

Economic Analysis

In September, annual inflation stood at 11.0%, in line with analysts' expectations

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Food inflation is highly volatile, while core inflation remains high

In September, monthly inflation was 0.54% and annual inflation was 11.0%. The results were in line with market analysts' expectations (0.54% for the monthly variation, according to Banco de la República's survey) and ours (0.50%). The result was 43 basis points (bps) lower than the previous month's figure. Food inflation, on the other hand, decreased from 12.4% in August to 11.5% in September, which meant a reduction of 95 basis points. Likewise, core inflation fell in annual variation for the third consecutive month, from 11.2% in August to 10.9% in September, with an adjustment of 31 bps (Figure 1).

Food inflation accelerated its decline in September, with the perishable sub-basket once again playing a leading role, rising from 15.2% in August to 15.6% in September, increasing by 37 bps compared to the previous month (Figure 2). Within this, products such as tomatoes, fresh fruits and onions made the largest upward contributions, while products such as bananas, cassava and tree tomatoes contributed to the decline. On the other hand, the processed foods and meat baskets continued to reduce their annual inflation, reaching 11.2% and 8.0%, respectively. Within the processed foods, products such as dried vegetables and edible oils put downward pressure, while within the meat subbasket, poultry meat put upward pressure.

In this sense, food inflation continues to show high variations associated with its most volatile sub-basket: perishables, while the processed and meat sub-baskets are favored by base effects. Additionally, it is possible that the effect of the El Niño phenomenon, which is expected to have a greater impact towards the last months of this year and the first months of 2024, will generate additional increases.

In terms of core inflation, it declined in annual variation for the third consecutive month, from 11.2% in August to 10.9% in September, a reduction of 31 bps. On a monthly basis, core inflation continues to approach its 2011-2019 average, but maintains relatively high monthly variations.

The largest decrease came from the basket of goods, which declined by 140 bps versus the previous month, from 11.8% in August to 10.4% in September. The reduction is mainly explained by base effects, following the high levels of 2022. However, these base effects are due to the fact that monthly inflation is approaching more rapidly (compared to the other baskets) to its historical average (Figure 3). Within this basket, subclasses such as vehicles are already registering negative monthly contributions, counteracting upward pressures from items such as personal care items and beer.

The other core inflation baskets did not register significant changes compared to the annual variation of August. On the one hand, the services basket reached 9.1%, a decrease of only 3 bps compared to the previous month. Within it, rents and school transportation showed the highest contributions to the increase in the month and inter-municipal transportation contributed to the decrease. In the case of rents and transportation, these increases are associated with indirect indexation effects, where high levels of total inflation impact agents' expectations and

generate greater rigidities in inflation. In comparison with its historical average (2011-2019), services inflation doubled that value in September (Figure 4).

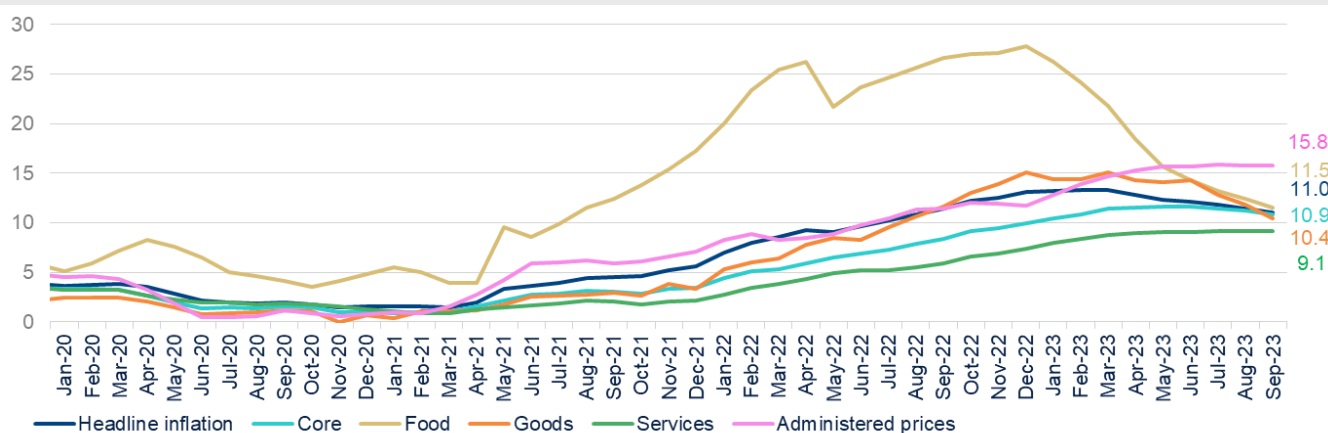
On the other hand, the administered prices basket registered an inflation rate of 15.8%, increasing by 7 bps compared to August. Upward pressures remain from the fuels subclass and those associated with education, while gas pressured downwards. In the case of fuels, the pressures are related to the increase in the price of gasoline, which, although lower in the last month, continues to be significant within the aggregate. The subclasses associated with education registered increases within the framework of tuition fees for B calendar schools, as well as for universities starting the second school semester in 2023. Additionally, reductions in gas prices may be associated with a lower average exchange rate in the month, leading to lower transmission of production costs to consumers. In the comparison against its historical average (2011-2019), the inflation of administered prices basket doubles the data for September (Figure 5).

