MONTHLY REPORT

ECONVIEWS
ECONOMÍA Y FINANZAS

December 2021
Issue #210

The legacy of 2021 and what comes for 2022

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The road to Qatar 2022

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THE MONTH AT A GLANCE

RECENT DEVELOPMENTS

- In November, US inflation hit a 39-year high at 6.8% year-on-year, while the monthly CPI rose 0.8%. European prices are also reeling due to energy and supply pressures, with Euro Area inflation at 4.9% last month, the highest in the history of the currency.
- The Merval index rallied 13% after an Argentine delegation travelled to Washington to meet with IMF staff but fell 6.7% last week as negotiations appear to be in an early stage.
- The Blue chip swap rate fell to ARS 202.8, leaving the FX spread with the official rate at 99.5%. The CB is depreciating at a slightly faster rate, around 22% annualized. The parallel dollar hovers around ARS 200, helped by an influx of tourists and lower demand during December.
- In the first full record after the price freeze, monthly inflation lowered 1 p.p. to 2.5% in November, with the "food and beverages" item rising 2.1%. Seasonal factor in fruit and vegetable prices also favored the month's low print.
- After some discussion, the Government announced an ARS 8,000 Christmas bonus for retirees. In its first year, the new formula for pensions (indexation to wages and tax revenues) resulted in a 52.7% year-on-year increase.

FIGURE OF THE MONTH

The last maturity of the year, an USD

1.9bn

capital payment to the IMF on December 22nd will leave liquid net reserves in the red

TO BE ALERT

Despite the fall in headline CPI, core inflation accelerated to

3.3%

between October and November.

WHAT'S COMING NEXT?

- The Federal Reserve took a more hawkish turn than expected, doubling the pace of tapering to conclude asset purchases by March 2022. The Board of Governors sees three rate hikes next year, to a 0.75-1% range, and a further three in 2023 to 1.5-1.75%.
- The ECB also cut bond buying but did not hint at higher rates. The Bank of England became the first G7 Central Bank to hike rates, by 15 bps to 0.25%. Closer to home, the Brazilian CB has already raised its Selic rate 725 bps this year, and it is expected to reach 12% in 2022.
- The opposition voted against the 2022 Budget Bill and the Government will be forced to allocate resources through discretionary measures next year. This may further extend negotiations with the IMF.
- Net reserves are available to pay an USD 1.9 billion maturity with the IMF on December 22nd. A deal should be reached before a compound 4.8 billion (between the IMF and Paris Club) mature in March.
- Secretary of Commerce Roberto Feletti is making plans for January 8th, when the three-month price freeze expires. In recent declarations, he proposed a "regulated basket" of around 1,350 staple products, with quarterly price revisions.

SUMMARY OF MAIN INDICATORS

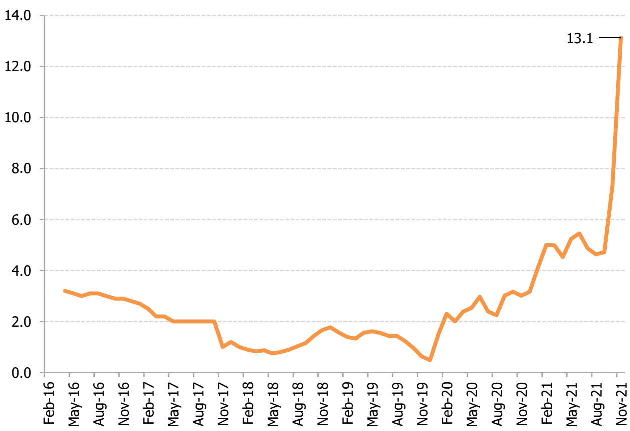
	Last	Previous		Last	Previous
Economic activity			**Financial data**		
Economic activity (MoM s.a.)	1.2%	1.4%	Inflation (monthly)	2.5%	3.5%
Consumer confidence (MoM)	-1.3%	-0.8%	FX spread (21day avg.)	106.8%	86.7%
Industrial activity (MoM s.a.)	-5.7%	5.3%	Country risk (bps 21day avg.)	1,763	1,701
International accounts			**External data**		
Current Account (USD BN)	2.76	0.54	Soybean price (per ton, 21day avg.)	462.9	451.8
CB Reserves (USD BN 21day avg.)	41.84	42.89	Brazilian activity (MoM s.a.)	-0.4%	-0.5%
Primary balance (ARS BN)	-209.17	-135.97	Financial Conditions Index	37.5	34.5

Source: Econviews base on multiple sources - Based on working days only

GRAPH OF THE MONTH:

Share of controlled prices in CPI

In p.p. - Greater Buenos Aires



Source: Econviews based on INDEC

NOV 26th	NOV 27th	NOV 30th	DEC 5th	DEC 10th	DEC 16th	DEC 20th
Econviews Monthly #209: IMF and the exchange rate + special analysis on inflation in Argentina	VP Cristina Kirchner posts open letter, **offering tacit support for IMF deal**, warns about social consequences.	**Country Risk hits 1,905 basis points**, its highest level since 2020 debt restructuring, falls in the following days.	Local bonds and stocks rally after Argentine delegation **travels to Washington to negotiate with the IMF.**	Mission to Washington concludes, **IMF says "further discussion needed"**, President and VP blast Fund.	**Government loses vote on 2022 Budget Bill**, with Congress's Lower House split 131 against vs 118 in favor.	**Econviews Monthly #210**

POLITICS

Although the announced "plurennial economic plan" hasn't materialized yet, the Government pressed fast-forward on the negotiations with the IMF. A team of BCRA and Ministry of Economy officials flew to Washington to meet with the Fund's staff. An IMF statement on December 10th disclosed that talks were advancing, with coincidences on "reducing monetary financing of the deficit" and a need for "wage-price coordination", but a closed deal still appears somewhat distant. The defeat of the budget showed a new reality for the government. Opposition is prepared to block key proposals if they do not agree. However, there is consensus that opposition would not jeopardize an agreement with the IMF.

PANDEMIC

Cases are shooting upwards, from 1,338 daily in mid-November to 4,465 today. However, with 69.4% of population fully vaccinated and 82.5% having received at least one shot, deaths remain very low, under 20 per day. Due to worries over the new Omicron variant, authorities have restricted travel from the African continent. Seniors and health workers are being called on for booster shots, which could be extended to all adults in 2022. Several provinces, such as Tucumán, Buenos Aires or Santa Fe, are requiring proof of vaccination to attend bars and restaurants and for certain administrative procedures. National authorities will implement a similar pass starting on January 1st, but only for crowded venues.

ECONOMIC ACTIVITY

Import restrictions weighted on industrial activity in October, leading it to a 5.7% monthly contraction s.a., which took the index back to August's level. On the other hand, Construction advanced 2.3% between September and October, s.a. Many sectors of the economy are growing above 2019's level, although still below the marks from before the 2018 currency crisis. We expect GDP to grow around 10% this year. What is pushing activity? Real wages are up 5.7% since February's floor, combined with the reopening and a sharp increase in mobility. During last year's quarantine, many households and companies improved their debt standing, and are making use of available credit as a safeguard against accelerating inflation.

