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## Marginal Improvement in Core Services

- The IPCA-15 fell 0.07% MoM in July, a steeper drop than both the consensus estimate (-0.03%) and our forecast (+0.09%). The YoY change decelerated to 3.19% (from 3.4% in June), the lowest reading since September 2020.
- Qualitative measures improved once again this month with a deceleration in core services inflation. Core services rose just 0.35% MoM (vs. our 0.60% forecast), leading the 3MMA-saar gauge to drop to 5.8% (from 6.5%).
- All the five main core inflation indexes followed by the BCB decelerated at the margin, with the average reaching 3.8% 3MMA-saar (from 5.0%), and the diffusion index falling to 51.0% s.a. (from 52.4%), a level compatible with inflation of around 3.0% in the medium term.
- All in all, the print continues to show that inflation is improving at the margin, even in services where prices tend to be stickier. Looking ahead, our tracking was kept unchanged at 4.9% for IPCA 2023 and 3.9% for IPCA 2024.
- The question now is whether this first improvement in months in core services inflation was the first step in a downward trend or just a data point.

The IPCA-15 fell 0.07% MoM in July, a steeper drop than both the consensus estimate (-0.03%) and our forecast (0.09%). The YoY change decelerated to 3.19% (from 3.4% in June), the lowest reading since September 2020. The headline trend (3MMA-saar) decelerated to 4.2% (from 4.8%).

In the breakdown of MoM numbers, monitored prices came in 1 bp (contribution to the headline forecast error) above our expectation. Meanwhile, food-at-home (-1 bp), industrial goods (-6 bps), and services (-9 bps) all came in lower than expected. Despite the discrepancy in the monthly headline with our forecast, the error was concentrated in just a few items. In services, rent (-3 bps), condominium fees (-1 bp), and airline tickets (-4 bps) explained most of the difference. For industrial goods, the difference was concentrated in new and used autos (-3 bps combined), and perfume (-3 bps). It's worth pointing out that rent and condominium fees are part of core services, while perfume is in core industrial goods group.

Qualitative measures improved once again this month with the first deceleration in core services inflation seen in recent months. Indeed, core services rose just 0.35% MoM, a big reason for the deceleration in the 3MMA-saar rate from 5.8% to 6.5%. The last time the 3MMA-saar rate showed a deceleration was back in February. In the breakdown of services, there were marginal improvements in the "inertial" (to 5.9% 3MMA-saar), "wages" (4.3% 3MMA-saar) and "volatile" (6.0% 3MMA-saar) groups while the "economic activity"-linked group was stable around 5.5% 3MMA-saar. In spite of the improvement, all groups continue to run at levels significantly above the 3.0% target.

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For other qualitative measures, industrial goods core inflation fell again, reaching 2.9% 3MMA-saar (from 4.6%). Thus, the EX3, which encompasses services core and industrial goods core, moved down to 4.6% 3MMA-saar (from 5.8%). **Moreover, all the five main core inflation indexes followed by the BCB decelerated at the margin, with the average reaching 3.8% 3MMA-saar (from 5.0%), and the diffusion index falling to 51.0% s.a. (from 52.4%), a level compatible with inflation below 3.0% in the medium term.**

**All in all, the print continues to show that inflation is improving at the margin, even in services where prices tend to be stickier.** Looking ahead, we project that there is still room for further relief in volatile prices, mainly the ones related to commodity prices in BRL terms. As for stickier, more core-related prices, we see an extension of their current decelerating trend, but maybe at a slower pace, as the tight job market tends to keep services prices high. **However, the question now is whether this first improvement in months in core services inflation was a first step in a faster downward trend or just a data point.** In annual terms, our IPCA tracking was kept unchanged at 4.9% for IPCA 2023 and 3.9% for IPCA 2024.



