

December's IPCA: ending 2021 at 10.06% YoY, 631 bps above the Mid-Target

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- December's IPCA registered a 0.73% MoM change, in line with our forecast (0.70%), but above the market's consensus (0.64%). With that result, the year of 2021 ends with 10.06% of YoY inflation, still very close to the highs of 4Q15-1Q16 and well above this year's target of 3.75% and its upper limit of 5.25%
- The major upside surprise came in industrial goods, due to a higher rebound of some Black Friday-related discounts, with the core industrial goods trend going back to the highs at 10.2% 3MMA-saar. Moreover, core services also accelerated in trend terms to 6.8% 3MMA-saar and core food-at-home accelerated to 12.7% 3MMA-saar. Finally, the diffusion index rose back to 68.4% (seasonally adjusted).
- All in all, this reading reinforces our concerns about the inflation outlook and we continue to project a "plateau" around 10.0% YoY until April 2022. After that, the disinflation process should become clearer, but still be a sticky, difficult and risky one, with an unfavorable composition: core-related items accelerating, with the deceleration coming from more volatile groups.

Another unfavorable monthly print, with the year ending much above the target

December's IPCA registered a 0.73% MoM change, in line with our forecast (0.70%), but above the market's consensus (0.64%). With that result, the year of 2021 ends with 10.06% of YoY inflation, still very close to the highs of 4Q15-1Q16 and well above this year's target of 3.75% and its upper limit of 5.25%. Although this small annual relief can be seen as a peak, strictly speaking we believe inflation will continue hovering around 10% until April 2022, meaning a plateau rather than a clear peak. As for the trend at the margin, it decelerated from 13.1% 3MMA-saar to 11.0%. We believe the 3MMA-saar measure should continue to cool down until it reaches around 5.0%, but then it should remain at that hefty level for most of the year, suggesting that the disinflation process will be a sticky, difficult and risky one.

The major upside surprise came in industrial goods, due to a higher rebound in some Black Friday-related discounts. Industrial goods rose 1.41% MoM (vs. 1.00% expected), contributing +10 bps with the headline forecast error. This was enough to push the headline industrial goods trend from 13.0% 3MMA-saar to 13.8%. Moreover, core industrial goods also accelerated in trend terms, reaching 10.2% 3MMA-saar, that is, back to the highs. Services came in line with expectations at 0.79% MoM, meaning its trend decelerated from 7.4% to 6.2% 3MMA-saar. However, core services actually accelerated from 6.1% to 6.8%, as the relief in the headline came more from volatile items—we highlight that services more related to wage pressures accelerated at the margin, and inertial ones remained at a high level. Food-at-home also came in line with expectations, rising 0.79% MoM and continuing its decelerating trend both in YoY and 3MMA-saar terms. Nevertheless, the food-at-home core gauge accelerated to 12.7% 3MMA-saar (from 9.3%). Finally, regulated prices surprised to the downside, rising 0.05% MoM (vs. 0.28% expected), contributing -6 bps to the headline forecast error. The surprise was concentrated in electrical energy.

In general, qualitative measures remained unfavorable. The average of the main core gauges rose 0.90% MoM and the trend remained basically stable at 8.9% 3MMA-saar (EX0, DP and P55 decelerated a bit, while EX3 and MS accelerated considerably). Moreover, the diffusion index—which had been cooling down during the last few

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readings—rebounded from 62.0% to 68.4% (seasonally adjusted), which is compatible with YoY inflation running around 9.0% a few months from now.

All in all, this reading reinforces our concerns about the inflation outlook. Despite some marginal reliefs, we think it is still too soon to be convinced that inflation is already at a consistent deceleration trend, especially because the qualitative measures are still quite unfavorable: services accelerating, while industrial goods remain under upward pressure (and surprising to the upside). Although our view is that inflation has no room to accelerate further in YoY terms, we think it should also not peak until Apr-22, so the dynamic we envision is a plateau around 10.0% and then a more clear relief to around 9.0% only in May-22 (mainly because of the base effect coming from the end of the Red 2 “Hydro Scarcity” tariff flag in electrical energy; the peak can become clear before that if this exceptional flag is dropped before May). Moreover, the disinflation process afterwards should be a difficult and sticky one, and not a sharp deceleration.

