



LATIN AMERICA ECONOMICS WEEKLY

LatAm central banks kick off easing cycles with a bang

Brazil and Chile spring dovish surprise

The decisions in the past week by central banks in both Chile and Brazil to cut interest rates confirm that Latin America remains at the front of the pack in this global monetary cycle.

Having been among the first central banks in the world to raise interest rates in 2021 (and doing so aggressively), it was widely expected that Brazil and Chile's central bank would be among the first to *cut*. But the size of the cuts and the dovish tone of the communications came as a bit of a surprise.

Indeed, on Wednesday, Brazil's central bank **delivered** a 50bp cut (both we and the consensus expected a 25bp move), to 13.25%, while Chile's central bank opted for an even larger 100bp reduction to 10.25%. And in both cases, officials used the accompanying statements to flag that more front-loaded easing was likely in the coming months.

This has prompted us to revise our interest rate forecasts. We now expect larger rate cuts in both countries this year, with easing set to slow in 2024. In Brazil, we now forecast the Selic rate to end the year at 11.75% (vs. 12.50% previously) while policymakers in Chile are likely to lower interest rates to 7.50% (vs. 9.25% previously).

Peru will probably be next in the region to begin easing. Inflation figures out this week, which showed that the headline rate dropped to a 20-month low of 5.9% in July, have made us more comfortable that a September cut is on the cards.

Meanwhile, in Colombia, the minutes to Monday's central bank meeting, at which rates were left on hold at 13.25%, were relatively hawkish, with the central bank highlighting that its "fight against inflation" was not over. But in its *Monetary Policy Report* (released on Wednesday) it somewhat surprisingly slashed its forecasts for inflation and growth for this year. And one of the **lessons from the "early cutters"** in EMs is that central banks shift

quickly from sounding hawkish to flagging rate cuts. As a result, we continue to expect Colombia's central bank to start lowering rates in October.

Mexico's central bank, Banxico, is likely to be the last in the region to embark on a monetary easing cycle. In a speech this week, Deputy Governor Jonathan Heath sounded quite hawkish, once again highlighting the tightness of the labour market as well as "some difficulty" with core inflation. As a result, he sees the need to keep monetary policy restrictive and even said another hike couldn't be ruled out. This, alongside the economy's resilience, as evidenced by the **robust Q2 GDP** data, mean that Banxico is all but certain to keep rates on hold at 11.25% at next week's meeting. And with wage growth still stuck at above 11% y/y (see Chart 1) and the Fed – which Banxico tends to keep a close eye on – seemingly favouring a "higher for longer" scenario, we think that rate cuts in Mexico will only materialise around the turn of the year at the earliest.

Chart 1: Daily Wage of Insured Workers (% y/y)



Sources: Refinitiv, Capital Economics

The week ahead

July inflation figures from Brazil and Mexico are likely to show that inflation edged up in the former and declined in the latter while central banks in Peru and Mexico are set to keep rates on hold. Finally, we'll be discussing Argentina's primary election – a dress rehearsal for the presidential election – and the potential macro and financial market implications in a *Drop-in* next week. Register [here](#).



Data Previews

Wed. 9th August – Mexico Consumer Prices (Jul.)

Forecasts	Time (BST/ET)	Previous	Consensus	Capital Economics
m/m (% y/y)	13.00/08.00	0.1(5.0)	-	+0.5(+4.8)

Inflation continued to drop back in July

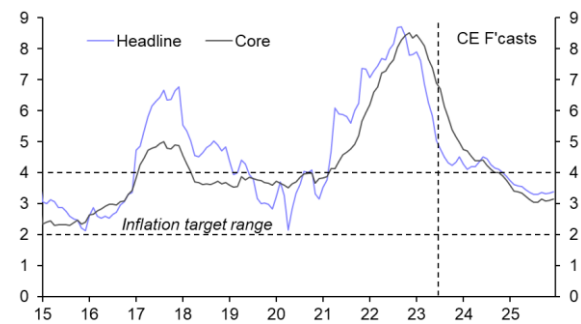
We expect data due to be released on Wednesday will show that Mexico’s headline inflation rate edged down to 4.8% y/y in July. But rate cuts by Banxico are still some way off.

