LATAM DAILY

November 8, 2024

Latam Daily: Chile, Colombia, and Brazil CPI; Colombia MPR and Mexico CPI Recap

- **Colombia: Domestic and external uncertainty favours cautious approach by BanRep's board, while the staff revised the neutral rate higher**
- **Mexico: October inflation—increase in fruits and vegetables led the rise in headline inflation, while services broke the 5.0% barrier**

A very quiet (nope) week is finally coming to an end ahead of the US and Canadian long weekend, with Asia hours giving markets little to go on until this morning's Chinese fiscal press conference shook up trading a bit—disappointing near-term measures were only offset by a pledge to implement forceful fiscal policy next year (we will see). It was all kind of as expected in terms of helping shore up local government finances, but with a smaller swap envelope for hidden debt than expected.

The G10 week closes with Canadian jobs data at 8.30ET, followed by US U Mich results at 10ET (note the survey ended Nov 4), all accompanied by political intrigue in Germany as Chancellor Scholz faces growing pressure to hold an earlier confidence vote following the dismissal of his Fin Min and coalition partner Lindner.

USTs held fairly rangebound in overnight Asia trading, not too far from post-Powell levels as the FOMC comms suite led to some choppy trading but was ultimately a net non-event for USTs and FX yesterday. A decent drop in global yields since the European open—with China's mostly disappointing presser somewhat behind it—leaves global curves richer across all maturities with an outperformance of the belly.

The USD is mixed to stronger as high-beta/commodity FX like NOK, AUD, and NZD trade 0.4–0.6% weaker on China disappointment while the JPY is the top gainer among the key FX thanks to a 0.5% gain that takes it to pre-election levels. News out of China has also hit iron ore and copper that are shedding about 3% and 2.5% off their respective prices, while also pulling crude oil lower by about 1.5%. Losses of 1% and 0.5% in SX5E and FTSE follow from Chinese developments that are also dragging US equity futures a touch lower given an overall risk-negative mood in trading.

We have three inflation releases in Latam today, starting with Chile in just a few minutes, followed by Brazil at 7ET, and then a long wait until Colombia's at 18ET after markets close. The first two releases are expected to show an acceleration in prices growth in both m/m and y/y terms, but Chile's data are expected to show a very muted 0.1% m/m rise in ex-volatiles prices as headline inflation is driven by electricity fees; after weak economic activity data released earlier this week, markets are roughly pricing in 25bps cuts at the next three meetings. On that note, Peru's BCRP (unsurprisingly?) surprised us and half of economists polled by Bloomberg with a 25bps rate cut last night to 5.00%, but adding that the real interest rate is approaching neutral—which to us suggests that the December meeting will be a rate hold (we had expected hold last night and cut in December, so this merely flips the timing).

In Colombia, headline and core inflation are expected to tick lower by about 0.1ppts only, to 5.71% and 6.45%, respectively, as inflation stickiness continues while BanRep is also challenged by domestic and external political and fiscal risks (see Colombia section). Regarding fiscal conditions, Pres Petro reportedly made a welcome move to reduce spending by COP33tn (USD7.6bn) in order to meet fiscal goals as his administration had recently sought to maintain spending despite lower revenues—and no concrete or believable plans to increase these.

—Juan Manuel Herrera

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COLOMBIA: DOMESTIC AND EXTERNAL UNCERTAINTY FAVOURS CAUTIOUS APPROACH BY BANREP'S BOARD, WHILE THE STAFF REVISED THE NEUTRAL RATE HIGHER

The central bank released minutes regarding October's monetary policy meeting late on Wednesday, November 6th. October was a new difficult meeting for the central bank; the surge of volatility in international markets plus Congress' discussion about the reform of the fiscal transfer to regions overshadowed the progress on inflation that in a traditional Taylor rule could have allowed a more aggressive cut.

In October's minutes, the board quoted that all the uncertainty could reduce the "manoeuvre margin to continue the easing cycle at the current speed," a quote that we also saw in the post-meeting communique; however, although it sounds aggressive, the wording during the press conference wasn't like that. The majority of BanRep's board assigned relevant weight to emerging uncertainties to continue cutting the rate by 50bps, while the minority group perceived the inflation reduction as an opportunity to impulse the economy with a more aggressive cut.

It is worth noting that on Tuesday, the central bank staff released the Monetary Policy Report, showing that they are very tilted to the cautious side since they favour a slightly higher interest rate path versus economist consensus to ensure the inflation converges towards the target. The staff also revised the neutral rate estimation for 2025 from 2.5% to 2.6%, which at least favours continuing cautious cuts at a 50bps pace in forthcoming meetings.

All the market developments during November will be key to assessing the future steps of the central bank in Colombia; in our perspective, international volatility could ease a bit. However, domestic discussions around fiscal proposals and minimum wage negotiations would not be resolved before the next BanRep meeting on December 20th. That said, we changed our call for December, and now we expect a 50bps cut, closing the year at 9.25%. However, the cautious approach could continue into the January meeting, and the acceleration in the easing cycle increases their chances in the March meeting, since by this time, we expect to see more evidence of inflation convergence towards the target product of lower indexation effects. Having said that, involving in our projections the estimation of the higher neutral rate, we revise to the upside the terminal rate to 5.75%, which will reflect the fact that international rates could stabilize at higher levels but also recognize the impact of fiscal uncertainty in Colombia risk premiums.

