March 10, 2021

Latam Daily: Mixed February Inflation Trifecta in Chile, Colombia, and Mexico

- **Chile: February inflation slowed to 0.2% m/m (2.8% y/y)**
- **Colombia: February inflation surprised to the upside as consumer confidence strengthened**
- **Mexico: February sequential inflation slowed, but level effects pushed annual inflation further into the upper half of Banxico's target range**

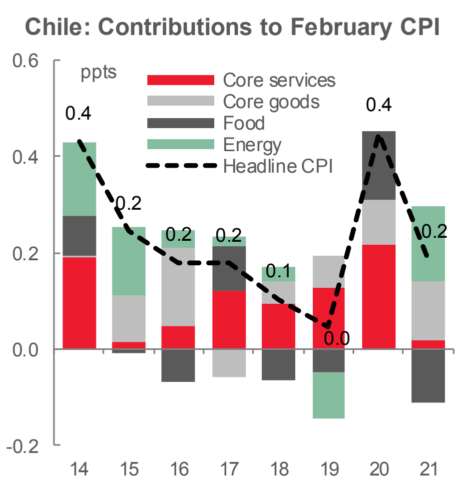
CHILE: FEBRUARY INFLATION SLOWED TO 0.2% M/M (2.8% Y/Y)

February CPI data, released on Monday, March 8, disappointed super inflationary views with a slowing in price gains from 0.7% m/m in January to 0.2% m/m in February; this brought headline annual inflation down from 3.1% y/y to 2.8% y/y. February's sequential monthly inflation rate came in slightly below our expectations of 0.3% m/m, and well under forward pricing of 0.44% m/m.

February's monthly inflation was largely explained by increases in fuel prices (i.e., gasoline and LPG) and sustained price pressures amongst core goods (ex. food and energy), both of which have a high transitory component (chart 1). On the other hand, February saw a significant decline in food prices (i.e., fruits, vegetables, and dairy products) that almost completely reversed the surprising rise we saw in January (chart 1, again). In addition, declines in the prices of recreational services, cultural products, and educational services brought down sequential core services inflation from January to February in a move that ran contrary to usual seasonal patterns.

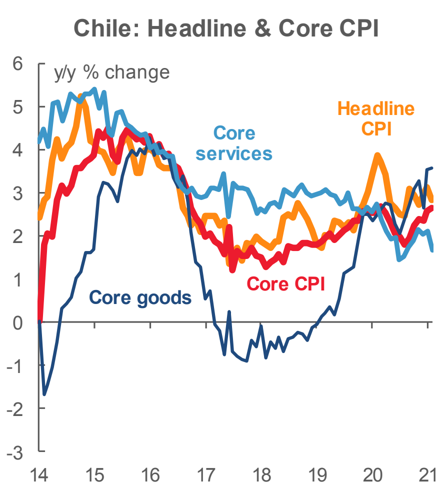
Among the rises in core goods prices, new cars (1.9% m/m), mobile phone equipment (3.3% m/m), and used cars (4.6% m/m) saw some of the most marked gains. The increases in these goods prices showed that the positive

Chart 1



Sources: Scotiabank Economics, INE.

Chart 2



Sources: Scotiabank Economics, INE.

CONTACTS

Brett House, VP & Deputy Chief Economist
416.863.7463
Scotiabank Economics
brett.house@scotiabank.com

Guillermo Arbe
51.1.211.6052 (Peru)
Scotiabank Peru
guillermo.arbe@scotiabank.com.pe

Sergio Olarte
57.1.745.6300 (Colombia)
Scotiabank Colombia
sergio.olarte@scotiabankcolpatria.com

Jorge Selaive
56.2.2619.5435 (Chile)
Scotiabank Chile
jorge.selaive@scotiabank.cl

Eduardo Suárez
52.55.9179.5174 (Mexico)
Scotiabank Mexico
esuarezm@scotiabank.com.mx

TODAY'S CONTRIBUTORS:

Carlos Muñoz
56.2.2619.6848 (Chile)
Scotiabank Chile
carlos.munoz@scotiabank.cl

Waldo Riveras
56.2.2619.5465 (Chile)
Scotiabank Chile
waldo.riveras@scotiabank.cl

Jackeline Piraján
57.1.745.6300 (Colombia)
Scotiabank Colombia
jackeline.pirajan@scotiabankcolpatria.com

Paulina Villanueva
52.55.5123.6450 (Mexico)
Scotiabank Mexico
pvillanuevac@scotiabank.com.mx

liquidity shock received by households stemming from the withdrawal of pension assets is still present. On the other hand, the low rate of inflation in core services was driven by flat prices for transport services during the month, an unusual development during February's usual vacations that reflects ongoing mobility restrictions.

