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Latam Weekly: BCCh and BanRep Decisions; The Economic Cost of Peru's Protests

ECONOMIC OVERVIEW

- Chile's and Colombia's central banks deliver policy decisions on Thursday and Friday, respectively, with the BCCh seen cutting 25bps and BanRep moving in the other direction with another large 100bps hike.
- Ongoing tumult in Peru should remain closely watched. Our team in Lima discusses the impact of the protests on their GDP growth forecasts in today's edition.
- In Mexico, economic activity for November and H1-Jan CPI prints will help refine expectations for Banxico's meeting on February 9—where no decoupling from the Fed is expected just yet.

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 & INDICATORS

- A comprehensive risk calendar with selected highlights for the period January 21–February 3 across the Pacific Alliance countries and Brazil.

Charts of the Week

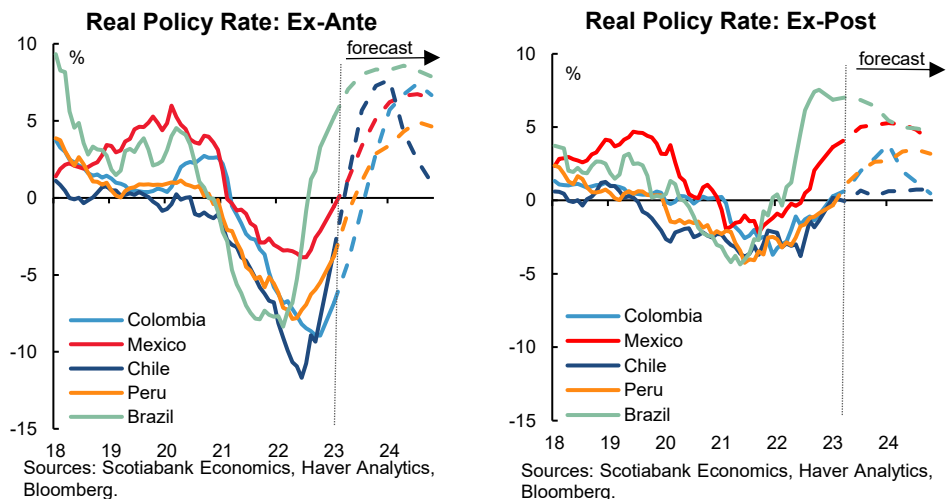


Chart of the Week: Prepared by: Anthony Bambokian, Economic Analyst.

Economic Overview: BCCh and BanRep Decisions; The Economic Cost of Peru's Protests

- **Chile's and Colombia's central banks deliver policy decisions on Thursday and Friday, respectively, with the BCCh seen cutting 25bps and BanRep moving in the other direction with another large 100bps hike.**
- **Ongoing tumult in Peru should remain closely watched. Our team in Lima discusses the impact of the protests on their GDP growth forecasts in today's edition.**
- **In Mexico, economic activity for November and H1-Jan CPI prints will help refine expectations for Banxico's meeting on February 9—where no decoupling from the Fed is expected just yet.**

Global markets will be shaped next week by a flood of company earnings releases, PMI prints that will provide early guides to economic growth at the start of the year, and the Bank of Canada's rate decision—all while they count down the days to the Fed's policy announcement on February 1. Holidays in Asia (namely in China for the Lunar New Year) may keep trading volumes somewhat subdued.

Those with a Latam focus will watch Chile's and Colombia's central banks deliver policy decisions on Thursday and Friday, respectively.

Our Santiago economists expect that the BCCh will begin its cutting cycle next week with a 25bps reduction. If, on the other hand, the bank chooses to leave its policy rate unchanged, the team foresees an aggressive cut at the BCCh's April meeting, which seems a long time away.

Colombia's BanRep is set to hike again by 100bps and maintain a data-dependent approach. In line with this decision framework, our Bogota economists anticipate a rates pause in March as inflation is not expected to remain excessively high. This is despite indexation practices, as some factors such as recent currency strength and declines in international prices help.

Meanwhile, ongoing tumult in Peru, with protesters also moving to Lima in greater strength should remain closely watched. In this week's report, Guillermo Arbe, our Peru chief economist discusses how the protests could impact the team's 2023 GDP growth outlook. November monthly GDP data out next week will present a picture of the economy before Castillo's removal in December.

In Mexico, economic activity for November and H1-Jan CPI prints will help refine expectations for Banxico's meeting on February 9. A decoupling from the Fed is not expected then, as Rodriguez Ceja's board will more than likely match Powell and co's 25bps hike. Beyond that point, the two central banks may diverge and recent comments from (usually hawkish) Heath suggest Banxico may only hike once more, in March.

Political developments in Brazil may have fallen out of focus for us as we centre our attention on Peru, but uncertainty around Lula's fiscal plans remains. Thankfully Fin Min Haddad has been more measured in his communications and is pushing for an early resolution to fiscal rule and tax reform plans. Watch mid-month inflation data out on Tuesday as the main on-calendar event in the country, with particular resilience expected in core prices. Still, the BCB's policy rate is well into restrictive territory—perhaps too restrictive for Lula's liking.

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Pacific Alliance Country Updates

Chile—Risk of Aggressive Cut in April if the BCCh Holds in January

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Next week (January 26), the central bank (BCCh) will hold its first monetary policy meeting of 2023, where we anticipate a 25bps cut in the reference rate, to 11%. In December, the BCCh conveyed a hawkish tone, expressing particular concern about the persistence of inflation and 2-year inflation expectations remaining above 3% (3.5% at the December meeting), despite declining in the last few months.

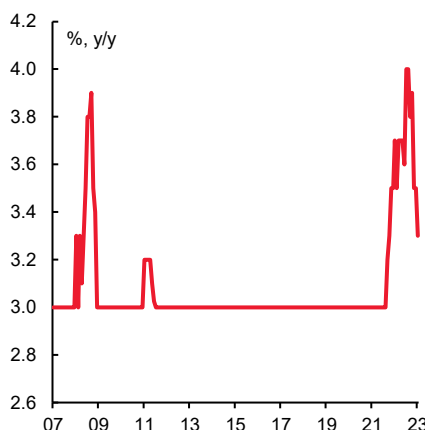
We see more risks of negative than positive surprises in inflation in the near-term. Since last December, 2-year inflation expectations have fallen according to various surveys, to 3.3% in the January Survey of Economic Expectations (chart 1). In our opinion, the inflation prints of the coming months will be mainly impacted by specific effects—such as the implementation of the VAT on services in Q1-2023—and indexing—educational services in March.

The main drivers continue to point to a softening in inflation figures in the coming months. The CLP’s ~6% appreciation since the December meeting, ongoing declines in international food prices, and a reduction in expected non-mining GDP in 2023, alongside elevated inventories are all factors that point to weaker inflation.

A more rapid turnaround in inflation would motivate the BCCh to modify its monetary policy stance before that implicit in its baseline scenario. In our view, if the central bank decides to keep the rate at its current level at the next week’s decision, the magnitude of the reference rate cut in April would be sizable, at least 150bps. After this, slowing inflation and thus benchmark rate cuts could be aggressive. We estimate that annual inflation will decrease to 3.7% y/y in December 2023, when we see the reference rate lowered to 4.0% (chart 2).

