LATAM Market Update

- **Chile: Central Bank intensifies liquidity provision in pesos and USD—Lawmakers agree a roadmap for new Constitution**
- **Colombia continued to outpace peers, Q3-2019 GDP growth met expectations (3.3% y/y); In September, manufacturing posted sluggish expansion; retail sales remained strong, while external deficit kept widening**
- **Mexico: Banxico cuts benchmark rate by 25 basis points to 7.50%**

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CHILE: CENTRAL BANK INTENSIFIES LIQUIDITY PROVISION IN PESOS AND USD—LAWMAKERS AGREE A ROADMAP FOR NEW CONSTITUTION

1. Given the recent social events and the usual lower liquidity observed in the last part of the year, the interest rates of short-term instruments in USD and CLP had increased in recent days, reducing the effectiveness of the monetary policy.

In this context, the Central Bank announced yesterday new measures to provide liquidity in the local financial market. In addition to the swap credit line previously announced to relieve the pressure in FX forward curve (30 and 90 days, of up US$4,000 million), the authority increases the frequency of operations and expands the type of instruments eligible as collateral, including deposits, bank bonds and liquidity facilities (the new statement of the Central Bank is at the following link).

At the market opening today, the peso is trading near $20 below yesterday's closing. In addition to these measures, what we consider the main driver of the appreciation of the peso observed today would be the agreement signed in the early hours by all political sectors, where they commit and define a road map to build a new Constitution (details below). Along with this, short-term rates in pesos and dollars show significant declines.

2. Chile took a big step toward solving the social crisis that has riven the nation for the past month when lawmakers from almost all the parties agreed early on Friday to a mechanism to rewrite the constitution (link to the agreement).

Chile will hold a referendum in April 2020 to decide first if voters want a new constitution, and if the answer is positive, which body draws up the constitution. One option will be a newly elected Constituent Convention, the other a mix of equal participation between the Congress and a Convention.

Members of this new constituent body will be elected in October next year and then have nine months to complete their work. Once written, the new constitution will be put back to Chileans in a ratifying referendum.

The constituent body that is elected by the citizenry will have the sole purpose of drafting the new Constitution, not affecting the functions of the other organs of the State and will be dissolved once the task entrusted to it has been completed. Additionally, it may not alter the quorum or procedures for its operation.

COLOMBIA CONTINUED TO OUTPACE PEERS, Q3-2019 GDP GROWTH MET EXPECTATIONS (3.3% Y/Y); IN SEPTEMBER, MANUFACTURING POSTED SLUGGISH EXPANSION; RETAIL SALES REMAINED STRONG, WHILE EXTERNAL DEFICIT KEPT WIDENING

- **September retail sales eased a bit and expanded at a 6.9% y/y pace (below market expectation of 7.5% y/y). Even so, Q3 balance continues to be positive for domestic demand.**
- **Manufacturing data showed a timid increased in September (+0.3% y/y), 22 out of 39 manufacturing activities expanded.**
- **Imports increased by 3.8% in September, consumption goods and raw material imports led the expansion, capital goods imports contracted interrupting 16 months of growth in a row.**

Retail sales and manufacturing:

DANE released September-2019 manufacturing and retail sales (RS) data. RS came in at 6.9% y/y below market expectation (7.5%). Manufacturing stood at 0.3% y/y, well below market expectation of 2.5% y/y. Although the manufacturing expansion was a little bit higher than August's result, once the series is cleaned by calendar effects, September's manufacturing activity deteriorated.

The expansion in retail sales reflected a positive balance in almost all items in the survey, 15 out of 16 items increased their real sales. Monthly result was especially strong on the back of Telecom-related sector sales that grew 22.9% y/y and added 1.6 pp to annual headline expansion. Foodstuff sectors expanded 5.9% y/y and added 1.4pp to total RS y/y growth. Vehicles sales added 0.9 pp to the total RS expansion. Worth noting, that books subcategory, again, had a negative annual expansion out of the sixteen sub-sectors. Retail sales data confirmed that Q3-2019 private consumption continue to outpace significantly GDP expansion.

On the manufacturing side, y/y variation came in below market expectations again (0.3% y/y vs +2.5% y/y expected). Although manufacturing expanded at a low rate, Q3 balance is better than in the previous quarter. YTD manufacturing expanded 1.5%, keeping a very gradual recovery path.

It is worth saying that in September, twenty-two subsectors, out of thirty-nine, showed y/y positive variation.

