Local markets waiting for a new rise in the MPR

We anticipate an increase of at least 75 basis points at next Tuesday's Monetary Policy Meeting

The economic figures released this week ratify that the economy is on a course of moderation. However, the still present inflationary pressures anticipate a new increase in the benchmark rate, which has impacted the prices of local assets.

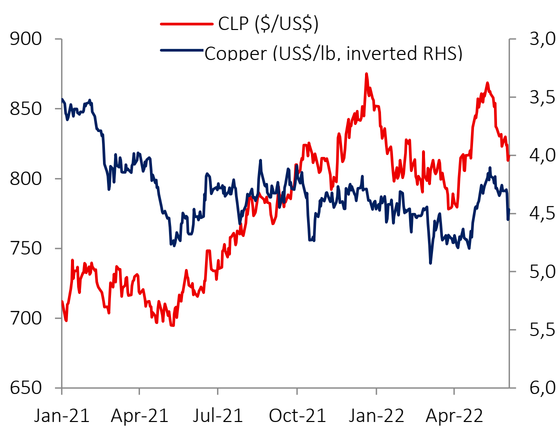
Activity data for April showed a -0.3% contraction in the margin, mainly explained by mining activity after the strong expansion in March. Although trade surprised on the upside (1.8% m/m seasonally adjusted), we estimate that it is a one-off effect, since there are a series of conditions that would not allow a high level of consumption to be maintained.

Employment still has a significant gap compared to its pre-pandemic trend, investment already showed a strong contraction in the last quarter, imports continue to fall and the IMCE continues to deteriorate in May, both in the general indicator and in the trade indicator and its current demand component. Thus, long-term rates responded with a slight drop (BTP5: 6.3%, -3 bp), also in line with their peers in the region.

On the other hand, short-term rates rose pending the monetary decision next week. Swap rates have risen around 30 bp since last Friday, anticipating an MPR somewhat above what financial operators forecast (9.5% vs. 9.0%, respectively).

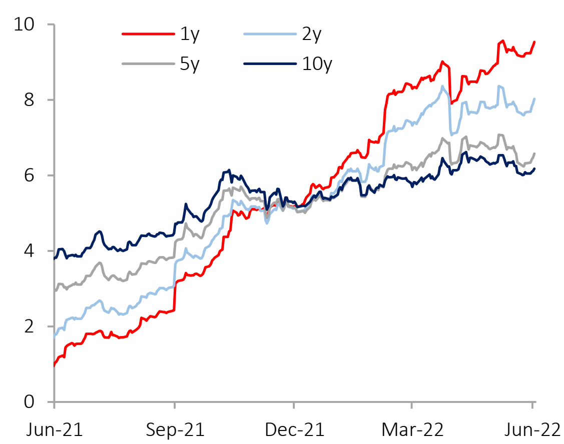
The expected increase in the governing rate together with the increase in the price of copper (US$/lb 4.6; 6%) –due to potential supply problems– has led to a strong appreciation of the exchange rate. The dollar is trading at $816 (-1% s/s), reaching a level not seen since the beginning of April. The increase in bets on the local currency by non-residents has also contributed to this appreciation, which in the last 15 days totaled revenues of US$ 2,000 million. Meanwhile, the IPSA ended the week with falls in line with international stock markets, closing at 5,327 points (-1%).

Local currency appreciates strongly as the Price of copper advances



Source: Bloomberg and Santander

Swap rates increases, indicating a new increase in the MPR



Source: Bloomberg and Santander

US labor market continues to show strength

In a week not without volatility, international markets showed divergent movements (global MSCI: +0.4%; Emerging: +1.8%; Latam: -1%), with a slightly stronger global dollar.

The North American stock markets ended with losses close to 1%, after important signs of the strengthening of the labor market and mixed activity figures were known, while the European markets also closed with losses (Stoxx 50: -1%), as it is now 100 days after the Russian invasion of Ukraine and inflation concerns are more relevant than ever.

At the close of this report, the non-agricultural payroll job creation figures were known, which were higher than expected in May (390 thousand vs. 318 thousand) and, in addition, the previous figures were corrected upwards (from 428 thousand to 436,000), which reversed the bias that the private employment data had previously given (ADP: 128,000 vs. 300,000 expected).

