Scotiabank

GLOBAL ECONOMICS

LATAM DAILY

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Latam Daily: Chile, Colombia, Mexico Inflation Recap; Mexico 2024 Budget Proposal

- **Chile: Inflation surprised to the downside, we reaffirm our forecast of 3.7% y/y for Dec 2023**
- **Colombia: Annual headline inflation fell less than expected, while monthly inflation surprised to the upside**
- **Mexico: Inflation moderates its pace in August, non-core rebounded; Notable gains in auto sector in August**

Overnight markets had handed over to Europe a more upbeat end to the week that had the USD broadly weaker, US equity futures a touch firmer and lower yields across the board showing a minor outperformance in the belly. Some of these moves have come off their lows/highs during the European session that is seeing somewhat erratic trading and a touchier risk mood.

As we head into the Americas session, crude oil prices have rallied over the past hour to notch a 0.6% increase (for +4.5% since Friday) supported by the Saudi/Russia production/export cuts extension, iron ore and copper are down 0.5% and 0.9%, respectively. Global rates curves are slightly twist steepening, as yields also move back from overnight lows, and US equity futures are down 0.2/3% with China's government reportedly extending iPhone bans to local governments and SOEs. The Canadian jobs roulette at 8.30ET is the G10 highlight of the day ahead of the Fed communications blackout starting tomorrow—and US CPI next week.

The MXN is reverting its losses during yesterday's US hours to hang back around 17.50, but still tracking a 2.2% drop for the week that makes it the worst performing major FX. Banxico's reduction of its FX hedging programme is still being digested, but rate differentials and a solid economy are solid supports that stand to prevent marked weakness. The title of worst currency among an expanded field of key FX this week goes to the CLP, on pace for a 3.7% depreciation.

The Chilean peso traded in the high 800s yesterday, its worst levels since December 2022, amid the broad dollar-positive mood so far in September but also as the BCCh's rate cuts weigh. This morning's CPI data, with a significant downside surprise in headline and ex volatiles inflation augurs an important rally in early trading in front-end Chilean rates markets alongside Chilean peso weakness.

On the flipside, the COP is up 0.6% since last Friday as the only expanded majors currency that is up against the USD this week, and may even get an extra push from the stronger-than-expected inflation data published yesterday that likely pushes out the start of the cutting cycle (see below).

In Latam, we don't have any more data to follow after this morning's release of August CPI in Chile (see below) and there's also not all that much to watch in the region from a scheduled data standpoint aside from Tuesday's Brazilian CPI, and Thursday's BCRP decision followed by Peruvian GDP on Friday.

The focus for our markets will be Mexico's 2024 budget proposal, due to be presented to Congress by FinMin Ramirez de la O at 19ET. Aside from the government's plans for spending and its macroeconomic projections, we're awaiting details on debt repayment support for Pemex that is reportedly included in the package. On a related note, the main opposition candidate, Xochitl Galvez, said yesterday that she aims to reopen the country's energy market, highlighting Brazil's Petrobras as a model to follow.

On the 'other side of the aisle', Ebrard, who lost the Morena candidacy race to Sheinbaum this week, said yesterday in a radio interview that "what is clear to me is that in Morena we have no room" and that he would be on the 2024 ballot "one way or another". We're keeping an eye on risks that Ebrard could run under the Movimiento Ciudadano banner, with the party still undecided on who will represent them next year. This would likely have a greater negative impact on Galvez than on Sheinbaum—thus increasing the odds that Morena stays in power.

—Juan Manuel Herrera

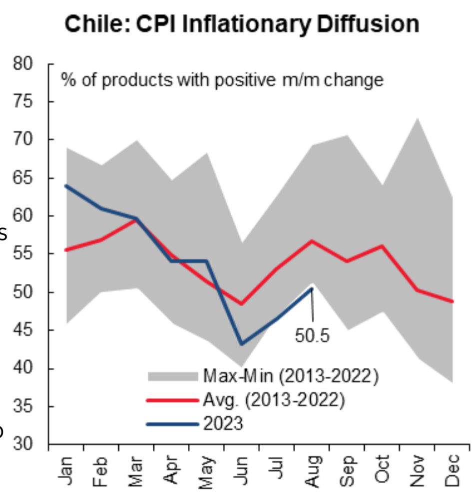
CHILE: INFLATION SURPRISED TO THE DOWNSIDE, WE REAFFIRM OUR FORECAST OF 3.7% Y/Y FOR DEC 2023

