Scotiabank

GLOBAL ECONOMICS

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Latam Daily: BCCh Cuts, Mexico's Economy Slows

- **Chile: Central Bank cuts the policy rate by 25 bps, as widely expected**
- **Mexico: Economic activity slows in Q2 amid persistent uncertainty**

CHILE: CENTRAL BANK CUTS THE POLICY RATE BY 25 BPS, AS WIDELY EXPECTED

- **A further rate cut in September is far from assured. The BCCh would be highly dependent on local and external data in the near term**

On Tuesday, July 29th, the Central Bank cut the monetary policy rate by 25 bps, to 4.75%. This was a widely expected cut, but the statement is far from guaranteeing an additional cut at the September 9th meeting. We see the BCCh reflecting on the surprise of core inflation and high wage dynamics, coupled with the challenging external scenario, which leads us to condition a further September cut on the evolution of these factors. Even if we see inflationary pauses at the core inflation and/or wage levels, the external scenario could evolve, injecting an unexpected inflationary supply shock in the event of an abrupt global appreciation of the US dollar. Consequently, we estimate that for now the BCCh will remain dependent on local and international data, without complete conviction in implementing a further cut in September.

Trade conflicts are once again the main risk in the external environment. The Central Bank Board expresses concern about Trump's new tariff announcements, noting that the average tariff level is higher than estimated in the June IPoM. Additionally, they point to growing upward inflationary risks given the increase in the US CPI stemming from products exposed to tariff changes. Perhaps the only good news highlighted by the Board in the external scenario is the drop in oil prices observed following the end of the Middle East conflict.

At the domestic level, while downward surprises in headline inflation are acknowledged, it is noteworthy that at the core level (excluding volatiles), the inflation surprise was upward, as we noted at Scotiabank when the June CPI was released. This is undoubtedly a reason for concern on the part of the Board. The reference to "high wage growth" locally and the emerging upward risks to external inflation linked to tariffs reveal less conviction or less urgency to cut further at the September meeting. Regarding activity, no surprises are revealed in the June IPoM's scenario, which contemplates GDP growth of around 2.5% for 2025.

The minutes of last June's meeting indicated that a rate cut at that time would not have been implemented for tactical and communication reasons. The risk of a misinterpretation due to the eventual interpretation of a lag in monetary policy led the Central Bank Board to be very explicit, indicating that the baseline scenario contemplated a rate cut at this July meeting. In this context, the decision to cut the policy rate by 25 bps on July 29th was not a surprise to the market or to Scotiabank.

The path forward for monetary policy would continue to be determined by the validity of the baseline scenario from the June IPoM. Despite the recent depreciation of the CLP linked to external uncertainty over copper tariffs and the ongoing trade negotiations, coupled with the global appreciation of the US dollar, the Central Bank's scenario remains in place. Regarding many concerns about the exchange rate's weakness, recall that the baseline scenario contemplated a real depreciation of the currency, which has materialized in a limited but significant manner (the RER has depreciated 3% since last June). Consequently, this does not constitute a surprise for the Central Bank's baseline scenario, nor does it jeopardize inflationary convergence for now. Thus, we expect the BCCh to roll out 25 bps cut in the policy rate in September, with a limited probability and provided there are no inflationary surprises and/or substantial depreciations of the CLP in the coming weeks. Rising wages and resilient core inflation lead us not to assume a subsequent cut is guaranteed, but rather to condition it on the aforementioned factors in conjunction with the evolution of the external scenario.

—Aníbal Alarcón

MEXICO: ECONOMIC ACTIVITY SLOWS IN Q2 AMID PERSISTENT UNCERTAINTY

The flash estimate of GDP for the second quarter of the year showed a moderation in economic activity from 0.8% to 0.1% year-over-year, in line with consensus and marking its weakest pace since 2020. Among the components, services slowed from 1.3% to 0.7%, and primary activities declined to 4.1% from the previous 7.2%. Meanwhile, industrial activities deepened their contraction, from -0.7% to -1.5% for a third consecutive quarter of declines. As a result, economic activity in the first half of the year shows a 0.4% YTD annual growth.

The sectors most affected by uncertainty have been those related to investment, such as construction and wholesale trade, which we believe will remain weak in the coming months. On the other hand, activities related to domestic consumption, such as services, may exhibit signs of stagnation, in line with the lack of new jobs in formal employment and smaller increases in remittances.

Despite this flash estimate, we consider there is a chance of a slightly downward revision in the final 2Q numbers. Earlier this week, the IMF revised its estimates for the Mexican economy upward, from a contraction of -0.3% to a growth of 0.2% for this year, while maintaining its GDP growth forecast for 2026 unchanged at 1.4% as the US-Mexico trade relationship hasn't deteriorated as much as initially thought. However, the coming announcement from the US regarding the duties that their partners would face starting August will also be key for the Mexican outlook.

—Rodolfo Mitchell & Miguel Saldaña