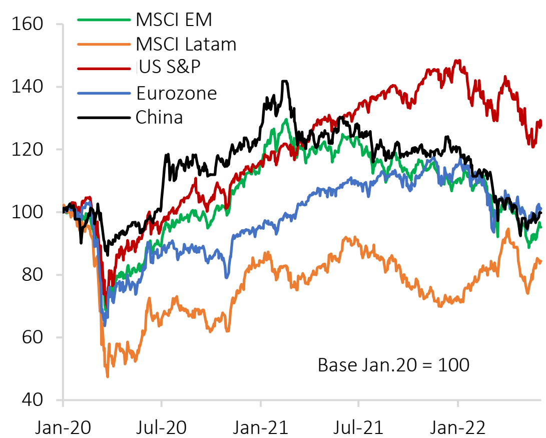
For its part, the unemployment rate remained at 3.6% and initial unemployment benefits at 200 thousand, minimum levels since the start of the pandemic, which confirms the strength and narrowness that the US labor market still maintains, despite have started the process of withdrawing monetary stimuli. In this regard, the Fed Vice President, Lael Brainard, mentioned that if a moderation in prices is not observed, a pause in September would be unlikely (after the 50 bp increases expected in June and July). Finally, the activity figures released for the week gave mixed results (industrial orders: 0.3% vs. 0.7% expected; durable goods orders: 0.5% vs. 0.4% expected; ISM manufacturing: 56.1 vs. 54.5 expected, composite PMI: 53.6 vs. 53.8).

In the Old Continent, the CPI figure for May once again surprised on the rise (0.8% m/m vs. 0.6% expected), reaching a record 8.1% in annual terms (7.7% expected). This puts pressure on the ECB ahead of its next meeting (June 9), where the start of the normalization of the reference rate will be discussed.

On the other hand, in an attempt to contain the rise in fuel prices, the main OPEC producing countries decided to increase crude oil production by 50%. Thus, they announced that July production would be adjusted upwards (648 thousand barrels per day vs. 432 thousand barrels in previous months). However, the price of oil continues its upward trend and is currently trading at around US$119 a barrel (+3% in the week).

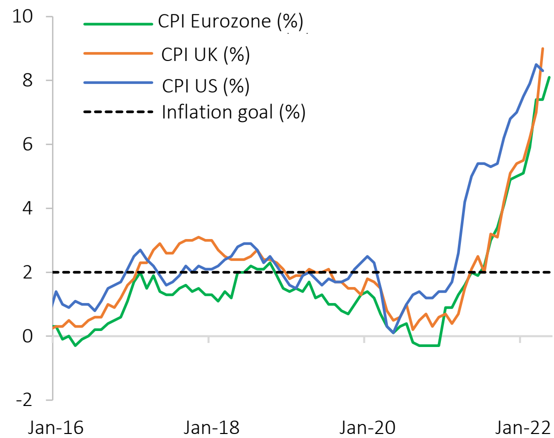
The Chinese stock market closed with increases of 2% due to the lifting of sanitary restrictions in Shanghai, after more than two months of strict confinement, which revives the outlook for the transport, business, production and consumption sectors. In turn, the PMI indices were known, both for the manufacturing and services sectors, which, although they had some upward surprises, were not enough to leave the pessimistic territory (manufacturing: 49.6 vs. 49 expected; services : 47.8 vs. 45.5 expected, Caixin manufacturer: 48.1 vs. 49 expected).

Global markets with a divergent trend



Source: Bloomberg and Santander

Inflation continues to cause concern



Source: Bloomberg and Santander

Coming up…

Next Tuesday's Monetary Policy Meeting, together with the policy framework that will be detailed in the Report to be published just one day later, would confirm a new increase in the MPR of at least 75 bp, leaving the rate at a floor of 9%. This increase responds to the activity levels still above their trend, to the surprises to the rise in the CPI and to inflationary expectations that remain above the target in the policy horizon.

Indeed, we anticipate that inflation for May – which will be known on the same day as the publication of the Report – will register a monthly increase of 1.5%, accumulating a large rise for the third consecutive month, as a result of higher international fuel prices and foods.

However, the activity data released this week reflect that the economy continues on a path of moderation, which puts a note of caution. After next week's increase in the MPR, we estimate only one additional movement, taking the rate to a maximum of 9.5%. This level would remain for the rest of the year, and as inflation moderates and the economy slows, we could see a reduction late this year or early next year.