

Short-term Inflation Remains Under Test Amid Upward Surprise in Regulated Prices

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- **IPCA-15 rose 0.69% MoM in March, above the consensus estimate and our forecast, both at 0.67% MoM. The YoY change decelerated to 5.4% YoY (from 5.6% in February). The trend (3MMA-saar) continued to rebound in March, reaching 6.7% 3MMA-saar (from 6.1%).**
- **Broad qualitative measures gave mixed signals, with some rising and some falling, and with the average remaining stable at 5.9% 3MMA-saar. The EX3 core gauge, which correlates the most with the output gap, fell slightly to 5.4% 3MMA-saar (from 5.5%). The diffusion index (seasonally adjusted) dropped to 59% (from 67%).**
- **All in all, we acknowledge that our benign view for short-term inflation remains under test, but the average of core gauges has remained stable. While we do not have enough evidence that the downward trend in inflation (and particularly core gauges) has halted, and that short-term inflation dynamics are back to being worrisome, the medium/long-term expectations continue to show signs of de-anchoring from the target, which is clearly a source of concern for the Brazil Central Bank (BCB), in our view.**

The IPCA-15 rose 0.69% MoM in March, above the consensus estimate and our forecast, both at 0.67% MoM. The YoY change decelerated to 5.4% YoY (from 5.6% in February). The trend (3MMA-saar) continued to rebound, reaching 6.7% 3MMA-saar (from 6.1%).

In the breakdown, upward surprises were concentrated in regulated prices: gasoline (+7 bps to the headline error) and electricity (+4 bps). Gasoline prices have been rising considerably with the reinstatement of federal taxes, despite the cut in prices at the refineries. Meanwhile, electricity prices have also been rising due to the inclusion of transmission and distribution tariffs in the tax-base. On the other side, downward surprises were concentrated in free prices: food-at-home (-2 bps), industrial goods (-1 bp) and services (-5 bps). Items related to vehicles (new vehicle, used vehicle and insurance) came in below expectation, more than offsetting the upward surprise in perfume (a volatile item). Education also surprised to the downside as there was no residual effect from February's adjustment.

In trend terms, headline services rose to 7.3% 3MMA-saar (from 6.0%). The services core gauge rose slightly to 4.7% 3MMA-saar. The industrial goods headline fell to 4.5% 3MMA-saar (from 5.0%), while its core gauge rose and remained high (8.1% vs. 7.8% 3MMA-saar). Broad qualitative measures gave mixed signals, with some rising and some falling, and with the average remaining stable at 5.9% 3MMA-saar. The EX3 core gauge, which correlates the most with the output gap, fell slightly to 5.4% 3MMA-saar (from 5.5%). The diffusion index (seasonally adjusted) dropped to 59% (from 67%).

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IMPORTANT DISCLOSURES/CERTIFICATIONS ARE IN THE "IMPORTANT DISCLOSURES" SECTION OF THIS REPORT.

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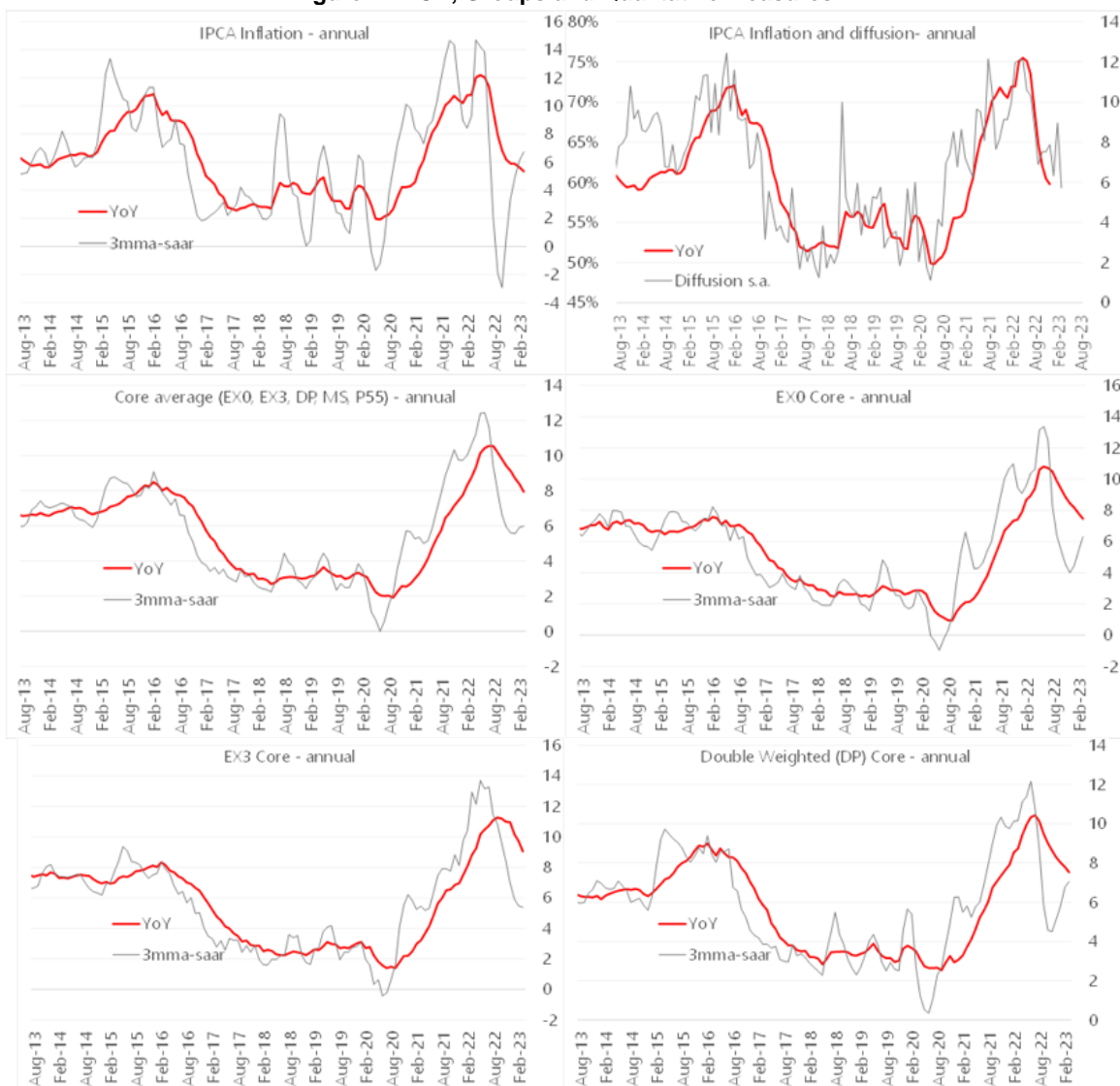
Figure 1. March's IPCA-15 Details (%)