INFLATION

After two consecutive records at 3.5%, monthly inflation decelerated to 2.5% in November. Price controls kicked in: the number of "frozen" items out of the total surveyed basket rose from 4.7% in September to 13.1% last month. Seasonality also helped out: after averaging 7.3% monthly in the previous two records, seasonal prices grew only 0.5%. On the negative side, core inflation accelerated slightly to 3.3%. Hotels and restaurants' prices (5%) increased the most, in line with the reopening, followed by apparel (4.1%). Regulated prices advanced 1%, their lowest in over a year. Against November 2020, CPI rose 51.2%. We expect December to close at 52% year-on-year, with inflation reaching 58% by the end of 2022.

MONETARY SECTOR

After the Central Bank stopped intervening and let the BCS "float", it went to ARS 202.8, an 99.5% spread. The parallel dollar sits at ARS 200, 95% above the official rate, and should keep calm due to seasonal supply in December (holidays + tourism). The BCRA is also depreciating the official FX at a faster rate than before the midterms, from 1 to 2% in monthly terms, or 12/15 to 22% annualized. We believe that in order to avoid a discrete devaluation, its policy rate must be higher than 38%, although a hike would damage the BCRA's balance sheet, as interest-paying liabilities amount to ARS 4.5 trillion. However, the USD 368 million of reserves sold over the last month imply the current regime is becoming too costly.

FISCAL ACCOUNTS

Higher than expected growth and extraordinary revenues (SDRs + tax on large fortunes + commodity boom) will leave 2021's primary deficit at 3.2% of GDP, halving 2020's 6.4% record. By November, revenues were increasing in real terms for 15 straight months, with taxes related to activity recovering after the Q2 lockdowns. In the eleventh month of 2021, revenues expanded 59.5% year-on-year, 8.3 points above inflation. Export duties (95.4%) made a big contribution together with import tariffs (71.8%), while VAT grew 62.3% against November 2020. In the framework of an IMF arrangement, we believe the primary deficit will lower to 3.2% of GDP in 2022, with an adjustment in energy subsidies and pensions.

I. What 2021 left behind and what 2022 can bring about

There were few achievements last year, but many of the problems that troubled the economy at the beginning of 2021 are still alive and kicking. The exchange rate, and the risk of a steep devaluation, was one of the main concerns since the beginning and has remained a main issue throughout the year. The government has been able to sidestep the problem thanks to a large increase in agricultural prices that generated a windfall of almost 16 billion dollars. But the issue has not disappeared as the additional dollars have vanished and international reserves dropped to worrisome levels.

Unfortunately, the election concerns made things worse. Since the second quarter the Central Bank slowed down the rate of depreciation from around 3.5% to just 1.2% per month in its efforts to reduce inflation, which remains north of three percent. There has been a strong real appreciation, a large spread between the official and alternative dollars of around 100% and huge concerns about how the problem will be solved.

Everyone is afraid about the costs of a potential devaluation, because of the risks that it might rekindle inflation in an economy where over 40% of the population lies below the poverty line. The IMF probably still feels guilty for forcing a maxi-devaluation in the 2018-19 program that did not work as it led to a macroeconomic crisis, when there were policy alternatives that would have worked better.

While nobody wants a devaluation, the truth is that no one has come up with an alternative policy to deal with the overvalued currency and to reduce the FX spread so that Argentina can beef-up the meager level of reserves. At some point it seems that a devaluation would be all but unavoidable, and that the costs of keeping the overvalued currency will be unbearable due to the shortage of reserves. **However, it seems that the government will try to postpone the devaluation as much as possible waiting for another stroke of luck**, while the IMF might look another way and not say that the king is naked as it does not want one more time to appear as the villain of the story.

Inflation was the second theme of the year. It started at full strength, and it peaked at 4.8% in March only to come down in the second half of the year on the back of a slowdown in the rate of depreciation, and regulated prices, which at some time needs to be reversed. **The government ignored and considered ineffective traditional policies such as containing monetary growth or increasing interest rates and reducing Central Bank financing to the Treasury.**

The outlook for 2022 appears to be gloomy. Especially because inflation has remained stubborn within the 50% range for four years in a row, and there is an inertia in price and wage setting that will be difficult to break. To make things worse, this year inflation remained high despite a rate of depreciation that was only 25% and increases in utility rates that were capped at 9%. **With corrections in these key prices expected next year, inflation will almost inevitably be higher.**

Net and Liquid International Reserves

In billion USD

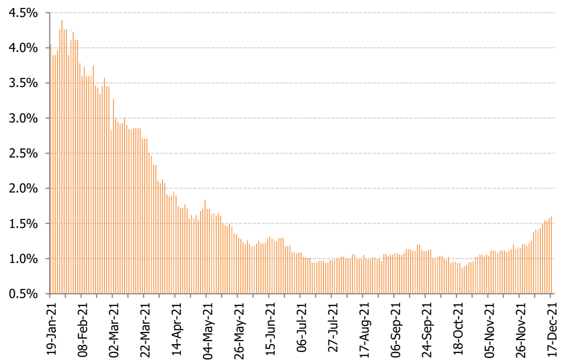
Gross reserves	**41.1**
Reserve requirements in USD	11.6
Swap with China	20.4
BIS & Repos	3.8
Net reserves	**5.4**
Gold	3.4
SDRs position	2.5
Liquid net reserves	**-0.5**

Source: Own estimates based on BCRA and IMF

Up to Dec-17

Rate of depreciation

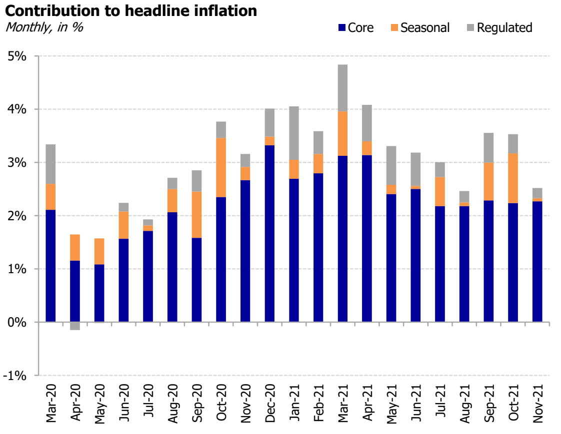
Accum. 30 days - Official exchange rate, Com. "A" 3500



Source: Econviews based on BCRA

Contribution to headline inflation

Monthly, in %



Source: Econviews based on INDEC

Argentina's country risk, which relentlessly continues to go up, deprives the government from access to financing and threatens any analysis of debt sustainability, as it would be impossible to rollover any debt that comes due. No country did ever repay its debt, instead, they improved their debt ratios through sustained growth, reductions (or even surpluses in the fiscal deficit), and in some cases eroding the value of debt through inflation. **Argentina's problems on this front arise from the lack of fiscal adjustment and the poor prospects of long-term growth that prevail at that moment**. The 2020 debt restructuring failed completely to improve the debt outlook, because it was done without a program and the policy framework was not conducive to improve confidence nor to promote investment and growth.

On the fiscal front there was some improvement, as the primary deficit was reduced from 6.5% of GDP last year to an estimated 3.2% in 2021. Much of the improvement took place thanks to the easing of the lockdowns which helped the recovery in GDP. The increase in inflation that helped the government to erode the costs of pensions, social programs, and public sector wages. The savings would have been larger if it had not been for the additional expenditures related to the elections.

