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Latam Daily: Peru and Colombia Data; Colombia's MTFF Points to Higher Deficits

- **Colombia: Medium term fiscal framework: A weaker economic outlook points to a higher deficit in 2023 and 2024**

Asia markets traded with a slight risk-off drift in the aftermath of the Fed's hawkish hold yesterday, with European trading deepening the risk-averse feel in rates and equity markets. China's central bank lowered its medium-term lending facility rate by 10bps, but this was widely expected and was not a significant risk tailwind overnight. SPX futures are down 0.4%, US yields are 4/5bps higher in the 2–10s space, crude oil is up 1%, outperforming iron ore's 0.7% gain and copper's 0.3% decline. The USD is broadly stronger, with the MXN among the worst performers, down 0.3% (but it's only a scratch at these levels).

We have a decent collection of data today in Latam and the US to keep markets busy, further to the reaction to the ECB's policy decision at 8.15ET (25bps hike expected).

In Peru, an acceleration in GDP is expected in April data out at 11ET, but the expansion may now prove disappointing versus what our economists had expected until recent comments from Fin Min Contreras. As our team wrote in Friday's Latam Weekly: "Our high hopes for a more normal figure, with growth rate between 1.3% to 2.0% y/y, have been shot down by comments made by Finance Minister Carlos Contreras that GDP growth would likely be around 0.7% y/y in April." The median submission to Bloomberg looks well off the mark in relation to those comments, expecting a 1.7% y.y gain. May unemployment rate data out at the same time is expected to show a decline to 6.8% from 7.1% according to our economists (vs 7% median).

Colombia's DANE will release industrial/manufacturing production and retail sales data at 11ET that are expected to show continuing economic weakness. However, the market will likely focus on yesterday's Medium Term Fiscal Framework presentation (see below) for moves in local markets. BanRep also publishes today the results to its economists survey.

In Brazil, April services activity figures out at 8ET came in weaker than expected, but with a nice positive revision to March, though signs of economic weakness would firm up pricing for an August rate cut (currently between 25 and 30bps). It will be political and fiscal developments that may be more interesting to follow. Yesterday, S&P revised the country's outlook to positive from stable (leaving it at BB-, i.e. not IG) owing to the country's new fiscal framework plans that ultimately have not been as loose as feared—while we wait for the final policy to take shape. Tax news (state sales tax reform and payroll tax cuts extension) are also worth watching.

Finally, Banxico's report on regional economies out at 14ET could shed some light on the varying performance of the various regions and how each has possibly benefited, or not, from near/friendshoring.

—Juan Manuel Herrera

COLOMBIA: MEDIUM TERM FISCAL FRAMEWORK: A WEAKER ECONOMIC OUTLOOK POINTS TO A HIGHER DEFICIT IN 2023 AND 2024

On Wednesday, June 14th, the Ministry of Finance (MoF) released the Medium-Term Fiscal Framework (MTFF), Colombia's most relevant fiscal-policy publication. It provides the clearest insights into the government's thinking about the country's economy in the long run and current fiscal results. In fact, it gives a general perspective on the most important factors influencing the main fiscal goals and their sustainability over a ten-year framework.

The MTFF-2023 revealed a more cautious approach from an economic perspective, which will increase the fiscal deficit in 2023 and 2024. The Min Fin expects weaker fiscal income than the projection in the financing plan released in December 2022 (table 1).

Table 1: Colombia—Fiscal Deficit Comparison (2023 vs 2024)

	2023				2024	
	Financing Plan (Dec-22)		MTFF (Jun-23)		Financing Plan (Dec-22)	MTFF (Jun-23)
	COP tn	% of GDP	COP tn	% of GDP	COP tn	% of GDP
Total income	319.6	20.6	309.1	19.3	347.6	20.5
Total expenditure	379.2	24.4	378.7	23.6	424.4	25.0
Interest	68.4	4.4	69.6	4.3	76.9	4.5
Primary expenditure	311	20	309	19	347	21
Primary expenditure without FEPC*	285	18	283	18	330	19
FEPC*	25.8	1.7	26.3	1.6	17.8	1.0
Primary balance	8.8	0.6	0.7	0.0	0.2	0.0
Total balance	-59.6	-3.8	-69.5	-4.3	-76.7	-4.5
Total balance allowed by tax reform	-	-	-69.8	-4.3	-76.7	-4.5
Surplus (+) / adjustment (-)	-	-	0.2	0.0	0.0	0.0

Sources: Scotiabank Economics, MTFF 2023. *FEPC: fuel prices stabilization fund.

This weaker economic context involves a lower tax collection from trade activity (lower imports) and more moderate oil prices. The fiscal deficit for 2023 is now estimated at 4.3% of GDP, increasing from the initial estimate of 3.8% of GDP, which means that Colombia will no longer achieve a primary surplus of 0.6% and instead will be neutral in that regard posting a 0% of the primary balance.