- **August CPI rose 0.1% m/m (5.3% y/y), below market expectations**

This morning, the statistical agency (INE) released August CPI data, showing a price rise of 0.1% m/m (5.3% y/y), below the market and our expectation (0.4%) mainly due to lower increases in food prices and tourism packages. Indeed, at the core level, the CPI decreased 0.1% m/m (7.4% y/y), below its historical average. Within this measure, services inflation stood at 0.2% m/m, while the CPI for goods fell 0.4% m/m, which is on the low side from a historical perspective.

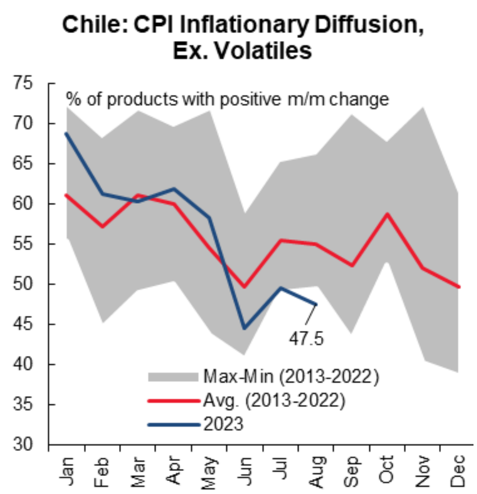
Inflationary diffusion remained at the lower end of its historical range. The number of price increases within the basket stood at 50.5% (chart 1), similar to the diffusion of CPI without volatiles (47.5%, see chart 2). In our view, these figures confirm that disinflationary pressures continue to be evident and widespread within the basket, both at the headline and core levels, having been observed for several months in goods and with greater strength recently in services.

Chart 1



Sources: Scotiabank Economics, INE.

Chart 2



Sources: Scotiabank Economics, INE.

—Aníbal Alarcón

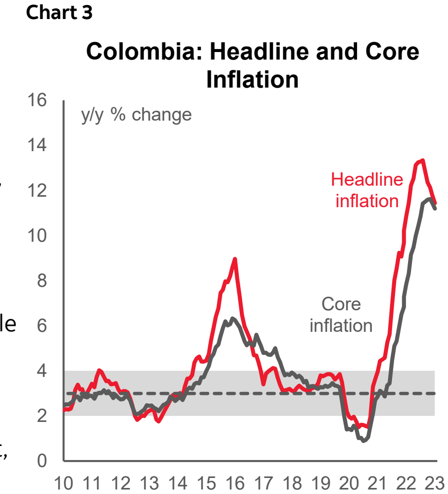
COLOMBIA: ANNUAL HEADLINE INFLATION FELL LESS THAN EXPECTED, WHILE MONTHLY INFLATION SURPRISED TO THE UPSIDE

Monthly CPI inflation in Colombia was 0.70% m/m in August, according to DANE data released on Thursday, September 7th. The result was, again, above the expectations of analysts in the BanRep survey (0.44% m/m) and above the forecast of Scotiabank Economics (0.45% m/m). The upside surprise came for the second month from food inflation at 1.13% m/m, up from 0.22% m/m in the previous month, mainly due to an increase in prices of alcoholic beverages and some fruits, probably reflecting the impact of supply disruptions due to landslides on relevant roads. Accommodation and public services and transport remain the main upward drivers of inflation, mainly due to increases in rental prices, reflecting the impact of indexation and gasoline prices.

Headline inflation declined for the fifth month, from 11.78% in July to 11.43% in August (chart 3), the lowest since August 2022 (10.84% y/y). However, headline inflation fell less than expected. Core inflation fell for the second consecutive month for the first time since October 2021; non-food inflation fell from 11.44% to 11.19%, while non-food non-energy inflation was 10.09% y/y, also down from the previous record of 10.54% y/y in July, mainly due to a moderation in tradable goods inflation.

