LATAM Market Update

- **Peru construction appears healthy; but most else is less encouraging**
- **Colombia June retail sales reflected a strong domestic demand, but manufacturing and imports data were not as rosy**

PERU: CONSTRUCTION SEEMS HEALTHY BUT MOST ELSE, FROM JUNE GDP TO POLITICS, IS LESS ENCOURAGING

GDP growth figures for June are to be out today, August 15. In the past the government has published the figures either at midnight (in which case they will have come out at the time of this reading) or at 10am. Some figures have already been released early. The most significant surprise in June GDP data released so far was the 1.5% y/y decline in Agriculture, as the sector had been growing at a 3% pace in the year to May. In the past, similar production swings, when not linked to weather events, were frequently due to late harvesting of key crops, and were reversed in the following months. Once the details are available, we'll be able to assess whether something similar was at play this June. Mining GDP fell 3% y/y. We had been expecting a decline, due to mine depletion, but of a more modest magnitude. Gold output fell 11.0% (Buenaventura -35% on Orcopampa's bottleneck reduction program; Barrick -36% on depletion at Lagunas Norte); copper fell 3.8% (Cerro Verde -12%; Las Bambas -14%; Chinalco -13%, all three presumably on lower ore grades; in contrast: Southern Peru Copper +24%). Finally, non-resource manufacturing growth was a woeful -1.3%. This is of significant concern, given that it is linked so strongly to domestic demand. The silver lining was cement demand, an early indicator for construction, which rose 11.9% y/y and suggests increasing government investment. The early release figures are in line with consensus of 2.6% aggregate GDP growth.

Rosa Bartra, a leading member of the hardcore wing of Fuerza Popular (Keiko Fujimori's party), was elected to preside the Congressional Constitutional Committee. This is a key appointment on a crucial issue: the presidential request to hold early elections, which is likely to be discussed in the Constitutional Committee, although there is an outside chance that the issue will be taken directly to the floor. Bartra's leadership suggests that Fuerza Popular's position on this issue will be paramount. However, it is not clear what this position is at this time. In the past, members of Congress of most parties have shown their unease over a shortening of their terms in Congress, with members of Fuerza Popular foremost among them. However, the recent decision by the courts to maintain Keiko Fujimori's current pre-sentencing imprisonment (Fujimori is in prison for the legal period of 36 months, while her trial for money laundering is prepared), could lead Fuerza Popular to weigh the advantages to Keiko's legal situation if she is a presidential candidate in early elections.

Another issue which is emerging, albeit tentatively, is the possibility of a motion in Congress to "vacate" (impeach) President Vizcarra. This motion has not been introduced, but it has become part of a political discussion among members of Congress. The basis for the motion would be the "damage" that President Vizcarra would presumably be doing to governing institutions and the rule of law on two

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fronts: 1. by negotiating with protest leaders a suspension of the Tía María construction permit, 2. by calling for early elections. Meanwhile, groups have begun protests against the Quellaveco copper project. Our concern is that the Quellaveco protests are a sign of how much the government´s decision to backtrack on Tía María following protests has emboldened leaders in other regions who see opposition to mining projects as an easy way to gain political advantage. If so, there is a clear risk that social conflicts will continue to emerge.

COLOMBIA: JUNE RETAIL SALES REFLECTED A STRONG DOMESTIC DEMAND. MANUFACTURING AND IMPORTS DATA WERE NOT AS ROSY.

DANE released June-2019 manufacturing and retail sales (RS) data. RS came in at 7.2% y/y, above market expectation (5.5%). Manufacturing stood at -1.1% y/y, affected partially by one less business day. However, once the series is cleaned of calendar effects, results are still negative. In our opinion, **June's coincident indicators were mixed, but still in line with the scenario of a domestic demand recovery included in our expectations**. (See charts on page 3).

Key to the retail sales expansion was foodstuff sales that grew 11.0% y/y and added 2.5 pp to annual headline growth. Vehicle sales added 1 pp to total RS expansion. Worth noting, just three out of sixteen sub-sectors had negative annual growth in June and subtracted 0.1 pps of overall expansion. **Retail sales data suggest that 2Q-2019 private consumption could post a better figure than in the 1Q-2019**, which is aligned with our view of gradual economic activity recovery.

