Latam Daily: Peru CPI, Chile Econ Activity; BCCh and Colombia U-rate and Rating Update Recap

Scotiabank

GLOBAL ECONOMICS

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- **Chile: BCCh keeps policy rate at 5.75%, surprising economists' expectations; U-rate remains at 8.3%, without changing the diagnosis of fragility in the labour market**
- **Colombia: The labour market deteriorated, showing weakness in the services sector; Fitch affirms the sovereign credit rating at BB+, maintaining the stable outlook**

Powell's dovish presser post-FOMC statement is supporting ex-US global rates this morning, while providing a risk-on offset to the risk-off mood that would emerge more clearly from reports that Ayatollah Khamenei has called for Iran to retaliate on Israel. It's another busy G10 and Latam day ahead, with the last of the week's key central bank decisions due at 7ET, the BoE (cut narrowly expected), followed by the release of US unit labour costs, jobless claims, and ISM manufacturing data which may check the somewhat stretched Fed cut bets.

US equity futures are little changed, erasing some overnight gains after positive earnings from Meta and follow-up moves to the Fed's decision, while European bourses are broadly offered, especially in the Eurozone. Currency weakness, like the GBP down 0.7% and the EUR down 0.4%, may be a better reflection of the slight risk-averse tone as havens trade flat to firmer (CHF, namely); the MXN is down 0.3/4% to trade around its pre-Fed levels. Crude oil is adding about 1% to yesterday's 2.7% rise in Brent to take the benchmark to its highest level since… Friday; OPEC+ meets today, but no changes to supply plans are expected. Iron ore choppiness continues with a 2% rise on the day, against a 0.5% decline in copper.

Yesterday's BanRep and BCB decisions were broadly as expected, with the former announcing a 50bps cut (see our team's recap **here**) and the latter holding its policy rate steady at 10.50%. At the margin, the BCB's hawkish tone implies greater odds that officials would even consider a hike at some point, though we think this is highly unlikely unless the BRL sharply depreciates. The BCCh's rate hold was a bit more unexpected as most economists saw a rate cut, but markets had moved ahead of it to only price in a 40% chance of a cut. Below, our Chile team outline their take on the decision.

Today, Peru's INEI publishes July inflation figures at 11ET for which, courtesy of the country's official journal, we already know that headline inflation undershot economists' forecasts. Lima CPI slowed in July to 2.13% y/y from 2.29% on a 0.24% m/m rise, undershooting the Bloomberg median of 2.24% and 0.40% by a decent margin (in line with our team's forecast). The official journal does not include details on core inflation or the drivers of price gains, however. But, if a similar miss is observed in core inflation figures in the INEI's fuller release we may just about get a sub-3% print that could motivate the BCRP to roll out a 25bps rate cut at its upcoming meeting next Thursday, following a two-meeting pause.

At 8.30ET, Chile's statistics agency release June economic activity figures. Yesterday's collection of industrial, manufacturing, and mining production and retail sales data points to small upside risks in today's data. While industrial output was dragged a bit lower than expected (-1% vs –0.8% median) due to a sharp drop in manufacturing production offset by mining and utilities, a strong retail sales gain (7.9% y/y vs 4% median) points to a higher economic activity rise than the 1.5% y/y expected by the median. The data should be of little consequence for local markets, however, that are bound to open to the BCCh's rate hold.

—Juan Manuel Herrera

CHILE: BCCH KEEPS POLICY RATE AT 5.75%, SURPRISING ECONOMISTS' EXPECTATIONS

- **BCCh's Board moves too cautiously, introducing greater uncertainty about the next move in the policy rate**

The central bank (BCCh) maintained the benchmark interest rate at 5.75%, meeting the expectations of the traders' survey, although contrary to the economists' survey and the Bloomberg median. Swap rates incorporated a partial cut. It should be noted that the IPoM scenario (still valid according to the Board) considers a 25bps cut in Q3 according to the center of the rate corridor.

