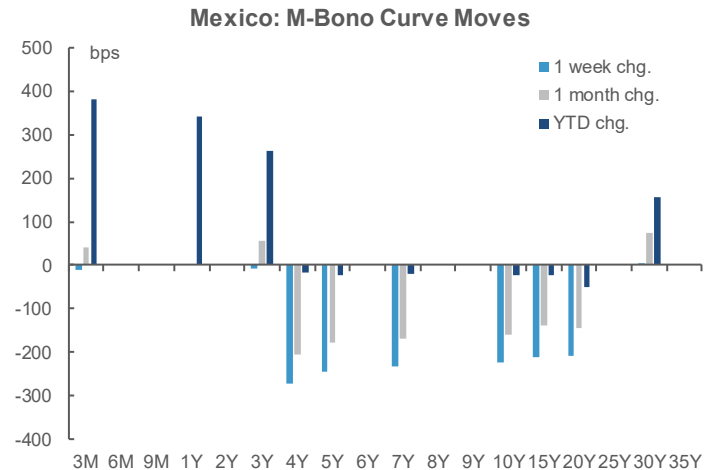
Yield Curves

Chart 13



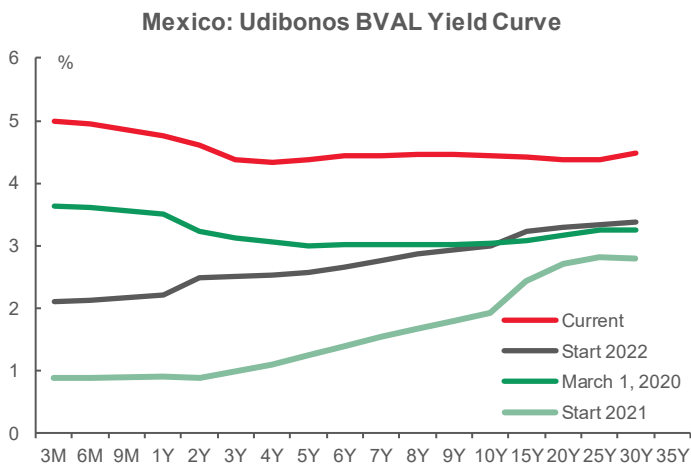
Sources: Scotiabank Economics, Bloomberg.

Chart 14



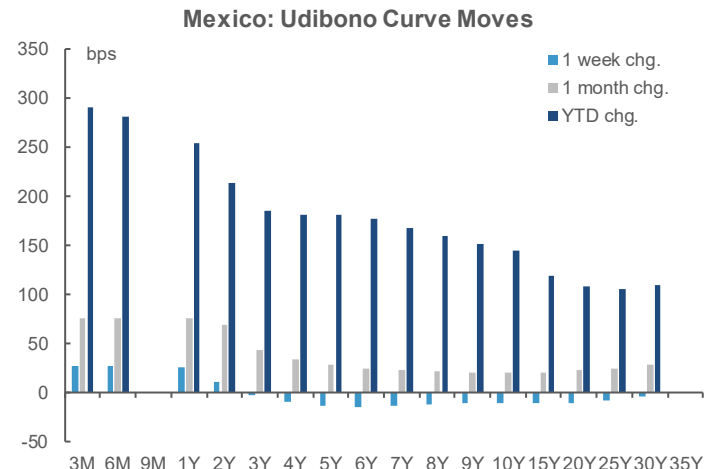
Sources: Scotiabank Economics, Bloomberg.

Chart 15



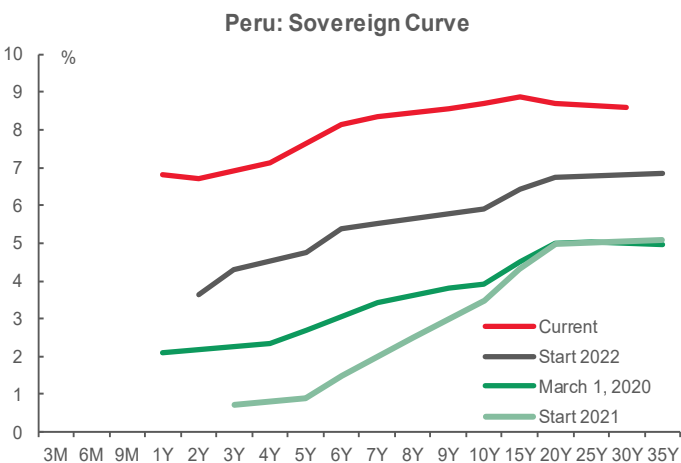
Sources: Scotiabank Economics, Bloomberg.

Chart 16



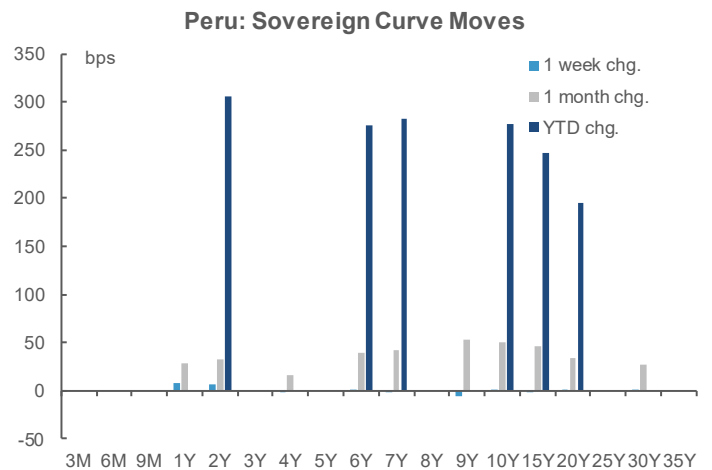
Sources: Scotiabank Economics, Bloomberg.

