



# LATIN AMERICA ECONOMICS WEEKLY

## Wage pressures, Mexico's Tesla plant

### Mixed labour market signals

Labour market data released this week from Brazil, Chile and Colombia flew under the radar, but they provide a useful guide to inflation risks.

The common theme is that labour markets are losing steam amid an economic slowdown. Brazil is the most obvious case of this happening. Our seasonally-adjusted measure of employment fell by close to 1% between October and December. So far, though, this is not dampening wage growth; it picked up in December to over 16% y/y.

We looked at the reasons behind surging wage growth [here](#). One key factor is that the labour force participation rate fell during the pandemic which reduced labour supply, making it harder for firms to fill vacancies from the pool of unemployed and forcing them to offer higher wages. Worryingly, this trend continued at the end of last year – over one million people stopped looking for work in Q4.

So even though demand for labour is softening as the economy weakens (Q4 figures out earlier this week showed that [GDP](#) contracted in q/q terms), the fall in labour supply may continue to put upwards pressure on wages. We continue to think that this is an under-appreciated upside risk to the inflation outlook.

We take a bit more assurance from the figures out of Colombia and Chile that inflationary pressures from the labour market may start to ease there. Like Brazil, both countries saw large falls in their participation rates during the pandemic, which helped to push up wage growth. But unlike Brazil, this is now reversing. Labour force participation rates rose in January, contributing to an increase in the unemployment rate (which has been edging up for some months now).

This suggests that more slack in the labour market is emerging, which should ease wage pressures. That said, we're sceptical that wage growth will fall far enough to allow inflation to return anywhere near central banks' targets this year. (See our [EM Focus](#).)

### Tesla, nearshoring and Mexico's growth prospects

The announcement this week that Tesla will build a factory in Mexico has attracted a lot of fanfare but we are sceptical that nearshoring will significantly boost Mexico's growth prospects.

The investment in the northern city of Monterrey is set to amount to at least \$5bn, creating 6,000 jobs and capacity to produce 1m electric cars. That follows a similar investment announced by BMW. These ventures suggest that Mexico is benefitting from so-called nearshoring as firms seek to shore up their supply chains and navigate complex geopolitical waters. It may also be a result of the US Inflation Reduction Act, which provides subsidies for electric vehicles built in the US, Mexico or Canada.

We will explore what nearshoring means for Mexico's economy in detail in upcoming research. But at this stage, we would guard against optimism that it will drive significantly faster growth. After all, Mexico has been a beneficiary from investments in its manufacturing sector for a long time thanks to Nafta, but overall GDP growth has been tepid since that deal was inked. The impediments that have prevented strong growth in the manufacturing sector from filtering through to economy-wide gains have not disappeared. Crime and corruption are common, red tape is excessive and competition is weak. And Amlo's erratic and nationalist policies have *lowered* investment since he took office. He has also threatened to undermine the country's already-weak institutions, evidenced recently by his attempt to slash funding for the electoral commission (INE) that fuelled widespread protests over the weekend.

### In case you missed it

We took a closer look at debt problems in Brazil's corporate sector [here](#).

### The week ahead

We think inflation fell in Brazil and Mexico last month. (See [Data Previews](#).) Meanwhile, Peru's central bank is set to leave interest rates unchanged.



# Data Previews

## Mexico Consumer Prices (Feb)

Thu. 9<sup>th</sup> Mar.

| Forecasts                    | Time (GMT/ET) | Previous   | Consensus | Capital Economics |
|------------------------------|---------------|------------|-----------|-------------------|
| Consumer Prices % m/m(% y/y) | 12.00/07.00   | +0.7(+7.9) | -         | +0.6(+7.7)        |

### *Inflation easing, but Banxico focussed on rising services inflation*

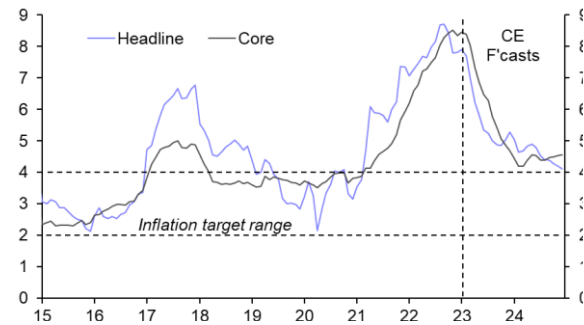
We think that Mexico’s headline inflation rate eased to 7.7% y/y in February.

