THE LATIN AMERICA ECONOMIC MONITOR

APRIL 3, 2020
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Brazil's industrial economy improved at the start of the year, but the momentum won't be sustained.

Mexico's PMIs fall sharply in March, underscoring the start of a severe hit to production.

Another downgrade; the pandemic hit to Colombia's public finances has led Fitch to cut its rating.

Markets are Stabilizing, but Incoming Data will Confirm a Deep Recession

LatAm financial and FX markets have behaved relatively well in recent sessions, thanks to the array of monetary and fiscal measures taken to counter the severe risk-off environment. Risks remain, but it seems that most LatAm markets have been pushed well below fair value. On the economic front, however, the strict containment measures to control the spread of the virus are having severe repercussions throughout the region and the economic outlook is turning more grim by the minute.

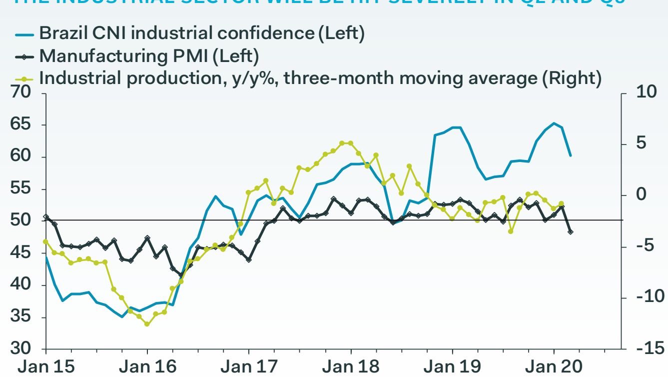
It is hard to obtain reliable statistics about the current situation of the virus outbreak in LatAm, due to lack of resources, limited testing and/or the ban on testing in private labs. It is difficult to tell if the virus and if the measures taken so far have been successful in flattening the curve. But the limited numbers available so far are frightening. Cases will continue to rise rapidly over the next few weeks, with the number of daily deaths jumping dramatically. But the epidemic likely will hit each country at a different pace, given the different responses imposed by individual governments.

Most Andean governments were ahead of the curve, and swiftly implemented measures to contain the epidemic, so we hope it will be less severe here than initially expected. But the governments of the biggest economies in the region, Brazil and Mexico, have been in complete denial of the situation and slow to act. Their presidents have been extremely concerned about the potential shock inflicted by the containment measures on the economy, and have downplayed the virus. The death toll, however, doesn't lie and it seems that these governments now are beginning to acknowledge the extent of the crisis. Most importantly, authorities at the local and state level have been extremely proactive, taking drastic measures to contain the virus, despite their presidents' reckless approach.

In any event, beyond the tragedy of the pandemic at a country level, the containment measures, and the appalling global conditions will hit LatAm severely this year. Most central banks have responded boldly, with aggressive monetary loosening, and some governments already have implemented large-scale fiscal stimulus. But more needs to be done to support the most vulnerable during the lockdown and to prevent a sharp economic contraction and social unrest.

Data in recent days have confirmed that most economies in the region were doing relatively well before Covid-19. In **Brazil**, for instance, industrial production rose 0.5% month-to-month in February, well above the consensus, -0.4%, and following an upwardly-revised 1.2% gain in January. On a year-over-year basis, production fell 0.4%, better than the 0.9% decline in January, and also above the consensus. The numbers confirmed a decent start to the year, but conditions will deteriorate soon.

THE INDUSTRIAL SECTOR WILL BE HIT SEVERELY IN Q2 AND Q3



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February production rebounded in two of the four major categories, and in 15 of the 26 sectors. A 1.2% jump in production of capital goods was the main driver of the month-to-month increase in February, following wild offsetting swings in previous months. Output of intermediate goods rose 0.5% in February, the third monthly increase on the spin.

These numbers, however, are now ancient history. *Recent global events and the measures now taken to contain the virus will put manufacturing under pressure.* Covid-19 has hit global supply chains, and both domestic and external demand in Brazil are now falling rapidly. Manufacturing output will plunge as a result, and a severe drop over Q2 and Q3 is inevitable.

March's external trade numbers, released on Wednesday, meanwhile, also don't reflect the coronavirus shock. Exports of raw materials remained relatively resilient in late Q1, and imports of capital goods rebounded sharply in March. Looking ahead, though, we expect the external accounts to start showing the shock of Covid-19 on the global economy, putting exports under severe strain. Most importantly, imports likely will be hit by the sudden stop of domestic demand and the shock on the supply chains in recent weeks.

