Fixed Income & Economics Daily

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FX & RATES STRATEGY RESEARCH

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STRATEGY

- **COLOMBIA: BanRep keeps rate on hold**
- **MEXICO: Banxico hikes 25bps**
- **POLAND: Non-residents sold Polish bonds again**

ECONOMICS

- **ARGENTINA: Pension reform vote postponed**
- **MEXICO: GDP in 2017 likely to grow 2.3% instead of our previous estimate of 2.5%; For 2018, we maintain a GDP growth estimate of 2.7%**

COLOMBIA: BanRep Keeps Rate On Hold

- The Central Bank of Colombia decided, unanimously, to keep the rate on hold at 4.75% in their last MPC meeting of the year, after cutting the interest rate in the previous two meetings.
- This decision was expected, as Minister Cardenas, one of the most dovish members of the board, had stated that the MPC should remain on hold after the S&P's decision to downgrade Colombia's sovereign rating, leaving almost null probability of a cut.
- According to the statement, the board believes that the balance of risks remains the same as one month ago. In effect, they maintain their view that inflation will converge to the 3% target by end 2018 and still estimate that the output gap remains wide.
- However, they now see a narrower space to cut and considered that they need more information on inflation and activity before reaching the end of cycle, as explained by Minister Cardenas in the press conference.
- The market had already expected the easing cycle to end soon, however, given the slightly hawkish tone to the statement, the Central Bank may not fully deliver the 75-bp cuts priced in the IBR curve.

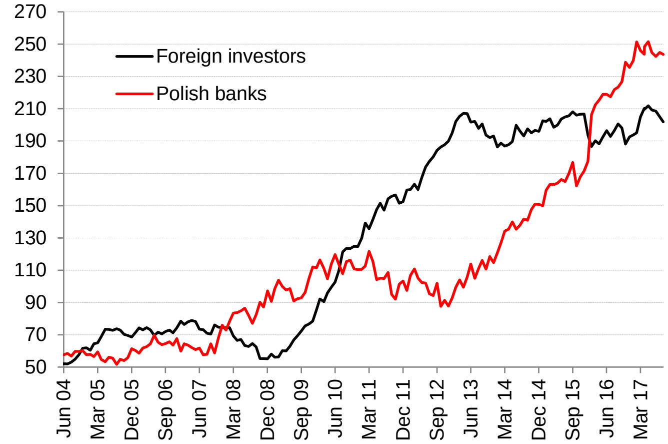
MEXICO: Banxico Hikes 25bps

- The Central Bank of Mexico (Banxico) hiked the interest rate by 25bps to 7.25%, after holding for five consecutive months, in line with consensus.
- The statement, however, surprised somewhat, as it maintains the hawkish tone from the previous month, stating that the balance of risks to inflation had deteriorated and they see a slower convergence to the target. Moreover, one governor voted to hike the interest rate by 50bps.
- In contrast, Banxico also considers that the growth balance is on the negative side due mainly to the NAFTA renegotiation uncertainty.
- According to our Economists, this hawkish stance opens the door for another hike in 1H18.

POLAND: Non-residents sold Polish bonds again

- The Ministry of Finance released data showing that October was the fourth month in a row in which foreign investors were selling Polish PLN marketable bonds. The outflow reached almost PLN3.2bn and was only slightly lower than in September (PLN3.45bn). As a result, non-residents' holdings bonds fell to c. PLN202bn, the lowest level since February. The biggest sellers of Polish bonds among non-residents were commercial banks (-PLN6.8bn) and the biggest buyers were central banks (+PLN7.5bn).
- Polish commercial banks reduced the bond portfolio by PLN1.15bn.

Holdings of Polish PLN marketable bonds (PLNbn)



Source: Ministry of Finance, BZ WBK.

LATAM ECONOMICS

ARGENTINA

ECONOMICS

Pension Reform Vote Postponed

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The Lower House postponed the voting for the pension reform in a confusing episode in which legislators from the opposition claimed that a quorum wasn't achieved (the officials claimed the opposite). Pension reform is one of the main bills of the reform package sent by the Executive to the Congress in late November and early December. Although the bill has been approved by the Senate, it still needs the approval of the Lower House (where consensus is more difficult to reach) to become a law. Chief of Cabinet Peña said yesterday that the government is convinced it has the necessary votes. At the time this report went to press, the government is trying to set a new date for voting.

The main goal of the bill is to modify the way in which pensions are adjusted. Currently, pensions are updated every six months on the basis of social security tax collection and salaries growth. If the pension reform bill becomes a law, pensions will be adjusted on a quarterly basis according to inflation and the RIPTE (average taxable remuneration of stable workers). The changes proposed by the government are aimed at diminishing the pressure that the social security system has over total spending. According to our calculations, the social security deficit amounts to nearly 4 pp of GDP (if we only take into account workers' and employers' contributions), over an overall fiscal deficit of 6% of GDP. According to our estimates, these changes would generate an almost half a point of GDP saving for the government.