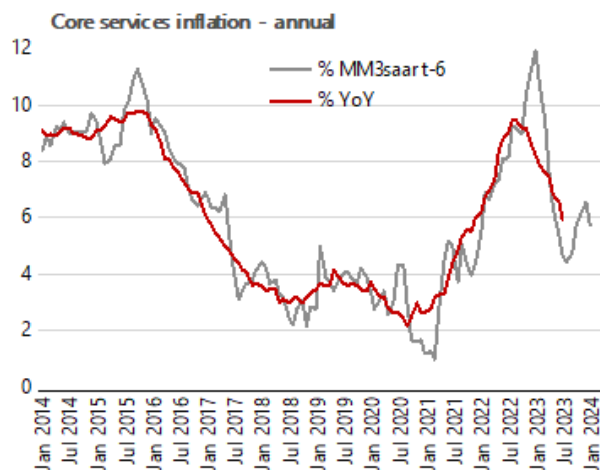
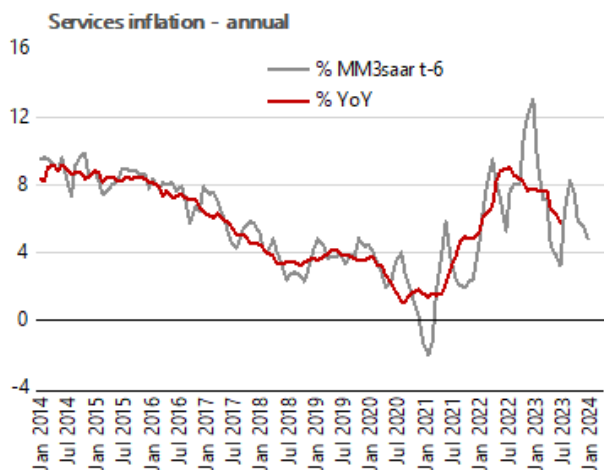
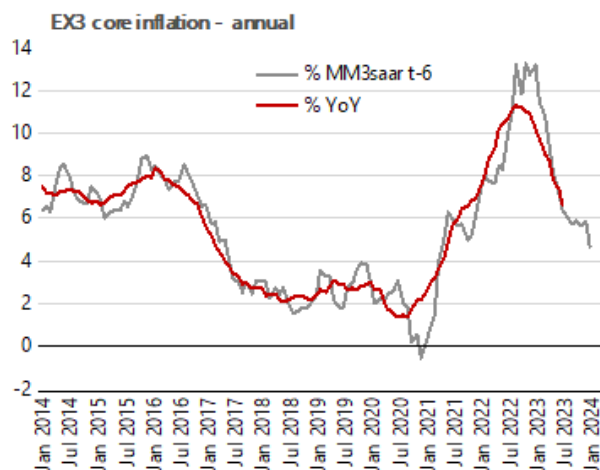
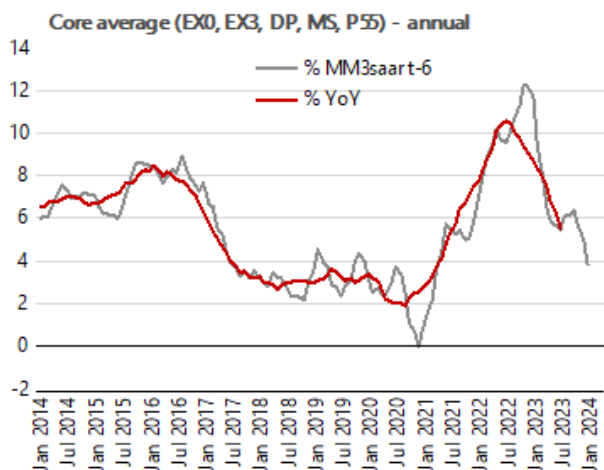
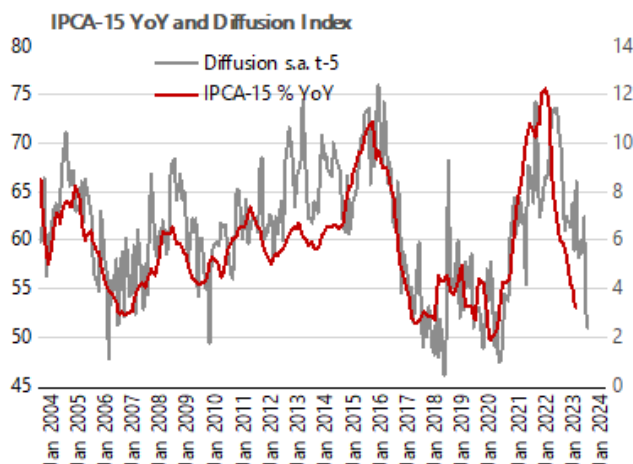
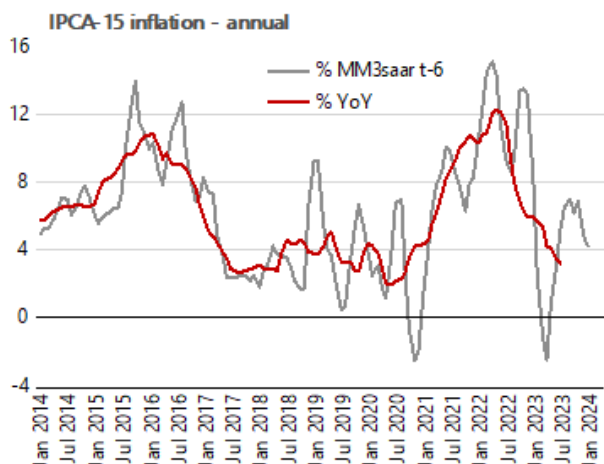
Figure 1. July's IPCA-15 Details (%)

