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GLOBAL ECONOMICS

## LATAM DAILY

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# Latam Daily: BCB and Fed; BCRP Preview and Peru Rains

- **Peru: BCRP preview: fourth consecutive cut; it's raining! yay!**

Markets traded range-bound through most of the overnight session (and most of the post-Europe US session) on narrow global drivers while we wait for the Fed's policy decision at 14ET with only US PPI at 8.30ET ahead of it. A larger than expected decline in UK GDP shook up markets and prompted a slight bid to rates. Chinese credit/money supply data released overnight also disappointed but the reaction in markets has been minimal.

USTs and EGBs are bull flattening (US 10s are back to pre-CPI levels) while gilts bull steepen on the data. The USD is stronger again all majors where the NZD is the top loser on kiwi banks revising their views on inflation. Other high-beta FX are mixed in between the majors' rankings with the MXN off about 0.2% while the ZAR and NOK lag. European bourses are up about 0.3% in line with a 0.2% rise in US equity futures. Crude oil's slide kept going to sub-$68/bbl in WTI before coming back to unchanged at writing in Brent and WTI. Iron ore and copper are hurting 2.0% and 0.8%, respectively, on a disappointing wishy-washy outcome of the China's annual economic work conference yesterday.

Today's main event in Latam will be the BCB's decision at 16.30ET, where a 50bps cut is widely expected. Ahead of the decision, services volumes data for October are expected to show a slight month-on-month contraction for a third straight negative month that reinforces the half-point pace of cuts by the BCB. November inflation data published yesterday came in very marginally below expectations. Markets believe the central bank will cut by 50bps at each of today's and the next two meetings with a roughly 60% chance that they do so at another meeting. The risk in today's decision is that the BCB changes its wording on the 50bps pace being appropriate "in the next meetings".

**—Juan Manuel Herrera**

### BCRP PREVIEW: FOURTH CONSECUTIVE CUT

We expect the BCRP to continue its interest rate cutting cycle in Thursday's decision. This would be the fourth consecutive cut of 25bps, taking the reference rate to 6.75%. The first December indicators for inflation suggest that it could drop from 3.6% in November to a range between 3.1% and 3.2%, below our current forecast of 3.6%. This new forecast is in line with what the authorities expected. Food prices have been reversing the supply shocks of previous months, to which is added a lower impact of El Niño, whose temperature metrics have seemingly faded during the latest readings. Likewise, the weakness of the economy would put pressure on a new decrease in core inflation, which would go from 3.1% to 2.9%, with which we see a probable return to the target range after 24 months.

Our forecast remains under a moderate/strong Niño scenario, the dominant probability until now, although we will evaluate a change of weak/moderate scenario if the reduction in the temperature anomalies that we have been observing until now is confirmed. We see a new revision to our forecast for 2024 as likely in coming weeks. The MoF estimated that inflation will reach 3.1% at year-end, approaching the BCRP's target range. The BCRP estimates that inflation will return to the target range as of April 2024. In a recent conference, Minister of Finance Alex Contreras considered that if inflation returns to the target range, it is likely that monetary policy will adopt a more expansionary stance. 12-month inflation expectations fell from 3.33% to 3.15% in the latest survey, so if the rate is cut by an additional 25bps this Thursday, the real interest rate would go from 3.7% to 3.6%, still well above the neutral level of 2%. Our 2024 forecast considers a cut of 200bps in the key rate to 4.75%.

**—Mario Guerrero**

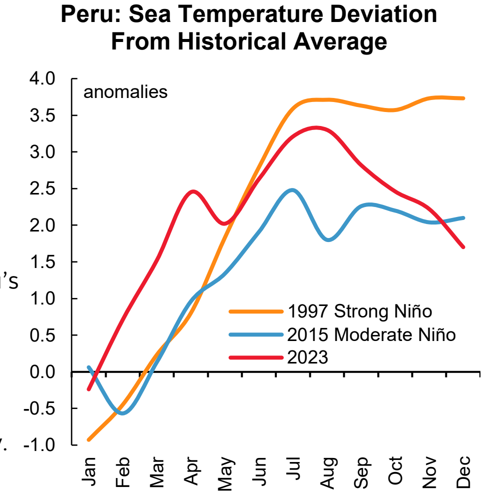
## PERU: IT'S RAINING! YAY!!!

One may wonder why we are happy that it's raining. Aren't rains a sign of the arrival of El Niño? It's all about location. El Niño brings with it torrential rains along the northern and central coast, but produces drought in the southern Andes. In fact, the type of drought that we had been experiencing since April this year. But the torrential rains so far this December have been taking place precisely in the heretofore drought-ridden southern Andes. And these rains are indicative of normal weather, not El Niño.

So, what happened to El Niño? Sea temperatures, as registered by NOAA (the U.S. National Oceanic and Atmospheric Administration) have fallen precipitously (if you can excuse the pun) since September, with the decline accelerating in early December. This is especially true for Peru's coastal sea where temperatures are now just inside the normal historical range for non-Niño years (typically defined as 1.5 degrees above or below the historical norm). This is the first time that this has happened since March (chart 1).

El Niño's temper tantrum during most of 2023 appears to be transitioning into a state of docility. Let's hope this lasts. The persistent decline in sea temperatures and the rains in the southern highlands, effectively interrupting the drought there, are two potent signs that it may.

**Chart 1**



Sources: Scotiabank Economics, NOAA.

**—Guillermo Arbe**