

Economic Analysis**Inflation continues its decline in July: 11.78%**

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Annual non-food inflation falls for the first time since October 2021, supporting moderation in the headline total

In July, monthly inflation was 0.50% and annual inflation 11.78%, above the average of market analysts' expectations in the Banco de la República survey (0.30%) and our forecast (0.38%). Compared to June, the annual figure decreased by 34 basis points (bps). Annual food inflation continued to show more moderate declines, as expected, standing at 13.2%, 104 bps below June's result. Annual non-food inflation was 11.4%, down 18 bps from the previous month's figure and falling for the first time since October 2021.

Although the annual change in the food basket continued to decline, within the food basket not all sub-baskets declined. The processed food basket went from an annual inflation rate of 17.4% to 15.4%, decreasing by 198 bps from the previous month, with reductions in annual changes in 82% of the items in the basket (weighted). The meat basket decreased from 10.6% to 9.7%, falling by 95 bps, with reductions in annual inflation in all sub-classes. On the contrary, the perishables basket registered an annual change 25 bps higher than the previous month, reaching 9.7%, despite this, 73% of the items in the basket (weighted by weight) showed decreases in the annual change.

As expected, food inflation continues to exhibit declines thanks not only to price moderation, but also to base effects, such as the meat and processed food sub-auctions. These base effects will be maintained in the coming months, ensuring a continuity in the downward path of food inflation. However, upward pressures could arise towards the end of the year close to the materialisation of the El Niño phenomenon.

Non-food inflation declined for the first time in almost two years. The sub-basket that explains this result to a greater extent is that of goods, which went from an annual inflation rate of 14.3% in June to 12.8% in July, decreasing by 142 bps. This result is mainly due to base effects. Within this, 20% of items (weighted) show reductions in annual variations, among which vehicles stand out. Meanwhile, other products that had also led the impulse within this basket months ago, such as clothing, cleaning and maintenance products, body care articles and beer and soft drinks, have shown moderations in recent months. This has been helped to some extent by the cumulative appreciation of the exchange rate so far this year and by a moderation in the international prices of these products.

The services basket, meanwhile, maintained some upward pressure on the aggregate core inflation outcome. In July, annual inflation reached 9.2% from 9.0% in June, increasing by 14 bps. In this case, the basis for comparison is relatively low. On the one hand, this result is explained by the existence of still high inflation pressures on rent and co-ownership related services, which show an indirect indexation to this index. Moreover, in the case of the former, measurement effects still show the adjustments made in the first half of the year on these prices. On the other hand, the increase is also explained by subclasses such as meals in table service establishments, which continue to reflect high demand, although it is beginning to moderate.

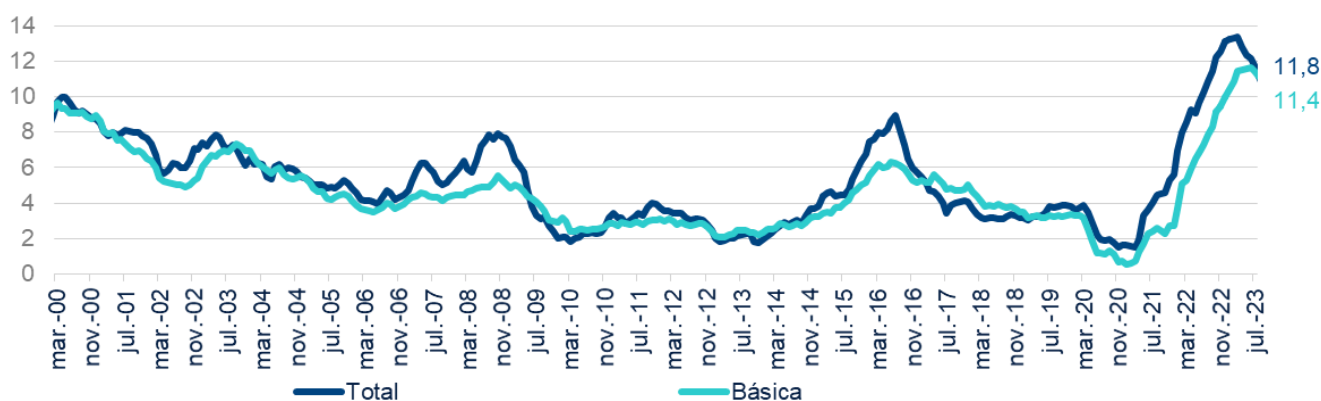
On the other hand, the basket of administered prices had an annual inflation rate in July of 15.8%, 21 bps above June's figure of 15.6%. In this result, 44% of the items in the basket (weighted) show reductions in annual

variations. Nevertheless, fuels continue to lead the upward pressures in view of the continuity of the increases decreed by the government. These increases are followed by increases in utilities such as water and sewerage and electricity, where the former is explained by the indirect indexation of this service to inflation, since by regulation entities are allowed to adjust tariffs after a cumulative inflation rate of 3%, an event that is repeated more frequently in a context of high monthly inflation.