Chart 1

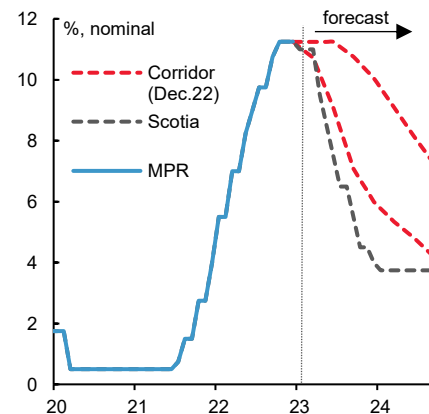
Chile: 2-Year Inflation Expectation



Sources: Scotiabank Economics, BCCh.

Chart 2

Chile: MPR Expectations and BCCh Corridor



Sources: Scotiabank Economics, BCCh.

Colombia—Developments Around Inflation at the Beginning of 2023

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Colombian CPI basket indexation effects continue to feed fears of higher-for-longer headline inflation. Market analysts believe that almost 50% of the CPI basket will be adjusted in line with December’s steeper than projected headline inflation print of 13.12% y/y. Items as important as rent fees (26% of the CPI basket), education tuition fees (4.1% of the CPI basket), or labour-intensive services such as restaurants and hotels prices (8.8% of the CPI basket) are expected to adjust in tandem with the Dec-2022 inflation reading.

What’s more, the year started with climate difficulties and above-seasonal rains, which have led to a lower food supply in some regions, also adding to expectation of high food inflation in January 2023. The above factors combined reduce the likelihood of a strong reduction in inflation. Instead, it should remain around 13% in the first quarter of the year, before beginning a slow reduction towards 8.8% by the end of 2023.

On the bright side, the year also started with strong FX appreciation and lower international prices in Colombian agricultural inputs, which eventually will help food inflation decelerate significantly. At the same time, goods inflation will also benefit from currency strength if the latest trend holds. By our calculations, this development into March and April will help headline inflation decelerate somewhat.

January 20, 2023

We see inflation at 1.63% m/m in January 2023, or 13.08% y/y with an upside bias to the indexations and climate effects described above that could play a larger role than food and services inflation. In light of this, BanRep is expected to deliver a new 100bps hike in a split vote at its January 27 meeting, while sticking to a data-dependent approach. However, since inflation is not expected to remain excessively high, the central bank may consider a pause at its March meeting. We expect a discussion on cuts when headline inflation reaches single digits again.

Mexico—H1-Jan Inflation Seen Lower, but Not Enough for Banxico

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Inflation for the first two weeks of January will continue on its downward trend, but not yet at the pace that Banxico would want. Core inflation will likely begin to reflect the impact of higher labour costs (due to the pension reform and minimum wage increase), while non-core could benefit from reduced supply shocks.

Overall, Banxico can't lower its guard just yet. Deputy Governor Heath stated this week his expectation of a terminal rate somewhere between 10.75% and 11.50%, but with a smaller likelihood that rates will top 11.00%. We've noted that he thinks it's appropriate to hold at the peak rate for at least six months, as inflation consistently eases. The ratification of Omar Mejia to the bank's board is not expected to change the bank's consensus in future policy meetings. On our end, we maintain our call for a 10.50% policy rate at the end of the year, though we believe uncertainty regarding inflation remains high. There isn't a narrow consensus view for Banxico's end-2023 rate, though we can all agree that headline inflation will continue to decelerate.

On the economic activity front, we anticipate that the GDP proxy IGAE for November out next week will show reflect buoyant services activity and, to a lesser extent, manufacturing output which has recently slowed from its uptrend.

Peru—The Toll of Political Turbulence on the Economy

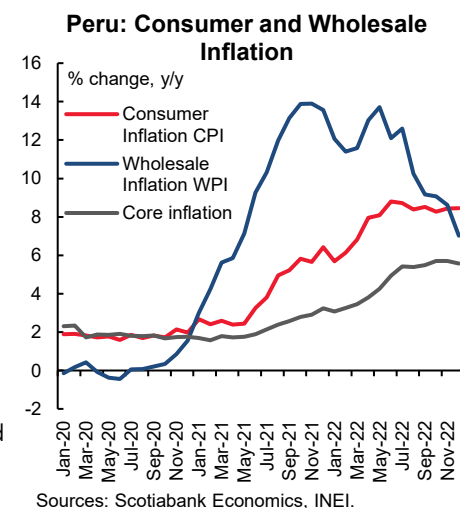
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Political turbulence in the country is beginning to take a greater toll on the economy, affecting growth, inflation, and markets.

Let's start with growth. The most recent monthly GDP growth figure was for November, which showed a paltry 1.7% y/y expansion. November was the fourth consecutive month with growth of 2% y/y or less. Thus, growth had already slowed before the turbulence that has followed the aborted coup attempt by ex-President Castillo in December. This slowdown was expected, and is the driver behind our expectation of sub-2% domestic demand growth in Q4-2022, with weakness continuing through 2023. What is expected to bring aggregate GDP growth above 2%—our latest full-year 2023 GDP growth forecast is 2.4%—is the coming online of the large Quellaveco copper mine, which we expect to add 0.6ppts to growth in the current year.

That was then. December and, especially, January will most certainly see the impact of the protests on growth. The south, the region where protests have had the greatest impact, represents 18% of GDP. Mines including Las Bambas, Minsur (tin) and Antapaccay have reported an impact on operations. Sectors that were expected to lead growth in 2023 are among the most vulnerable to news of violence, namely hospitality and tourism, transportation, and mining. While most of the country and economy are operating fairly normally, the southern region is large and roadblocks are having a wider impact than just in the south. Depending on the duration of the current situation, there is a real risk that GDP growth in January could be nil, or even negative. This, of course, will mean that we will likely need to reassess our forecast for 2.4% growth in 2023. It is still premature to do so, as events are still evolving.

Chart 1



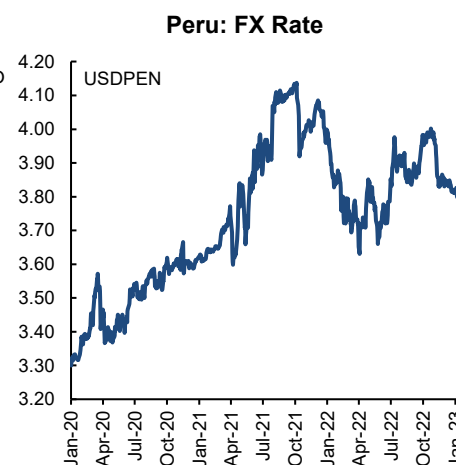
The protests have also impacted inflation dynamics over the December–January period. The roadblocks are impeding normal supply, which is driving up the prices of agricultural products. We had already stated that this was the reason that inflation rose in December from 8.4% to 8.5% y/y, rather than a decline to 8.1% that was expected (chart 1). Something similar is likely to happen in January, as roadblocks are once again impacting agricultural prices at least as much as last month.

