Scotiabank

GLOBAL ECONOMICS

LATAM DAILY

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Latam Daily: Chile Inflation Overshoot

CHILE: JULY CPI AT 0.9% (4.3% Y/Y), WITH WIDESPREAD INCREASES ACROSS ALL DIVISIONS

- **Monetary policy has no room for cuts in the face of consecutive surprises in core inflation and an acceleration in non-mining GDP. A likely path to neutral bias on monetary policy.**

On August, Friday 8th, the INE released the July CPI, which rose 0.9% m/m and leaves annual inflation at 4.3%, representing a significant upside surprise for the market and the central bank (BCCh) scenario. While awaiting the August CPI prior to the September Monetary Policy Report (IPoM,) it is highly likely that the central bank will revise upwards its projection for headline and core inflation, postponing convergence to 3% and, consequently, the arrival of the policy rate to its neutral level.

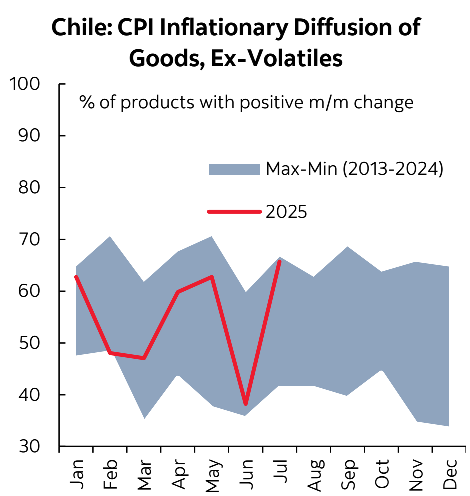
The surprise did not come from volatile items but from those more closely linked to domestic demand, which has shown renewed dynamism, as evidenced in the June GDP growth, with a seasonally adjusted acceleration in all sectors except mining. Furthermore, this is the second upward surprise in core inflation (+0.2 ppts in July) after the one observed in the June CPI (+0.2 ppts in June).

We estimate that the central bank could opt, as it did last January, to introduce a neutral bias at the September meeting given the increased inflationary risks stemming this time from domestic activity (which is accelerating) as well as recent inflationary developments. A further postponement in the inflation convergence estimate could lead to symptoms of inflationary de-anchoring in prices similar to those observed at the end of 2024 and the beginning of this year, which would warrant a neutral bias, as was the case in the January 28th statement.

Of particular relevance will be the economy's capacity to absorb the new cost shock from the electricity rate hike reflected in this CPI and, additionally, the increase in the mandatory pension contribution next August, along with a further increase in the minimum wage in January 2026. Too many temporarily concentrated supply shocks, high core inflation, external uncertainty, and accelerating non-mining activity may be sufficient ingredients to move to a neutral stance.

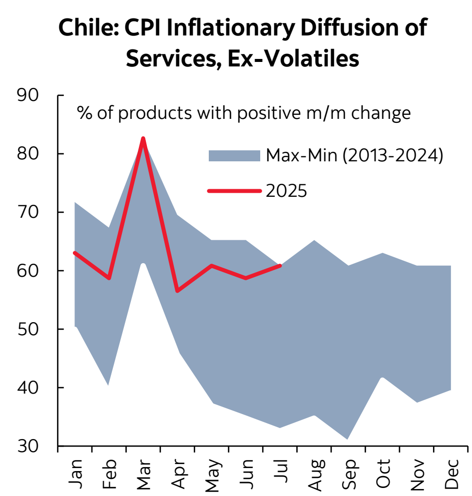
Inflationary diffusions show persistent upward pressures in services, along with a recovery at the goods level, as expected following CyberDay events (charts 1 and 2). The total CPI diffusion reached a new high for July of 62.2% after hitting a low last month. While this behaviour was expected at the goods level, as a result of retail commercial strategies

Chart 1



Sources: Scotiabank Economics, INE.

Chart 2



Sources: Scotiabank Economics, INE.

during CyberDay events, the persistently high diffusion revealed by services, which remain at the upper end of their historical range, is concerning. This month, some services stand out for which we do not have visibility for pricing (accommodation services, dental services, restaurants, other health services), but which could be reflecting the impact of the high and successive increases in labour costs.

Electricity rates increased by 7% (+0.24 ppts). The housing division was the largest contributor for the month, followed by the food division, which was explained by higher prices for meat, dairy products, and non-perishables. Similarly, within the restaurants and hotels division, the increase in accommodation services was notable, with a 0.05 percentage point increase.

The main surprises were concentrated in the services CPI (excluding volatiles) and food. The most significant price increases in this regard were observed in telecommunications packages, accommodation services, and dental services, for which we have no visibility and therefore constituted a genuine upside surprise. In the food division, although the surprises were also significant, inflation in this division is at average levels for July, so we do not expect reversals in the next CPI. With this, combined with the core CPI surprise last June, we have revised upward our 2025 annual inflation projection from 3.5% to 4.0% y/y.

—Aníbal Alarcón