

Latam Daily: Colombia October CPI, Affirms Our Call for December Hike

- Colombia: October CPI lands below expectations due to VAT holiday; dynamic affirms our call for December hike

COLOMBIA: OCTOBER CPI LANDS BELOW EXPECTATIONS DUE TO VAT HOLIDAY; DYNAMIC AFFIRMS OUR CALL FOR DECEMBER HIKE

Monthly CPI inflation was 0.01% m/m in October 2021, according to DANE data published on Friday, November 5. This result was below the median forecast in BanRep's survey (0.18% m/m), Bloomberg's survey (0.22% m/m), and Scotiabank Economics' projection (0.20% m/m). Foodstuff inflation led the gains, while the VAT holiday more than offset price increases.

October's CPI result brings annual headline inflation to 4.58% y/y, up from **4.51% y/y in September** (chart 1), still above the ceiling of BanRep's target range (2%–4%) for the third month in a row and the highest since mid-2016. Core inflation fell again from 3.03% to 2.86% y/y, while ex-food and regulated goods inflation was 2.02% y/y (down from 2.28% in the previous month). Reduction in core inflation was mainly due to the temporary impact of the VAT holiday, however, it would contribute to lower indexation effects and should have a more lasting effect since November and December will also have more VAT holidays.

The previous dynamic could lead to ongoing divided opinions at the central bank's Board in relation to inflation expectations and rates. Our base-case scenario is now of a 50 bps hike at the December 17 monetary policy meeting. For 2022 we expect the monetary policy rate to close at 5% (from a previous expectation of 4.50%). Find all our recently updated forecasts in Friday's *Latam Weekly* [here](#).

Looking at the Colombia's October CPI numbers in detail, 2 out of 12 sectors retreated (charts 2 and 3), which was enough to offset positive pressures of foodstuff prices. The main highlights are:

- Foodstuff and restaurants inflation had the larger contributions (+15 bps and +9 bps, respectively).** In the case of foodstuff inflation (+0.89% m/m), main gains came from meat (+1.54% m/m), milk (+1.94% m/m) and fresh fruits (+3.53% y/y). Meat and milk prices are showing impacts of scarcity due to climate issues but in the case of meat due to a higher trade effect since this year Colombia increased meat exports.
- However, some key prices continued declining, mainly eggs (-2.83% m/m) pointing to some normalization after the significant impact from the nationwide strike earlier this year, and rice (-3.68% m/m).** Restaurant & hotel's inflation in October contributed to the overall inflation to the same degree as in the previous month, due to higher food prices.
- The VAT holiday contributed to reducing the overall inflation figure as clothing prices posted a contraction of 3.45% (-12bps), a similar**

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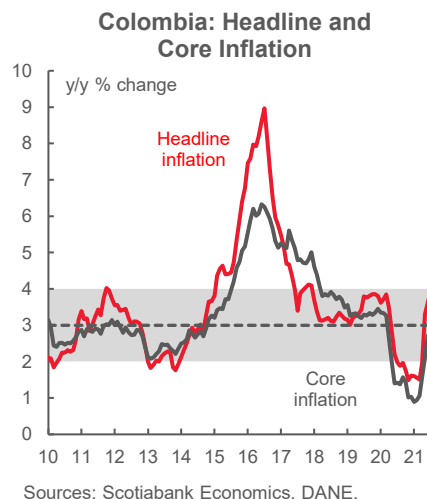
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Chart 1



reduction to that observed the previous year during the VAT holiday of November. This effect would contribute to a moderate indexation effect ahead of 2022, however it is a temporary factor that will be reversed early in 2022.

- **Another negative contribution came from the information and communications sector (-6.79% and -26pbs), as a result of a new campaign from the new competitor in the telecom services sector.** We don't expect this to happen again in the near future.

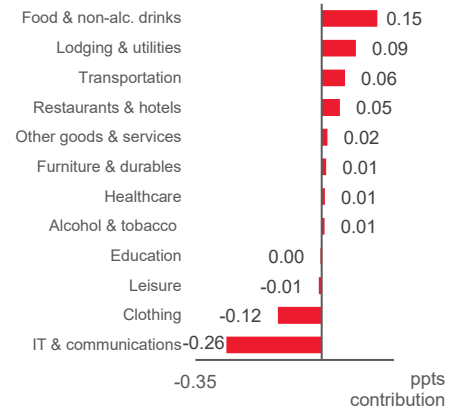
Looking at annual inflation across major categories, goods inflation fell to 2.63% y/y (versus 2.97% y/y in September), while services inflation fell by 23 bps from 2.01% y/y to 1.79% y/y. Regulated-price inflation increased by 20 bps to 6.14% y/y, due to utility fees which are facing effects from the exchange rate depreciation but also normalization after subsidies implemented one year ago.

Having landed below expectations, October's inflation will likely moderate overall year-end inflation expectations, which is key since indexation effects would be lower. The core inflation metric also fell due to a temporary factor (VAT holiday), however, we think it won't significantly change the central bank's discussion as normalization in the monetary policy rate is responding more to a better economic activity expectations. That said, in terms of monetary policy, our base case scenario is now of a 50 bps rate hike for the December 17 BanRep meeting, likely still with a split decision. In 2022, we would face a new acceleration in inflation as VAT holiday effects would be reversed, which is why despite Friday's good news regarding inflation, we still expect a hawkish rate hike in December.

—Sergio Olarte & Jackeline Piraján

Chart 2

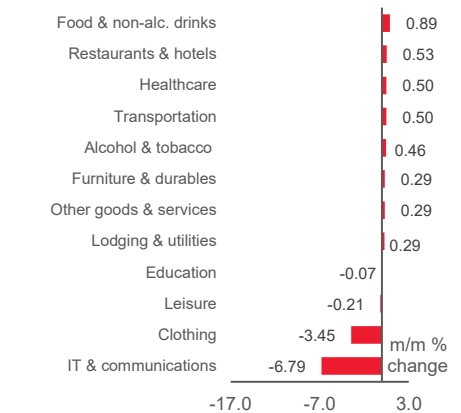
Colombia: Consumer Price Index Components



Sources: Scotiabank Economics, DANE.

Chart 3

Colombia: Consumer Price Index Components



Sources: Scotiabank Economics, DANE.

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