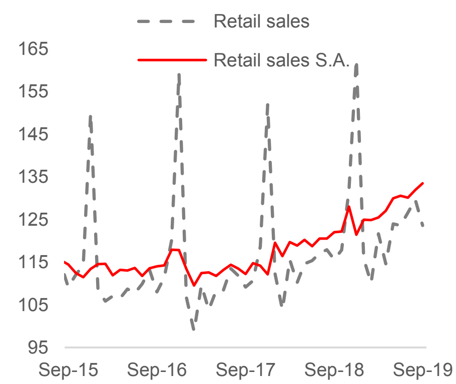
All in all, September's coincident indicators posted somewhat positive results, which is aligned with our economic activity growth forecast for all of 2019 (3.2% y/y). Domestic demand is strong, and manufacturing is in a modest recovery path.

Imports and trade balance:

September's imports growth came in at +3.8% y/y or US$4.2bn. Imports growth eased on the back of a contraction on capital goods imports (-1.61% y/y), result that was offset by the positive increase in consumption good imports (+7.47% y/y) and raw materials imports (+5.27% y/y).

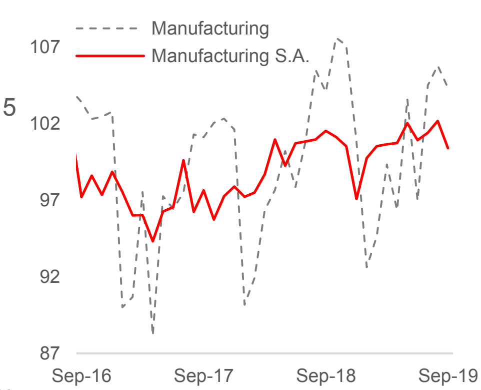
Capital imports contracted 1.61% y/y, although construction sector imports grew at a healthy pace (+14.51% y/y) in line with good numbers in civil works, the result was offset by contraction on imports of agricultural sector (-23.8% y/y), industrial sector (-2.62% y/y) and transport sector (-5.12% y/y). Consumption imports increased 7.5% y/y due to non-durable goods imports (14.8% y/y) and in line with strong private consumption. External deficit continued to widen. In fact, September's trade deficit was US$916 million. YTD, the deficit has increased by US$3.5 bn to US$7.8 bn.

Colombia: Retail Sales
(Index, 2013=100)



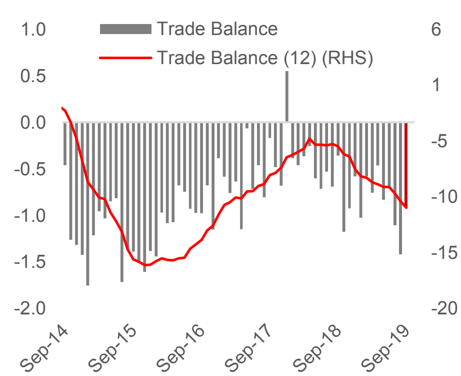
Sources: DANE, Scotiabank.

Colombia: Manufacturing
(Index, 2014=100)



Sources: DANE, Scotiabank.

Colombia: Trade Balance
(USD millions)



Sources: DANE, Scotiabank Economics.

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. Regarding import dynamics, the increase in non-durable goods imports and contraction in capital goods imports are things to keep an eye on.

Q3-2019 GDP growth met expectations and expanded at 3.3% y/y; Domestic demand remained strong; YTD GDP grew 3.1%:

DANE released 19Q3 GDP growth. It came in at 3.3% y/y, in line with Bloomberg consensus and below our expected 3.7% y/y. DANE also revised Q1 2019 GDP growth up to 3.2% from 2.1%. All in all, YTD GDP growth posted the strongest figure since 2015 (3.1% y/y), which confirms that economic activity is in a recovery path and consolidated as the best-behaved economy in the region. Seasonally-adjusted data showed that real GDP advanced 0.6% q/q, SA in Q3, slowing from the 1.3% of the Q2-2019 (revised upward from 0.8%). We continue to think that economic recovery will consolidate in Q4-2019. Therefore we stick with 3.2%, and a monetary policy rate of 4.25% for the rest of 2019.

From the sectors perspective, services were the strongest in Q3-2019 growing well above headline expansion. Commerce, restaurant & hotels posted a 5.6% y/y growth, the most robust pace since 2013 and adding 1pp to total GDP growth; public services (defense and social security) added 0.6pp in line with the usual increase in the expenditures of regional governments in the last year of their periods and financial services grew 8.2% y/y adding 0.4pp.