| | MoM | | | YoY | | 3MMA-saar | |
|---------------------------------|--------------|-------------|--------------|-------------|-------------|------------|------------|
| | Mar-23 | Santander | Desv. | Feb-23 | Mar-23 | Feb-23 | Mar-23 |
| IPCA-15 | 0.69 | 0.67 | 0.02 | 5.6 | 5.4 | 6.1 | 6.7 |
| Food and beverage | 0.20 | 0.24 | -0.01 | 10.6 | 8.7 | | |
| Food-at-home | 0.02 | 0.16 | -0.02 | 11.8 | 9.1 | 6.1 | 3.9 |
| Food service | 0.68 | 0.48 | 0.01 | 7.5 | 7.6 | | |
| Housing | 0.81 | 0.73 | 0.01 | 0.2 | 0.5 | | |
| Electrical energy | 2.85 | 1.73 | 0.04 | -17.9 | -15.8 | | |
| Household articles | -0.18 | 0.08 | -0.01 | 6.0 | 4.3 | | |
| Apparel | 0.11 | 0.05 | 0.00 | 15.8 | 14.9 | | |
| Transportation | 1.50 | 1.32 | 0.04 | -1.2 | -0.4 | | |
| Airline tickets | -5.32 | -2.50 | -0.02 | 44.3 | 47.8 | | |
| Gasoline | 5.76 | 4.30 | 0.07 | -24.7 | -21.0 | | |
| Health and personal care | 1.18 | 1.15 | 0.00 | 12.1 | 11.9 | | |
| Personal spending | 0.28 | 0.33 | 0.00 | 7.3 | 7.2 | | |
| Education | 0.08 | 0.66 | -0.04 | 8.3 | 8.2 | | |
| Communication | 0.75 | 0.19 | 0.03 | 0.6 | 1.3 | | |
| Administered | 1.90 | 1.50 | 0.10 | -2.6 | -1.4 | 6.4 | 9.4 |
| Free | 0.29 | 0.40 | -0.08 | 8.6 | 7.8 | | |
| Food-at-home | 0.02 | 0.16 | -0.02 | 11.8 | 9.1 | 6.1 | 3.9 |
| Industrial goods | 0.47 | 0.51 | -0.01 | 8.0 | 7.2 | 5.0 | 4.5 |
| Services | 0.29 | 0.43 | -0.05 | 7.6 | 7.6 | 6.0 | 7.3 |
| EX3 Core | 0.50 | 0.56 | -0.02 | 9.7 | 9.0 | 5.5 | 5.4 |
| Average of cores | 0.43 | - | - | 8.4 | 7.9 | 5.9 | 6.0 |

Sources: Brazilian Central Bank, IBGE, Santander.