Inflation peaked in September last year at 8.7% y/y, but it has been slow to come down and stood at 7.9% y/y in January, still well above the central bank’s 3% target. The mid-month inflation figures suggest that the headline rate edged down to 7.8% y/y in the first half of February and we think price pressures eased a bit further over the second half of the month. Non-core inflation probably drove the decline in the headline rate. And while core inflation may have also edged down, services inflation probably rose further.

Stronger services inflation was a key factor behind Banxico’s decision to deliver a larger-than-expected 50bp interest rate hike last month and this

latest increase will only add to the hawkish mood on the Board. We have pencilled in a 25bp increase in rates this month and there is a growing chance of another 50bp hike and/or that the tightening cycle continues for a bit longer.

Chart 1: Mexico Consumer Prices (% y/y)



Sources: Refinitiv, Capital Economics

## Brazil Consumer Prices (Feb.)

Fri. 10<sup>th</sup> Mar.

| Forecasts                    | Time (GMT/ET) | Previous   | Consensus | Capital Economics |
|------------------------------|---------------|------------|-----------|-------------------|
| Consumer Prices % m/m(% y/y) | 12.00/07.00   | +0.5(+5.8) | -         | +0.6(+5.3)        |

### *Inflation dipping, but temporarily*

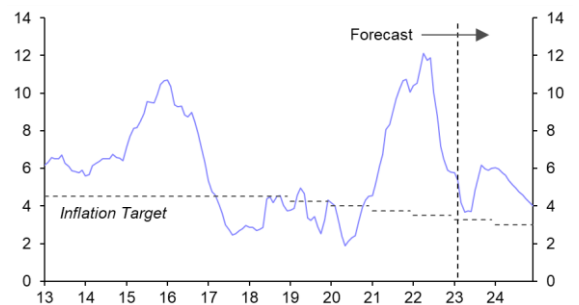
We think that data out next Friday will show that inflation in Brazil dropped to 5.3% y/y.

Having fallen sharply over the middle of last year, the disinflation process has faded in recent months, with inflation hovering a touch under 6%. We’re likely to see a renewed drop in the February data though. The mid-month inflation rate for February eased to 5.6% y/y and we think this continued over the second half of February. Most of the decline is likely to have been driven by food inflation, which should re-enter single digits, as well as a further easing of petrol price inflation.

The headline rate is likely to ease further in the next few months as favourable base effects start to take hold. But with core inflation pressures still running strong (see main article), we think the headline rate

will edge up again before the end of the year. (See Chart 2.) And this, taken together with ongoing fiscal risks, means that Copom will stick to the hawkish tone of its recent communications. Interest rate cuts are unlikely before Q4.

Chart 2: Brazil Consumer Prices (% y/y)



