The diffusion of the CPI in February (i.e., the percentage of items with positive monthly inflation) was 50.2%, at the bottom of the historical range for the month. This was explained by low diffusion in services prices (36.3%), which was under the record low for the month due to ongoing mobility restrictions and still-weak domestic demand. The second withdrawal of pension assets mostly supported purchases of consumer goods rather than services, and even this effect began to fade in February. Diffusion of goods prices stood at 56.5%, around its historical average for the month.

Although headline annual inflation slowed in February, a cycle-high in annual core goods inflation offset a further dampening in core services price gains (chart 2)—in line with patterns reflected in the sequential monthly numbers. February's print validated view that the high inflationary numbers we saw in December and January reflected the temporary effects set off by the second withdrawal of pension assets and public liquidity measures focused on sustaining household incomes.

Regarding the imputation of prices while pandemic-control measures continue to impede usual data collection methods, the INE reported that its carry-over method (i.e, zero monthly price variation) was maintained in February for air-transport services, tourist packages, and movie tickets, among others. For March we do not expect changes to these methods unless the INE reports otherwise in the coming days.

Looking forward, we project a sequential inflation rate of 0.4% m/m in March. Given current international prices, fuels should continue to inject some inflation into Chilean prices until at least April. This expectation also considers the seasonal change (i.e., increase in quality premiums) that ENAP applies in March to fuel sold in the Santiago metropolitan region, which implies price increases at the wholesale level. Likewise, in March we should see gains in educational services prices, which are normally adjusted this month. A monthly rate of 0.4% m/m implies annual inflation would reach 3.0% y/y this month.

We maintain our 3.0% y/y projection for December 2021. The inflationary pressures we saw in December 2020 and January 2021 should abate in the coming months as the weakness of the labour market and the multilateral appreciation of the peso come to be reflected more fully in domestic prices. Finally, products with high weights in the CPI, such as electricity and multimodal transport, are set to have their prices continue to be reported under the imputation method, which would also dampen official inflation numbers.

—Carlos Muñoz, & Waldo Riveras

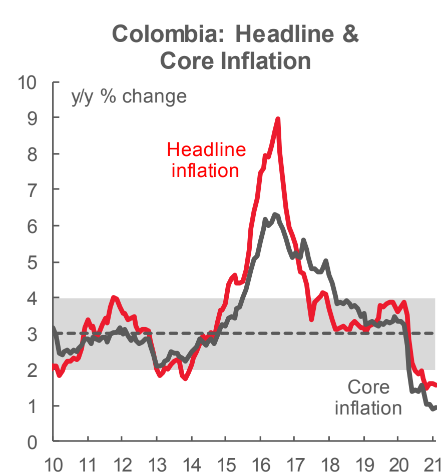
COLOMBIA: FEBRUARY INFLATION SURPRISED TO THE UPSIDE AS CONSUMER CONFIDENCE STRENGTHENED

I. February inflation surprised to the upside and affirmed our expectation of BanRep rate hikes later in 2021

February inflation, published late on Friday, March 5, by DANE, came up from January's 0.41% m/m to 0.64% m/m, above market consensus and our own projection (0.51% m/m Bloomberg and 0.45% m/m Scotiabank Colpatria). Core inflation at 0.67% m/m (up from 0.21% m/m in January) was also above the market consensus expectation of 0.51% m/m, reflecting increased price pressures outside of volatile foodstuffs—a signal of a strengthening economic environment and further normalization of prices. In core prices, the education sector led increases as Colombia's re-opening strategy drove the resumption of in-person classes.

