



# Inflation Observatory

July 7, 2009

After several months of falls, June inflation increases by 0.3%

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- In June inflation rose by 0.3%, exceeding expectations.
- Over twelve months, inflation has increased by 1.9%, below the Central Bank's target range.
- The sectors which made the largest positive contributions were Transport and Accommodation, Water, Electricity, Gas and other Fuels.
- We have revised our inflation forecast for the end of 2009 to -0.1%.
- Inflation and activity indicators hint at a 25 bps cut in the Monetary Policy Rate.

**June inflation:** After several months of falling prices (with the exception of March), the general price index increased by 0.3% compared to May, and by 1.9% over twelve months. It should be noted that, whilst this is above expectations (0% BBVA), it implies that for the first time since October 2004 annual inflation is under 2%, which is the lower limit of the Central Bank's target range.

The sectors which mainly accounted for this increase were Transport, which increased by 1.5% with an incidence of 0.284, and Accommodation, Water, Electricity and other Fuels, which changed by 1.6% with an incidence of 0.203. Food increased by 0.2%, contributing 0.028 to the change in the month. The price falls for Clothing and Shoes and Leisure over recent months continued, although their incidence of -0.1% was not sufficient to offset price increases elsewhere.

Core inflation (CPIX), which excludes non-processed food and fuel, performed as expected (0%), whilst CPIX1, which also excludes regulated prices, dropped by 0.2%. In year-on-year terms, the CPIX was 3.6%, and the CPIX1 was 3.0%.

**Wages:** In May, the accrued nominal change in the General Hourly Wage Index for twelve months was 6.7%, a change in real terms of 3.6%. The nominal change in the General Labor Cost Index over 12 months was 7.3%.

**Inflation Outlook:** For July, August and September, we expect inflation rates of 0.2%, 0.1% and 0.2%, respectively. It should be noted that the high basis for comparison for the CPI for these months in 2008 means that the twelve month inflation rate for July will fall to 1%, and from September it will be negative, finishing the year at -0.1%.

## Appraisal:

**The Monthly Economic Activity Indicator (IMACEC) for May (-4.4%) hints that the recovery in economic activity is being pushed back to the third quarter, and this is contributing to the low inflation rates seen in the first months of the year.**

**As a result, we expect the Central Bank to reduce the monetary policy rate by 25 bps at its next meeting.**

## INFLATION FORECASTS

BASE SCENARIO

Date: July 7, 2009

MONTHLY CHANGE			
	CPI	CPIX	CPIX1
Jan-09	-0.8	-0.2	-0.4
Feb-09	-0.4	-0.3	0.2
Mar-09	0.4	0.6	0.8
Apr-09	-0.2	-0.2	-0.1
May-09	-0.2	-0.3	-0.5
Jun-09	0.3	0.0	
Jul-09	0.2	0.1	
Aug-09	0.1	-0.1	
Sep-09	0.2	0.0	
Oct-09	0.1	0.1	
Nov-09	0.1	0.2	
Dec-09	-0.1	0.0	
Jan-10	-0.2	-0.2	
Feb-10	0.5	0.2	
Mar-10	0.3	0.2	
Apr-10	0.0	-0.1	
May-10	0.0	-0.2	
Jun-10	0.0	-0.1	
Jul-10	0.2	0.0	
Aug-10	0.3	0.0	
Sep-10	0.3	0.0	
Oct-10	0.4	0.0	
Nov-10	0.4	0.1	
Dec-10	0.0	0.0	

YEAR-ON-YEAR CHANGE			
	CPI	CPIX	CPIX1
Jan-09	6.3	8.0	6.9
Feb-09	5.5	6.7	6.7
Mar-09	5.0	6.5	6.2
Apr-09	4.5	5.5	5.3
May-09	3.0	4.4	3.7
Jun-09	1.9	3.6	3.0
Jul-09	1.0	2.6	
Aug-09	0.1	1.8	
Sep-09	-0.8	0.9	
Oct-09	-1.5	0.4	
Nov-09	-1.2	0.0	
Dec-09	-0.1	0.0	
Jan-10	0.5	0.0	
Feb-10	1.3	0.4	
Mar-10	1.2	0.1	
Apr-10	1.4	0.2	
May-10	1.7	0.3	
Jun-10	1.4	0.3	
Jul-10	1.3	0.2	
Aug-10	1.5	0.2	
Sep-10	1.7	0.2	
Oct-10	2.0	0.1	
Nov-10	2.3	0.0	
Dec-10	2.4	-0.1	