However, the reading that we believe the BCCh is making is that these 25bps may be delayed or increased depending on short-term inflation figures. From our view, the conditions were in place to cut 25bps in this meeting given that there was a negative surprise at the core inflation level (which the BCCh itself recognizes) and a clear scenario of a decrease in the expectation of GDP growth in 2024, beyond the fact that it is for now explained by weather factors (supply) in May and June. We believe that the BCCh did not make the latest cut in the core IPoM scenario simply out of caution ahead of the July CPI. However, this tactical decision has costs in terms of lower predictability of the next step and magnitude of the monetary policy rate.

The decision to hold significantly increases the uncertainty regarding the next move in the policy rate making it particularly dependent, for the reading of market agents, on July inflation. In simple terms:

- On the one hand, if the July CPI surprises upwards of the base scenario of the June IPoM, it will be difficult to see a cut by the BCCh in September, which will have to wait for additional inflation records before materializing. All of the above, in a scenario where the Fed would have already started the cutting process.
- On the other hand, if the July CPI satisfies the BCCh's baseline scenario, the BCCh would cut the policy rate in September by 25bps, temporarily coupling it to the first Fed cut that would occur two weeks later.
- Alternatively, if the July CPI surprises to the downside, confirming the few inflationary pressures observed in the June CPI, the BCCh would cut the rate in September. However, it could also present a new baseline scenario in that month's IPoM with additional cuts in line with a reduction in its 2024 inflation and GDP growth projection, as well as incorporating a Fed promptly initiating the cutting process.

These previous alternatives make it more difficult to anticipate the next movement of the policy rate by leaving it particularly subject to very short-term inflation.

CHILE: U-RATE REMAINS AT 8.3%, WITHOUT CHANGING THE DIAGNOSIS OF FRAGILITY IN THE LABOUR MARKET

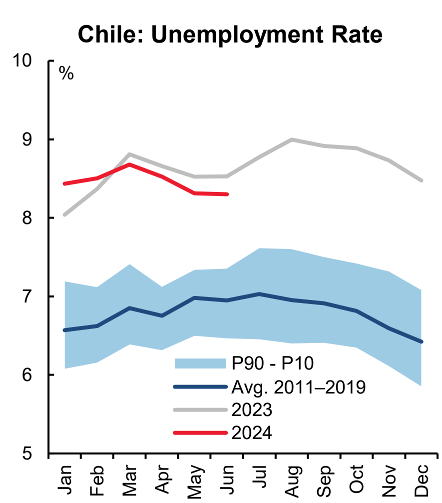
- **Limited and seasonal loss of total employment**

The unemployment rate satisfies our projection and the consensus (8.3%, chart 1) in the April–June moving quarter but shows considerable sectoral heterogeneity. The maintenance of the unemployment rate is explained by a similar fall in the labour force and total employment, both in line with what was expected according to the seasonality of the month.

At the sectoral level, the strong recovery in the quality of employment in commerce is noteworthy, which created slightly more than 40k jobs with respect to the previous quarter, most of them salaried (chart 2). On the other hand, the transportation and health sectors destroyed more than 40k salaried jobs.

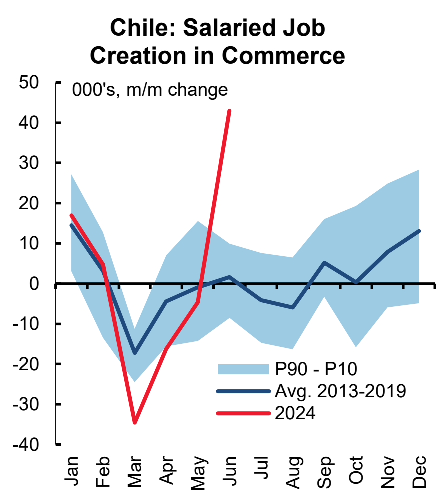
Taking all of the above into account, the labour market seems to be in line with the cycle of weak economic activity, without changing the diagnosis of fragility and still with ample room for recovery.