The previous change in the fiscal deficit target for 2023 has been anticipated since the discussion of budget addition; that said, the big surprise came from the fiscal deficit estimation for 2024, which now points to a deficit of 4.5% of GDP, increasing versus 2023 and increasing versus the most recent guidance in the MTFF-2022 of 2% of GDP (chart 1).

Deterioration in deficit perspectives is motivated from a weaker economic perspective since economic growth is expected to decelerate from 1.8% in 2023 to 1.5% in 2024 and higher fiscal spending, which is expected to represent 25% of GDP (chart 2) vs. the estimation in the MTFF-2022 of 21.5% of GDP.

All in all, debt to GDP is expected to close at 55.8% of GDP in 2023, closer to the longer anchor of the fiscal rule. However, in 2024, debt will jump to 57.1% of GDP (chart 3).

The previous dynamic means more financing needs in 2023 and 2024. COLTES issuances in 2023 are expected to increase by around COP 7 tn due to the pre-financing of the 2024 obligation, while the excess deficit of 2023 will be financed using foreign sources. Ahead of 2024, issuances in the COLTES market are projected to increase to COP 37 tn (+COP 10 tn higher than in 2023, ~2% of GDP).

Chart 1

Colombia: Fiscal Deficit—Central Government

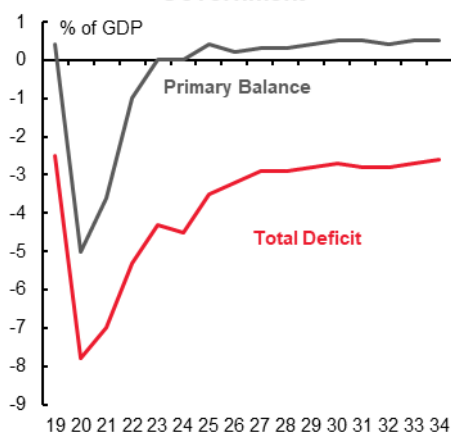


Chart 2

Colombia: Fiscal Income and Expenditures

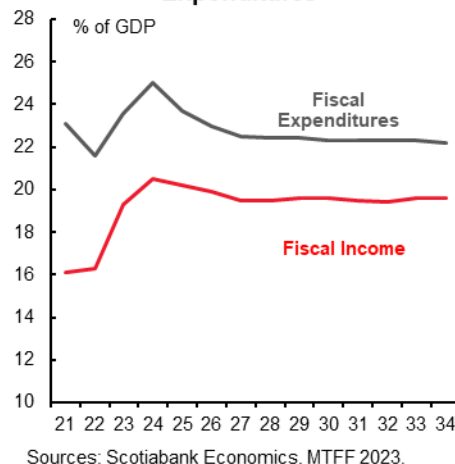
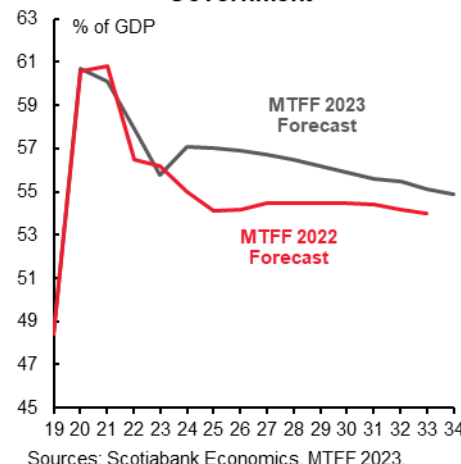


Chart 3

Colombia: Gross Debt—Central Government



Fiscal perspectives point to an interruption in the convergence process to the long-term level of debt to GDP ratio of 55%. Despite having achieved the approval of an ambitious fiscal reform, expected spending is increasing at a higher pace. Previous development is a headwind to achieving a better credit rating in the medium term, which probably will maintain a higher risk premium in COLTES. We think markets can absorb new issuances. However, fiscal perspectives could result in a curve with higher slope since issuances are more concentrated in the long-end tenors.

Either way, in forthcoming months, the peak in inflation and the potential pause in BanRep's hiking cycle could contribute to maintaining value in the COLTES market. As mentioned before, the fiscal picture probably will affect the slope of the curve but not significantly the level.

On the positive side, we see macro projections in the MTFF-2023 are more conservative, which probably would prevent sudden changes in fiscal plans in forthcoming publications. Questions that are still in the air is the related to the fiscal cost of social reforms. On the other side, a thing to pay attention to is the budget execution. In 2023, COP 30 tn (~2.8% of GDP) wasn't executed, while in the YTD of 2023, budget execution, excluding interest payments, is at its lowest level since 2001 (~21% of execution).

Minister Bonilla highlighted that MTFF-2023 is complying with the fiscal rule mandate. However, it is important to wait for the Autonomous Fiscal Rule Committee statement to see their opinion about the previous plan.

Further details about today's publication.

Macro assumptions:

- Economic growth was revised to the downside in 2024. In 2023 the composition of the GDP points to a lower trade balance, which plays against the tax income from imports (table 2).