Thus, 12-month inflation could continue climbing. This increases the likelihood that the BCRP raise its reference rate to 8.00% in February. The BCRP will be in somewhat of a dilemma, as it knows that inflation will start declining relatively sharply starting in March, in response to declining wholesale prices inflation which reflects the falling cost of key imports.

Finally, a shift in sentiment in the FX market seems to be unfolding. The PEN, which has frequently shrugged off political turbulence in the past, has begun to weaken over the past few days, spooked by local events (chart 2).

There is some risk that the violence and political transcendence of the protests opens the door to further political change in the country. President Boluarte is under pressure to resign, and the likelihood that she will do so has risen, although on Thursday night she firmly stated that she would not do so.

Chart 2



Sources: Scotiabank Economics, BCRP.

Key Economic Charts

Chart 1

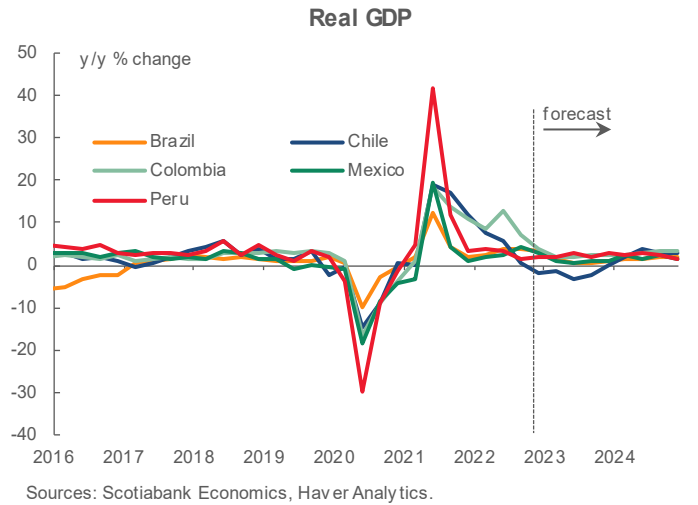


Chart 2

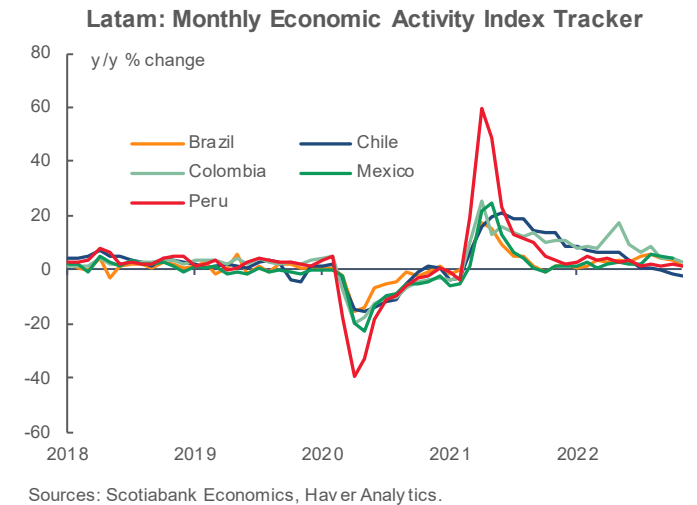


Chart 3

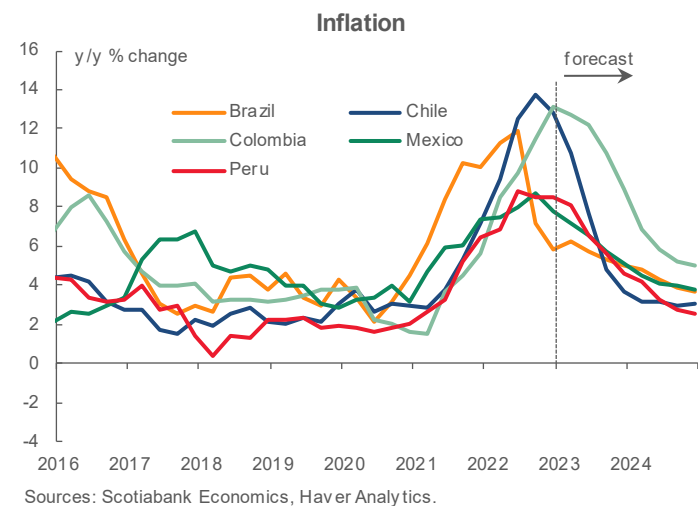


Chart 4

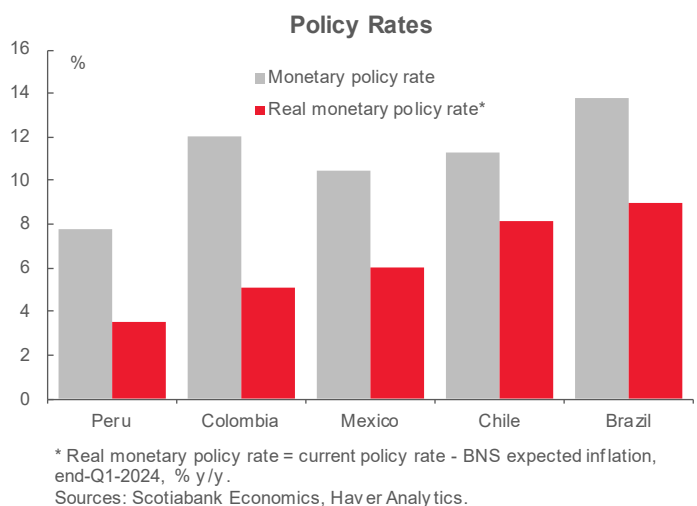
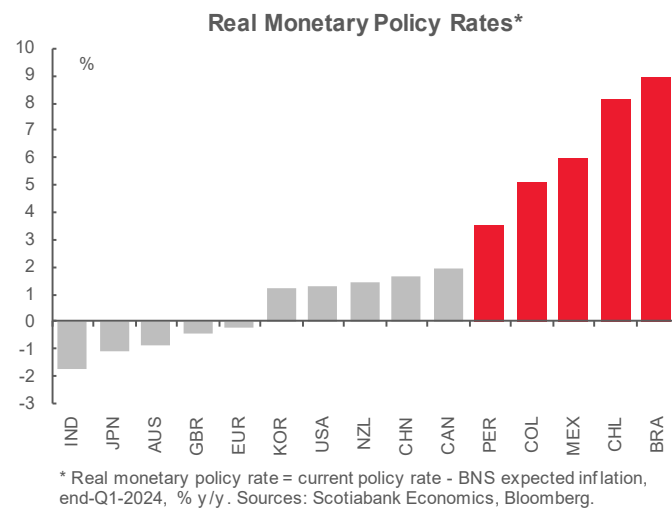