Sources: Refinitiv, Capital Economics



## Economic Diary & Forecasts

### Upcoming Events and Data Releases

| Date   | Country   | Release/Indicator/Event                 | Time (GMT) | Time (EST) | Previous*     | Median* | CE Forecasts* |
|--|---|---|------------|------------|---------------|---------|---------------|
| 6 <sup>th</sup> Mar                              |    | <b>Ecu</b> CPI (Feb.)                   | 14.00      | 09.00      | +0.1%(+3.1%)  | -       | -0.1%(+2.8%)  |
| 7 <sup>th</sup> Mar                              |    | <b>Chl</b> Trade Balance (Feb.)         | 11.30      | 06.30      | \$2.6bn       | -       | -             |
|  |    | <b>Chl</b> Wage Growth (Jan.)           | 12.00      | 07.00      | (+10.8%)      | -       | -             |
| 8 <sup>th</sup> Mar                              |    | <b>C.Rc</b> CPI (Feb.)                  | -          | -          | +0.2%(+7.7%)  | -       | +0.2%(+6.7%)  |
|  |    | <b>Chl</b> CPI (Feb.)                   | 11.00      | 08.00      | +0.8%(+12.3%) | +0.1%   | +0.1%(+12.1%) |
|  |    | <b>Mex</b> CPI (Feb.)                   | 12.00      | 07.00      | +0.7%(+7.9%)  | -       | +0.6%(+7.7%)  |
| 9 <sup>th</sup> Mar                              |    | <b>Arg</b> Industrial Production (Jan.) | 19.00      | 14.00      | (-2.7%)       | -       | -             |
|  |    | <b>Per</b> Interest Rate Announcement   | 23.00      | 18.00      | 7.75%         | -       | 7.75%         |
| 10 <sup>th</sup> Mar                             |    | <b>Brz</b> IPCA Inflation (Feb.)        | 12.00      | 07.00      | +0.5%(+5.8%)  | -       | +0.6%(+5.3%)  |
|  |    | <b>Mex</b> Wage Growth (Feb.)           | -          | -          | (+10.9%)      | -       | -             |
| <b>Also expected during this period:</b>         |   |   |            |            |               |         |               |
| 8 <sup>th</sup> – 13 <sup>th</sup>               |    | <b>Dom</b> CPI (Feb.)                   | -          | -          | +0.6%(+7.3%)  | -       | -             |
| <b>Selected future data releases and events:</b> |   |   |            |            |               |         |               |
| 13 <sup>th</sup> Mar                             |    | <b>Mex</b> Industrial Production (Jan.) | 12.00      | 07.00      | +0.7%(+3.0%)  | -       | -             |
| 14 <sup>th</sup> Mar                             |   | <b>Arg</b> CPI (Feb.)                   | 19.00      | 14.00      | +6.0%(+98.8%) | -       | -             |
| 15 <sup>th</sup> Mar                             |  | <b>Per</b> Unemployment (Feb.)          | 15.00      | 10.00      | 8.0%          | -       | -             |
|  |  | <b>Col</b> Industrial Production (Jan.) | 15.00      | 10.00      | +0.7%(-1.8%)  | -       | -             |
|  |  | <b>C.Rc</b> Interest Rate Announcement  | -          | -          | 9.0%          | -       | -             |
| 17 <sup>th</sup> Mar                             |  | <b>Pan</b> CPI (Feb.)                   | -          | -          | +0.1%         | -       | -             |
|  |  | <b>Brz</b> Unemployment (Jan.)          | 12.00      | 07.00      | -             | -       | -             |
|  |  | <b>Col</b> Trade Balance (Jan.)         | 15.00      | 10.00      | -\$0.9bn      | -       | -             |
|  |  | <b>Col</b> Economic Activity (Jan.)     | 16.00      | 11.00      | (+1.3%)       | -       | -             |

\*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<br>(3 <sup>rd</sup> Mar.) | Last Change        | Next Change                | Forecasts    |              |
|----------------------------|----------------------------------|--------------------|----------------------------|--------------|--------------|
|                            |                                  |                    |                            | End<br>2023  | End<br>2024  |
| Brazil Selic Target        | 13.75                            | Up 50bp (Aug. '22) | <b>Down 50bp (Q4 '23)</b>  | <b>12.75</b> | <b>10.00</b> |
| Mexico Overnight Rate      | 11.00                            | Up 50bp (Feb. '22) | <b>Up 25bp (Mar. '23)</b>  | <b>10.25</b> | <b>8.25</b>  |
| Colombia Intervention Rate | 12.75                            | Up 75bp (Jan. '23) | <b>Up 50bp (Mar. '23)</b>  | <b>11.00</b> | <b>7.25</b>  |
| Chile Overnight Rate       | 11.25                            | Up 50bp (Oct. '22) | <b>Down 50bp (May '23)</b> | <b>7.25</b>  | <b>5.25</b>  |
| Peru Reference Rate        | 7.75                             | Up 25bp (Jan. '23) | <b>Down 25bp (Q3 '23)</b>  | <b>6.50</b>  | <b>5.00</b>  |

Sources: Refinitiv, Capital Economics

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

| Currency      | Latest<br>(3 <sup>rd</sup> Mar.) | Forecasts    |              | Stock<br>Market | Latest<br>(3 <sup>rd</sup> Mar.) | Forecasts      |                |
|---------------|----------------------------------|--------------|--------------|-----------------|----------------------------------|----------------|----------------|
|               |                                  | End 2023     | End 2024     |                 |                                  | End 2023       | End 2024       |
| Brazil BRL    | 5.21                             | <b>5.25</b>  | <b>5.00</b>  | Bovespa         | 104,049                          | <b>109,250</b> | <b>126,000</b> |
| Mexico MXN    | 18.0                             | <b>20.0</b>  | <b>19.0</b>  | Bolsa           | 54,001                           | <b>57,500</b>  | <b>62,100</b>  |
| Argentina ARS | 198                              | <b>300</b>   | <b>375</b>   | Merval          | 245,688                          | -              | -              |
| Colombia COP  | 4,779                            | <b>4,400</b> | <b>4,400</b> | IGBC            | 1,206                            | <b>1,380</b>   | <b>1,520</b>   |
| Chile CLP     | 807                              | <b>820</b>   | <b>780</b>   | IPSA            | 5,470                            | <b>5,950</b>   | <b>6,500</b>   |
| Peru PEN      | 3.78                             | <b>3.80</b>  | <b>3.70</b>  | S&P/BVL         | 22,086                           | <b>25,100</b>  | <b>27,400</b>  |