Next year we expect a reduction in the deficit within the framework of an IMF agreement, probably to around 2.5% of GDP, which would be good news if it comes true, though it would need to be followed by additional reductions in coming years if it were to help Argentina to regain access to the international financial markets.

Monetary policy brought few changes in the strategy, as money supply will increase around 50% and the policy interest rates have remained unchanged throughout the year. Perhaps the only surprise is that interest rates did not increase despite higher inflation and a larger FX spread. It remains a puzzling issue that the Central Bank has been stubbornly reluctant to use interest rates as an instrument of monetary policy.

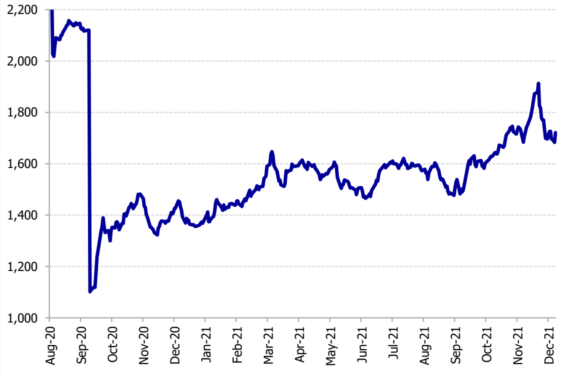
The Central Bank continued to be the main source of financing to the Treasury, which led to increases in the monetary base and in the stock of Leliqs and other interest-bearing liabilities. Medium-term, the concern is that an increase in interest rates that is needed to deal with the financial imbalances or additional financing to the Treasury could have a snowballing effect on the stock of Leliqs.

We expect the Central Bank to tighten monetary policy, and to comply with the IMF request to have positive real interest rates, though it is unlikely that it will do an overkill as it happened during the Macri administration when the interest rates on Leliqs reached almost 75%.

Perhaps the only good news is that there was a strong recovery from the depths of last year's recession. The economy is expected to grow 10% this year, to a large extent a rebound from the relaxation of the last year's extremely tight lockdowns and the implementation of expansionary policies in an election year.

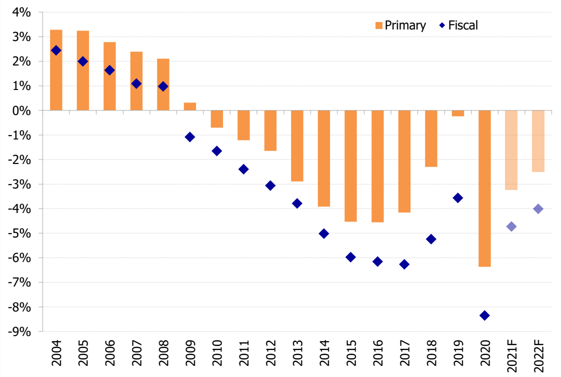
For 2022 the outlook looks challenging for two reasons. First, the effects of the easing of the lockdowns have already taken place. Second, the long-awaited adjustment in utility rates and the exchange rate is likely to take place. After all, this is a non-election year, in which governments have

Argentina Risk Premium
In basis points



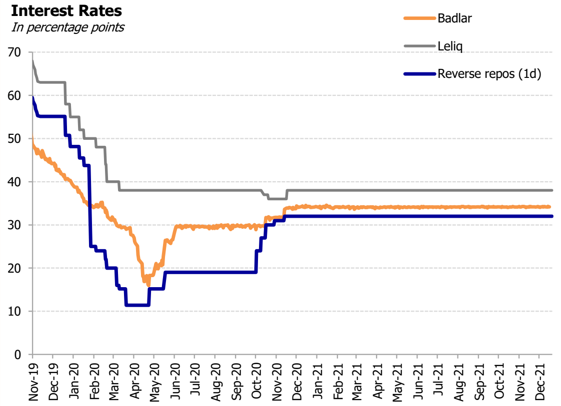
Source: Econviews based on JP Morgan

National Government - Fiscal accounts
As % of GDP



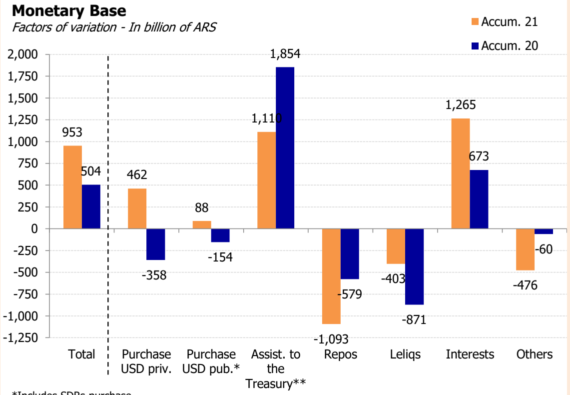
Source: Econviews based on MECON

Interest Rates
In percentage points



Source: Econviews based on BCRA

Monetary Base
Factors of variation - In billion of ARS



*Includes SDRs purchase
**Temporary Advances, CB profits and other operations
Source: Econviews based on BCRA

historically made the difficult and costly policy measures. The main question that hovers around is whether the government can avoid the adjustment, that has managed to avert this year. **Experience indicates that it is difficult and that the odds are against it, and much will depend on whether there is an agreement with the IMF and on what the agreement might include.**

All eyes are now focused on the negotiations between Argentina and the IMF, and the chief question is whether and how the two parties will be able to bridge the gap in the negotiations on the fiscal deficit, on interest rates, on the exchange rate and the FX spread and on regulated prices.

Although the government has maintained a fluid dialogue with the IMF since its inauguration, the discussions remained at a general level and the details of a possible plan were never discussed. It seems that only in the recent mission of government officials to Washington both sides started to talk about what was needed to reach agreement by the end of February avoid a scenario in which Argentina falls into arrears with the Fund and in default with the Paris Club.

The path to the agreement won't be easy. The government last Friday failed to get approval of the 2022 budget, which was supposed to be the basis for the negotiations with the Fund. In addition, so far it has not taken any decisive action regarding the exchange rate, interest rates or any other policy measures. It continues to be in muddle through mode.

The next couple of months will be tense and crucial, though everything indicates that at the end there will be an agreement, though it will take place at the last minute. While there are many fronts in the negotiations, the exchange rate seems the thorniest issue where there are few alternatives, and all the paths seem to lead to the most dreaded one.