In any case, both headline and core inflation remain well above BanRep's 3% target. The above dynamics confirm our expectation that BanRep will not consider a rate cut in September. In fact, although our official call for a rate cut starting in October remains, recent CPI data put an important bias to a later start of BanRep's easing cycle. Now we see higher probability of a kick-

Chart 3



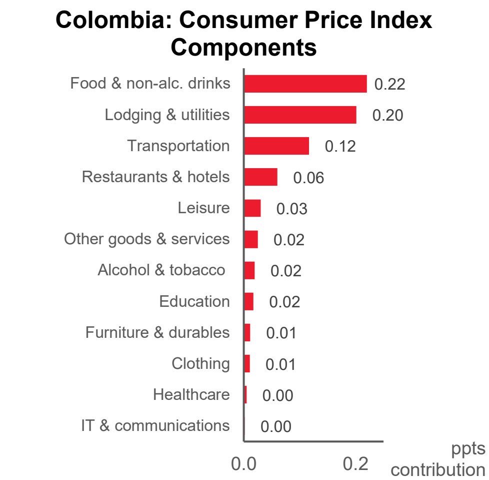
Sources: Scotiabank Economics, DANE.

off in December 2023 due to the slower pace of inflation deceleration.

Our current forecast shows that Colombia could only reach single-digit inflation by the end of the year (November), which is still very high compared to the central bank's target (3%) and represents a risk of inflationary inertia given the indexation effects for 2024.

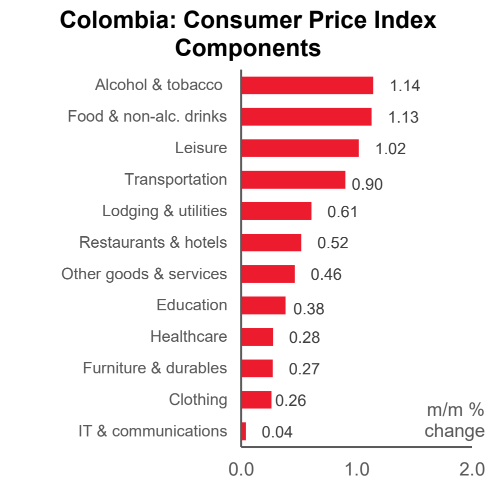
Regulated prices, especially the price of gasoline and then diesel, the El Niño weather phenomenon and the minimum wage negotiations remain the main risk factors that could prevent BanRep from starting the easing cycle. On the other hand, a moderate slowdown in economic activity and currency appreciation could favor lower inflation. Nevertheless, BanRep's data-dependent approach is expected to continue, and only a scenario of greater decline in inflation and inflation expectations could trigger the easing cycle.

Chart 4



Sources: Scotiabank Economics, DANE.

Chart 5



Sources: Scotiabank Economics, DANE.

August CPI surprise, shows that the decline in inflation remains fragile and there is still considerable uncertainty ahead, which undoubtedly reduces the chances of an early rate cut at the September meeting.

Looking at the August figures in detail, food inflation is the group that generated the most pressure on inflation during the month (charts 4 and 5).

The highlights are:

- Food inflation once again surprised to the upside and once again became the main contributor to the rise in monthly inflation, recording an inflation of 1.13% m/m and contributing to the headline by 22 bps. There were significant increases in food items such as tomatoes, onions, and fresh fruits. On the other hand, food items such as poultry meat, bananas and carrots show moderation. It is important to note that inflation has peaked thanks to food inflation. However, July and August's results, show that these prices are very volatile, and the cumulative progress observed in recent months could pose risks to the pace of the decline in inflation. In the short to medium term, the main challenge remains the El Niño weather phenomenon. However, we estimate that the possible upside impact on food prices could start to be reflected in H1-2024 if this phenomenon turns out to be intense.

- The second contributor to the rise in monthly inflation was the accommodation and public services group. The group recorded a contribution of +0.61% m/m and +19 bp. Rents fees continued to rise as imputed rent (0.55% m/m) and effective rent (0.60% m/m) were higher than in July (both 0.45% m/m), showing that indexation effects are still present. Public services fares increased by 0.72% m/m. Waste collection rates fell by 0.84% m/m this month. However, this was offset by increases in gas (+1.11% m/m), sewerage (+0.84 m/m), electricity (0.82% m/m) and water (+0.64% m/m).