Chart 1



Sources: Scotiabank Economics, INE.

Chart 2



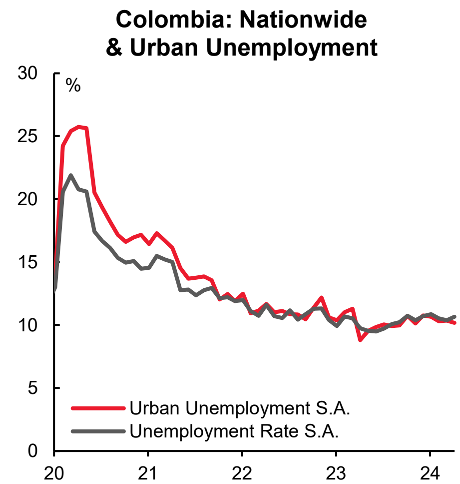
Sources: Scotiabank Economics, INE.

—Aníbal Alarcón

COLOMBIA: THE LABOUR MARKET DETERIORATED, SHOWING WEAKNESS IN THE SERVICES SECTOR

On July 31st, DANE published the labour market data for June. The national unemployment rate stood at 10.3%, increasing by 1 pp from 9.3% in June 2023, breaking the downward trend of the last two months, and remaining in double digits for the seventh consecutive month. The urban unemployment rate registered a significant deterioration from 8.8% in June 2023 to 10.2% in June 2024. On a seasonally adjusted basis, the national unemployment rate stood at 10.7%, representing an increase of 0.3 ppts from 10.4% in the previous month. In comparison, the urban unemployment rate fell from 10.4% in May to 10.2% in June (chart 3).

Chart 3

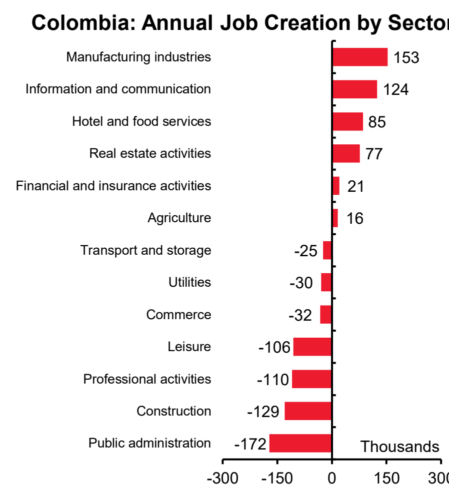


Sources: Scotiabank Economics, DANE.

The surprise of the weakening in the labour market could be explained not only by the economic slowdown but also by the Government's recent austerity plans. In June, 130k jobs were lost, with public administration and defense activities contributing the most to the negative result, with the loss of -172k jobs, associated with the recent cuts in government spending and the austerity plans that have been proposed. Construction, which groups 6.5% of the employed population, was the second activity to reduce labour with -129 k jobs y/y, in line with the recent situation of the sector that keeps a weak dynamism in terms of the initiation of new housing projects, something that occurs similarly in the commerce sector (chart 4).

The behaviour of employment would reflect a weakening in service activities. The tertiary sector has indeed been the most resilient to the economic cycle, however, recent employment data suggests that it could be slowing down at the margin, given that the services sector reduced -167k, the largest reduction in jobs since March 2021 (the first reduction since the pandemic). Although it is a concern in terms of economic activity, this could be contributing to lower inflation in services, which in June stood at 8.23% y/y, and which remains one of the main concerns in terms of economic policy.

Chart 4



Sources: Scotiabank Economics, DANE.