Further details about BanRep's minutes and Monetary Policy Report:

- **The macroeconomic scenario has had positive developments, which allowed the central bank to continue cutting rates. The board considers that the easing cycle is effective in controlling inflation and promoting economic activity recovery.**
- **New risk in the macro scenario demand to maintain a cautious approach.** Among the mentioned risks are the FX depreciation, oil price reduction, uncertainty around the financing of the fiscal budget in 2025, and the debate in Congress about regional budgets.
- **The majority group that voted for the 50bps cut said that it is not prudent to accelerate the easing cycle since it could compromise the compliance of the inflation target.** There is uncertainty around the fiscal situation and FX depreciation. Regarding the macro picture, they mentioned the still-sticky behaviour of services prices and the uncertainty around the minimum wage negotiations.
- **The group who voted for a 75bps cut recognized that the economic activity is consolidating a recovery and the labour market has been resilient despite monetary policy being contractive.** However, they said that inflation reduction provides a window to stimulate the economy further with a more prominent cut. It was curious that in the communique they said that current conditions opened "the last opportunity window to the monetary policy to offer an impulse to the economy." This group shares concerns about local and global uncertainties; however, they are more optimistic regarding the potential resolution around the fiscal discussion. One member said that it is important to assess how structural the recent FX depreciation is.
- **About the monetary policy report.** The central bank staff projects the persistence of a scenario with a positive inflation gap and a negative output gap. However, they see a higher number of upside risks on inflation, while negative risks on economic growth are limited to the possibility of having a public sector with less capacity to spend. All in all, the staff sees that it is necessary to maintain a restrictive monetary policy rate and projects an average interest rate path above current economists' consensus projections that point to a 6.1% average rate in the fourth quarter of 2025. The central bank recognizes that if there is no structural inflationary pressure from the FX depreciation, if the services inflation decreases more than expected, and if the minimum wage increase is not higher than 6.5%, the monetary policy path could be lower.

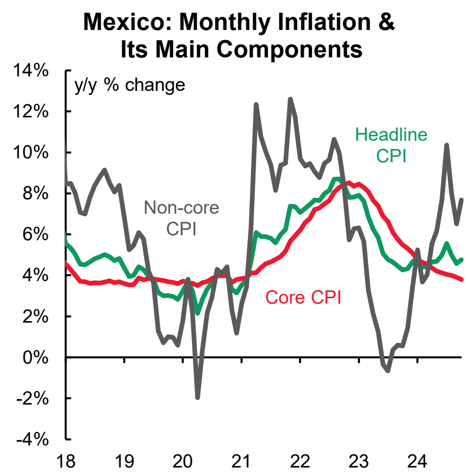
- **Our take:** Despite inflation progress and the still negative output gap generates space to speed up the easing cycle, we recognize the uncertainty is high on many fronts; that is why we revised to the upside our expected path for the monetary policy rate, passing from an estimated terminal rate of 5.50% to 5.75%, which according to our inflation projection for the year-end implies a real rate between 2% to 2.5%. We see the chance of having an acceleration in the easing cycle after the first quarter of 2025, when the effect of lower indexation will be better reflected on inflation indicators. For now, we change our call for 50bps rate cuts in the December and January meetings.

—Jackeline Pirajàn

MEXICO: OCTOBER INFLATION—INCREASE IN FRUITS AND VEGETABLES LED THE RISE IN HEADLINE INFLATION, WHILE SERVICES BROKE THE 5.0% BARRIER

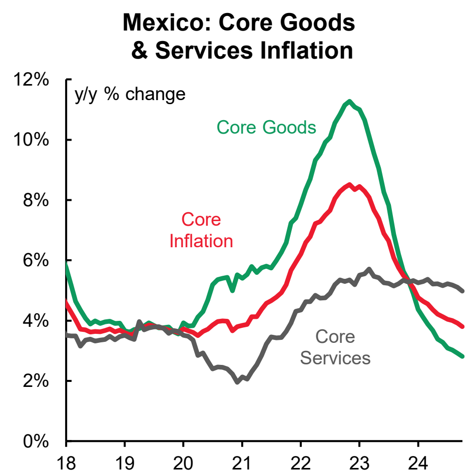
In October, inflation rose to 4.76% y/y from 4.58% (vs. 4.73% consensus in the Citibanamex Survey) because of a sharp increase in non-core inflation. It is noteworthy that core inflation moderated to 3.80% from 3.91% (vs. 3.84% consensus), where merchandise decelerated 2.81% (2.92% previously), and services broke the 5% barrier, for the first time since July 2022, to stand at 4.98% (5.10% previously), see charts 1 and 2. On the other hand, non-core inflation showed an increase of 7.68% (6.50% previously), with agricultural inflation standing out, which rose 10.92% (6.76% previously), given a 15.90% expansion in fruits and vegetables. In its monthly comparison, headline inflation rose 0.55% m/m (0.05% previously, 0.52% consensus), the core component 0.28% (0.28% previously, 0.33% consensus) and the non-core component 1.41% (-0.72% previously). Despite the increase in headline inflation, we maintain our expectation that Banxico will cut the reference interest rate by 25 basis points on November 14th to set the reference interest rate at 10.25%.

Chart 1



Sources: Scotiabank Economics, INEGI.

Chart 2



Sources: Scotiabank Economics, INEGI.

—Rodolfo Mitchell, Brian Pérez & Miguel Saldaña