Inflation dropped from 5.8% y/y in May to a 27-month low of 5.1% y/y in June. And the inflation data for the first half of July pointed to a further easing of price pressures, with the headline rate falling to 4.8% y/y. (See Chart 2.) That was driven by softer non-core inflation and, while core inflation ticked down, there was a concerning rise in services inflation. The latter has been a concern for officials at Banxico regarding the persistence of inflation. We expect inflation was unchanged from the mid-month figures over July as a whole.

The fall in inflation in July is unlikely to prompt Banxico to follow other central banks in the region

in cutting interest rates, at least in the very-near future. Indeed, with inflation unlikely to return to Banxico’s 2-4% tolerance band until late-2024, rate cuts are unlikely until the turn of the year and we think they will be more gradual than most expect.

Chart 2: Consumer Prices (% y/y)



Sources: Refinitiv, Capital Economics

Thu. 10th August – Mexico Interest Rate Announcement (Aug.)

Forecasts	Time (BST/ET)	Previous	Consensus	Capital Economics
Policy Rate (%)	20.00/15.00	11.25	11.25	11.25

Rates on hold, loosening still a little way off

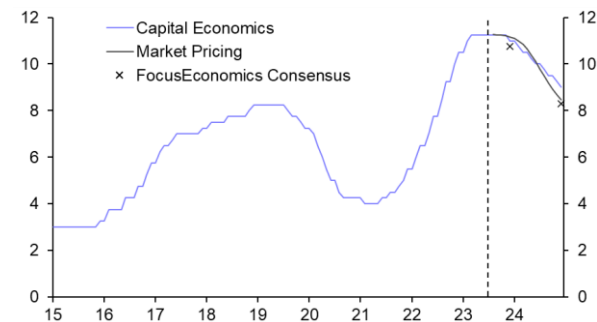
We expect Banxico to leave interest rates on hold at 11.25% next week.

Banxico has left policy unchanged at its last two meetings as inflation has subsided. And the further expected decline in July (see Preview above) means that it is likely to hold steady again on Thursday.

In contrast to other major central banks in Latin America, such as those in Chile and Brazil, policymakers at Banxico have continued to strike a hawkish tone (see main article). The renewed rise in services inflation observed in July’s mid-month inflation data, coming alongside continued rapid wage growth and robust economic activity, means that rate cuts are unlikely to be seriously discussed until later this year. And when they are delivered,

policy loosening will be a more gradual process than most currently anticipate. Indeed, our forecast for the policy rate to end next year at 9.00% is above market and consensus expectations. (See Chart 3.)

Chart 3: Mexico Policy Rate (%)



Sources: Refinitiv, Capital Economics



Thu. 10th August – Peru Interest Rate Announcement (Aug.)

Forecasts	Time (BST/ET)	Previous	Consensus	Capital Economics
Policy Rate (%)	00.00/19.00	7.75	-	7.75

Shifting towards rate cuts?

We think that Peru’s central bank will leave interest rates on hold at 7.75% when it meets next Thursday. That said, policymakers might use the meeting to flag that interest cuts may come soon.

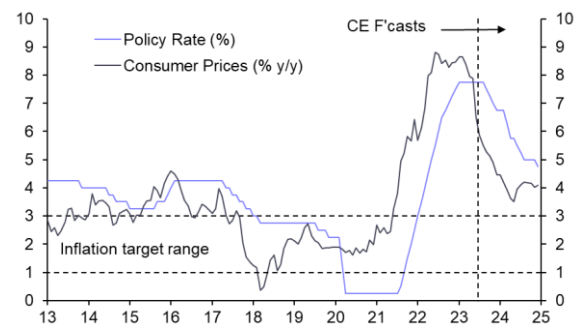
Peru’s central bank has left its policy rate unchanged for five consecutive meetings and the statement each time stated that this decision did not “necessarily imply an end to the BCRP’s monetary tightening cycle”. But there’s little in the latest data to prompt policymakers to consider hiking rates again. Indeed, recently-released inflation figures showed that inflation fell to a 20-month low of 5.9% in July. (See Chart 4.) And the latest activity data suggest that Peru’s economy is struggling.

While we think it’s still a bit too early for policymakers to lower rates at next week’s meeting, we think that they might signal that rate cuts might

be coming soon (for example by dropping the line on future rate hikes).

