Latam Economic Update

- **Argentina: Industrial production and construction fell off a cliff in April**
- **Chile: Unexpected change in cabinet signalling more credit to SMEs; May inflation undershoots consensus with new methodology**
- **Peru: Government launches an enhanced Phase 2 for unlocking the economy; surprise credit rating downgrade by Fitch Ratings**

ARGENTINA: INDUSTRIAL PRODUCTION AND CONSTRUCTION FELL OFF A CLIFF IN APRIL

Industrial production and construction, which together account for about a quarter of GDP, extended March's massive cuts in activity through April, the first complete month of lockdown, in data released late on Thursday, June 4 (chart 1). While the numbers are eye-popping, we would have expected an even greater month-to-month contraction in industrial activity in April since activity was shuttered for the entire month versus 11 calendar days in March.

- **Industrial production,** which accounts for about 22% of GDP, dropped by -18.3% m/n sa in April, roughly matching the pace of the -17.3% m/m sa drop in March. The monthly change translated into a fall of -33.5% y/y in April, steepening the annual decline from a -16.5% y/y drop in March. All 16 sectors saw pullbacks, with the worst in vehicle production, where output was down -87.9% y/y. Given that no vehicles were produced in the country in April, the fact that this decline wasn't -100% y/y is a reflection of fixed costs and residual activity in a few essential sectors.

- **Construction,** which contributes around 3.6% of GDP, accelerated its decline from -37.9% m/m sa in March to -51.5% m/m sa in April, in line with expectations. Compared with a year ago, activity fell by -75.6% y/y versus -47.0% y/y in March.

Overall, April's activity numbers remain in line with the nearly -8% y/y contraction in GDP we forecast for 2020.

—Brett House

CHILE: UNEXPECTED CHANGE IN CABINET SIGNALLING MORE CREDIT TO SMEs; MAY INFLATION UNDERSHOOTS CONSENSUS WITH NEW METHODOLOGY

President Piñera made an unexpected change to his cabinet on Thursday, June 4. The most notable shuffle was the appointment of Sebastián Sichel, former Minister of Social Development, as President of BancoEstado. We read this as a strategic move to signal the government's intention to have BancoEstado deepen and increase the flow of credit to individuals and SMEs, which are the particular focus of the state bank's mandate. For context, the mission of the Ministry of Social Development is to contribute to the design and application of social

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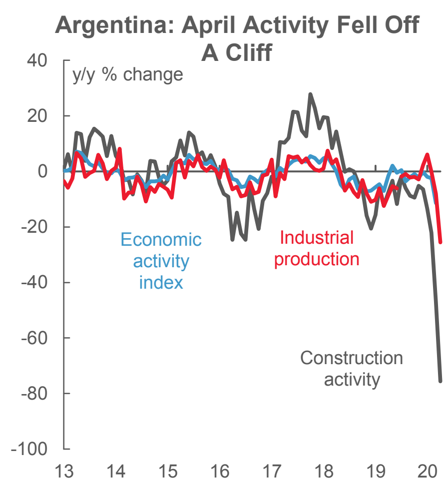
Chart 1



Sources: Scotiabank Economics, INDEC, FIEL.

development policies, plans and programs, especially those aimed at eradicating poverty and providing social protection to vulnerable people, with a view to promoting mobility and social integration.

It's worth recalling that BancoEstado has been closely involved in the implementation of Fogape-COVID-19, the state-guaranteed credit facility created in response to the pandemic. This facility consists of a state guarantee of USD 3 bn, which, according to the government, could be leveraged for up to USD 24 bn in credit for SMEs with sales below USD 35 mn/year. Since the initiation of the program on April 28 through May 31, banks had deployed close to USD 6.9 bn in credits to SMEs.

After the INE abruptly changed the imputation methodology for some important products, inflation for May ended up in negative territory at -0.1% m/m, for 2.8% annually. Core CPI had a monthly variation of 0.1% (2.1% y/y). Specifically, the core CPI for goods registered an advance of 0.3% m/m (2.3% y/y), signaling inflationary pressures related to the exchange rate depreciation at the beginning of the month and greater demand for food. On the other hand, core CPI for services showed a monthly null variation (1.9% y/y), reflecting signs of the weakness in internal demand.

—Jorge Selaive & Carlos Muñoz

PERU: GOVERNMENT LAUNCHES AN ENHANCED PHASE 2 FOR UNLOCKING THE ECONOMY; SURPRISE CREDIT RATING DOWNGRADE BY FITCH RATINGS

On June 4, the government decreed the start of Phase 2 of the re-opening of the economy. Phase 2 will include many of the sectors previously scheduled for Phase 3 (July) and even Phase 4 (August). This enhanced Phase 2 will likely raise the proportion of the economy that has been operating from just under 70% at the end of May, to over 80%, in our broad estimate, by the end of June, rather than in July. This, in effect, brings the unlocking of the economy ahead one month earlier than previously planned. The debate over which is the greater concern, COVID-19 or the economy, is clearly leaning towards the economy. In addition, companies will be able to begin operating as soon as they submit a health plan, as opposed to obtaining an individual authorization from the government as before, which should streamline their return to activity. The following list includes the more significant activities that will be allowed in Phase 2:

- Mining exploration;
- The entire gamut of mining operations, from small to large (previously, only large open-pit operations were allowed);
- Manufacturing and processing of animal feed, beer, wine and alcoholic beverages (yay!), shoes, medical supplies;
- Repair of transportation equipment;
- All investment projects, including private, public sector and public-private projects;
- Sale, maintenance, and repair of automobile and motorcycle vehicles and parts;
- Law, accounting, auditing, tax, architecture, engineering, scientific and veterinarian services, investigation and activities;
- Private security activities;
- Car rentals;
- Rental of machinery and equipment;
- Telecom, postal and messenger services;
- Maintenance, repair, and improvement of roads, train tracks, public services, water services; and
- Domestic passenger land transport throughout the country.

Fitch Ratings downgraded Peru's sovereign debt rating from A- to BBB+ on June 3, thereby aligning it with its global debt rating. Fitch Ratings expressed concern over Peru's public finances, as the public debt-to-GDP ratio rises from 26.8%, to 31.9% (Fitch estimate) in 2020. The downgrade came as a bit of a surprise, as Fitch had not given advance notice of concern by lowering Peru's "neutral" outlook.

—Guillermo Arbe

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