The ABC of an agreement with the Fund

Fiscal policy	- Reduction of the fiscal deficit through: - Increase in revenues - Reduction of expenditures (energy subsidies, social security expenditures, public sector wages)
Monetary policy	- Increase in interest rates - Limiting of the financing of the CB to the Treasury
FX policy	- Reduction of the FX spread - Accumulation of reserves
Structural reforms	- Tax and capital markets reform - Pension system reform - Labor reform
Debt sustainability	- Reduction of country risky - Regaining acces to capital markets

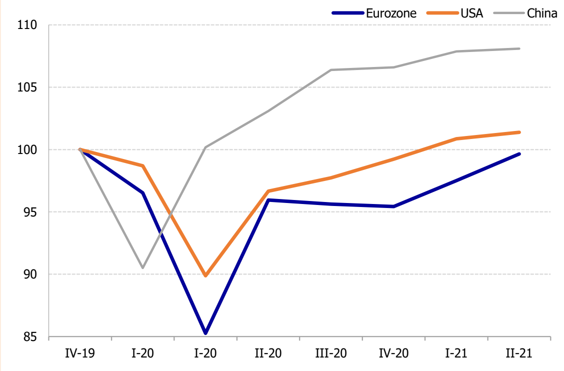
Source: Econviews based on IMF

II. The world in 2022

We are closing an unusual year of economic recovery. In 2021 we witnessed the greatest worldwide vaccination campaign in human history and the return of inflation on a global scale. Locally, the abandonment of the stringent lockdowns of 2020 has allowed the recovery of economic activity, which has sped up in recent months in part thanks to the reopening of many activities, but also thanks to higher exports. GDP will grow more than 10%.

But the recovery of activity is coupled with great macroeconomic instability. Argentina enters 2022 with scarce reserves, high inflation, tough FX restrictions and in urgent need of signing an agreement with the IMF before March, when it may not have to money to pay debt maturities. Against this background**, we analyze what the world will look like in 2022 and what it means for Argentina.**

GPD Recovery
4Q -2019 =100, seasonally sdjusted

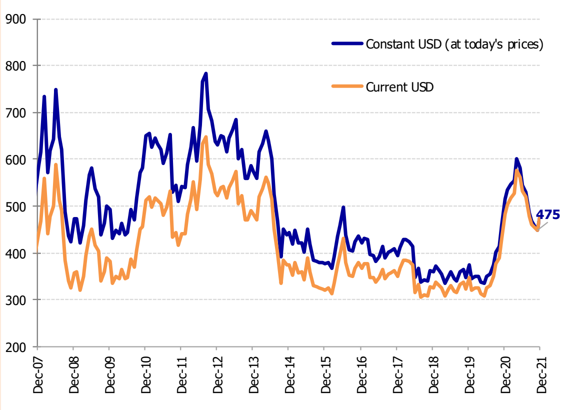


Source: Econviews based on Fred Economic Data & Statista.

<u>A solid global recovery in 2021, but with a few clouds on the horizon</u>

Despite the ongoing pandemic, for the most part 2021 has been a significantly better year than 2020. The development and distribution of vaccines meant the return of massive gatherings, the reduction of restrictions or the straightforward abandonment of lockdowns. And in turn, **economic improvement followed: in most countries, an unprecedented V-shaped recovery has taken place globally.**

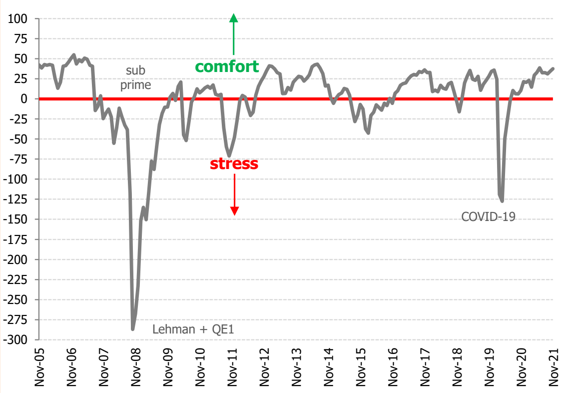
Soybeans
USD per ton



Massive fiscal and monetary stimuli resulted in record liquidity. Outside Argentina, equity markets have soared, and the S&P 500 has consistently broken records, many times despite some temporary setbacks in the evolution of the real economy. **And that has meant an era of plenty and cheap money, with negative real interest rates. But Argentina, isolated from international credit markets, has not been able to reap any benefit from the sea of liquidity.**

Cheap money and strong demand also meant a boom in commodities prices. The international price of soybeans shot up, despite falling short of the records from 2012. And yet, the boom brought about an unexpected shower of dollars for Argentina that allowed the government to get through the year without implementing any important reforms. **The oilseed and cereal sector will have brought an additional USD 16.2 billion relative to 2020 by year's end. And yet, the Central Bank will have finished the year almost without accumulating reserves.**

Index of Finantial Conditions
Subindex of External Conditions



This external tailwind has meant very positive financial conditions that Argentina could have benefitted from had it already signed an agreement with the IMF and presented a plan to tackle the FX, fiscal and monetary imbalances. **The truth is, once again Argentina has missed an opportunity** and 16 months after the restructuring of the external debt with the private sector, country risk is flying high at 1,700 basis points.

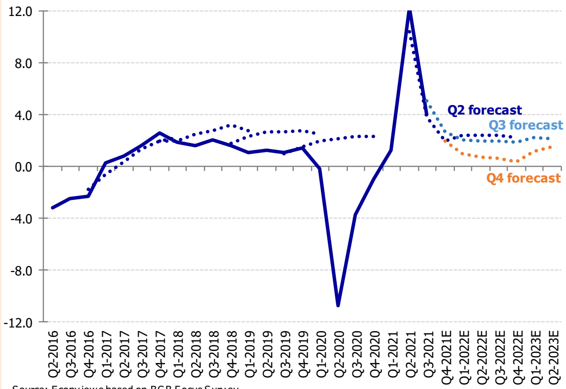
And as the year ends, the external winds seem to have made a U-turn. Inflation has been steadily growing around the world and many countries have already adopted higher interest rates, **but all eyes are on the United States.**

Bottlenecks and shortages have complicated things and what in some economies, like Brazil, what was a strong rebound now threatens to turn into a deceleration or a straightforward recession. **And to top this, agricultural commodity prices have gone down while oil price has gone up.** Argentina is a net energy importer, albeit not a huge one.

Tackling the many imbalances of the Argentine economy while sustaining the economic recovery will not be an easy task. **The global outlook will be a key ingredient. The upcoming football (soccer) World Cup will be played in November and December 2022 in Qatar. In the next section, "the road to Qatar", we summarize the world economic outlook for next year, and how the "major players" and Argentina may perform.**

Brazilians are less optimistic

GDP forecasts and actual GDP, year-on-year variation in %



Source: Econviews based on BCB Focus Survey

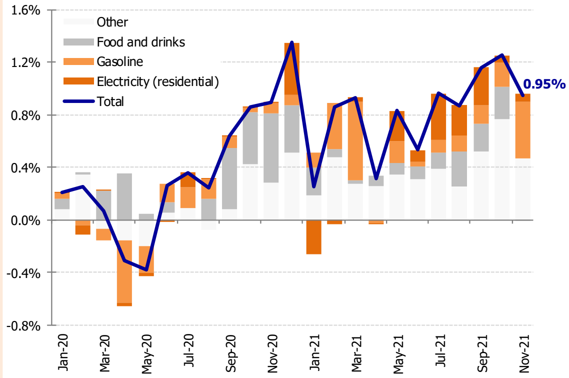
Growth in 2022: the road to Qatar

Argentina is in dire need of reserves and the performance of exports is key to the overall evolution of the economy. **But our exports depend on the economic activity of the trading partners**. And ultimately, what happens in Brazil, China and the US will be crucial for our partners and ourselves.