	MoM			YoY	
	Jul-23	Santander	Contrib.	Jun-23	Jul-23
<b>IPCA-15</b>	<b>-0.07</b>	<b>0.09</b>	<b>-0.16</b>	<b>3.4</b>	<b>3.2</b>
<b>Food and beverage</b>	<b>-0.40</b>	<b>-0.33</b>	<b>-0.02</b>	<b>5.0</b>	<b>3.3</b>
Food-at-home	-0.72	-0.67	-0.01	4.1	2.2
Food service	0.46	0.57	-0.01	7.1	6.3
<b>Housing</b>	<b>-0.94</b>	<b>-0.75</b>	<b>-0.03</b>	<b>4.0</b>	<b>3.9</b>
Electrical energy	-3.45	-3.40	0.00	-0.5	0.7
<b>Household articles</b>	<b>-0.40</b>	<b>-0.31</b>	<b>0.00</b>	<b>1.1</b>	<b>0.3</b>
<b>Apparel</b>	<b>0.04</b>	<b>-0.02</b>	<b>0.00</b>	<b>10.3</b>	<b>8.9</b>
<b>Transportation</b>	<b>0.63</b>	<b>0.97</b>	<b>-0.07</b>	<b>-5.4</b>	<b>-3.8</b>
Airline tickets	4.70	10.00	-0.04	5.0	1.7
Gasoline	2.99	2.90	0.00	-27.4	-21.3
<b>Health and personal care</b>	<b>0.07</b>	<b>0.25</b>	<b>-0.02</b>	<b>10.6</b>	<b>9.9</b>
<b>Personal spending</b>	<b>0.38</b>	<b>0.49</b>	<b>-0.01</b>	<b>6.5</b>	<b>6.1</b>
<b>Education</b>	<b>0.11</b>	<b>0.04</b>	<b>0.00</b>	<b>8.2</b>	<b>8.3</b>
<b>Communication</b>	<b>-0.17</b>	<b>0.02</b>	<b>-0.01</b>	<b>0.7</b>	<b>0.6</b>
<b>Administered</b>	<b>0.17</b>	<b>0.14</b>	<b>0.01</b>	<b>-1.5</b>	<b>0.2</b>
<b>Free</b>	<b>-0.15</b>	<b>0.07</b>	<b>-0.16</b>	<b>5.2</b>	<b>4.3</b>
Food-at-home	-0.72	-0.67	-0.01	4.1	2.2
<i>Food-at-home core</i>	-0.03	0.03	0.00	7.3	6.4
Industrial goods	-0.55	-0.28	-0.06	4.4	3.6
<i>Industrial goods core</i>	-0.11	0.03	-0.02	8.5	7.5
Services	0.36	0.63	-0.09	6.1	5.6
<i>Services core</i>	0.35	0.60	-0.05	6.5	5.9
<b>EX3 Core</b>	<b>0.15</b>	<b>0.35</b>	<b>-0.08</b>	<b>7.4</b>	<b>6.6</b>
<b>Average of cores</b>	<b>0.09</b>	<b>0.25</b>	<b>-</b>	<b>6.2</b>	<b>-</b>

Sources: Brazilian Central Bank, IBGE, Santander.