Chart 5



Key Market Charts

Chart 1

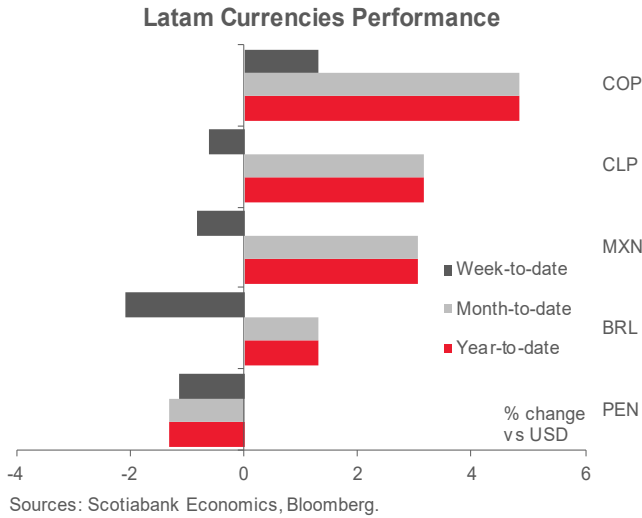


Chart 2

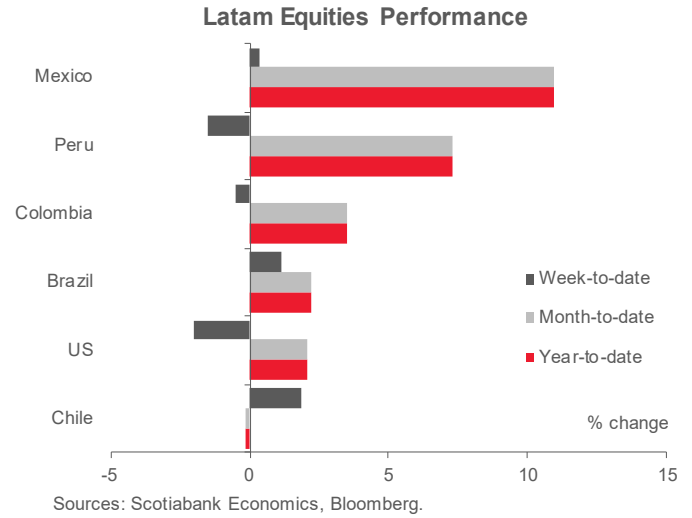


Chart 3

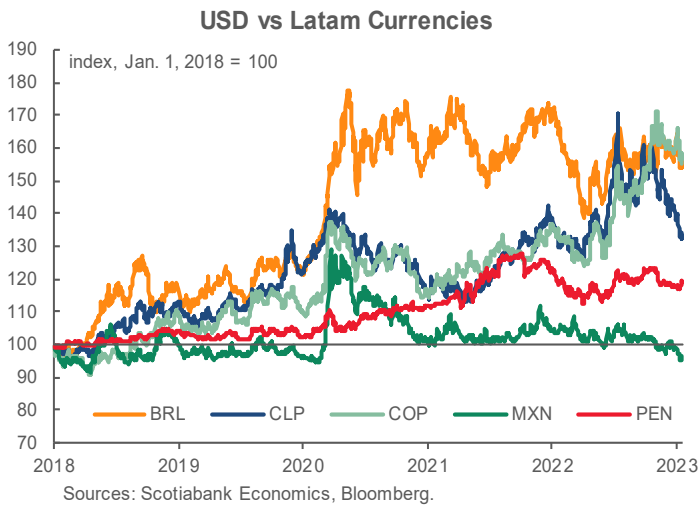
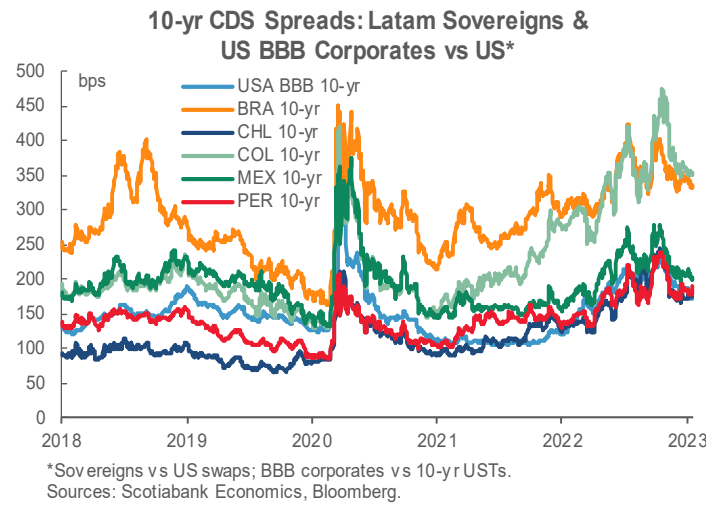
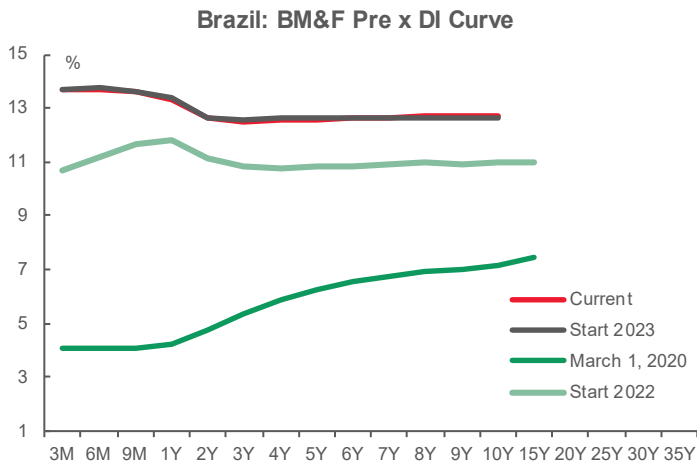


Chart 4



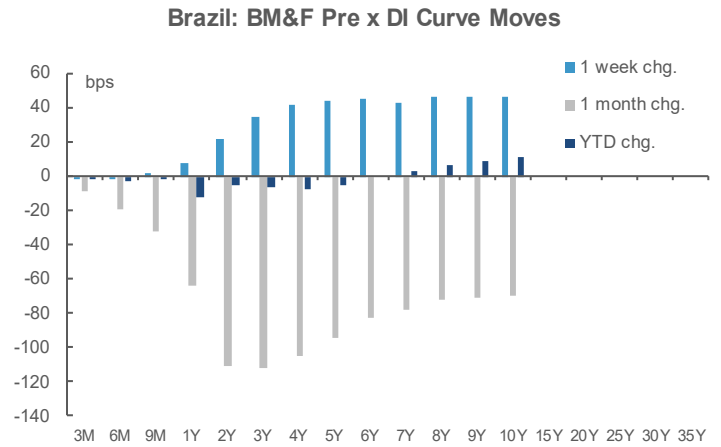
Yield Curves

Chart 1



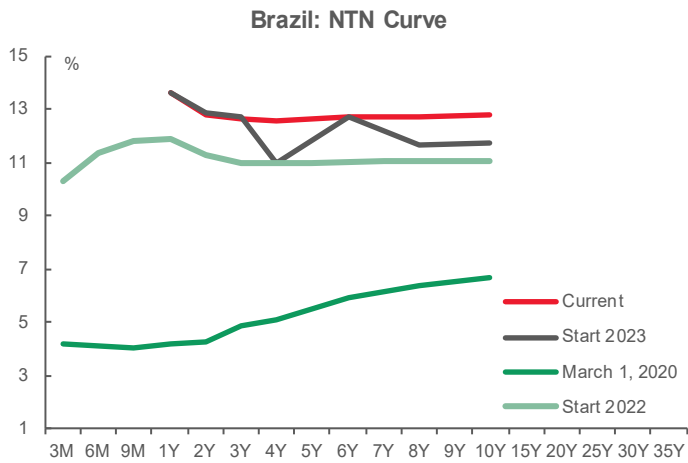
Sources: Scotiabank Economics, Bloomberg.

