



LATIN AMERICA ECONOMICS WEEKLY

Petro spooks investors (once again), Brazil's fiscal rule

Colombia: here comes the state

Concerns about the direction of policymaking under President Petro have once again lead to a sharp sell-off in Colombia's financial markets this week.

The catalyst this time was the government's health reform bill, which was presented to congress on Monday. If passed, it would severely weaken the role of private healthcare providers and increase the role of the state in the provision of healthcare.

It's still early days, but at this point we would highlight three points. First, the health bill will serve as an indicator of the government's ability to pass some of its other key reform proposals, such as pension reform. (Recall that Petro relies on his coalition partners to pass bills in congress.) Second, there would be a fiscal cost. The government estimates that the cost associated with the bill could amount to over COP 50trn (~3.5% of GDP) – more than twice the size of the additional revenues raised in last year's [tax reform](#). And finally, the bill supports [our view](#) that the state will play a more prominent role in the economy under the Petro administration. (Yesterday's decree allowing the government to set electricity tariffs fits in with this narrative.)

Unsurprisingly, these developments were not met well by investors. Sovereign bond yields have jumped. And the Colombian peso is down by 2% against the dollar this week, making it by far the worst performing major Latin American currency.

One key reason for the peso's sensitivity to political news is Colombia's large [current deficit](#) (as well as its financing) – the deficit stood at over 6% of GDP in Q3, one of the largest shortfalls among major EMs. In this regard, there are at least encouraging signs that the economy is at the start of an adjustment process. [GDP data](#) out this week showed that domestic demand and imports both contracted in Q4, suggesting that the current account deficit narrowed last quarter. And the sharp slowdown we expect in Colombia's economy this year will help to

rein in the current account deficit which, combined with [low valuations](#), should support the currency. Despite Petro's interventionism, we expect the peso to end the year at 4,400 /\$, from ~4,900 currently.

Brazil: new fiscal rule on the horizon

Brazil's Economy Minister Fernando Haddad this week brought forward the planned announcement of a new fiscal rule to March (previously Q2) in an overture to investors. One option discussed prior to last year's election was amending the existing spending cap (which limits federal government spending growth to inflation), by allowing expenditure growth of inflation plus a few percent, or only applying the cap to current spending (i.e. freeing up capital expenditure). But Mr. Haddad's latest comments suggest that he's keen to move away from an expenditure-based rule altogether. That would point to likely options being a (structural) budget target (as exists in Chile) or a net debt target.

The literature suggests that there are several ingredients that make a good fiscal rule: an 'escape clause' allowing the government to deviate from the rule when necessary; an independent fiscal body overseeing compliance; and broad coverage (i.e. covering the entire government, not just the federal government). (For more, see our [Focus](#).)

But as important as a good fiscal rule is for Brazil, it's also key to reduce the extent of mandatory government expenditure (due to various rules and indexation) which limits policymakers' room for maneuver. Moreover, it's hard to escape the conclusion that the government's plans for a new rule are primarily aimed at providing more fiscal headroom, putting public debt sustainability at risk. Convincing the markets otherwise will be the real test for Mr. Haddad.

The week ahead

Mid-month CPI figures from Brazil and Mexico are likely to show that inflation edged down in both countries in the first half of February.



Economic Diary & Forecasts

Upcoming Events and Data Releases

Date	Country	Release/Indicator/Event	Time (GMT)	Time (EST)	Previous*	Median*	CE Forecasts*
21 st Feb	Mex	Retail Sales (Dec.)	12.00	07.00	-0.2%(+2.4%)	-	-
22 nd Feb	Arg	Trade Balance (Jan.)	19.00	14.00	\$1.1bn	-	-
	Arg	Budget Balance (Jan.)	-	-	-441.5bn	-	-
23 rd Feb	Mex	Bi-Weekly CPI (15 th Feb.)	12.00	07.00	+0.4%(+7.9%)	-	+0.5%(+7.6%)
	Mex	Bi-Weekly Core CPI (15 th Feb.)	12.00	07.00	+0.4%(+8.5%)	-	-
	Mex	MPC Meeting Minutes Released	15.00	10.00	-	-	-
24 th Feb	Arg	Economic Activity Index (Dec.)	19.00	14.00	-0.7%(+2.6%)	-	-
	Mex	IGAE Activity Index (Dec.)	12.00	07.00	-0.5%(+3.3%)	-	-
	Mex	GDP (2022)	12.00	07.00	+4.8%	-	+3.0%
	Mex	GDP (Q4, Final Estimate)	12.00	07.00	+0.4%(+3.5%)	-	+0.5%
	Brz	IPCA-15 Inflation (Feb.)	12.00	07.00	+0.6%(+5.9%)	-	+0.5%(+5.4%)
	Mex	Current Account Balance (Q4)	15.00	10.00	-\$5.5bn	-	-
	Col	MPC Meeting Minutes Released	-	-	-	-	-
Also expected during this period:							
20 th – 24 th	Per	GDP (Q4)	-	-	(+1.7%)	-	-
Selected future data releases and events:							
27 th Feb	Mex	Trade Balance (Jan.)	12.00	07.00	+\$0.98bn	-	-
28 th Feb	Chl	Unemployment Rate (Jan.)	12.00	07.00	7.9%	-	-
	Brz	Unemployment Rate (Jan.)	12.00	07.00	8.1%	-	-
	Chl	Industrial Production (Jan.)	12.00	07.00	(-1.0%)	-	-
	Chl	Retail Sales (Jan.)	12.00	07.00	(-11.1%)	-	-
	Brz	Primary Budget Balance (Jan.)	12.30	07.30	-\$70.8bn	-	-
	Brz	Nominal Budget Balance (Jan.)	12.30	07.30	-\$11.8bn	-	-
1 st Mar	Dom	Interest Rate Announcement	-	-	-	-	-
	Brz	S&P Global Manufacturing PMI (Feb.)	13.00	08.00	47.5	-	-
	Per	CPI (Feb.)	15.00	10.00	+0.2%(+8.7%)	-	-
	Mex	S&P Global Manufacturing PMI (Feb.)	15.30	10.30	48.9	-	-
	Brz	Trade Balance (Feb.)	18.00	13.00	+\$2.7bn	-	-
	Mex	IMEF Manufacturing Index (Feb.)	18.00	13.00	50.0	-	-
	Mex	IMEF Non-Manufacturing Index (Feb.)	18.00	13.00	52.2	-	-
	Col	Current Account Balance (Q4.)	-	-	-\$6.2bn	-	-
2 nd Mar	Brz	GDP (Q4, q/q(y/y))	12.00	07.00	+0.4%(+3.6%)	-	-
	Mex	Budget Balance (Jan.)	-	-	-	-	-
3 rd Mar	Brz	S&P Global Manufacturing PMI (Feb.)	13.00	08.00	50.7	-	-
	Uru	CPI (Feb.)	17.00	12.00	+1.6%(+8.1%)	-	-