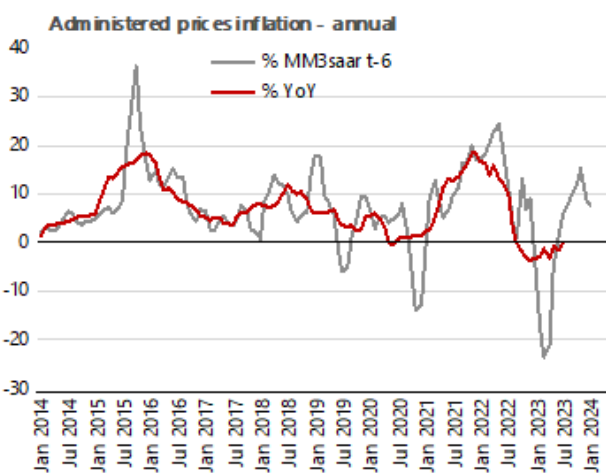
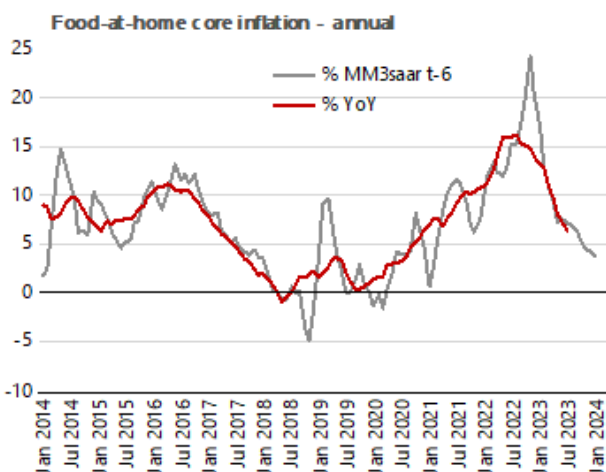
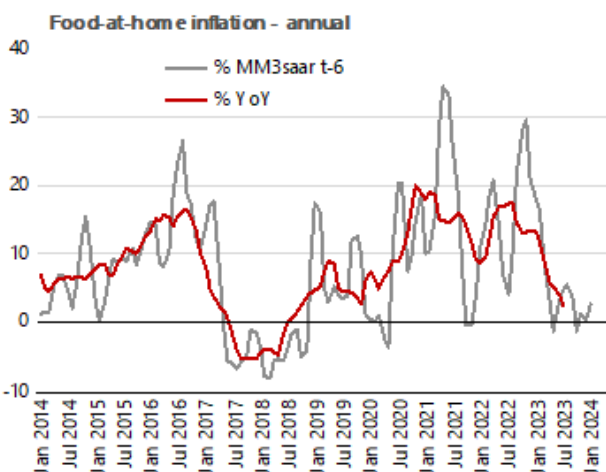
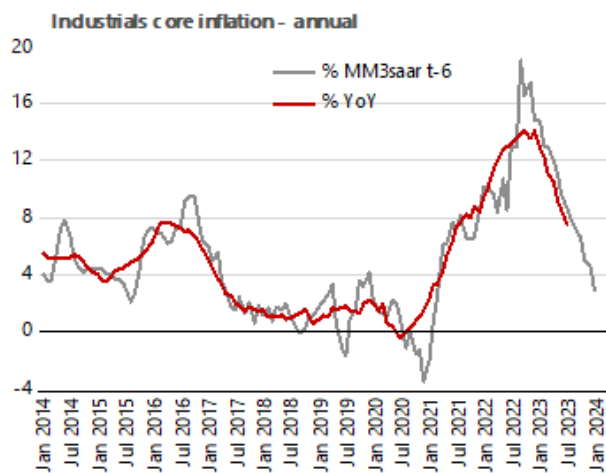
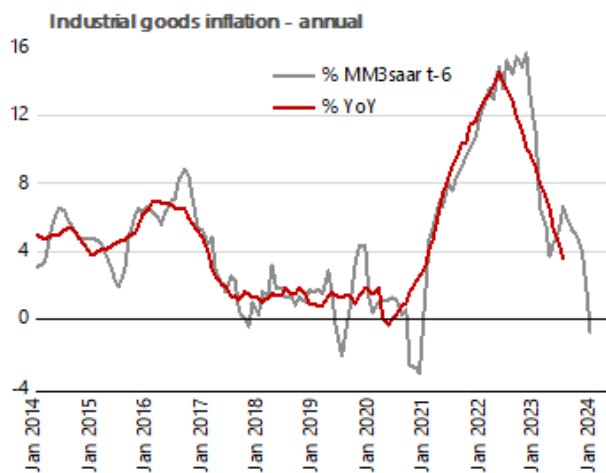
Figure 2. IPCA-15, Groups and Qualitative Measures



Sources for all charts: IBGE and Santander.