Elsewhere, **Mexico's** data on Wednesday showed that the IMEF manufacturing PMI slumped last month, to 45 from 48 in February, reaching its lowest level since early 2017. The new orders component was badly hit, followed by a sharp contraction of the output index. *Both indexes fell to their lowest levels ever.* The headline index didn't collapse further due to a rebound in "delivery times", which is normal just before a supply shock.

A SEVERE RECESSION IS UNDER WAY IN MEXICO

This is a very bad headline, but we were expecting the drop. More pain is ahead, as we are still at the early stages of the economic crisis. Supply chain shocks and subpar external demand were already hurting the manufacturing sector, even before Covid-19. The Mexican manufacturing sector is heavily dependent on supplies from the U.S., where the disease is spreading quickly; this will create severe disruption. Moreover, the pandemic will hit Mexican imports of the intermediate goods the country needs for its own production. *And exports will plummet as Mexico's main trading partners, the U.S. and Canada, are just starting to suffer with the crisis.*

Meanwhile, the IMEF non-manufacturing PMI for March has collapsed to a record low, to 39.5 from 48.6 in February, all but certifying that a bad recession is coming. The decline was most severe in the new orders and output components, even though the country has yet to implement lockdown measures similar those in Italy or Spain, apart from limited measures at the federal level. Our base case is that the services index will fall further as the government imposes stricter measures to contain the outbreak. These numbers suggest that the Mexican economy will collapse more than 5% this year. *AMLO's refusal to take bolder fiscal action will make things very difficult.* Local and state government bodies are acting decisively, but the lack of coordination with the central government will throw the economy into disarray.

Finally, Fitch on Wednesday cut **Colombia's** rating to BBB-, the lowest IG level, citing a loss of fiscal credibility, alongside plunging oil prices amid the expected economic downturn due to Covid-19. Colombia's solid macro fundamentals support the IG rating, but the government will have to work hard to improve the medium-term fiscal picture, which has deteriorated lately. Moody's is the next in line to cut the country's rating in the near term to the same levels as Fitch and S&P. Our base case is that the country will stay in the IG club. But all will depend on Covid-19 and how long oil prices remain at the current levels.

The *Latin America Economic Monitor* will not be published from Monday, April 6 through Monday, April 13. Publication will resume on Tuesday, April 14.

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THIS WEEK IN BRIEF

Note: "**D**" prefix denotes Datanotes for these releases.

Monday, March 30

• **Argentina Economic Activity Index (1)/16:00 Local**
The index fell **1.8%** year-over-year, down from a 0.3% fall in December. Argentina is set for the deep recession since the financial crisis as Covid-19 ravages the economy.

Tuesday, March 31

• **D: Brazil Unemployment Rate (2)/9:00 Local**
The unadjusted unemployment rate rose to **11.6%,** from 11.2% in January, but it fell from 12.4% in February 2019.

• **D: Chile Industrial Production (2)/9:00 Local**
Industrial output rose **5.6%** year-over-year, up from 1.8% in January. The sector will be under severe strain in Q2.

• **D: Chile Retail Sales (2)/9:00 Local**
Retail sales jumped **4.5%** year-over-year in February, up from 0.1% in January. A solid Q1, but a downtrend looms.

• **Chile Unemployment Rate (2)/9:00 Local**
The unadjusted unemployment rate rose to **7.8%** in February, from 7.4% in January. The rate in February 2019 was 6.7%. Covid-19 will hurt the labour market in Q2.

• **Colombia Urban Unemployment Rate (2)/10:00 Local**
The unadjusted jobless rate fell to **11.5%** in February, from 12.9% in January. The rate in February 2019 was 12.4%.

• **Chile Overnight Rate Target /18:00 Local**
The BCCh cut its interest rate by 50bp to **0.50%,** following its emergency meeting on March 16 when the Board cut the rate by 75bp. Risks are tilted sharply to the downside.

Wednesday, April 1

• **Peru CPI Inflation (3)/6:00 Local**
The index rose **0.7%** month-to-month in March. In year-over-year terms, inflation edged lower to **1.8%,** from 1.9% in February. We expect inflation to fall further in Q2.

• **Chile Economic Activity Index (2)/8:30 Local**
The IMACEC index rose 0.6% month-on-month in February. The unadjusted index rose **2.7%** year-over-year, up from 1.5% in January. A recession is looming.