*m/m(y/y) unless otherwise stated; † = previous day

Sources: Bloomberg, Capital Economics



Main Economic & Market Forecasts

Table 1: Central Bank Policy Rates (%)

Policy Rate	Latest (17 th Feb.)	Last Change	Next Change	Forecasts	
				End 2023	End 2024
Brazil Selic Target	13.75	Up 50bp (Aug. '22)	Down 50bp (Q4 '23)	12.75	10.00
Mexico Overnight Rate	11.00	Up 50bp (Feb. '22)	Up 25bp (Mar. '23)	10.25	8.25
Colombia Intervention Rate	12.75	Up 75bp (Jan. '23)	Up 50bp (Mar. '23)	11.00	7.25
Chile Overnight Rate	11.25	Up 50bp (Oct. '22)	Down 50bp (Q2 '23)	7.25	5.25
Peru Reference Rate	7.75	Up 25bp (Jan. '23)	Down 25bp (Q2 '23)	6.50	5.00

Sources: Refinitiv, Capital Economics

Table 2: FX Rates vs. US Dollar & Equity Markets

Currency	Latest (17 th Feb.)	Forecasts		Stock Market	Latest (17 th Feb.)	Forecasts	
		End 2023	End 2024			End 2023	End 2024
Brazil BRL	5.19	5.25	5.00	Bovespa	109,543	109,500	126,500
Mexico MXN	18.5	20.0	19.0	Bolsa	53,706	57,500	62,100
Argentina ARS	193	300	375	Merval	252,020	-	-
Colombia COP	4,898	4,400	4,400	IGBC	1,210	1,380	1,520
Chile CLP	787	820	780	IPSA	5,344	5,950	6,500
Peru PEN	3.84	3.80	3.70	S&P/BVL	21,926	25,100	27,400

Sources: Refinitiv, Capital Economics

Table 3: GDP & Consumer Prices (% y/y)

	Share of World ¹	GDP					Consumer Prices			
		2011-20 Ave.	2021	2022	2023	2024	2021	2022	2023	2024
Brazil	2.3	0.3	5.0	3.0	1.0	1.5	8.3	9.3	5.0	5.3
Mexico	1.8	1.3	4.7	3.0	1.0	1.8	5.7	8.0	5.3	4.0
Argentina	0.7	-0.7	10.4	5.5	0.8	1.0	48.4	72.5	89.0	81.0
Colombia	0.6	2.5	11.0	7.5	0.8	2.0	3.5	10.3	11.8	5.5
Chile	0.4	2.1	11.7	2.8	-1.3	2.3	4.5	11.8	8.0	4.8
Peru	0.3	2.4	13.6	2.5	2.3	2.3	4.0	8.0	6.5	3.8
Dom. Rep.	0.2	4.1	12.3	4.8	4.0	4.8	8.2	8.8	4.8	4.3
Ecuador	0.1	1.6	4.2	3.0	2.3	2.0	0.1	3.5	1.8	1.0
Venezuela	-	-12.7	5.0	10.0	7.5	5.0	1,589	170	110	60
Panama	0.1	3.5	15.3	7.8	2.5	4.5	1.6	2.8	0.3	0.5
Costa Rica	0.1	2.8	7.8	4.5	2.5	2.3	1.7	8.3	3.3	3.0
Uruguay	0.1	1.5	4.4	4.8	1.5	2.0	7.7	9.0	7.0	8.0
Latin America²	6.7	1.0	7.0	3.8	1.0	1.8	6.2	8.8	5.8	4.6

Sources: Refinitiv, Capital Economics. 1) % of GDP, 2021, PPP terms. 2) GDP Excl. Venezuela; Consumer Prices Excl. Argentina & Venezuela.



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