Key information on employment data:

- **In annual terms, 130 thousand jobs were destroyed.** The public administration sector was the one that contributed the most to the negative variation with the loss of -172k jobs, followed by construction with -129k and professional activities with -110k. On the positive side, the manufacturing industries were the ones that added the most jobs with +153k, followed by information and communications with +124k.
- **The destruction of jobs was concentrated in the female population.** The male employed population remained stable compared to June of the previous year at 13.5 million, while 131k jobs were lost in the female population, reaching an employed population of 9.4 million (41% of the total employed). In annual terms, the female unemployment rate increased by 1.3 ppts to 12.9%, while the male unemployment rate increased by 0.7% due to an increased labour force that was not compensated with jobs.
- **Informality increases slightly.** The proportion of informal employment stood at 56%, rising by 0.3 ppts compared to 55.7% in June 2023, showing a greater increase in informality in rural areas where the proportion reaches 84%.

—Sergio Olarte & Daniela Silva

COLOMBIA: FITCH AFFIRMS THE SOVEREIGN CREDIT RATING AT BB+, MAINTAINING THE STABLE OUTLOOK

Colombia's credit rating remains at BB+ with a stable outlook. As usual, Fitch highlighted Colombia's track record of macroeconomic and financial stability, the independent central bank, and the free-floating currency regime. However, they highlighted that there are fiscal challenges since the government fiscal deficits are projected above 5% in 2024 and 2025, and debt burden for the general government is expected to increase from 53.7% in 2023 to 57.7% of GDP. Fitch's decision is positive for Colombia; some weeks ago, Moody's also

Table 1: Colombia—Credit Rating Profile

	Rating	Outlook
Fitch	BB+	Stable
S&P	BB+	Negative
Moody's	Baa2	Negative

Sources: Scotiabank Economics, Fitch, S&P, Moody's.

affirmed the Baa2 (outlook negative), a rating still above the investment grade. Fitch's and Moody's decision at least guarantees stability in credit assessment around Colombia in the forthcoming months. However, pursuing a more efficient budget implementation and having a better economic recovery is still key to maintaining the current credit status in forthcoming years. The Government has emphasized that the target up to 2026 is at least to have an improved credit rating outlook by Fitch and S&P, but the country should deliver a better macro picture before that (table 1).

From the macro perspective, the fiscal risk premium is properly priced in the FI and the FX market. In the case of FI, the current slope of the curve reflects fiscal concerns and the fact that the debt supply in long-term tenors is increasing significantly. In the case of the FX, a USDCOP ranging from 4000 to 4150 pesos is compatible with pricing of a risk premium of around 200 pesos due to fiscal concern. Having said that, both markets shouldn't concentrate more on a potential credit spread deterioration; instead, they should focus more on the monetary policy fundamentals.

Key points about Fitch's decision:

- The credibility of the country's institutions is robust. As usual, the opening comment in any credit rating assessment highlights the tradition of macroeconomic and financial stability, which we think is Colombia's most valuable asset.
- Fiscal perspectives point to a deterioration, the most concerning part is related to interest payments. According to Fitch calculations, the interest to revenues ratio is expected to rise to 14.5% in 2024, well above the BB median of 11.1%, which could be the most concerning part of the fiscal sustainability if Colombia doesn't achieve better growth numbers in the future.
- Fitch's economic perspectives are broadly aligned with market consensus. Economic growth is expected to accelerate but still grow below potential. The forecast for 2024 GDP growth is at 1.5%, while for 2025 it's at 2.8%. Inflation will continue falling to 5.8% by the end of 2024, while the central bank is expected to cut rates to 8.50% in Dec-2024, with the terminal rate at 6.5% by Dec-2025.

Finally, Fitch emphasized that a downgrade in the credit rating will be triggered by a more sustained deterioration in Colombia's general government debt-to-GDP ratio, weaker medium-term economic growth perspectives, and unsustainable external deficits. For now, this is not the base case scenario at Scotiabank Colpatria; instead, we expect a gradual economic recovery that could help Colombia maintain its current credit rating levels.

—Sergio Olarte & Jackeline Piraján