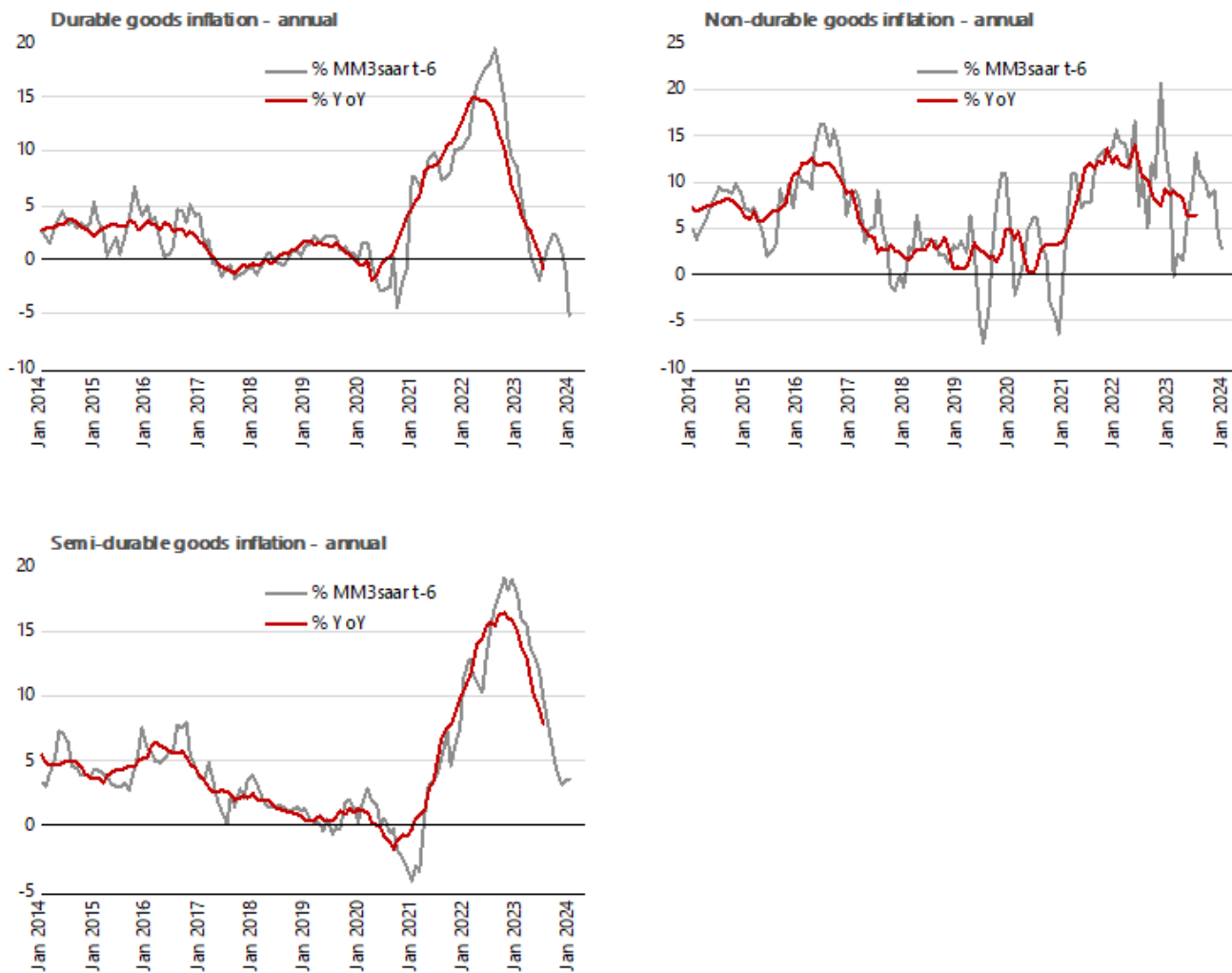
Figure 3. IPCA-15, Groups and Qualitative Measures