Chart 2



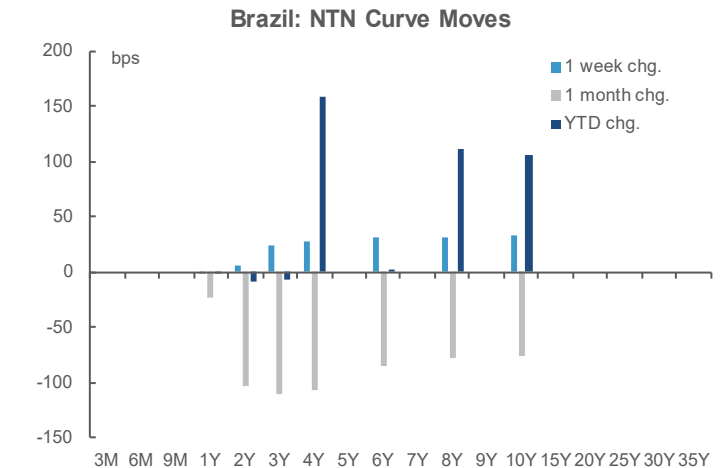
Sources: Scotiabank Economics, Bloomberg.

Chart 3



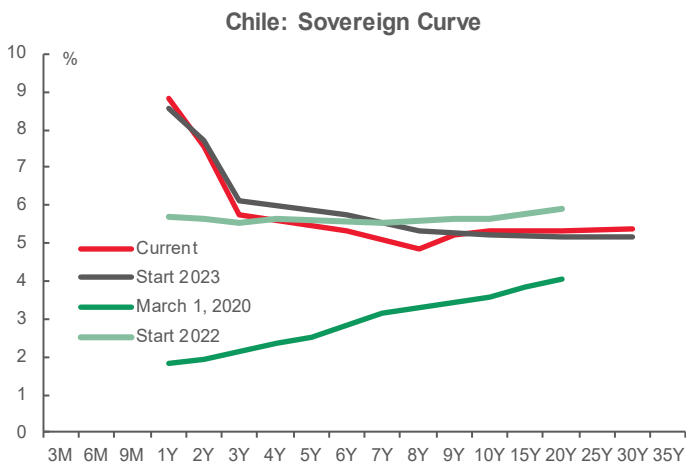
Sources: Scotiabank Economics, Bloomberg.

Chart 4



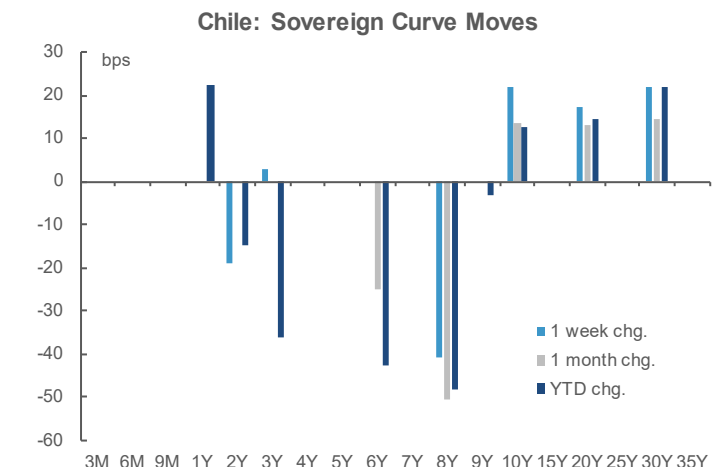
Sources: Scotiabank Economics, Bloomberg.

Chart 5



Sources: Scotiabank Economics, Bloomberg.

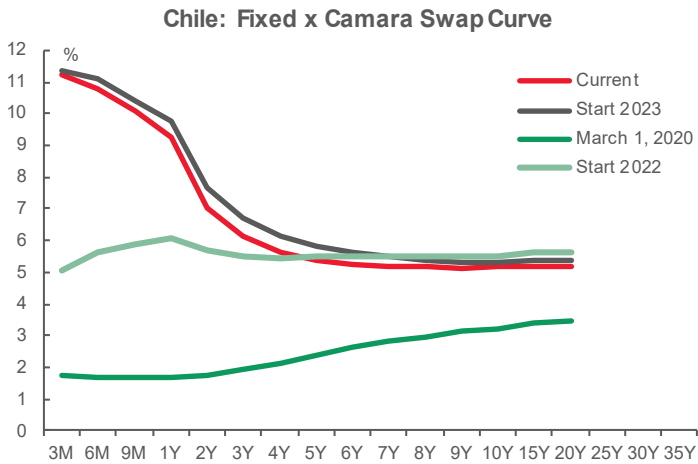
Chart 6



Sources: Scotiabank Economics, Bloomberg.

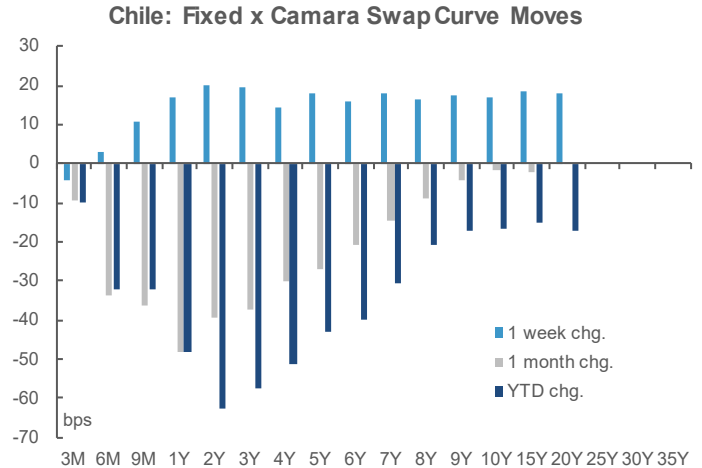
Yield Curves

Chart 7



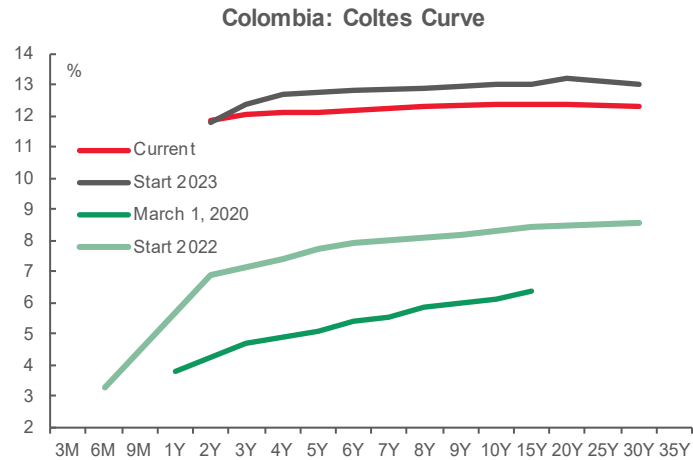
Sources: Scotiabank Economics, Bloomberg.