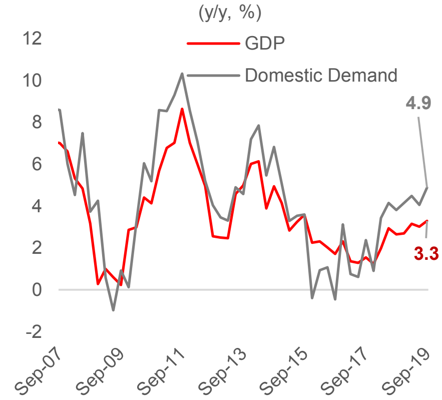
Worth noting that two sectors contracted: communication activities (-0.6% y/y) and Construction (-2.6% y/y), the last one due to a contraction on building sector (-11.1% y/y) that offset the expansion in civil works (+13% y/y); building sector result was affected by statistical base effects, the sector has a better balance in seasonally adjusted basis (+5.7% q/q). Manufacturing segment advanced a subdued 1.5% y/y, while mining grew a mild 1.0%y/y explained by a 1.3% y/y decline in coal output that partially offset positive results in other mining products.

On the demand side, domestic demand grew at a faster pace in five years (+4.9% y/y) led by private consumption (+4.9% y/y) and business investment (+5.5% y/y). Business investment dynamic was compatible with the expansion of civil works activities, and also reflected positive dynamics in machinery and equipment investments (+10.3% y/y).

Net exports contributed negatively due to imports growth of 10% y/y and a mild export expansion (+1.9% y/y). Net exports deficit stood at COP 19 tn in Q3-2019 (real terms), the worst balance in recent history. The weakening on mining exports, especially coal, and the muted reaction of non-traditional exports contributed to a widening deficit in volumes. External balance subtracted 1.9 pp from total Q3-2019 GDP expansion, which continues to point to a high current account deficit this year. We forecast a current account deficit of 4.2% of GDP this year. Yesterday's results continue to show that the recovery in domestic demand has its counterpart in a further deterioration of external deficit.

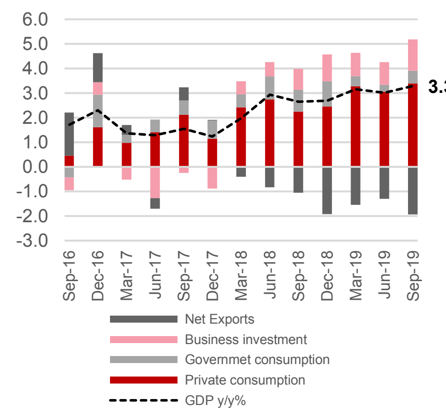
Bottom line, GDP figures showed that economic activity acceleration continued. It is noteworthy that the recovery was explained by a better performance of domestic demand led by the private sector. However, economic recovery will also imply a higher external deficit. The scenario of positive economic growth, a temporary pickup in inflation, and a wider external deficit reinforce our expectation of monetary policy rate stability for the rest of 2019, and a hike of 25 bps in 1H-2020.

Colombia: GDP vs Domestic Demand
(y/y, %)



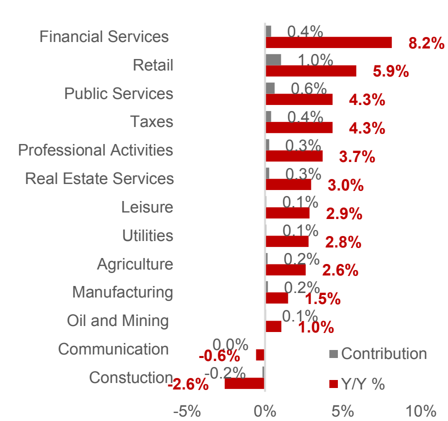
Sources: DANE, Scotiabank.

Colombia: GDP (y/y) Contributions by Expenditures



Sources: DANE, Scotiabank.

Colombia: GDP by Sector (y/y) and Contribution



Sources: DANE, Scotiabank.

—Sergio Olarte & Jackeline Piraján

MEXICO: BANXICO CUTS BENCHMARK RATE BY 25 BASIS POINTS TO 7.50%

In its seventh monetary policy meeting of the year, Banco de México's Board of Governors decided to lower the overnight interbank rate by 25 basis points (bps), to 7.50%, in line with market expectations. Once again, the decision wasn't unanimous since two members of the Board voted to cut the rate by 50 bps, to 7.25%.

According to Banxico's press release, the stagnation that economic activity has been showing for several months continues, suggesting that slack conditions have widened more than anticipated. Additionally, the institution mentions that certain downward risks to non-core inflation have materialized in the last months. Thus, it is likely that the foreseen trajectory of GDP growth and inflation will miss Banxico´s Second Quarterly Report estimates, probably leading to a downward revision in the Central Bank´s forecasts of both GDP growth and inflation in its next Quarterly Report, published on November 27. The Central Bank stressed that it will "maintain a prudent monetary policy stance" and keep a close eye on the potential exchange rate pass-through to prices; the relative monetary position between Mexico and the United States; the behavior of economic slack conditions; and on cost-related pressures in the economy.

The minutes from yesterday's monetary policy decision will be released on November 28th and the next decision is scheduled for December 19th.

—Alejandro Stewens