Chart 17



Sources: Scotiabank Economics, Bloomberg.

Chart 18



Sources: Scotiabank Economics, Bloomberg.

Market Events & Indicators for October 8–21

**BRAZIL**

Date	Time	Event	Period	BNS	Consensus	Latest	BNS Comments
Oct-10	7:00	FGV CPI IPC-S (%)	07-Oct	--	--	--	0.0
Oct-10	7:25	Central Bank Weekly Economist Survey		--	--	--	--
Oct-10	14:00	Trade Balance Weekly (USD mn)	09-Oct	--	--	--	113.2
Oct-11	4:00	FIPE CPI - Weekly (%)	07-Oct	--	--	--	0.1
Oct-11	8:00	IBGE Inflation IPCA (m/m)	Sep	--	--	-0.3	-0.4
Oct-11	8:00	IBGE Inflation IPCA (y/y)	Sep	--	--	7.1	8.7
Oct-14	8:00	IBGE Services Volume (y/y) NSA	Aug	--	--	--	6.3
Oct-14	8:00	IBGE Services Volume (m/m) SA	Aug	--	--	--	1.1
Oct-17	7:00	FGV CPI IPC-S (%)	15-Oct	--	--	--	0.0
Oct-17	7:25	Central Bank Weekly Economist Survey		--	--	--	--
Oct-17	8:00	Economic Activity (m/m)	Aug	--	--	--	1.2
Oct-17	8:00	Economic Activity (y/y)	Aug	--	--	--	3.9
Oct-17	14:00	Trade Balance Weekly (USD mn)	16-Oct	--	--	--	113.2
Oct-18	4:00	FIPE CPI - Weekly (%)	15-Oct	--	--	--	0.1
Oct-18	7:00	FGV Inflation IGP-10 (m/m)	Oct	--	--	--	-0.9
Oct 20-26		Tax Collections (BRL mn)	Sep	--	--	--	172314.0

**CHILE**

Date	Time	Event	Period	BNS	Consensus	Latest	BNS Comments
Oct-12	7:30	Central Bank Economist Survey		--	--	--	--
Oct-12	17:00	Overnight Rate Target (%)	12-Oct	11.25	11.25	10.75	We expect an increase of 50 bps in the reference rate, to 11.25%.

**COLOMBIA**

Date	Time	Event	Period	BNS	Consensus	Latest	BNS Comments
Oct-10		Consumer Confidence Index	Sep	--	--	-3.2	-2.4
Oct-14	11:00	Manufacturing Production (y/y)	Aug	--	--	--	5.2
Oct-14	11:00	Retail Sales (y/y)	Aug	5.5	--	--	7.7 We expect the industry sector to continue to show some slowdown
Oct-14	11:00	Industrial Production (y/y)	Aug	6.4	--	--	4.3 in August due to persistent pressures on the prices of inputs and raw materials. Retail sales are expected to continue a trend of moderation due to the effects of inflation that restrict households' disposable income, in addition to the fact that in the reference month there are no events that can cause an upward bias.
Oct-14		Central Bank Economist Survey		--	--	--	--
Oct-18	12:00	Economic Activity NSA (y/y)	Aug	6.9	6.4	6.4	6.4 In August, we expect the economy to continue with a trend of moderation. In the primary sector, there is still a lag in production, especially in mining. In the secondary sector, construction seems weak, especially because of civil work. Meanwhile, the tertiary sector maintains a positive dynamic but at a more moderate pace.
Oct-19	11:00	Trade Balance (USD mn)	Aug	--	--	--	-494.2
Oct-19	11:00	Imports CIF Total (USD mn)	Aug	--	--	--	6890.9

**MEXICO**

Date	Time	Event	Period	BNS	Consensus	Latest	BNS Comments
Oct-10		Nominal Wages (m/m)	Sep	--	--	--	5.0
Oct-11	10:00	International Reserves Weekly (USD mn)	07-Oct	--	--	--	196918.0
Oct-11		ANTAD Same-Store Sales (y/y)	Sep	--	--	--	11.5
Oct-12	7:00	Manuf. Production NSA (y/y)	Aug	--	--	--	5.1
Oct-12	7:00	Industrial Production NSA (y/y)	Aug	--	--	--	2.7
Oct-12	7:00	Industrial Production SA (m/m)	Aug	--	--	--	0.4
Oct-13	10:00	Central Bank Monetary Policy Minutes		--	--	--	--
Oct-18	10:00	International Reserves Weekly (USD mn)	14-Oct	--	--	--	196918.0
Oct-20		Banamex Survey of Economists		--	--	--	--
Oct-21	7:00	Retail Sales (m/m)	Aug	--	--	--	0.9
Oct-21	7:00	Retail Sales (y/y)	Aug	--	--	--	5.0

**PERU**

Date	Time	Event	Period	BNS	Consensus	Latest	BNS Comments
Oct-17		Economic Activity (y/y)	Aug	2.0	--	--	1.4 Economic activity is largely driven by sectors linked to domestic demand, such as commerce and services, mainly hotels and restaurants.
Oct-17		Lima Unemployment Rate (%)	Sep	7.0	--	--	7.3 Gradual recovery in the labour market, mainly commerce and services.

Forecasts at time of publication.  
Sources: Scotiabank Economics, Bloomberg.

## Scotiabank Economics Latam Coverage

## Local Market Coverage

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