Chart 8



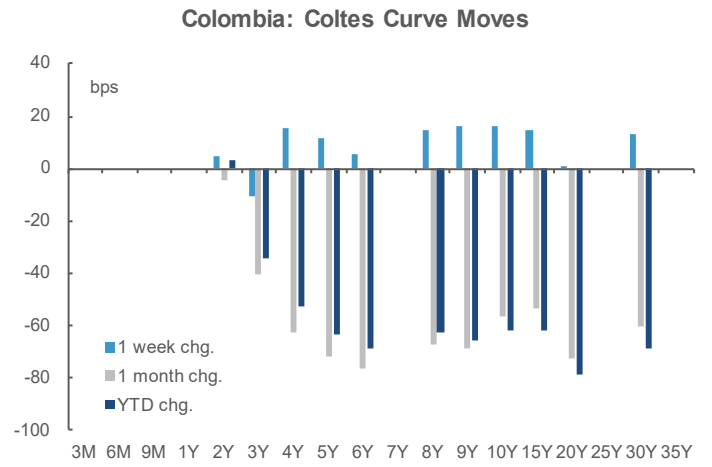
Sources: Scotiabank Economics, Bloomberg.

Chart 9



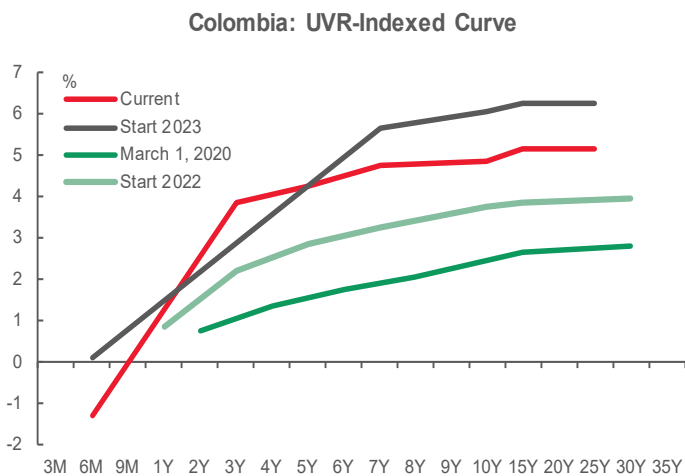
Sources: Scotiabank Economics, Bloomberg.

Chart 10



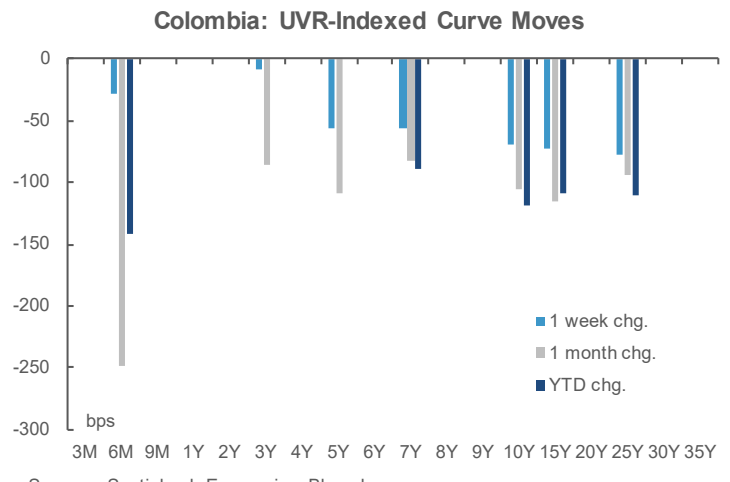
Sources: Scotiabank Economics, Bloomberg.

Chart 11



Sources: Scotiabank Economics, Bloomberg.

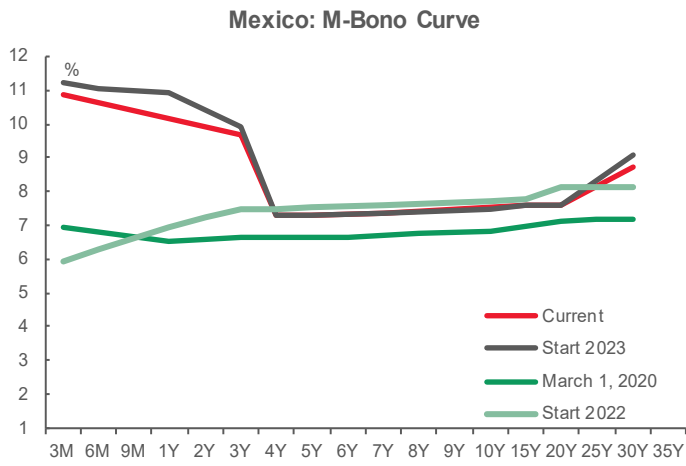
Chart 12



Sources: Scotiabank Economics, Bloomberg.

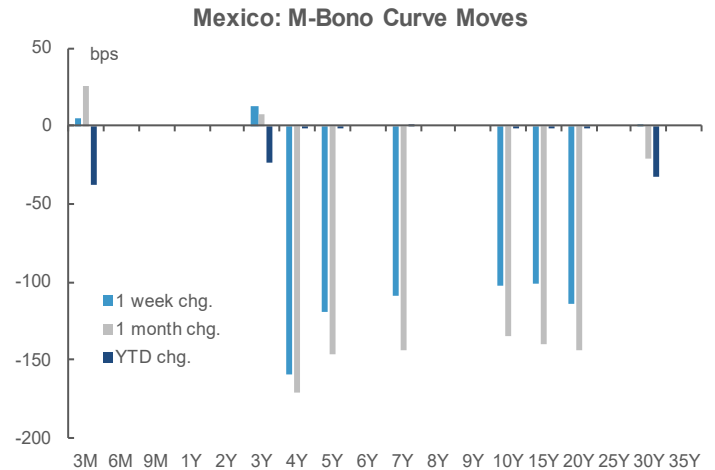
Yield Curves

Chart 13



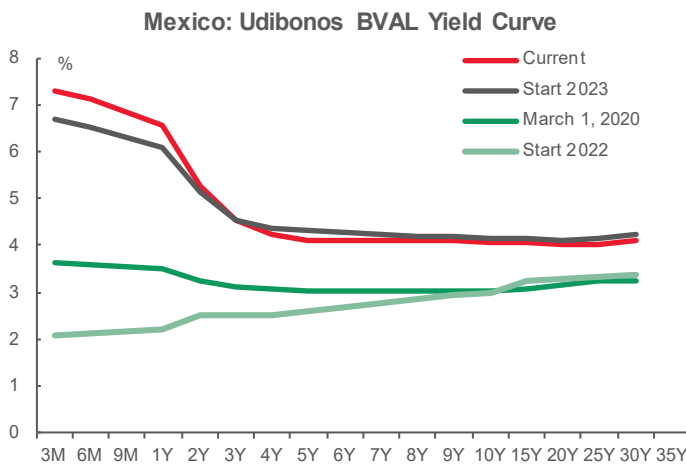
Sources: Scotiabank Economics, Bloomberg.