Two of Argentina's main trade partners are expected to slow down in 2022. Brazil formally went back into recession in Q3-2021, with a 0.1% q/q drop following its autumn lull, revised to –0.3%. Initial data for Q4 is not promising. Activity fell by 0.4% between September and October, leaving it below February 2020 levels. Estimates for next year have worsened almost 2 points since March, going from 2.5 to 0.5%. Brazil's top bank, Itaú, goes further and expects a new recession in 2022.

Gas and electricity are pushing prices in Brazil

Each item's contribution to monthly CPI variation



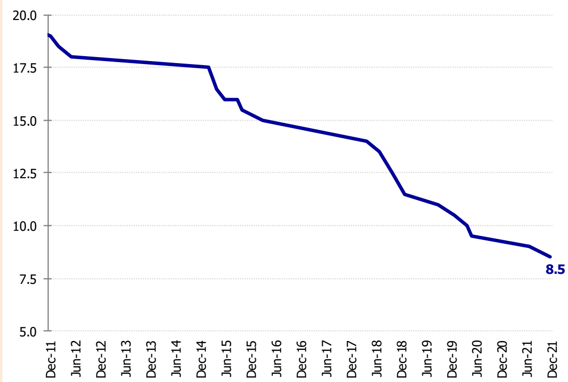
Fuente: Econviews en base a IBGE

A severe drought was this year's main villain: agriculture fell 9% year-on-year in Q3. As over two-thirds of Brazil's power is hydroelectric, bad weather also drove electricity bills up 31.9% y/y, hitting manufacturing. **Climate forecasts for 2022 are uncertain**: the Central Bank expects the drought to continue, while sources report improved conditions in the Mato Grosso region but ongoing dryness elsewhere. Forecasts for Agriculture GDP next year have improved in recent months, from 2% in mid-October to 2.5% today, while Industry and Services lost 1 point.

In March, the BRL sunk to nearly 5.90 per USD after Bolsonaro shook up state oil giant Petrobras' board. **This episode fed into a narrative of political instability hampering growth in 2022**, as presidential elections will be held in October. What's really at stake? Paulo Guedes' big reforms had already lost steam before the pandemic. Market fears of Lula may be exaggerated, taking into account his track record from 2002 and his likely choice of a moderate, such as ex-PSDB Gerardo Alckmin, as running mate. However, FX turbulence before the elections can further derail already weak growth.

China has lowered reserve requirements again

Rate for small and medium banks, in p.p.



Source: Econviews based on Refinitiv

Trade partner no. 2 is also in problems. According to the IMF, China will grow 5.6% in 2022, its lowest since 1990 (aside from 2020). The People's Bank recently lowered reserve requirements by 50 basis points to 8.5% on average, the 14th cut since 2018. This loose monetary policy, at odds with other CBs' plans for 2022, seeks to inject liquidity and avoid another Evergrande or Kaisa crisis (both real estate developers were cut to default by Fitch after missing interest or principal bond payments). On political matters, China will be inwards focused, as Xi Jinping may further consolidate his grip at the CCP's scheduled five-year Congress in

November. **Tensions with the US are on the rise again,** as the Winter Olympics boycott and ban on imports from Xinjiang show. **Is a new trade war on the way?** With import prices up 10% year-on-year, Biden might be loath to hike tariffs as in 2018-19, but further scuffles cannot be ruled out.

Also, mask up! While most countries are struggling with Delta and Omicron in one way or another, **China was one of the few to adopt a "zero Covid" policy to face the pandemic**. This implies that lockdowns and massive tests are imposed when there is a positive case in a city. In terms of contagion and deaths, this policy has been highly effective, at least according to Chinese data. These measures allowed manufacturing to stay strong while other countries faced harsh outbreaks, **boosting China's exports**. But such strict sanitary controls hampered recovery in other areas related to consumption or tourism.

Additionally, **export growth led to RER appreciation**, so Chinese products are losing competitiveness as the external demand starts to normalize and switch from goods to services. Looking ahead, **it is likely that the "zero Covid" policy will stay in place for several more months,** considering large scale events such as the Winter Olympics or the five-year Congress.

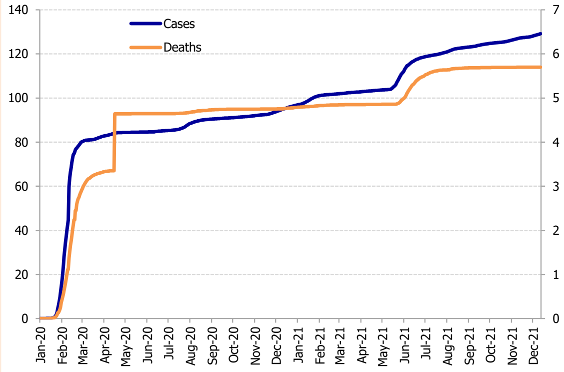
As for trade partner no. 3, the US has a lot of problems, but growth shouldn't be one in 2022. Most forecasts agree the economy's boom will extend into next year, growing around 4%. Unless a new variant wreaks havoc, upward trends in manufacturing (which has been growing at a 1% monthly pace in October and November). **In the following section we will detail how the Fed will take action to curb inflation**, but given their low base, rate hikes shouldn't affect activity too much in the short term. In addition, Powell seems committed to the dual goals of keeping prices in check but also recovering full employment and will thus keep an eye on the labor market.

US unemployment fell to 4.2% in November. The economy added 6.1 million nonfarm jobs this year, and vacancies are above 11 million. Weekly unemployment insurance claims are averaging under 200,000 in December, figures not seen since the late sixties. **How many more jobs are needed?** 2.4 million workers stopped searching for employment after March 2020: counting them, unemployment would be closer to 5.7%. Out of these, 1.5 million are women. As the pandemic fades away, many will re-enter the workforce, increasing demand. The White House is also interested in running a tight labor market to push up real wages, one of Biden's slogans. As of November, **average hourly pay was up 4.8% year-on-year**, still behind inflation. But higher wages do not provide positive news for inflation.

Consumer confidence is another issue. Retail sales only grew 0.2% monthly s.a., in November, but are still growing strong. Yet according to the University of Michigan, confidence is at 66.8 points, its lowest since 2011. Some analysts point out that as savings from pandemic stimuli dry up, **families feel they cannot sustain their current consumption in the face of rising prices**. Although the US Congress recently raised the debt limit by USD 2.5 trillion, another round of checks seems very unlikely.