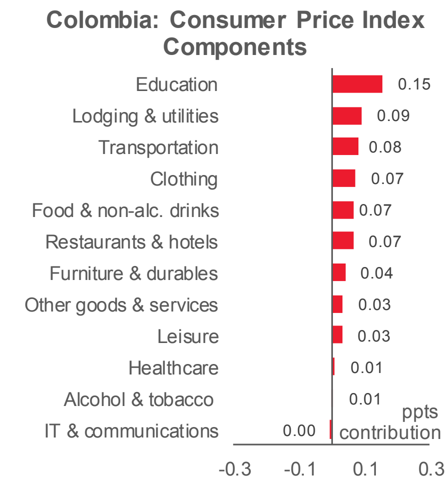
The sequential monthly numbers translated into a slight drop in annual headline inflation from 1.60% y/y in January to 1.56% y/y in February, close to a record low (chart 3). At the same time, annual core inflation increased from 0.89% y/y in January to 0.93% y/y in February.

Chart 3



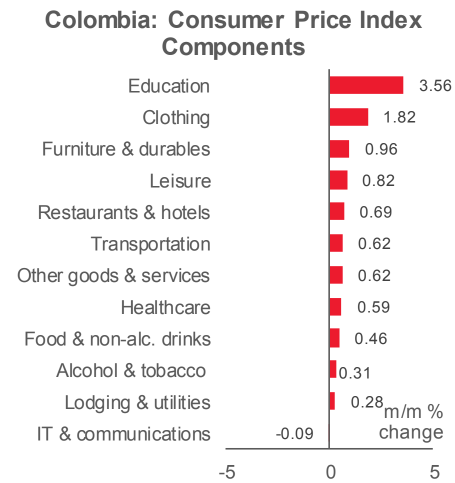
Sources: Scotiabank Economics, DANE.

Chart 4



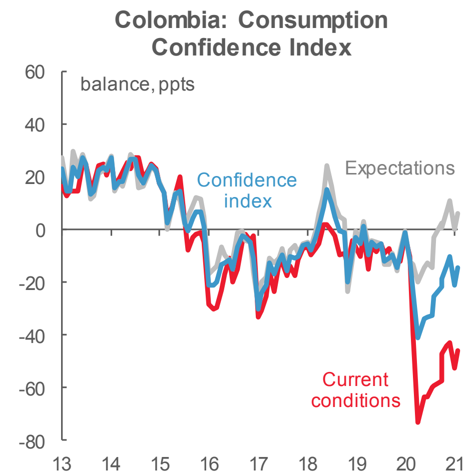
Sources: Scotiabank Economics, DANE.

Chart 5



Sources: Scotiabank Economics, DANE.

Chart 6



Sources: Scotiabank Economics, Fedesarrollo.

February's inflation print is a positive surprise since it likely stemmed from a consolidation of the economy's recovery path. In fact, 11 out of the 12 sectors contributed positively to the monthly inflation rate of 0.64% m/m (chart 4). The education sector made the strongest monthly contribution at 15 bps from a sectoral rise in prices of 3.56% m/m (chart 5), which showed the effects of the second round of Colombia's re-opening. Lodging and utilities prices were the second strongest contributors to February's inflation rate at 9 bps on the back of 0.28% m/m gains; rental fees added 6 bps, as extraordinary deferrals and freezes expired and rental rates resumed gains at a pace in line with that of the previous year. Other items, such as transportation (0.62% m/m), restaurants & hotels (0.69% m/m), clothing (1.82% m/m), and furniture and durables (0.96% m/m) contributed positively too. Clothing prices and prices of some home appliances showed a reversal effect (i.e., gains) in the wake of the VAT holiday in November, gains that also reflected DANE's data collection procedures and higher import costs. Foodstuff inflation was lower than in the previous February (0.46% m/m versus 0.93% m/m in February 2020) as this year's climate effects have been less aggressive than in 2020.

Looking at annual inflation across major broad categories, goods inflation increased by 65 bps to 1.07% y/y, services inflation fell -13 bps from 1.04% y/y to 0.91% y/y, and regulated-price inflation came down by -11 bps to 0.83% y/y. As previously noted, core inflation rebounded: ex-food inflation came in at 0.93% y/y (up about 5 bps from January), while ex-food and regulated-price inflation increased by 9 bps from January to 0.96% y/y in February. Low-income households continued facing higher annual inflation (2.15% y/y) than high-income households (0.95% y/y).