We think that, by September, policymakers will feel comfortable enough to start easing policy. Overall, we expect a 25bp cut at each of the upcoming meetings this year, taking the policy rate to 6.75% by December.

Chart 4: Peru Consumer Prices & Policy Rate



Sources: Refinitiv, BCRP, Capital Economics

Fri. 11th August – Brazil Consumer Prices (Jul.)

Forecasts	Time (BST/ET)	Previous	Consensus	Capital Economics
m/m (% y/y)	13.00/08.00	-0.1(+3.2)	+0.1	+0.1(+3.9)

Inflation jump won’t deter Copom

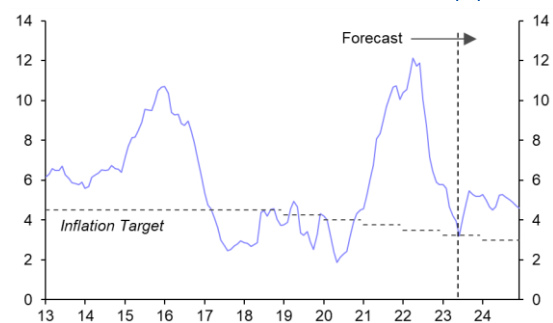
Brazil’s inflation jumped last month, probably to 3.9% y/y. But the central bank will be expecting this and it won’t stop it from delivering another 50bp interest rate cut at its next meeting in September.

The recent period of below-target inflation readings in Brazil is now at an end. That drop in inflation was driven by favourable base effects that pushed energy inflation down, but these are now beginning to unwind. As a result, the year-on-year rate of inflation will jump back up.

This won’t alter the central bank’s thinking. It’s expecting such a rise. Moreover, the underlying m/m rise in prices – which we think will be around 0.1% – is still soft. With the exception of last year, it would be the lowest July figure since 2014. Copom gave a clear steer at its meeting on Wednesday that another

50bp interest rate cut is on the cards. These data aren’t likely to change that path. Equally, with inflation unlikely to fall to or below target for the foreseeable future, the monetary stance will remain tight. (See Chart 5.)

Chart 5: Brazil Consumer Prices (% y/y)



Sources: Refinitiv, Capital Economics



Economic Diary & Forecasts

Upcoming Events and Data Releases

Date	Country	Release/Indicator/Event	Time (BST)	Time (EDT)	Previous*	Median*	CE Forecasts*
Fri 4 th	Ecu	CPI (Jul.)	15.00	10.00	+0.4%(+1.7%)	-	+0.0%(+1.6%)
Mon 7 th	Col	Trade Balance (Jul.)	13.30	08.30	+\$1.6bn	-	-
Tue 8 th	Brz	Central Bank Meeting Minutes	12.00	07.00	-	-	-
	Chl	CPI (Jul.)	13.00	08.00	-0.2%(+7.6%)	+0.3%(+6.4%)	+0.2%(+6.3%)
	C.Rc	CPI (Jul.)	-	-	-0.2%(-1.0%)	-	+0.6%(-1.5%)
Wed 9 th	Col	CPI (Jul.)	00.00	19.00	+0.3%(+12.1%)	+0.3%(+11.6%)	+0.5%(+11.7%)
	Brz	Retail Sales (Jun.)	13.00	08.00	-1.0%(-1.0%)	-	-
	Mex	CPI (Jul.)	13.00	08.00	+0.1%(+5.0%)	-	+0.5%(+4.8%)
	Arg	Industrial Production (Jun.)	20.00	15.00	(+1.1%)	-	-
Thu 10 th	Mex	Interest Rate Announcement	20.00	15.00	11.25%	11.25%	11.25%
Fri 11 th	Per	Interest Rate Announcement	00.00	19.00	7.75%	-	7.75%
	Brz	IPCA Inflation (Jul.)	13.00	08.00	-0.1%(+3.2%)	+0.1%	+0.1%(+3.9%)
	Mex	Industrial Production (Jun.)	13.00	08.00	+1.0%(+3.9%)	(+2.9%)	-
	Brz	Economic Activity Index (Jun.)	13.00	08.00	-2.0%(+2.2%)	-	-

Selected future data releases and events:

13 th Aug	Arg	Referendum	-	-	-	-	-
14 th Aug	Chl	Central Bank Meeting Minutes	13.30	08.30	-	-	-
	Col	Industrial Production (Jun.)	16.00	11.00	(-1.0%)	-	-
	Col	Retail Sales (Jun.)	16.00	11.00	(-5.1%)	-	-
	Pan	CPI (Jul.)	-	-	+0.1%	-	-
15 th Aug	Per	Unemployment Rate (Jul.)	16.00	11.00	6.60%	-	-
	Per	Economic Activity Index (Jun.)	16.00	11.00	(-1.4%)	-	-
	Col	Economic Activity Index (Jun.)	17.00	12.00	(+0.7%)	-	-
	Col	GDP (Q2, q/q(y/y))	17.00	12.00	+1.4%(+3.0%)	-	-
	Arg	CPI (Jul.)	17.00	12.00	+6.0%(+115.6%)	-	-
	Uru	Interest Rate Decision	-	-	10.75%	-	-
18 th Aug	Mex	Retail Sales (Jun.)	13.00	08.00	-0.5%(+2.6%)	-	-
	Chl	Current Account (Q2)	13.30	08.30	+\$0.8bn	-	-
	Chl	GDP (Q2)	13.30	08.30	+0.8%(-0.6%)	-	-

*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 (4 th Aug.)	Last Change	Next Change	Forecasts	
				End 2023	End 2024
Brazil Selic Target	13.25	Down 50bp (Aug. '23)	Down 50bp (Sep. '23)	11.75	9.50
Mexico Overnight Rate	11.25	Up 25bp (Mar. '23)	Down 25bp (Q4 '23)	11.00	9.00
Colombia Intervention Rate	13.25	Up 25bp (Apr. '23)	Down 50bp (Q4. '23)	12.25	7.25
Chile Overnight Rate	10.25	Down 100bp (Oct. '22)	Down 100bp (Sep. '23)	7.50	4.75
Peru Reference Rate	7.75	Up 25bp (Jan. '23)	Down 25bp (Sep. '23)	6.75	4.75

Sources: Refinitiv, Capital Economics

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

Currency	Latest (4 th Aug.)	Forecasts		Stock Market	Latest (4 th Aug.)	Forecasts	
		End 2023	End 2024			End 2023	End 2024
Brazil BRL	4.86	5.25	5.00	Bovespa	120,908	111,750	149,500
Mexico MXN	17.0	20.0	21.0	Bolsa	53,556	44,600	59,300
Argentina ARS	279	400	600	Merval	453,258	-	-
Colombia COP	4,064	4,500	4,200	IGBC	1,173	910	1,210
Chile CLP	846	825	775	IPSA	6,325	5,100	7,000
Peru PEN	3.68	4.00	3.70	S&P/BVL	23,674	19,300	25,650

Sources: Refinitiv, Capital Economics

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

	Share of World ¹	2011-20 Ave.	GDP				Consumer Prices			
			2022	2023	2024	2025	2022	2023	2024	2025
Brazil	2.3	0.3	2.9	2.3	0.8	1.5	9.3	4.8	5.0	4.0
Mexico	1.8	1.3	3.0	3.0	1.3	2.0	7.9	5.5	4.3	3.5
Argentina	0.7	-0.7	5.0	-2.8	-1.3	2.5	72.4	115.0	134.5	103.5
Colombia	0.6	2.5	7.3	1.0	1.5	2.5	10.2	11.5	5.5	3.8
Chile	0.4	2.1	2.4	0.3	2.5	2.8	11.6	7.5	3.8	3.5
Peru	0.3	2.5	2.7	1.5	2.3	2.5	7.9	6.5	4.0	3.3
Dom. Rep.	0.2	4.1	4.9	3.8	5.0	5.0	8.8	5.0	4.3	4.0
Ecuador	0.1	1.6	2.9	2.5	2.0	2.5	3.5	1.8	1.3	1.8
Venezuela	-	-12.7	15.5	6.5	5.0	5.0	185	320	65	50
Panama	0.1	3.5	10.5	1.8	2.8	3.0	2.8	1.5	1.3	1.3
Costa Rica	0.1	2.8	4.3	3.5	2.5	2.5	8.3	1.5	2.5	2.8
Uruguay	0.1	1.5	4.9	1.5	2.5	2.3	9.1	6.0	6.3	6.5
Latin America²	6.7	1.0	3.7	1.6	1.1	2.1	8.7	5.8	4.5	3.7

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



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