MEXICO

ECONOMICS

GDP in 2017 Likely to Grow 2.3% Instead of Our Previous Estimate of 2.5%; For 2018, We Maintain a GDP Growth Estimate of 2.7%

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The weakness of oil production and the activities associated with it, as well as the fall in the construction of civil engineering works, have precipitated once again a decline in industrial activity. Throughout the year, these factors have affected the growth of the economy. Thus, in the annual balance, we estimate that the Gross Domestic Product will grow 2.3% instead of our previous estimate of 2.5%. For 2018, we maintain a GDP growth estimate of 2.7%.

INEGI reported that in its monthly comparison (seasonally adjusted figures), industrial production registered a 0.1% fall in October versus to September, accumulating two consecutive months of declines. In the annual comparison, considering the original series without seasonal adjustment, in October, industrial production recorded a decrease of 1.1%. Mining fell 10.2% YoY (oil fell 10.3%), construction dropped 1.7% annually and electricity, gas and water contracted 3.2%. Manufacturing production showed a positive performance with a 2.7% annual growth, which was trimmed by the 28.7% annual drop in the manufacture of petroleum and coal products (17.4% YoY from January to October).

Thus, from January to October, industrial production registered an annual drop of 0.6% and despite the 3.3% annual increase in manufacturing activity, falls were registered in mining of 10.1% YoY (oil dropped 10.4% YoY), in electricity, gas and water of 0.6% YoY, as well as construction of 1.2% YoY. Within the construction sector, construction of housing and commercial spaces grew modestly 0.4% YoY (January-October), but the construction of civil engineering works (infrastructure) plummeted 10.9% YoY (Jan-Oct).

Throughout the year, we have observed the unfavorable behavior of the oil industry, not only in the production of crude oil and gas, but also in the production of oil derivative products. Additionally, there is once again a sharp drop in infrastructure construction (associated with government spending), which has not been able to recover.

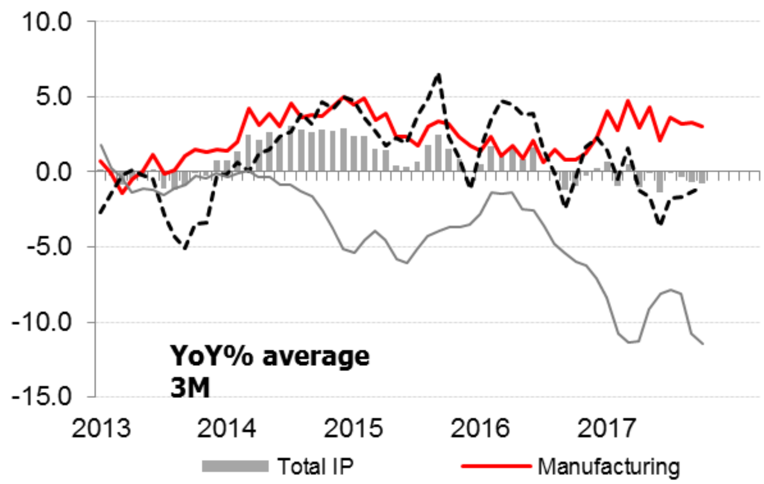
These elements register a worse-than expected performance, also determining a weaker-than-anticipated growth of the economy as a whole. This despite the favorable results in manufacturing and services. Thus, in the annual balance, we estimate that the Gross Domestic Product will grow 2.3% instead of our previous estimate of 2.5%.

However, for 2018, we maintain our growth estimate at 2.7% based on: (1) a favorable expectation for the growth of the United States' economy and, therefore, Mexico's non-oil exports; (2) favorable conclusion of the negotiations of the North American Free Trade Agreement and that it will prevail; (3) a moderate recovery in real wages in the local market; (4) growth of the government's current expenditure; (5) a "soft" political transition, which implies the continuity of economic policy in terms of maintaining macroeconomic stability; as well as (6) stability of oil production and its related branches.

In the latter case, the Income Budget presented by the Tax Ministry (SHCP) and approved by the Congress assumes a platform of 1,983 thousand barrels per day, which would imply an increase of 1.5% with respect to the average of 1,954 thousand barrels per day with which production is estimated on average in 2017.

But if the average daily production of oil stabilizes at 1,900 thousand barrels per day during 2018, which is the last data known as of November, it would represent a 2.7% annual drop. This would imply a downward adjustment factor in the estimated GDP growth for 2018. We shall wait for more information in this regard.

Industrial Production



Source: INGI and Santander.

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