February's inflation results combined with better economic activity data affirmed our baseline forecasts that anticipate the beginning of a normalization path in monetary policy rates in the latter part of 2021—and removed the possibilities of rate cuts in the short term. We still expect that the 2021 annual inflation rate should converge to a level slightly below BanRep's 3% y/y target by end-2021 (i.e., 2.8% y/y). We also anticipate that base effects could dampen year-on-year inflation numbers in March 2021, but the annual inflation rate is expected to begin rising again by Q2-2021 as the economy continues on its recovery path. Nevertheless, we expect the BanRep Board to keep its benchmark policy rate on hold at 1.75% until at least September-2021, when we look for a first hike.

II. February consumer confidence indicators neared pre-COVID-19 levels on increased optimism about the future

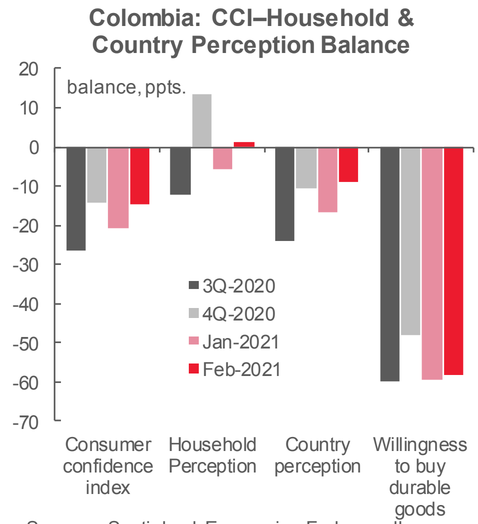
February's Consumer Confidence Index (CCI), in a release on Monday, March 8, stood at -14.6 ppts, an improvement of 6.2 ppts from January's level of -20.8 ppts. This brought the index closer to levels observed one year ago (Feb 2020: -11.2 ppts, chart 6). February's rebound in sentiment came during a reduction in new COVID-19 cases, which enabled a fresh round of economic re-opening amid announcements of the rollout of vaccines. Expectations about the future remain even better than their pre-pandemic levels. This being said, ebbs and flows in pandemic-related restrictions are still the key drivers of consumer confidence these days, and we expect household sentiment to keep improving as the current re-opening phase rolls on.

Looking at February's details (chart 6 again):

- **The CCI increased to -45.8 ppts versus January's -52.5 ppts.** This occurred on the back of less pessimism about current households' conditions; and
- **The Expectations Index rebounded to 6.2 ppts, an increase of 5.9 ppts from January and better than Feb-2020 reading of -12 ppts.** This gain was led by a better assessment of the future economic situation from -34.8 ppts in January to -19.1 ppts in February.

Despite these overall gains, Colombian consumers' willingness to buy durable goods remained soft, with a small improvement from -59.4 ppts in January to -58.2 ppts in February (chart 7). We expect this sentiment to improve as the latest phase of the re-opening extends further amidst the distribution of vaccinations.

Chart 7



Sources: Scotiabank Economics, Fedesarrollo.

At the regional level, consumer confidence numbers improved in four out the five major cities surveyed, with Bucaramanga leading the gains. On the other hand, Bogota and Medellin were still the cities with the worst consumer sentiment. Consumers' willingness to buy houses improved by 1.7 ppts on better sentiment in Cali and Bucaramanga and in the middle-income population.

By socio-economic levels, February's indices painted a positive picture for middle- and low-income earners' confidence, which improved by 4.3 ppts and 9.6 ppts, respectively. In contrast, the overall index for high-income populations fell by -4.7 ppts.

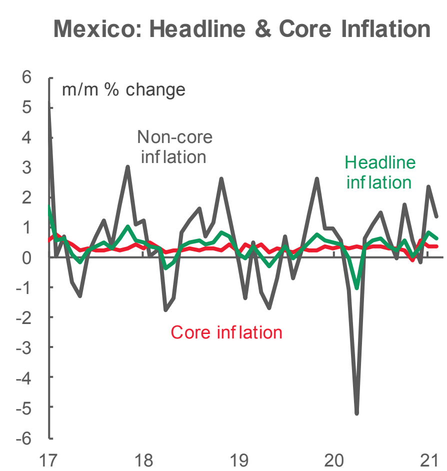
Following February's rebound in consumer sentiment, we expect confidence to keep improving with the new re-opening's further advance, but the pace of gains will be slow in the midst of still-challenging labour-market dynamics.