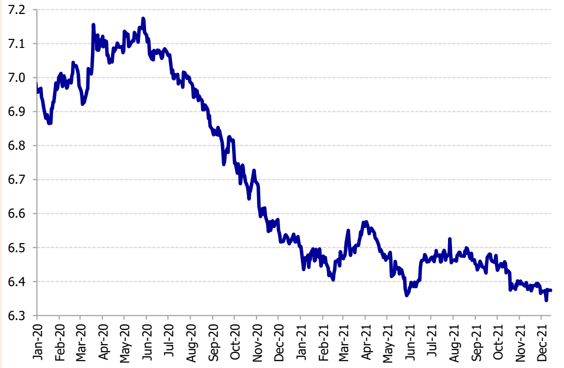
The situation in Chile must be also closely watched. On top of the uncertainty regarding the new administration led by Gabriel Boric, the return of inflation is probably the most important event of the last

Chinese COVID cases and deaths
Accumulated - In thousands



Source: Econviews based on WHO

Exports growth led to an exchange rate appreciation
Dollar to Yuan



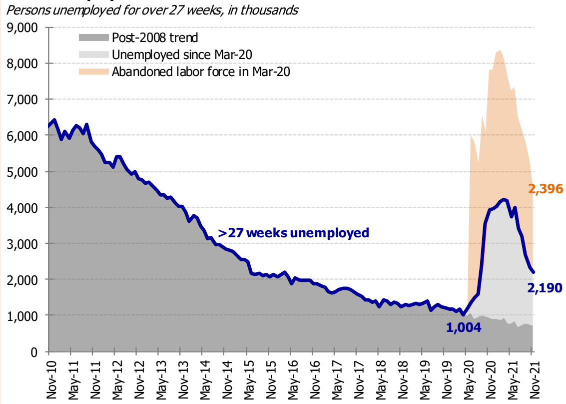
Source: Econviews based on Investing

Fed still optimistic on growth
FOMC median forecast

		2021	2022	2023	2024	Long term
GDP growth	**Dec-21**	**5.5%**	**4.0%**	**2.2%**	**2.0%**	1.8%
	Sep-21	5.9%	3.8%	2.5%	2.0%	1.8%
Unemployment	**Dec-21**	**4.3%**	**3.5%**	**3.5%**	**3.5%**	4.0%
	Sep-21	4.8%	3.8%	3.5%	3.5%	4.0%
Inflation (PCE)	**Dec-21**	**5.3%**	**2.6%**	**2.3%**	**2.1%**	2.0%
	Sep-21	4.2%	2.2%	2.2%	2.1%	2.0%

Source: Econviews based on FRED

Core unemployment
Persons unemployed for over 27 weeks, in thousands



Source: Econviews based on FRED

couple of months. In November, the CPI skyrocketed to 6.7% y/y, its highest mark since the international crisis in 2008 when it touched 9.9%. The Chilean Central Bank has claimed that local inflation is not "just imported inflation", but that it's rather fueled by the recovery of domestic aggregate demand.

Boosted by cash transfers given by the government, the withdrawals of pension funds and fewer sanitary restrictions, **activity is expected to grow more than 11% in 2021. However, the recovery is losing momentum and growth forecasts for 2022 and 2023 have been declining month over month.**

Several factors explain this deceleration in economic activity. On the one hand, we must consider the **uncertainty regarding the new president and about the new National Constitution. The pension funds withdrawals also contributed to increasing the turmoil.** Since the third withdrawal from late April, the exchange rate has depreciated roughly 20%. In this sense, in the first days of December, the bill of the fourth withdrawal was rejected by Congress. But Boric's rhetoric threatens the future of private pension funds. We shall be alert to the cabinet nominations.

But politics is not the only reason for the worsening perspectives, there are some economic factors too. First, the Central Bank started to increase interest rates in July in response to price increases that are high above the inflation target. In this manner, at its last monetary policy meeting that took place last Tuesday, **authorities decided to increase the reference rate by 125 basis points,** bringing it to 4% and warned that it will continue increasing in the short term. This turn towards a tighter monetary policy, combined with less fiscal stimulus will impact economic growth. Additionally, like other commodities, with the strengthening of the dollar, **copper prices are expected to decline next year, which means lower revenues and a smaller capacity for increasing expenditures.**

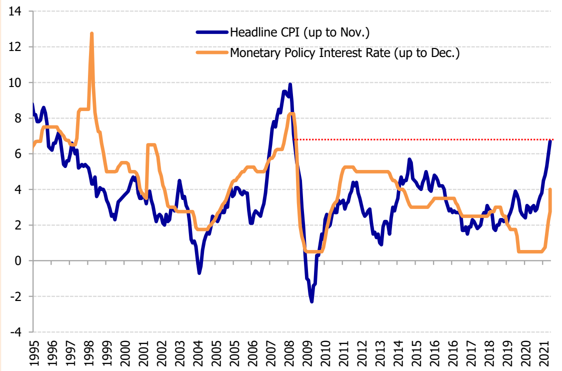
<u>**Higher rates are just around the corner**</u>

On its last meeting of the year, the Federal Open Market Committee (FOMC) unveiled the Fed's strategy for next year. First, the pace of tapering will double, to conclude asset purchases by March. Second, **the dot-plot shows three 25-basis point rate hikes in 2022**, from a current range of 0-0.25% to 0.75-1%. This move would be repeated in 2023, taking the Fed Funds to a 1.5-1.75% range, still quite negative in real terms.

While it was certainly more hawkish than previous FOMCs, **by the Fed's own projections real interest rates will remain negative well into 2024**. Powell has abandoned the "transitory" label for inflation, with CPI at a record 6.8%, but continues to stress that expectations and wages, two forces which have cemented high inflation in the past, are not on an upwards spiral.

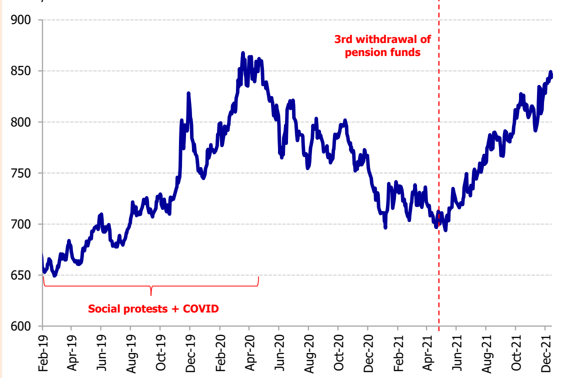
The Fed's bet appears to be hiking rates enough to anchor expectations, but not so much as to disrupt the job market recovery. However, **experience shows that Fed rate hikes which barely troubled the US economy have proved very recessive in emerging markets**, especially those vulnerable to quick capital outflows.

Inflation Was Not That High Since 2008
In percentage points



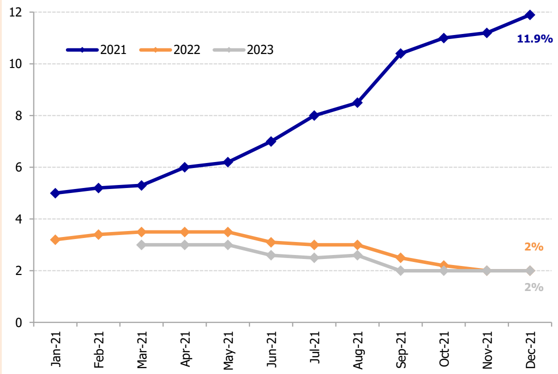
Source: Econviews based on BCCh

Chilean exchange rate
Pesos per US Dollar



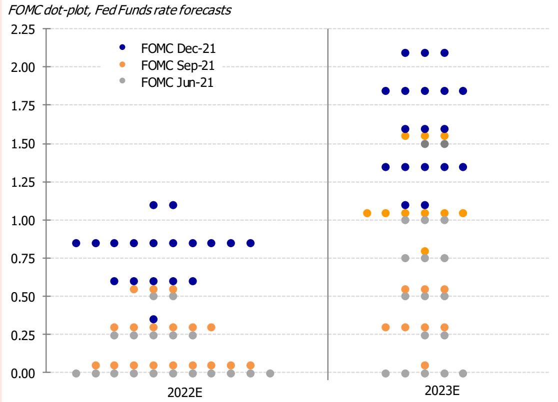
Source: Econviews based on BCCh

Expected GDP Growth
Forecasts for December of each year - In p.p.



