

Brazil | Inflation stopped falling in May but will continue to trend down going forward

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After falling significantly in the last three months, annual inflation reached 9.32% in May, slightly higher than in April (9.28%) thanks to higher-than-expected pressure from food and regulated prices. Even though these factors create upside risks, we expect inflation to continue to lose steam in the next few months.

As in April, inflation surprised to the upside in May...

Inflation reached 9.32% YoY (0.78% MoM) in May, somewhat higher than expected (BBVA: 9.22% YoY; consensus: 9.28% YoY). As in April, pressures from food and mainly regulated prices were the main drivers of higher-than-expected inflation. Food inflation reached 12.7% YoY in May, less than in April but more than expected, mainly due to supply issues. Regarding administered prices, they increased 10.9% YoY in May, in comparison to 10.7% YoY in April. In monthly terms they increased 1.4% MoM (vs. 0.7% in April and 1.22% MoM in May 2015) mainly due to adjustments in the tariffs of water, sewage and electricity as well as in medicine prices.

... adding an upward bias to our forecasts and making a monetary easing in the next few months less likely

In our view, inflation will continue to ease during the remainder of the year, as both food and regulated prices are expected to moderate moving forward and, moreover, the ongoing recession should further impact domestic prices. We forecast Brazil's IPCA to reach 8.8% YoY, 8.2% YoY, and 6.8% YoY at the end of 2Q16, 3Q16 and 4Q16, respectively. However, after the recent upward surprises in inflation, we add an upward bias to these forecasts. Anyway, although prospects of falling inflation remain in place, recent upward surprises reinforce our view that a monetary easing cycle will not be launched by the BCB in the short-term.

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