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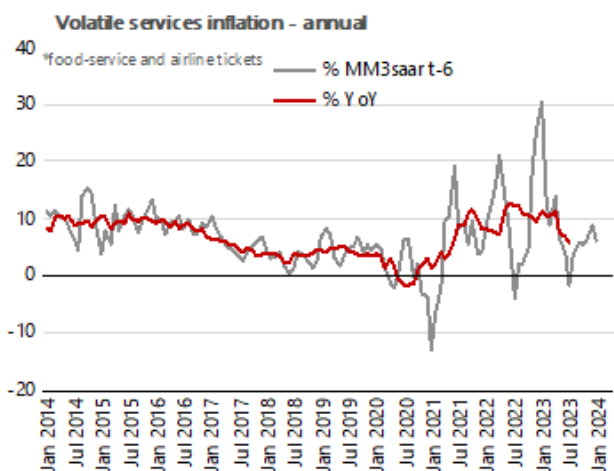
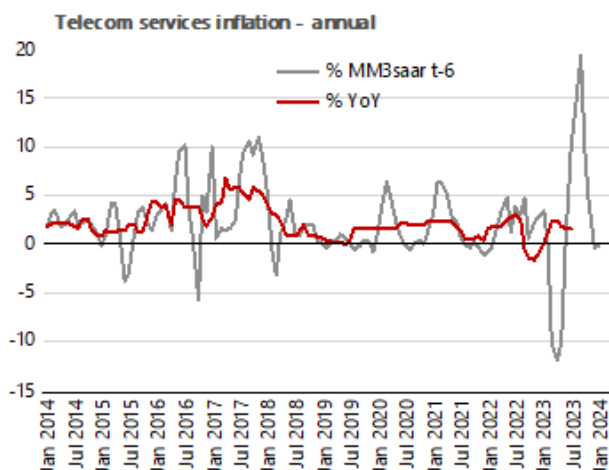
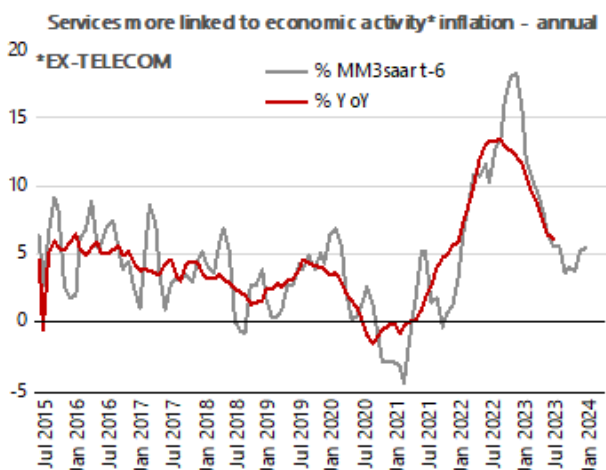
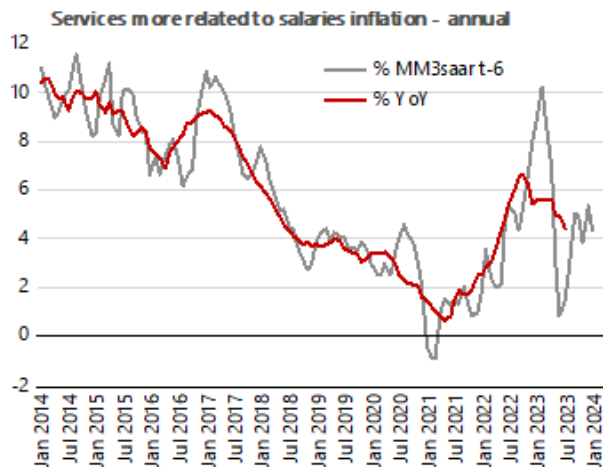
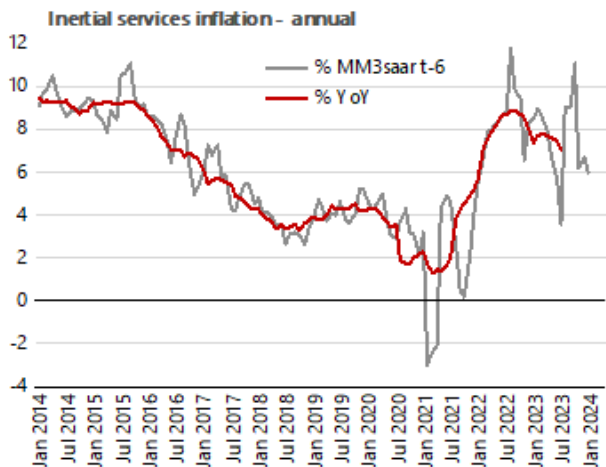
Figure 4. IPCA-15, Groups and Qualitative Measures



Sources for all charts: IBGE and Santander.



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