• **D: Brazil Industrial Production (2)/9:00 Local**
Production rose 0.5% month-to-month in February, following an upwardly-revised 1.2% gain in January. The unadjusted year-over-year rate rose to **-0.4%**, from -0.9% in January. A good start to 2020, but a downtrend looms.

• **Brazil Trade Balance (3)/14:00 Local**
Brazil had a **USD4.7B** unadjusted trade surplus in March, above the USD4.3B recorded a year ago. We expect the trade balance to improve this year, due to the recession.

• **Mexico IMEF Manufacturing Index (3)/12:00 Local**
The index plunged to **45**, from 48 in February. The manufacturing sector will struggle in Q2 and early Q3.

Thursday, April 2

• **No significant data released.**

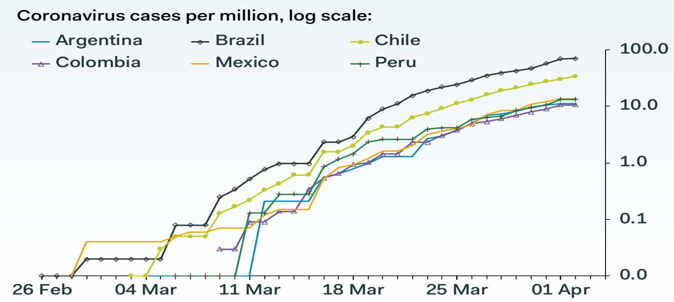
Friday, April 3

• **Mexico Consumer Confidence (2)/8:00 Local**
The seasonally adjusted index likely fell to **39**, from 43.9 in February. Uncertainty is high. **Consensus: 40.**

PANTHEON'S LATAM FINANCIAL CONDITIONS DASHBOARD

	Currency			Benchmark Stock index		
	Value	Week, %	YTD (%)	Value	Week, %	YTD (%)
Argentina	64.41	-1.0	-7.0	24,059	8.9	-42.3
Brazil	5.10	-0.7	-21.1	73,429	9.5	-36.5
Chile	834.9	3.4	-9.8	3,228	4.9	-30.9
Colombia	3,973	3.7	-17.3	1,148	27.5	-31.0
Mexico	23.34	4.6	-18.9	33,799	-1.4	-22.4
Peru	3.42	3.2	-3.1	13,893	-3.5	-32.3
Venezuela	--	--	--	88,643	-9.8	-1.8

CORONAVIRUS CASES PER MILLION, LOG SCALE

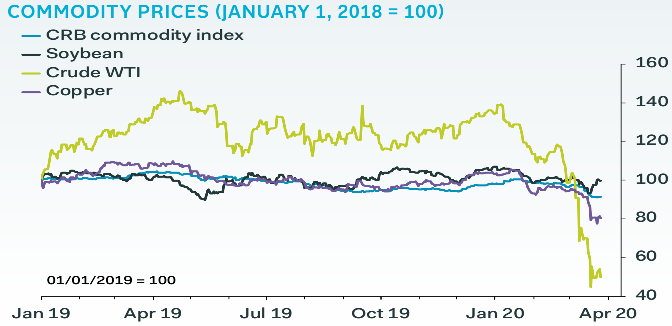


PANTHEON'S ECONOMIC FORECASTS

SUBJECT TO CHANGE WITHOUT NOTICE DUE TO COVID-19

	Real GDP, y/y%		Inflation, Avg.		Interest rate, Q4	
	2019	2020	2019	2020	2019	2020
Argentina	-2.2	-5.5	53.6	45.0	63.00	35.00
Brazil	1.1	-1.0	3.7	3.5	4.50	3.50
Chile	1.2	-4.0	2.3	2.4	1.75	0.50
Colombia	3.3	-0.5	3.5	3.2	4.25	3.00
Mexico	-0.1	-1.0	3.7	3.3	7.25	5.00
Peru	2.2	-0.5	2.1	2.1	2.25	1.00
Venezuela	-30.0	-50.0	130K	55K	--	--

COMMODITY PRICES (JANUARY 1, 2018 = 100)



PANTHEON'S FINANCIAL FORECASTS

	Currency			Benchmark Stock index		
	Q2F	Q3F	Q4F	Q2F	Q3F	Q4F
Argentina	68	72	75	26,000	27,000	27,500
Brazil	5	4.7	4.3	68,000	70,000	80,000
Chile	850	810	800	3,600	4,000	4,100
Colombia	3,900	3,500	3,400	1,100	1,200	1,400
Mexico	23.2	22.8	21.5	35,000	36,200	37,000
Peru	3.42	3.4	3.35	15,100	15,800	16,500

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