Source: Econviews based on BCCh

A more hawkish Fed
FOMC dot-plot, Fed Funds rate forecasts



Source: Econviews based on FRED

ECONVIEWS
ECONOMÍA Y FINANZAS

Bloomberg recently ranked Argentina, Turkey and Brazil at the top of a "vulnerability to US monetary policy list". The Turkish Lira has sunk 49% YTD and 23% only in the last month, partly due to Erdogan's insistence on low interest rates. **Today the Lira rebounded 11% after authorities promised insurance on FX losses**. Brazil's Real, despite a more orthodox CB, floundered 9.2% in 2021 against the US dollar. The Fed's last cycle of hikes in 2015-18 took rates from 0.12 to 2.4%, up 225 basis points. The acute phase in 2018, with 4 hikes, wreaked havoc on the Lira and the Peso, then a free floater. The dollar gained 40% and 100% against those currencies that year, respectively. While Argentina's current account position is more solid than that year, it counts with much less FX reserves (and has already spent the go-to-the-IMF card).

Vulnerability to US monetary policy

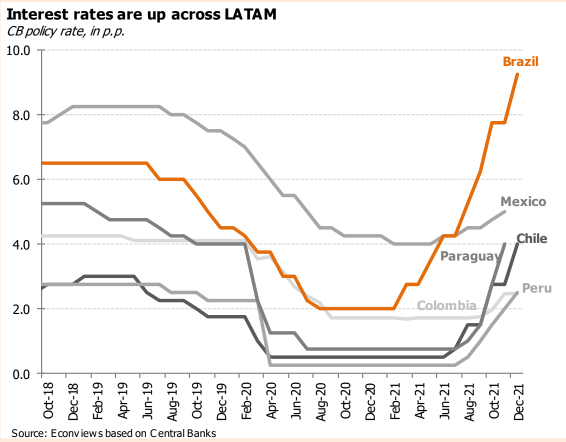
	Current Account	External Debt	Govt. Debt	Reserve Coverage	Real Policy Rate	Governance	Vulnerability Ranking
Argentina	0.8	17.5	102.8	68.5	-14.1	-0.2	**16.8**
Turkey	-1.6	25.9	37.8	76.4	-3.9	0.0	**14.7**
Brazil	-1.7	8.9	90.6	163.8	-2.9	-0.4	**13.8**
Egypt	-3.7	4.3	91.4	58.2	2.0	-0.5	**13.3**
South Africa	-0.9	16.4	68.8	75.2	-1.5	0.3	**13.0**
Colombia	-4.0	11.3	66.7	144.6	-2.1	0.0	**13.0**
Poland	1.6	25.5	55.5	138.5	-6.3	0.4	**11.7**
Chile	-2.2	9.7	34.4	84.0	-3.3	1.0	**11.2**
Malaysia	3.7	33.7	70.7	118.3	-1.2	1.0	**10.7**
Phillippines	-1.8	5.4	59.1	237.6	-2.6	0.1	**10.5**
Mexico	-0.3	4.8	59.8	128.9	-1.5	-0.2	**10.2**
China	1.5	11.3	68.9	74.8	1.5	0.6	**10.2**
Peru	0.1	6.6	35.0	287.0	-4.3	-0.2	**10.0**
India	-1.4	9.4	90.6	190.7	-0.5	0.4	**9.7**
Thailand	2.1	15.2	58.0	251.3	-1.9	0.3	**9.0**
South Korea	4.2	13.2	51.3	99.0	-2.5	1.4	**8.8**
Indonesia	-1.0	6.0	41.4	125.2	1.8	0.4	**7.8**
Taiwan	15.2	25.2	27.2	170.2	-1.5	1.6	**6.0**
Russia	4.4	8.7	17.9	359.2	-0.6	0.0	**5.2**
Saudi Arabia	3.8	5.0	29.7	327.0	0.2	0.1	**4.5**

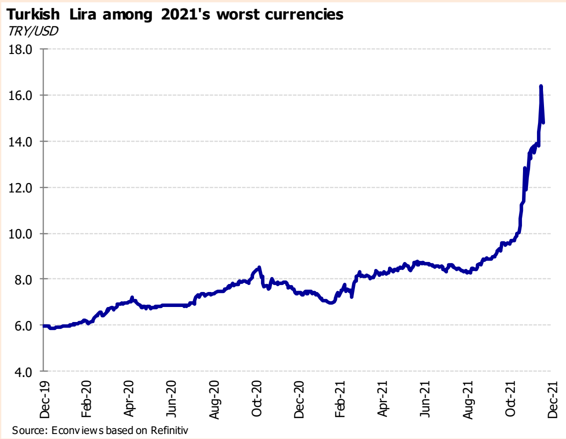
Source: Bloomberg Economics

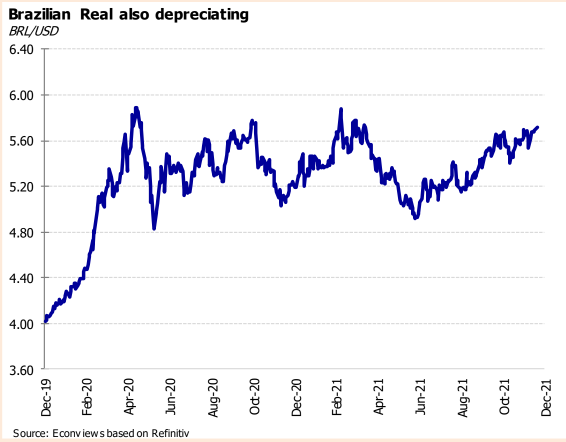
Inflation is a global problem, not just an American one. And as the dollar strengthens, Central Banks will also hike rates to defend their currencies. On Thursday 16th, the Bank of England stood out as the first G7 Bank to raise its policy rate, by 15 basis points to 0.25%. The ECB has said nil on rates, but plans to cut its asset purchases faster than expected. In emerging markets, 2021 already saw many hikes and more are expected next year. **Brazil's Selic rate jumped 725 basis points since January and might rise another 250 in 2022**. Peru hiked by 225 points, Mexico by 125.

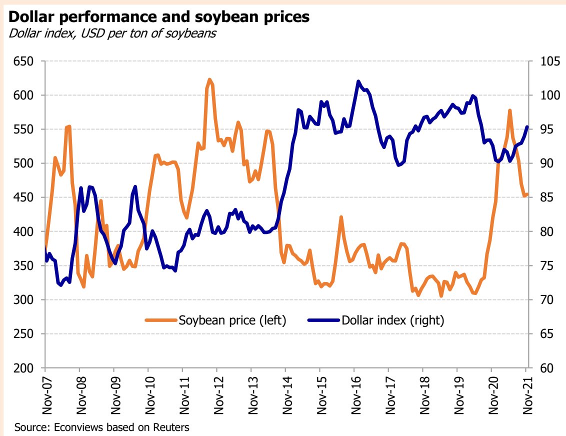
Investors "flight-to-safety" doesn't just hit emerging market bonds. **Agro commodity prices usually take a toll as well**. While weather conditions, harvest yields and global demand –China explains much of it- all play a part, the evolution of the dollar is a factor of utmost importance.