Chart 14



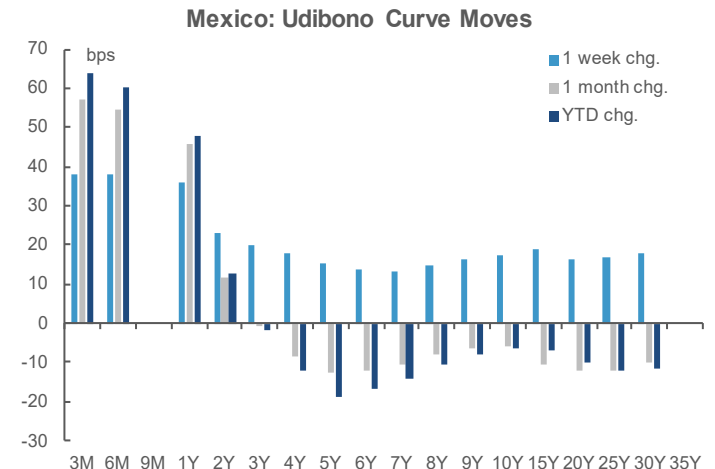
Sources: Scotiabank Economics, Bloomberg.

Chart 15



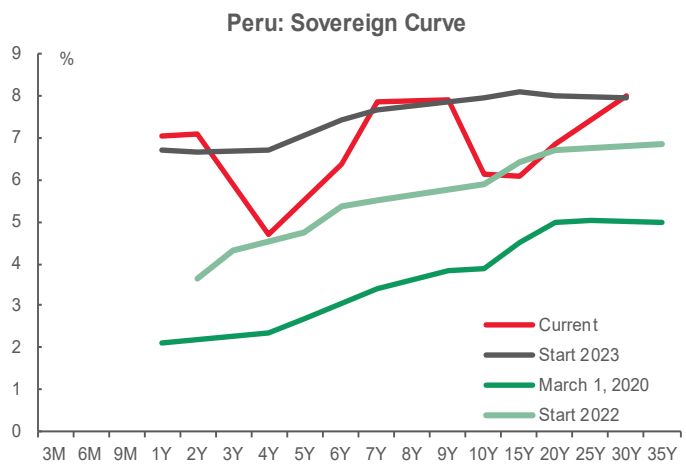
Sources: Scotiabank Economics, Bloomberg.

Chart 16



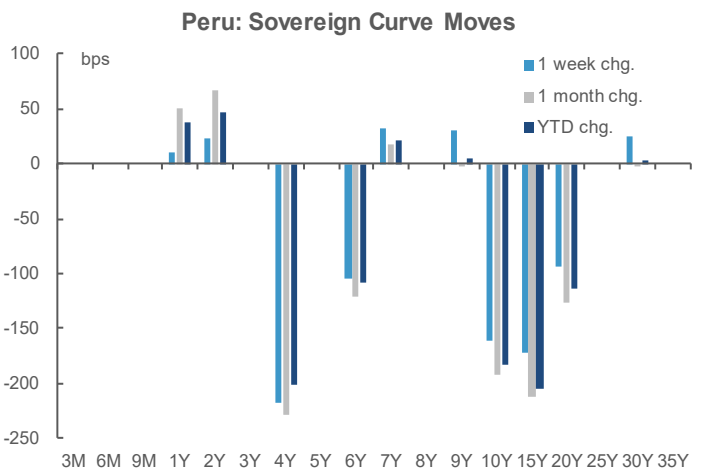
Sources: Scotiabank Economics, Bloomberg.

Chart 17



Sources: Scotiabank Economics, Bloomberg.

Chart 18



Sources: Scotiabank Economics, Bloomberg.

Market Events & Indicators for January 21–February 3

BRAZIL

Date	Time Event	Period	BNS	Consensus	Latest BNS Comments
Jan-23	6:00 FGV CPI IPC-S (%)	22-Jan	--	0.55	0.49
Jan-23	6:25 Central Bank Weekly Economist Survey				
Jan-23	13:00 Trade Balance Weekly (USD mn)	22-Jan	--	--	36
Jan-24	7:00 IBGE Inflation IPCA-15 (y/y)	Jan	--	5.82	5.90
Jan-24	7:00 IBGE Inflation IPCA-15 (m/m)	Jan	--	0.51	0.52
Jan-25	6:00 FGV Consumer Confidence	Jan	--	--	88
Jan 17-25	Formal Job Creation Total	Dec	--	-325000	278489
Jan 20-25	Tax Collections (BRL mn)	Dec	--	211500	172038
Jan-26	3:00 FIPE CPI - Weekly (%)	23-Jan	--	--	0.67
Jan-26	6:00 FGV Construction Costs (m/m)	Jan	--	0.24	0.27
Jan-26	7:30 Current Account Balance (USD mn)	Dec	--	-63	-60
Jan-26	7:30 Foreign Direct Investment (USD mn)	Dec	--	5000	8338
Jan-26	12:30 Federal Debt Total (BRL bn)	Dec	--	--	5871
Jan-27	7:30 Total Outstanding Loans (BRL bn)	Dec	--	5322.5	5264.2
Jan-27	7:30 Outstanding Loans (m/m)	Dec	--	1.1	1.0
Jan-27	7:30 Personal Loan Default Rate (%)	Dec	--	--	5.92
Jan-27	12:30 Central Govt Budget Balance (BRL bn)	Dec	--	1.5	-14.7
Jan-30	6:00 FGV Inflation IGPM (m/m)	Jan	--	--	0.45
Jan-30	6:00 FGV Inflation IGPM (y/y)	Jan	--	--	5.45
Jan-30	6:25 Central Bank Weekly Economist Survey				
Jan-30	7:30 Net Debt % GDP	Dec	--	--	57
Jan-30	7:30 Nominal Budget Balance (BRL bn)	Dec	--	--	-70.371
Jan-30	7:30 Primary Budget Balance (BRL bn)	Dec	--	--	-20.089
Jan-30	13:00 Trade Balance Weekly (USD mn)	29-Jan	--	--	36
Feb-01	6:00 FGV CPI IPC-S (%)	31-Jan	--	0.55	0.49
Feb-01	8:00 S&P Global Brazil Manufacturing PMI	Jan	--	--	44.2
Feb-01	13:00 Trade Balance Monthly (USD mn)	Jan	--	--	4779
Feb-01	13:00 Exports Total (USD mn)	Jan	--	--	26645
Feb-01	13:00 Imports Total (USD mn)	Jan	--	--	21866
Feb-01	16:30 Selic Rate (%)	01-Feb	13.75	13.75	13.75
Feb-02	3:00 FIPE CPI - Monthly (%)	Jan	--	--	0.54
Feb-03	7:00 Industrial Production (m/m)	Dec	--	--	-0.1
Feb-03	7:00 Industrial Production (y/y)	Dec	--	--	0.9
Feb-03	8:00 S&P Global Brazil Composite PMI	Jan	--	--	49.1
Feb-03	8:00 S&P Global Brazil Services PMI	Jan	--	--	51
Feb 01-03	Vehicle Sales Fenabrave	Jan	--	--	207015