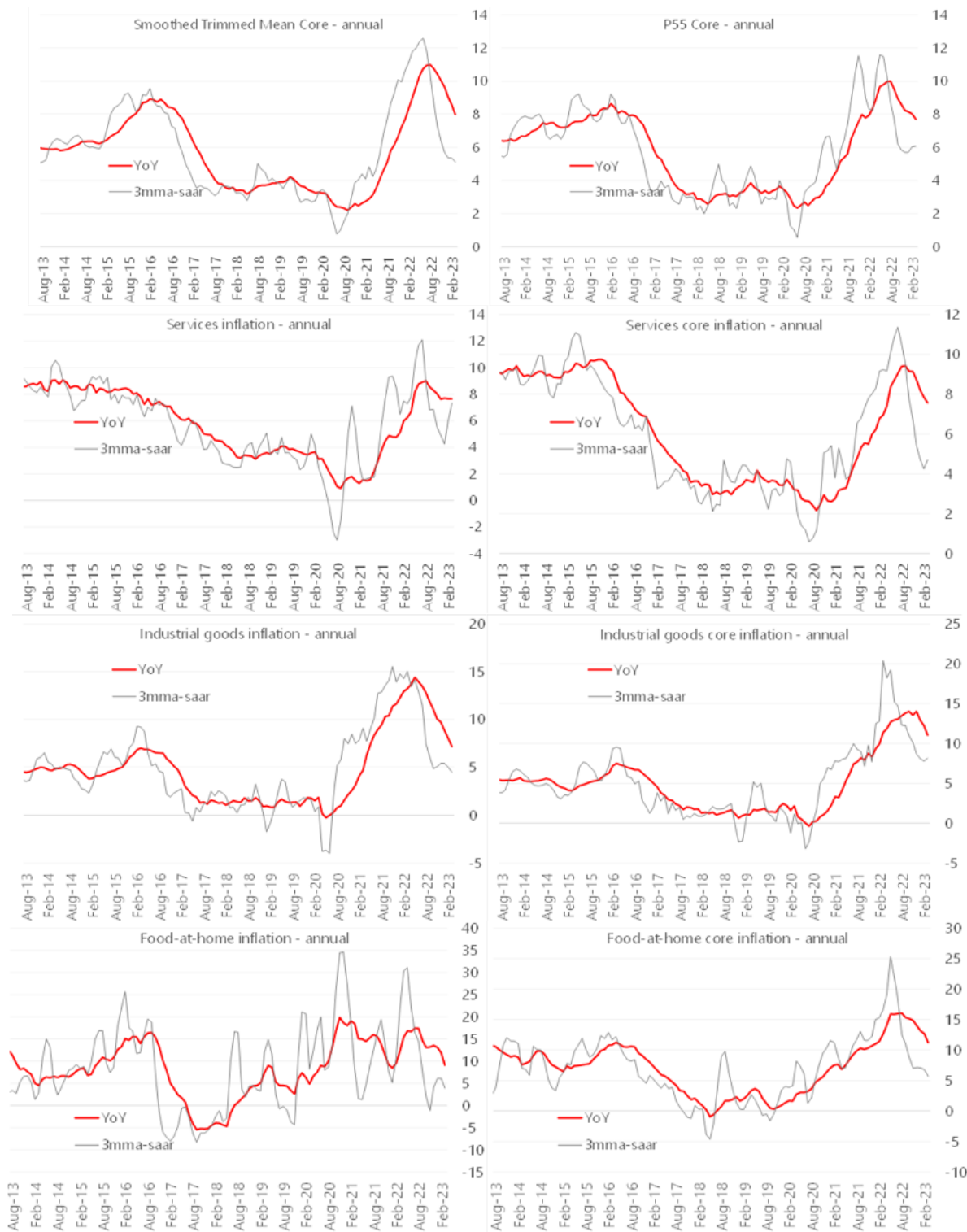
Figure 2. IPCA, Groups and Qualitative Measures



Sources for all charts: IBGE and Santander.



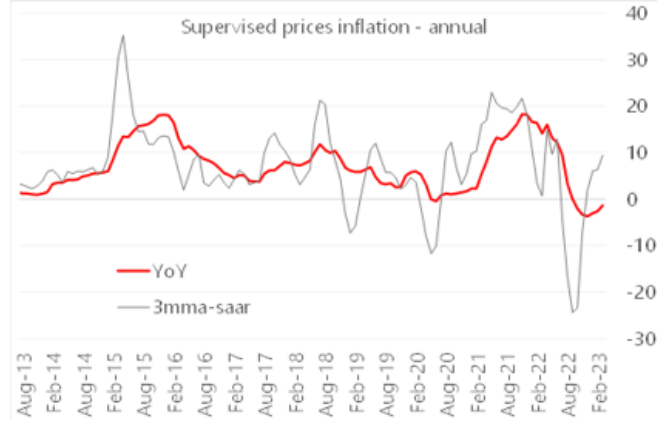
Figure 3. IPCA, Groups and Qualitative Measures (continued)



Sources for all charts: IBGE and Santander.



Figure 4. IPCA, Groups and Qualitative Measures (continued)



Sources: IBGE and Santander.



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