When the dollar index rose roughly 20% between July 2014 and April 2015, soybeans' price fell 23% in the same period. Since May 2021, the dollar index on average has recovered by 5.6%, as of November. And in the same period, the price of soybeans fell by 21%. After the latest FOMC, a more hawkish Fed has already been priced in by investors. But that doesn't mean that the dollar won't keep rising. The evolution of US economic activity and inflation will be determinant. If the current tendency goes on, **it could have enormous implications for commodity prices. And in turn, Argentinian exports.**









Never ending Covid

Local cases came abruptly down once the vaccination campaign accelerated. Then authorities decided the reopening of many places whose windows had been shut for many months: shopping centers, theaters, cinemas came back, everybody was allowed again in public transportation and even massive events resurrected. The elections played a role convincing politicians to move forward. And while Argentina's situation improved, so did the world's, allowing the return -still partially restricted- of international travel.

But news from South Africa have made the alarms go off. Two years will have passed since Covid began spreading worldwide in January 2020. And though many countries have advanced in their vaccination plans, a considerable part of their populations is unwilling to take a shot.

Even if most economic forecasts show a continuous economic recovery in 2022, Covid keeps on playing its part and most economists seem unable to get ahead of it. While the Omicron variant is way too new to evaluate its true impact, **the threat is real: the appearance of a more contagious and even deadly variant might slow growth and force restrictions again.**

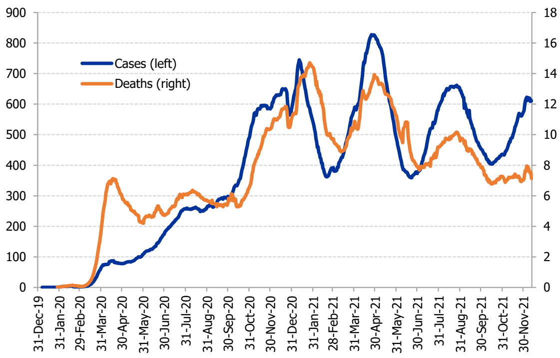
In Europe, the number of cases has reached a new record, positioning the region as the epicenter of the pandemic once again. Therefore, measures were imposed with special emphasis on the unvaccinated population. **Many countries are adopting a "sanitary pass"**, which is required for access to public and private spaces like restaurants, museums, nightclubs, and the list goes on. **The idea behind it is promoting vaccination and avoiding lockdowns that might be much costlier for the economy**. Tourism might be one of the activities that is the most exposed to new restrictions, so its recovery could be delayed.

Only 46.11% of the world population is fully vaccinated, an unsettling percentage in the fight to end the pandemic. At the onset of Covid, it was estimated that some 70% of the population had to be vaccinated to reach the famous "herd immunity", but the virus has managed to survive even in countries like Israel, with huge coverage. Still, **the impact of the virus is strongly reduced among the vaccinated.**

Beyond some people's reluctance to get the shot and the adaptability of the virus, **the increase in the length of the pandemic is also due to the slow rhythm and the unequal distribution of vaccines among countries**. Even in the European Union, which has almost 68% of its population fully vaccinated, disparities between countries are evident. For instance, while Spain has 80.65% of the population fully vaccinated, Bulgaria has only reached 26.6%. And in poor countries the situation is much worse. In Africa, only 12.6% of the population received one shot and barely 8.6% are fully vaccinated, with countries like Ethiopia not even reaching 2%.

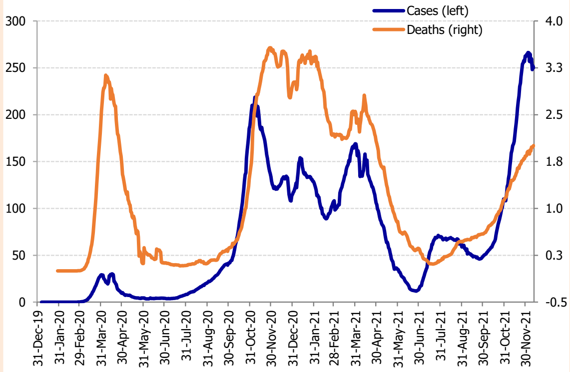
The latest numbers show that while cases have soared, death numbers are much milder, and this could be attributed to the vaccination campaign. **Advancing with the vaccination plan, promoting an equal distribution of them with a worldwide scope and learning to live with Covid seem fundamental to go through the following year without a huge impact in the economy, as evidenced in 2020.**

Daily Covid-19 cases vs. deaths - World
In thousands, moving avarage 7 days



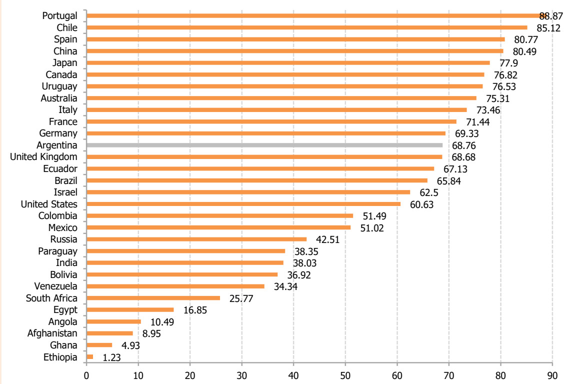
Source: Econviews based in Our World in Data

Covid-19 cases vs. deaths - Europe
Thousands, moving avarage 7 days



Source: Econviews based in Our World in Data

Fully Vaccinated People
Per hundred - Up to Dec 15



Source: Econviews based on Our World in Data

Base Scenario

	2019	2020	2021 F	2022 F	2023 F
Inflation (eop)	53.8%	36.1%	51.4%	58.0%	38.0%
Exchange rate ARS/USD (eop)	59.90	84.15	104.86	178.30	244.27
Real exchange rate ARS/USD (eop, Dec-01=100)	150.8	158.3	137.6	154.0	157.9
Paralell exchange rate ARS/USD (eop)	74.6	140.3	209.7	276.4	378.6
Spread with official exchange rate (eop)	24.6%	66.8%	100.0%	55.0%	55.0%
Gross reserves (USD billion, eop)	44.8	39.4	40.6	46.6	49.6
Policy rate (eop)	55.0%	38.0%	38.0%	44.0%	33.0%
GDP (YoY)	-2.0%	-9.9%	10.0%	2.5%	2.5%
Private consumption (YoY)	-7.3%	-13.8%	10.5%	3.0%	3.0%
Primary surplus (% GDP)	-0.4%	-6.5%	-3.2%	-2.5%	-1.5%
EMBI Argentina (spread in bps, eop)	1744	1350	1600	950	750
Public net debt (% GDP)	43.6%	53.3%	44.3%	44.8%	46.0%
Soybean price in USD per ton (annual average)	327	350	500	480	480
Exports of goods (USD billion)	65.1	54.9	77.7	82.4	86.9
Imports of goods (USD billion)	49.1	42.4	63.5	67.8	73.2
Trade balance (USD billion)	16.0	12.5	14.1	14.6	13.7
Current account (% GDP)	-0.8%	0.9%	0.6%	0.7%	0.5%

Source: EconViews

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