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Latam Daily: Chile CPI and Peru Rate Decision Previews, Petroperu Fiscal Risks

- **Chile: Inflation will continue its trip back to target in January**
- **Peru: Monetary policy to remain steady as inflation fades; Petroperu grows as a fiscal concern**

CHILE: INFLATION WILL CONTINUE ITS TRIP BACK TO TARGET IN JANUARY

At Scotiabank Economics, we project January inflation to be between 0.4 and 0.5% m/m, mainly explained by the positive contribution of food, although it ensures that the year-on-year variation continues to approach the target of 3%. Along these lines, our projection is that the inflation target will be reached in March of this year, a similar view to that adopted by the board of the BCCh after recognizing the downside surprise in December, both in headline and core inflatoin. This has also influenced the view that the Board has on the trajectory for the benchmark rate, which will be updated at the April IPoM and which, according to the minutes of the January meeting, will consider that the reference rate will reach its neutral level in the second half of this year. At Scotiabank, we do not rule out that this level will be reached towards the middle of the year if there are no inflationary surprises in the January and February CPI prints.

—Aníbal Alarcón

PERU: MONETARY POLICY TO REMAIN STEADY AS INFLATION FADES; PETROPERU GROWS AS A FISCAL CONCERN

The BCRP can breathe more easily now. After two years, inflation has finally returned (albeit just barely) to its target range. In January, 12-month inflation came in at 3.0%, the cusp of the BCRP target range. Monthly inflation for January was nil.

With inflation at the door of its target range, the question is whether this might tempt the BCRP to lower rates more aggressively on February 8th, say by 50bps, rather than its usual monthly pace 25bps.

Don't bet on it. It's tempting, it's true, as there seems to be so much light between the current reference rate of 6.50% and inflation expectations, which currently stand at 2.8%. That's a real rate of nearly 3.75%, which is significantly above the 2.0% which the BCRP considers the neutral rate. Add to this the statement made last week by the BCRP's chair, Julio Velarde, that his balance of concerns is shifting from inflation to growth, and a case can be made for the BCRP to be more aggressive when it meets next week.

So, why not? The first reason, as we've mentioned before, is that the BCRP has yet to become more accommodating in providing liquidity to the system. This reveals that it still has concerns. To begin decreasing the reference rate more aggressively without easing liquidity constraints would generate a policy mismatch that would be hard to understand. Furthermore, the BCRP is currently in its comfort zone and there is no hurry to vary its policy. The BCRP can lower rates by 25bps per month throughout most of the year without raising eyebrows. In contrast, if the BCRP were to lower the reference rate by any amount except 25bps (say 50bps), this would create unnecessary turbulence in market expectations, and henceforth put the BCRP under pressure to continue reducing rates aggressively. We do not see the BCRP putting itself in this position.

Let's see, we seem to be forgetting something here… oh, yes! El Niño! How could we forget what we long considered the main risk factor for 2024? Well, that's because the risk has all but disappeared. As we approach the mid-point of the normal El Niño period, there has been no impact at all so far in 2024. Moreover, the local El Niño monitoring system, ENFEN, now reports that the El Niño is likely to be weak, tending to non-existent.

The change in outlook regarding El Niño has brought about a change in outlook for the economy in 2024. We've reported our new forecasts in previous Latam Dailies and Weeklies as we've made them, but it might be helpful if we provide a summary of the main changes here (table 1).

Table 1: Peru—Forecast Changes 2024

		New	Previous
1.	GDP Growth	2.7%	2.3%
2.	Inflation	2.4%	3.5%
3.	Reference Rate (eop)	4.25%	4.75%
4.	Fiscal Deficit	2.5%	2.0%

Sources: Scotiabank Economics.

On a final note, the plot thickens in the saga of the Petroperu's financial troubles. Fitch Ratings announced last week that it had downgraded Petroperu's rating to B+ from BB+. This comes after the government of Peru denied Petroperu's request for a USD2.5bn bail-out program to service its USD6bn debt. Instead, the government set up a committee to seek a solution. Still, the message that was sent is clear, the government will not give Petroperu a blank check, or any check at all if it can be avoided. It is this lack of clear government backing for Petroperu's debt which led Fitch to downgrade its debt.

Petroperu's downgrade raises the question of what it may mean for Peru's own sovereign debt ratings. Fitch stated that changes in Peru's sovereign debt ratings would impact Petroperu's ratings but did not mention an inverse relationship. Our read is that that Fitch would not automatically change its sovereign debt rating for Peru based on Petroperu's downgrade per se. But, at the same time, the developments overall imply the recognition that the very existence of Petroperú's financial quandaries constitutes a degree of risk.

Down the line, much will depend on how events play out. It's hard to see the government simply allowing Petroperu to fail, which would be scary on different levels. So, what it is likely to come down to is how great an ability the government has to rescue Petroperu, while avoiding having this rescue turn into an overriding and persistent burden.

—Guillermo Arbe