Thus, three elements stand out for the analysis of non-food inflation. On the goods side, a moderating demand that will continue to facilitate reductions in annual basket inflation, albeit with risks from exchange rate volatility. From the services side, demand seems to be holding up, however, it is expected to moderate as consumption in general will do during the second half of the year, so it could also consolidate a moderation of the path, although with some limitations due to the effects of indexation and persistence present in this sub-basket. On the other hand, from the administered prices, indexation effects will be maintained by a certain spiral dynamic; however, to the extent that total inflation manages to consolidate higher deceleration rates, so will this basket. Its main risk is centred on the potential effects of the El Niño phenomenon on energy and gas costs, and the government's strategy of fuel price increases.

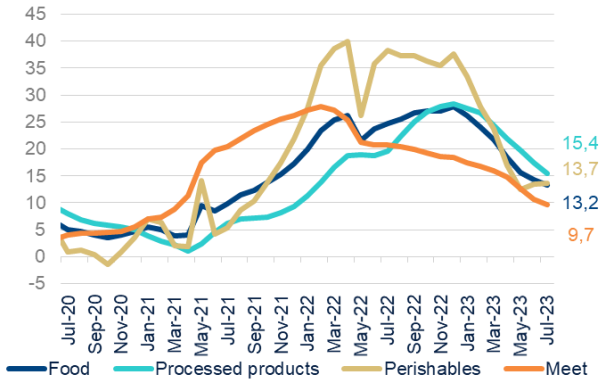
On the food side, we expect annual food inflation to continue moderating at a more gradual pace, with some upward pressure from the El Niño phenomenon. For core inflation, we anticipate a cycle of moderation in the coming months, limited by the increase in fuel prices. All in all, total inflation could close the year at around 9% and will continue to ease in 2024.

Figure 1. **HEADLINE INFLATION AND CORE INFLATION (ANNUAL CHANGE, %)**



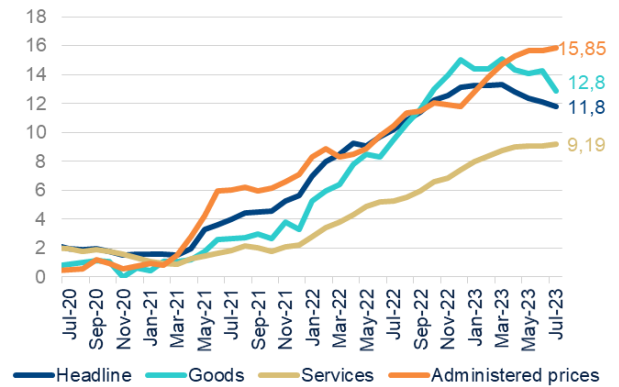
Source: BBVA Research with data from DANE

Figure 2. **FOOD INFLATION AND MAIN BASKETS (ANNUAL CHANGE, %)**



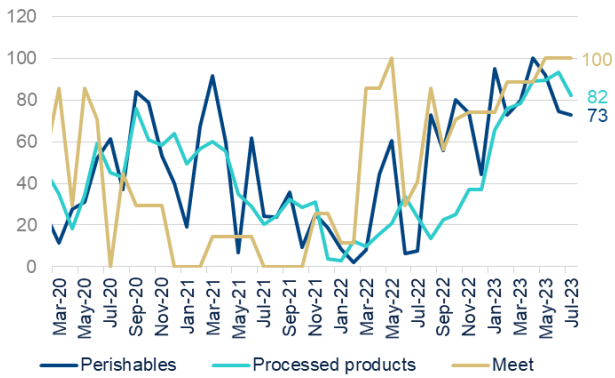
Source: BBVA Research with data from DANE

Figure 3. **CORE INFLATION AND MAIN BASKETS (ANNUAL CHANGE, %)**



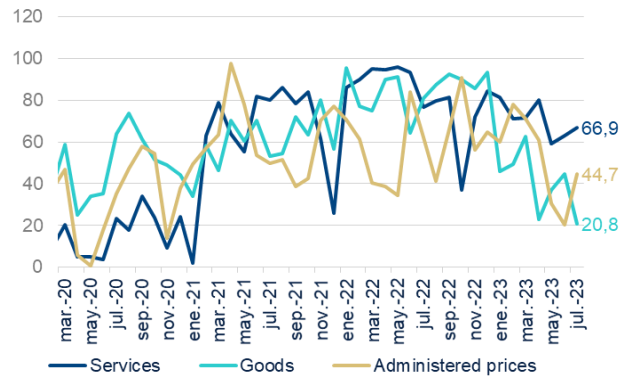
Source: BBVA Research with data from DANE

Figure 4. **FOOD SUB-CLASSES WITH REDUCTIONS IN ANNUAL CHANGES (WEIGHTED PERCENTAGE OF TOTAL BASKET)**



Source: BBVA Research with data from DANE

Figure 5. **NON-FOOD SUBCLASSES WITH REDUCTIONS IN ANNUAL CHANGES (WEIGHTED PERCENTAGE OF TOTAL BASKET)**



Source: BBVA Research with data from DANE

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