

# The absence of inflationary pressure and need for greater monetary stimulus is reaffirmed

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Have the MPR cuts finished? The message from the Central Bank - which had been followed to the letter by a significant part of the market - was that there would be no further MPR cuts in the foreseeable future under this baseline scenario. However, this CPI record confirms the economy's extremely constrained inflationary pressures, the misalignment of the baseline scenario and puts the anchoring of inflation expectations at serious risk, backing up our forecast of an imminent cutback.

This month's monetary policy meeting should at least include the cutback option to pave the way for a 25 bp. adjustment not beyond August as we have been saying over the last few months.

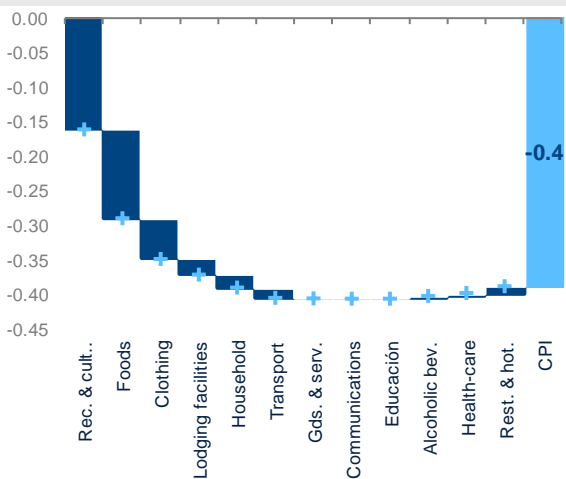
Night has fallen on inflation, with a genuine surprise not just for the market but also for the Central Bank. Indeed, we were hoping for a more constricted fall in prices, but the fact that we have had some surprises with respect to our disinflationary bias (IPC June -0.4%; BBVA -0.1%/-0.2%, Bloomberg 0%; EEA 0.1%, EOF 0%) only backs up our forecast that after a respite, a new round of cuts will be backed up not by downturns in activity but by a fall in inflation. The task of bringing inflation back towards the centre of the target range will not be easy and must be accompanied by the necessary currency depreciation the Central Bank so fears.

The CPI for May recorded a monthly variation of 0.1% m/m (2.6% YoY), in the middle portion of the different market expectations (Forwards: 0%; Bloomberg: 0.1%; EEA: 0.2%, BBVAe: 0% MoM) At division level, the main positive impacts come, surprisingly, from Leisure and culture, due to the sharp rise shown by the "tourist" package product, which increased 25.7% MoM, with an impact of +0,2pp on the month's inflation, followed by the Housing and basic services division (+0.08pp). We remind you that since January this year the INE started to apply a methodological adjustment on this asset. The striking thing about it is the significant volatility it has injected into the series. Furthermore, this rise is difficult to digest when compared with historical patterns, despite the justification the INE provides of a rise in the exchange rate (2.4% MoM) and increase in demand, as furthermore, we must remember that there is a significant increase in the competition and price offer in this sector (Graph 1). **Here we raise a (high) risk of reversal of the tourist package for the June CPI, although, without waiting for adjustments in the new methodology implemented by the INE, it is becoming more likely that the new volatility of this asset will have a very significant impact in the opposite direction.**

The SAE inflation, which excludes the basket's most volatile products (food and energy), recorded a rise of **0.3% MoM (2.5% YoY)**, above market expectations (**0.1% MoM**), due to the **0.2pp impact of the tourist package, not foreseen by the market**. Thus, the assets SAE increased 0.7% MoM (0.8% YoY) and the services SAE 0.1% MoM (3.6% YoY). Among the services, the main impacts come from the air transport (+0.03pp) and common expenditure service (+0.05pp).

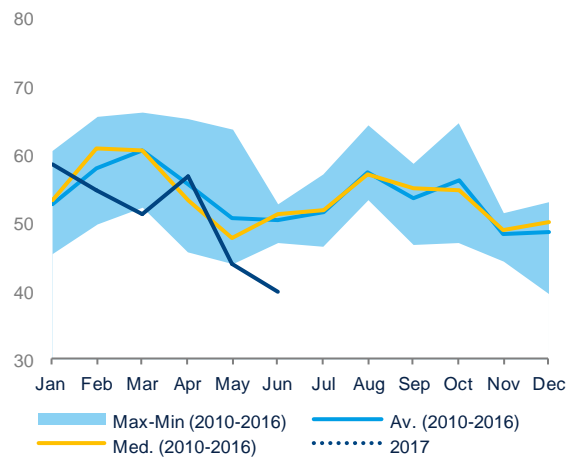
**Inflationary diffusion (percentage of products that increase in price in the month) stood at 43.9%**, at the minimum of the range observed in the period 2010-2016 (Graph 2). This confirms that the basket shows very low inflationary pressures. If the high impact of the tourist package and air transport service had not occurred, inflation would have fallen markedly into negative territory, both in its total level and in its SAE assets and services analytic indicators.

**Figure 1.** Monthly impacts on the June CPI (var. % MoM)



Source: INE and BBVA Research

**Figure 2.** Inflationary diffusion (% products with positive monthly inflation)



Source: INE and BBVA Research