—Sergio Olarte & Jackeline Piraján

MEXICO: FEBRUARY SEQUENTIAL INFLATION SLOWED, BUT LEVEL EFFECTS PUSHED ANNUAL INFLATION FURTHER INTO THE UPPER HALF OF BANXICO'S TARGET RANGE

Inflation for February, released by INEGI on Tuesday, March 9, came in at 0.63% m/m, down from 0.86% m/m in January (chart 8). This was slightly above the average expected by the market (0.58% m/m) and our 0.50% m/m forecast. Most of the upside surprise came from the advance in energy prices.

Chart 8

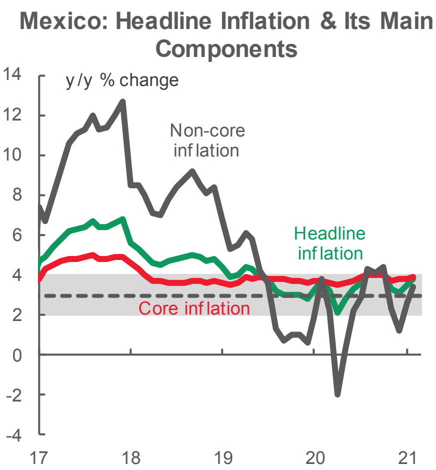


Sources: Scotiabank Economics, INEGI.

Owing to level effects, February's print pushed annual inflation further into the upper half of Banxico's target range of 3% y/y +/- 1 ppt, rising from January's 3.54% y/y to 3.76% y/y (chart 9). Price rigidities showed themselves in core inflation's rise from 0.36% m/m (3.84% y/y) to 0.39% m/m (3.87% y/y). CPI's non-core component advanced from 2.63% y/y in January to 3.43% y/y in February**.** Energy-products' price inflation accelerated from 2.66% y/y in January to 6.83% y/y in February, the highest pace since April 2020 (chart 10). Disruptions in the energy market have driven this rise. Agricultural-product price increases partially offset the rise in energy prices, moderating from 2.65% y/y in January to 0.66% y/y in February—owing mainly to the -8.57% drop in fruit and vegetable prices.

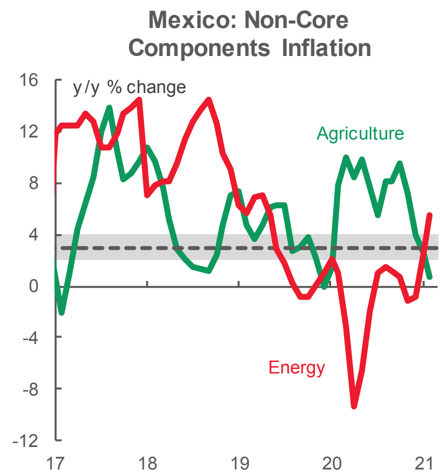
Annual goods inflation rose from 5.41% y/y in January to 5.54% y/y in February (chart 11). Meanwhile, annual services inflation declined from 2.13% y/y in January to 2.06% y/y in February.

Chart 9



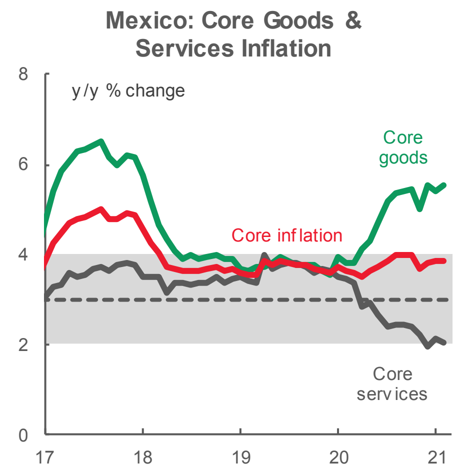
Sources: Scotiabank Economics, INEGI.

Chart 10



Sources: Scotiabank Economics, INEGI.

Chart 11



Sources: Scotiabank Economics, INEGI.

The trajectory of inflation remains within the range of variability established by Banco de México. The February price numbers were in line with the most recent forecasts published by Banxico. Inflation is still expected to moderate toward the third quarter of the year and the February print doesn't change our rate outlook where we foresee a window of opportunity for at least one more -25 bps rate cut during Q2/Q3.

—Paulina Villanueva