Table 2: Colombia—Key Macroeconomic Assumptions

Variable	2022	2023		2024	
		Financing Plan	MTFF	Financing Plan	MTFF
Real GDP (%)	7.3	1.3	1.8	2.8	1.5
Nominal GDP (%)	22.6	7.9	9.8	6.8	5.6
Brent (USD per barrel)	99.1	94.2	78.6	84.5	74.5
Oil production (KBPD)	754	743	769	762	788
Exchange rate (USDCOP, avg)	4255	4758	4640	4611	4603
Current account deficit (%)	-6.2	-3.7	-4.0	-4.1	-3.5
Inflation eop (%)	13.1	7.2	9.2	5.1	5.7

Sources: Scotiabank Economics, MTFF 2023.

- Oil prices projection is more conservative. However, oil production is expected to increase.

Fiscal deficit :

- The fiscal deficit target increased on the Government's horizon. A more modest perspective of economic growth and a path of high spending is leading those forecasts to the upside.
- Debt to GDP in 2023 is expected to decrease from 57.9% in 2022 to 55.8%, however, it will rebound in 2024 to 57.1 of GDP, still close to the anchor defined in the fiscal rule, but interrupting the reduction trajectory. Something which could maintain Colombia with low possibilities of gaining the investment grade in the medium term.

Oil stabilization fund:

- Minister Bonilla said that in six months, the increases in gasoline prices would be done; either way, diesel prices remain below the fair value, and the stabilization fund for oil prices will have a deficit of COP 17.8 tn (lower versus the 2022 deficit of COP 36.7 tn).

Financing Plan 2023:

- Comparison between projections from the Fiscal Plan 2023 (December 2022) and MTFF 2023 (today).

- The expected fiscal deficit in 2023 increased by COP 10 tn. Financing will come from higher external indebtedness (+ COP 3.2 tn / +USD 820 million vs. Financing Plan projection). Liability management operations (+ COP 1.9 tn), COP +1 tn from other sources, and around COP 4 tn from domestic sources, which will be related to the disbursements associated with the COLTES ETF (table 3).
- In 2023, COLTES auctions are expected to increase by COP 7 tn as a pre-financing operation for 2024. That said, issuances won't stop at COP 27 tn, instead will reach COP 34 tn, which is the usual number the market has managed with in the past, and it could lead to the end of auctions between October/November 2023.

Financing Plan for 2024:

- The MoF estimates fiscal income of around 20.5% of GDP, which is above the 19.3% of GDP in 2023 (table 4).
- On the other side, fiscal expenditures are expected to represent 25% of GDP, above the 2023 expectation of 23.6% of GDP.
- The primary balance is expected at 0.0% of GDP (chart 1 again), while the total deficit will increase to 4.5%, which is still in compliance with the fiscal rule, according to the Ministry calculations. However, our take is less constructive since the government is interrupting the convergence towards a lower debt level.

Table 3: Colombia—Uses and Sources 2024

		MTFF-2023 (Jun-23)
Sources (COP tn)		132.3
Disbursements		73.4
Foreign sources	(USD 6.0 bn)	27.4
Local sources		46.0
COLTES auctions		37.0
Green bonds		1.0
Treasury operations		7.1
Other sources		24.5
Initial availability		27.3
		MTFF-2023 (Jun-23)
Uses (COP tn)		132.3
Fiscal deficit		76.7
Local interests		56.5
External interests	(USD 4.1 bn)	20.3
Amortizations		45.7
External	(USD 5.4 bn)	26.5
Local		19.3
Payment of obligations with debt service		1.4
Final availability		8.5

Sources: Scotiabank Economics, Financing Plan 2023, MTFF 2023.

Table 4: Colombia—Uses and Sources 2023

	Financing Plan 2023 (Dec-2022)		MTFF-2023 (Jun-23)
Sources (COP tn)	109.4		122.7
Disbursements	60.5		70.7
Foreign sources	(USD 5.1 bn)	(USD 5.9 bn)	27.5
Local sources	36.2		43.2
COLTES auctions	27.0		27.0
Green bonds	1.0		1.0
Prefinancing 2024 using COLTES issuances			7.0
ETF and direct placements			8.5
Treasury operations	4.1		6.0
Other sources	23.7		24.7
Initial availability	21.2		21.3
		Financing Plan 2023 (Dec-2022)	MTFF-2023 (Jun-23)
Uses (COP tn)	109.4		122.7
Fiscal deficit	59.6		69.5
Local interests	51.3		52.2
External interests	(USD 3.3 bn)	(USD 3.6 bn)	17.4
Amortizations	27.2		25.1
External	(USD 2.2 bn)	(USD 2.4 bn)	11.4
Local	15.8		13.7
Payment of obligations with debt service	0.3		0.8
Final availability	22.3		27.3

Sources: Scotiabank Economics, Financing Plan 2023, MTFF 2023.

—Sergio Olarte, Jackeline Piraján & Santiago Moreno

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