- Transportation was the third largest contributor to headline inflation, with a rate of 0.90% m/m and a contribution to headline inflation of 0.12 pp. Gasoline inflation rose by +3.53% m/m due to a COP 600 increase. We expect the government to continue raising gasoline prices until the end of the year; however, the big question at this point is whether the government will decide to raise diesel prices, which poses a significant upside risk due to possible spillovers to other key elements of the CPI basket.

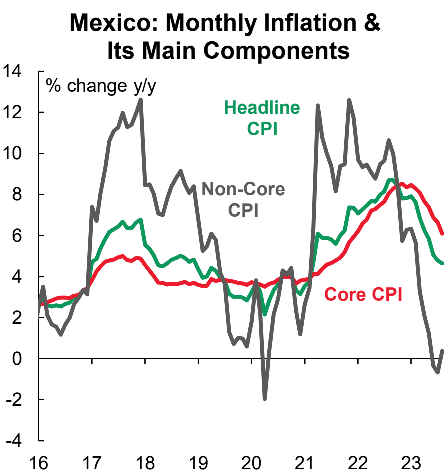
- The transportation group continues to show an interesting dynamic stemming from currency appreciation and lower demand: vehicle inflation was -0.13% m/m, the second monthly contraction since January 2019 (along with -0.19% m/m from the previous month). The vehicle sector is showing the effects of lower demand, as new car sales continue to contract by more than 40% y/y, and a trend of sellers trying to update inventories at lower exchange rates.

- Inflation by major groups: Durables inflation continued to decline from 0.20% m/m to -0.07% m/m, the first monthly decline since May 2021. On an annual basis, consumer durables continued to rise from 15.71% y/y in July to 14.12% y/y in August. Services inflation rose from 9.36% y/y to 9.50% y/y due to still significant indexation effects in labour-intensive sectors and rent fees. On a monthly basis, it rose from 0.41% m/m in July to 0.43% m/m in August.

MEXICO: INFLATION MODERATES ITS PACE IN AUGUST, NON-CORE REBOUNDED

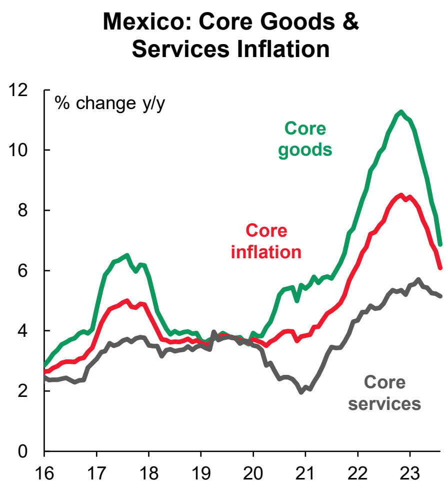
In August, inflation slowed to 4.64% y/y from 4.79% previous (4.62% consensus), core inflation also moderated to 6.08% y/y from 6.64% prior (6.12% consensus), derived from a slowdown in merchandise to 6.86% (7.82% prior), and marginally in services to 5.15% (5.24% prior). Non-core rose 0.37% y/y from -0.67%, energy fell -2.68% (-3.90% previous), though agriculture rose 3.94% (3.16% previous). In its monthly comparison, headline inflation increased 0.55% m/m (0.48% previous, 0.53% consensus), core inflation fell to 0.27% m/m (0.39% previous, 0.30% consensus), with a slower pace in merchandise and services. Finally, the non-core registered a strong increase 1.44% m/m (-0.77%, charts 6–8).