Sources: Refinitiv, Capital Economics

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

|                                  | Share of<br>World <sup>1</sup> | 2011-20<br>Ave. | GDP        |             |             |            | Consumer Prices |             |             |             |
|----------------------------------|--------------------------------|-----------------|------------|-------------|-------------|------------|-----------------|-------------|-------------|-------------|
|                                  |                                |                 | 2021       | 2022        | 2023        | 2024       | 2021            | 2022        | 2023        | 2024        |
| Brazil                           | 2.3                            | 0.3             | 5.0        | <b>2.9</b>  | <b>1.0</b>  | <b>1.5</b> | 8.3             | <b>9.3</b>  | <b>5.0</b>  | <b>5.3</b>  |
| Mexico                           | 1.8                            | 1.3             | 4.7        | <b>3.0</b>  | <b>1.0</b>  | <b>1.8</b> | 5.7             | <b>8.0</b>  | <b>5.5</b>  | <b>4.0</b>  |
| Argentina                        | 0.7                            | -0.7            | 10.4       | <b>5.5</b>  | <b>0.8</b>  | <b>1.0</b> | 48.4            | <b>72.5</b> | <b>93.0</b> | <b>83.5</b> |
| Colombia                         | 0.6                            | 2.5             | 11.0       | 7.5         | <b>0.8</b>  | <b>2.0</b> | 3.5             | <b>10.3</b> | <b>11.8</b> | <b>5.5</b>  |
| Chile                            | 0.4                            | 2.1             | 11.7       | <b>2.8</b>  | <b>-1.3</b> | <b>2.3</b> | 4.5             | <b>11.8</b> | <b>8.0</b>  | <b>4.8</b>  |
| Peru                             | 0.3                            | 2.4             | 13.6       | <b>2.5</b>  | <b>2.3</b>  | <b>2.3</b> | 4.0             | <b>8.0</b>  | <b>6.5</b>  | <b>3.8</b>  |
| Dom. Rep.                        | 0.2                            | 4.1             | 12.3       | <b>4.8</b>  | <b>4.0</b>  | <b>4.8</b> | 8.2             | <b>8.8</b>  | <b>4.8</b>  | <b>4.3</b>  |
| Ecuador                          | 0.1                            | 1.6             | 4.2        | <b>3.0</b>  | <b>2.3</b>  | <b>2.0</b> | 0.1             | <b>3.5</b>  | <b>1.8</b>  | <b>1.0</b>  |
| Venezuela                        | -                              | -12.7           | <b>5.0</b> | <b>10.0</b> | <b>7.5</b>  | <b>5.0</b> | 1,589           | <b>170</b>  | <b>110</b>  | <b>60</b>   |
| Panama                           | 0.1                            | 3.5             | 15.3       | <b>7.8</b>  | <b>2.5</b>  | <b>4.5</b> | 1.6             | <b>2.8</b>  | <b>0.3</b>  | <b>0.5</b>  |
| Costa Rica                       | 0.1                            | 2.8             | 7.8        | <b>4.5</b>  | <b>2.5</b>  | <b>2.3</b> | 1.7             | <b>8.3</b>  | <b>3.5</b>  | <b>3.3</b>  |
| Uruguay                          | 0.1                            | 1.5             | 4.4        | <b>4.8</b>  | <b>1.5</b>  | <b>2.0</b> | 7.7             | <b>9.0</b>  | <b>7.0</b>  | <b>8.0</b>  |
| <b>Latin America<sup>2</sup></b> | <b>6.7</b>                     | <b>1.0</b>      | <b>7.0</b> | <b>3.8</b>  | <b>1.0</b>  | <b>1.8</b> | <b>6.2</b>      | <b>8.8</b>  | <b>5.9</b>  | <b>4.6</b>  |

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



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