The analysis of core inflation pressures is relevant insofar as this proportion of inflation tends to adjust less rapidly, and therefore may give signals as to how long the high inflation cycle in the country may be prolonged. Core inflation seems to be decelerating at a slower rate than expected. Although a greater moderation of the goods cycle has favored reductions from this basket, the administered prices basket continues to be pressured by indexation effects (directly or indirectly), a similar case to that of the services basket, which faces this effect and an additional one related to a more resilient demand than expected. Thus, core inflation remains rigid due to indexation and demand factors.

However, there is one factor that will continue to favor the decline in core inflation: the base effect. This will continue to be significant in the basket of goods for the remainder of the year and even in the first two months of 2024. However, it is possible that the basket of services, which is the one that weighs the most in core inflation, will experience little of this effect in the remaining months and will rather see it in 2024. This element puts a brake on the downward effect provided by the basket of goods.

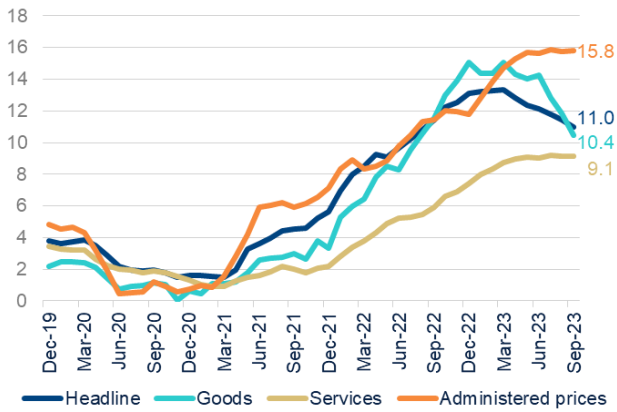
Based on the above, BBVA Research expects inflation to continue on a downward path in the last quarter of the year, which, however, will be pressured by food inflation with upward risks due to the El Niño phenomenon, and with core inflation decreasing moderately.

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



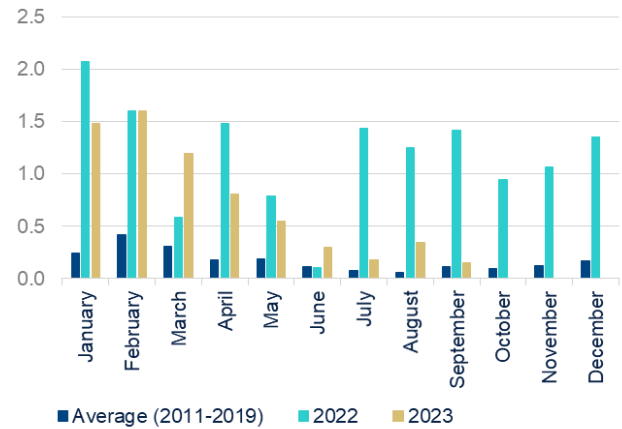
Source: BBVA Research with data from DANE

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



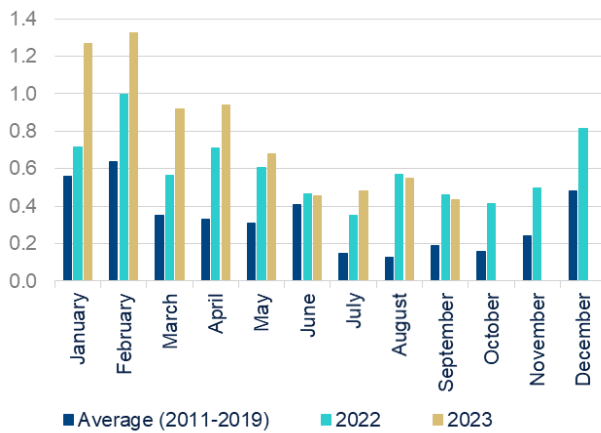
Source: BBVA Research with data from DANE

Figure 3. **GOODS BASKET INFLATION**
(MONTHLY CHANGE, %)



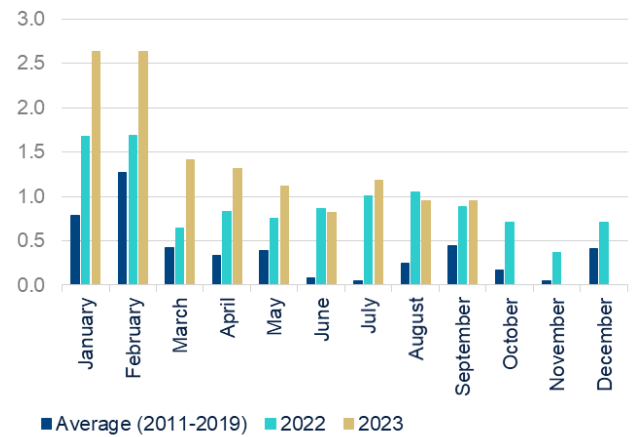
Source: BBVA Research with data from DANE

Figure 4. **SERVICES BASKET INFLATION**
(MONTHLY CHANGE, %)



Source: BBVA Research with data from DANE

Figure 5. **ADMINISTERED PRICES BASKET INFLATION**
(MONTHLY CHANGE, %)



Source: BBVA Research with data from DANE

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