CHILE

Date	Time Event	Period	BNS	Consensus	Latest BNS Comments
Jan-24	7:00 PPI (m/m)	Dec	--	--	0
Jan-26	16:00 Overnight Rate Target (%)	26-Jan	11.00	11.25	11.25 We project aggressive rate cuts through 2023 towards 4% by the end of the year.
Jan-30	7:00 Unemployment Rate (%)	Dec	7.9	--	7.9 The unemployment rate will remain at 7.9% due to similar employment growth compared to the expansion of the labour force.
Jan-31	7:00 Manufacturing Production (y/y)	Dec	--	--	-7.78
Jan-31	7:00 Industrial Production (y/y)	Dec	--	--	-5.02
Jan-31	7:00 Copper Production Total	Dec	--	--	459229
Jan-31	7:00 Commercial Activity (y/y)	Dec	--	--	-9.32
Jan-31	7:00 Retail Sales (y/y)	Dec	-15.0	--	-15.2 We observe a more intense usage of credit cards in low-income segments amid restrictive credit conditions.
Feb-01	6:30 Economic Activity (y/y)	Dec	-2.7	--	-2.5 We forecast a GDP contraction of 2.7% in December, consistent with a GDP expansion of 2.6% in 2022.
Feb-01	6:30 Economic Activity (m/m)	Dec	--	--	-0.79
Feb 01-07	IMCE Business Confidence	Jan	--	--	35.61

COLOMBIA

Date	Time Event	Period	BNS	Consensus	Latest BNS Comments
Jan-25	Retail Confidence	Dec	--	--	19.2
Jan-25	Industrial Confidence	Dec	--	--	0.1
Jan-27	13:00 Overnight Lending Rate (%)	27-Jan	13.00	13.00	12.00 The central bank is expected to deliver a 100bps hike, pointing to ongoing heavy concerns over the recent increase in inflation expectations. According to recent activity data, economic activity has weakened, which increases the possibility of a split dovish vote. The next rate decision occurs in March. By this time, we expect to have more clues about inflation stabilization and economic deceleration to affirm our call for rate stability.
Jan 23-27	Exports FOB (USD mn)	Dec	--	--	4519.46
Jan-31	10:00 Urban Unemployment Rate (%)	Dec	9.4	--	9.1 The unemployment rate will close in the single-digits, showing the effect of the
Jan-31	10:00 National Unemployment Rate (%)	Dec	9.0	--	9.5 employment recovery due to the holiday season and a low participation rate.
Jan-31	17:00 Colombia Monetary Policy Minutes				
Feb-01	10:00 Davivienda Colombia PMI Mfg	Jan	--	--	51.1

Forecasts at time of publication.

Sources: Scotiabank Economics, Bloomberg.

Market Events & Indicators for January 21–February 3

MEXICO					
<u>Date</u>	<u>Time Event</u>	<u>Period</u>	<u>BNS</u>	<u>Consensus</u>	<u>Latest BNS Comments</u>
Jan-24	7:00 Bi-Weekly CPI (%)	15-Jan	0.39	0.37	0.10
Jan-24	7:00 Bi-Weekly Core CPI (%)	15-Jan	0.4	0.3	0.2
Jan-24	7:00 Bi-Weekly CPI (y/y)	15-Jan	7.86	7.83	7.86
Jan-24	7:00 Bi-Weekly Core CPI (y/y)	15-Jan	8.4	8.3	8.3
Jan-24	10:00 International Reserves Weekly (USD mn)	20-Jan	--	--	200620
Jan-25	7:00 Economic Activity IGAE (m/m)	Nov	--	-0.12	0.03
Jan-25	7:00 Economic Activity IGAE (y/y)	Nov	--	4.31	4.41
Jan-26	7:00 Unemployment Rate NSA (%)	Dec	--	2.86	2.85
Jan-27	7:00 Trade Balance (USD mn)	Dec	--	800	-96.15
Jan-27	7:00 Imports (USD mn)	Dec	--	--	49407.42
Jan-27	7:00 Exports (USD mn)	Dec	--	--	49311.27
Jan 23-27	ANTAD Same-Store Sales (y/y)	Dec	--	--	6.1
Jan-30	Budget Balance YTD (MXN bn)	Dec	--	--	-611.15
Jan-31	7:00 GDP NSA (y/y)	4Q P	2.6	--	4.3
Jan-31	7:00 GDP SA (q/q)	4Q P	--	--	0.89
Jan-31	10:00 International Reserves Weekly (USD mn)	27-Jan	--	--	200620
Jan-31	10:00 Net Outstanding Loans (MXN bn)	Dec	--	--	5435.9
Feb-01	10:00 Remittances Total (USD mn)	Dec	--	--	4801.1
Feb-01	10:00 Central Bank Economist Survey				
Feb-01	10:30 S&P Global Mexico Manufacturing PMI	Jan	--	--	51.3
Feb-01	13:00 IMEF Manufacturing Index SA	Jan	--	--	51.8
Feb-01	13:00 IMEF Non-Manufacturing Index SA	Jan	--	--	53.5
Feb-02	7:00 Vehicle Domestic Sales	Jan	--	--	120862
Feb-02	7:00 Leading Indicators (m/m)	Dec	--	--	-0.05
Feb-03	7:00 Consumer Confidence	Jan	--	--	42.53
Feb 01-08	Formal Job Creation Total	Jan	--	--	-345.7
PERU					
<u>Date</u>	<u>Time Event</u>	<u>Period</u>	<u>BNS</u>	<u>Consensus</u>	<u>Latest BNS Comments</u>
Feb-01	10:00 Lima CPI (m/m)	Jan	0.35	--	0.79 Rise in food and transport prices in the context of social protests and road blocks.
Feb-01	10:00 Lima CPI (y/y)	Jan	8.8	--	8.5 Risk of a new inflation peak being reached (previous peak: Jun 2022. 8.81%).

Forecasts at time of publication.

Sources: Scotiabank Economics, Bloomberg.

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