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# Latam Daily: Peru's Inflation Drops in August

- Peru: Lower inflation brings end of hiking cycle into focus

## PERU: LOWER INFLATION BRINGS END OF HIKING CYCLE INTO FOCUS

Month-on-month inflation was **0.67% m/m** in August, slightly above our forecast and the Bloomberg market consensus (**0.6%**), but lower than that of July (**0.94%**) and August 2021 (**0.98%**).

Year-on-year inflation slowed more visibly for the second consecutive month, falling from **8.7% y/y** to **8.4% y/y**, though it remained above the 3% upper limit of the target for 15th consecutive month, approaching the previous prolonged period in which it remained outside the target range (16 months, between March 2015 and June 2016). Since 2000, the longest period with inflation above 3% was 21 months (between October 2007 and June 2009).

August's inflation reflected increases in food prices with a large weight in the consumer basket, but also showed the reduction in fuel and transportation prices. Of the 586 products that make up the consumer basket (base 2021), 410 (70%) rose, 105 (18%) fell, and 71 (12%) remained unchanged (table 1). **Core inflation also slowed, going from 5.43% in July to 5.38% in August**, this being the first sign of moderation in the more structural component of inflation. Other prices, such as wholesale, construction materials, and machinery and equipment prices likewise moderated. Moreover, inflation fell in 25 of the 26 most important cities in the country, reducing the number of cities where inflation exceeds 10% from 16 to 8.

Going forward, we expect the slowdown in inflation to continue, albeit at a gradual pace. The downward trend in inflation is supported by the effect of a higher statistical base given that inflation began to rise in July 2021 (around 1%) and remained high thereafter. In addition, we anticipate lower inflation resulting from the already visible reversal in soft commodity prices (grains), port costs, and fertilizers, although these have stabilized in recent weeks. Cost pressures are easing, with the drop of -0.27% m/m in wholesale inflation in August, reflected in a decrease from 12.6% to 10.3% in its year-on-year trajectory, the lowest rate since June 2021. This makes it more likely that inflation may have peaked in June (see chart 1).

Chart 1

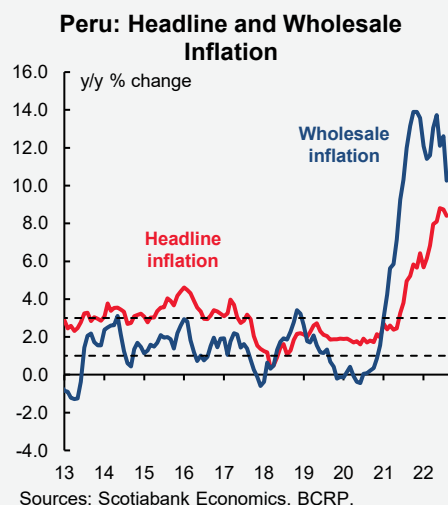


Table 1: Peru—Lima CPI Basket—August 2022

Groups of consumption	Base 2021	% m/m	% y/y
1. Food and non-alcoholic beverages	22.97	1.71	13.3
2. Alcoholic beverages, tobacco, drugs	1.61	0.28	2.3
3. Apparel and footwear	4.20	0.26	1.7
4. Housing, water, electricity, gas and others	10.55	1.23	7.7
5. Furniture and home maintenance	5.11	0.33	4.4
6. Health	3.48	0.67	3.8
7. Transport	12.40	-0.87	12.8
8. Communications	4.77	-0.13	1.3
9. Recreation and culture	3.96	0.21	7.1
10. Education	8.61	0.68	3.8
11. Restaurants & hotels	15.89	0.63	9.5
12. Other goods and services	6.47	0.51	5.6
<b>Total CPI</b>	<b>100.00</b>	<b>0.67</b>	<b>8.4</b>

\*Adjusted base to 12 from 8 groups of consumption.  
Sources: Scotiabank Economics, INEI.

September 2, 2022

**Our inflation forecast remains at 7.4% for 2022 and 4.0% for 2023, as published in the July 29, 2022 edition of the Latam Weekly.** We think the pace of disinflation will be slow going forward. This will become clear in September, since inflation is likely to be similar to or somewhat higher than that of September 2021 (0.40% m/m), which would stabilize the year-on-year trajectory. However, the statistical base will again play out in favor of disinflation in October, as the October 2021 rate was 0.58% m/m.

In the last twelve months, the central bank raised its reference rate by 625 basis points to 6.50% and raised reserve requirements three times. The 12-month inflation expectations began to break in July, going from a record of 5.35% to 5.16% according to the July BCRP survey. We see this trend as likely to have continued into August. The real interest rate (1.36%) is close to the neutral rate (1.50%), so we believe that we are close to the end of the BCRP interest rate hike cycle. **We assign a significant probability that the reference rate will remain at 6.50% at its next meeting on Thursday, September 8. A 25bps hike is less likely, but possible if the BCRP seeks to ensure convergence towards the target range.**

—Mario Guerrero

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