On the manufacturing side, in the 2Q-2019 manufacturing grew 0.2% compared to the same period of 2018, below our expectations for tomorrow's GDP data (0.7%). **It is worth saying that in June we saw a negative signal** that should be monitored, because just **18% of total activities posted positive results**, the weakest since mid-2016.

All in, June coincident indicators posted mixed results. On the one hand, domestic demand is stronger than expected, but on the other hand, manufacturing posted a weak result even when we remove the calendar effects. We think that expansionary monetary policy rate (MPR) and core inflation under control contribute to the recovery in economic activity. In terms of monetary policy, we do not expect that today's results will affect the base case scenario for BanRep. Therefore we continue thinking that the Board will keep the MPR at 4.25% for the rest of 2019, waiting for more data to confirm that the output gap is closing up.

Tomorrow DANE will publish results on GDP growth for 2Q19. We expect 2Q19 GDP to grow 3.27% y/y, above market consensus (2.9% y/y). Our higher number lies in a better-than-expected investment recovery (especially civil works) and a small recovery in government consumption.

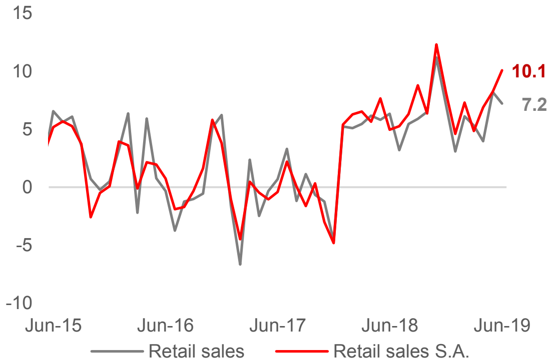
Imports fell 5.7% in June, external deficit keeps widening

June imports came in at -5.7% y/y or US$4.0 bn, the first contraction since March-2018. Capital imports grew 1.2% y/y, especially in transportation sector (+20.9% y/y), while agricultural and industrial sectors imports contracted. Consumption imports fell 6.4% y/y due to durable goods imports (-9.8% y/y). External deficit continued to widen, and June´s trade deficit was US$760.9 mn. YTD, the deficit increased by US$1.6 bn to US$4.4 bn. (See charts on page 3).

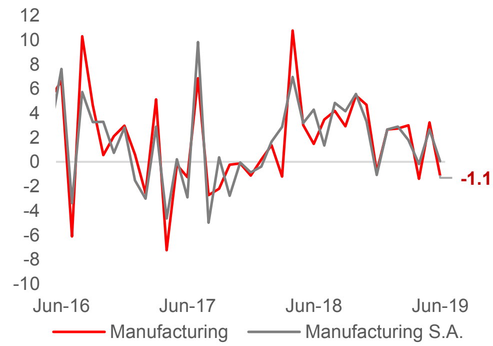
Although capital goods imports for agricultural and industrial sectors contracted in June, overall YTD capital imports growth is still positive on the back of the transportation sector. The black sheep continues to be the agricultural sector; agricultural capital goods imports continue to have a negative trend for the year, which is also reflected in other indicators, such as the contraction in the sector´s employment creation. Regarding consumption imports, both durable and non-durable goods imports were negative, but YTD results are still in line with our expectation of a gradual recovery in domestic demand.

Colombian external imbalance continues to be one of the more significant concerns for the Colombian economy in the short run, although so far it still enjoys healthy financing coming from FDI.

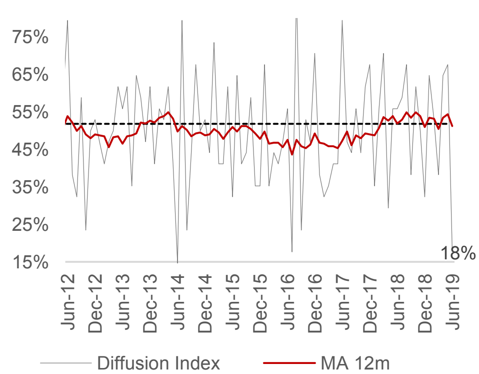
Retail Sales
(Y/Y, %)
Source: DANE, Scotiabank



Manufacturing
(y/y, %)
Source: DANE, Scotiabank)



Diffusion Index- Manufacturing
% of sectors with positive m/m variation SA
Source: DANE, Scotiabank Economics



Imports
(USD mn, y/y, %)
Source: DANE, Scotiabank