Chart 6



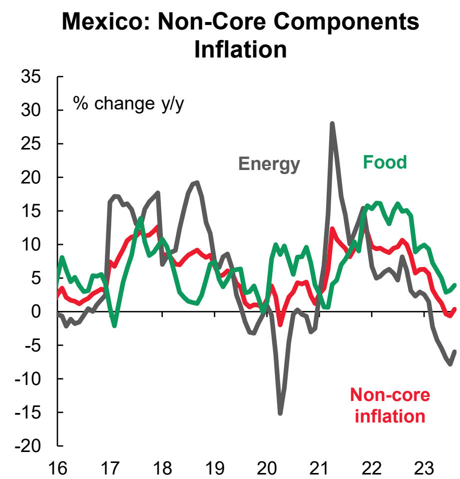
Sources: Scotiabank Economics, INEGI.

Chart 7



Sources: Scotiabank Economics, INEGI.

Chart 8



Sources: Scotiabank Economics, INEGI.

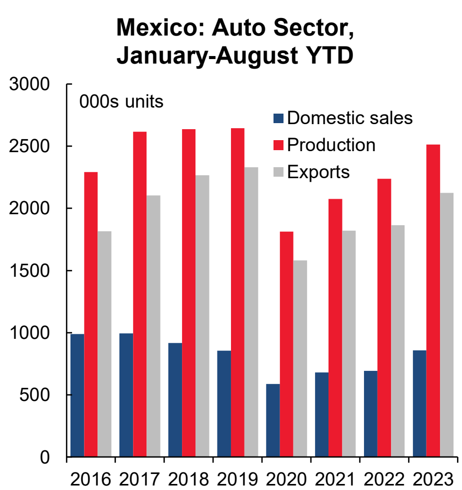
Given this print, we anticipate that inflation will continue to slow down, although the non-core component is already influencing the monthly readings, which could lead to a slower rate of slowdown, even some annual increase, even though the core component falls. The surprise came from the merchandise, which fell 95.8 basis points, although it is too soon for the perspective of persistence to change, since services have been exceeding 5.0% for 13 months. Looking ahead, we will pay attention to the behavior of agricultural products, which reached their minimum in June, and have already risen 104.7 bps. In the last Citibanamex Survey, the average inflation for the end of 2023 rose slightly to 4.71%, while the response range is between 4.30%-5.50%.

NOTABLE GAINS IN AUTO SECTOR IN AUGUST

During August, sales of light vehicles were 113,873 commercialized units, which represented an annual increase of 23.8% y/y (32.6% previous), 325,676 units were produced, decelerating in the annual comparison 2.8% y/y (13.2% previous), and exported 287,845 units, decelerating to 15.7% y/y (31.2% previously). In the cumulative January–August period, sales remained with an increase of 23.6% YTD, production moderated to 12.3% (13.8% previous), and exports rose 14.0% (13.7% previous, charts 9 and 10).

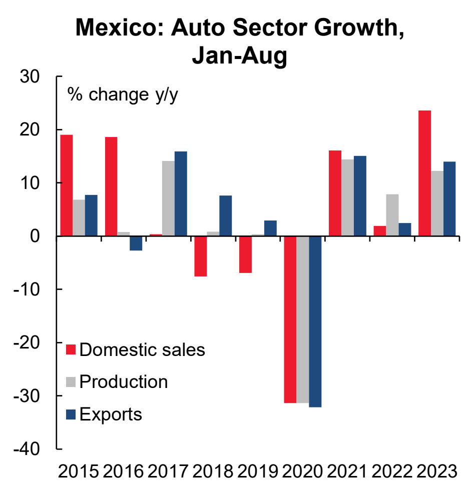
The automotive industry has seen an important recovery this year, since year to date numbers far exceeds the units of August

Chart 9



Sources: Scotiabank Economics, INEGI.

Chart 10



Sources: Scotiabank Economics, INEGI.

2020 in the three items (0.6 million YTD sales, 1.8 mn YTD production and 1.6 mn YTD exports), while it is barely reaching the levels prior to the pandemic (0.9 YTD million sales, 2.6 YTD production and 2.3 YTD exports up to August 2019), however, there is still a long way to go in both production and exports. The normalization of supply chains has brought stability and better performance to the sector, linked to the strength of the Mexican economic activity observed this year, although production may be affected by the high demand for microchips and semiconductors for technological innovation, mainly owing to advances in AI, so it can bring new problems to the sector in the medium term.

—Miguel Saldaña & Brian Pérez