Our IPCA 2022 high frequency tracking is at 6.0%, while for IPCA 2023 it is at 3.5%. Both numbers are above the target of the BCB (3.5% for 2022 and 3.25% for 2023, both with +/-1.5% tolerance band).

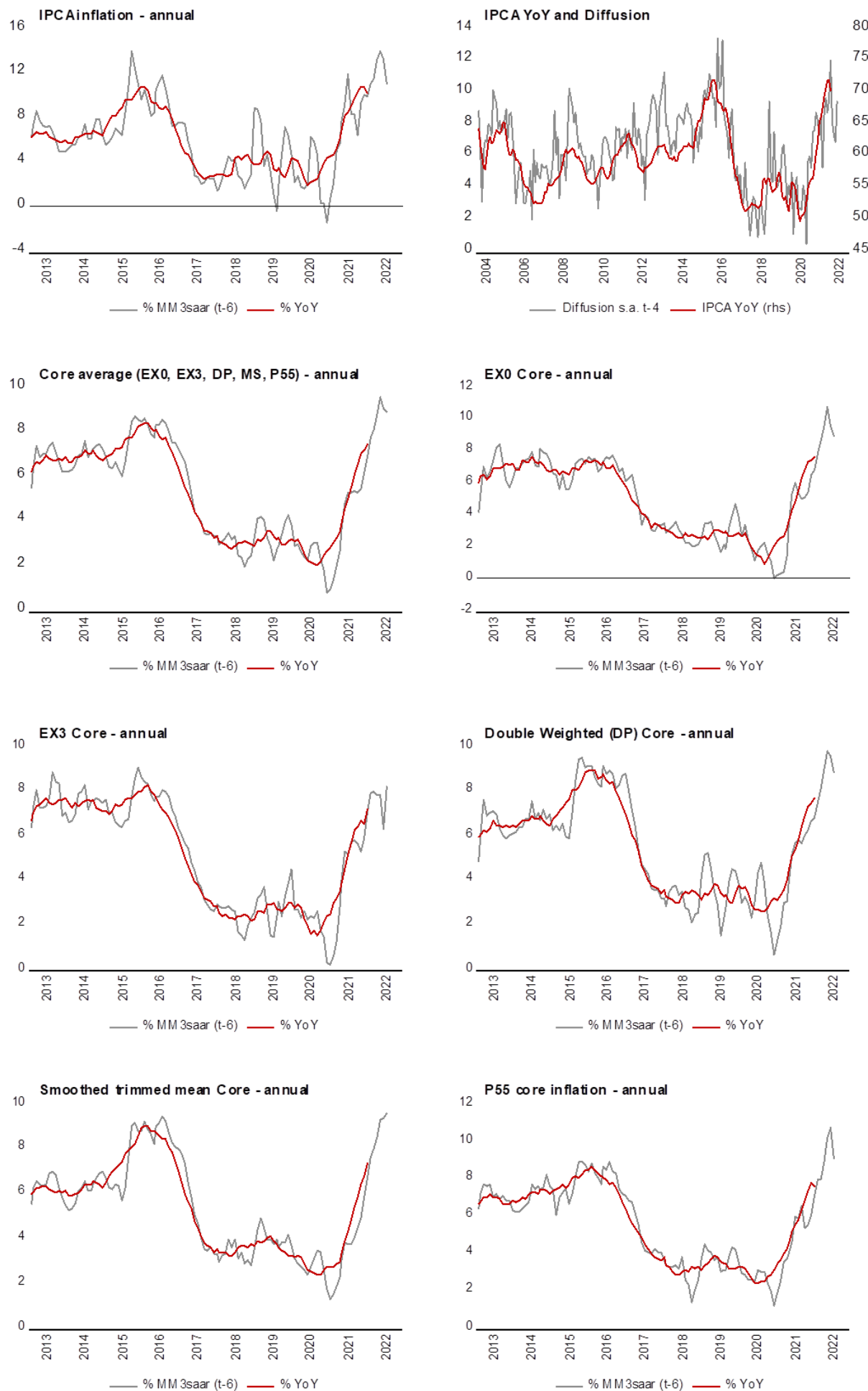
Figure 1. IPCA by Group and Forecasting Errors

	MoM			YoY	
	Dec-21	Santander	Desv.	Nov-21	Dec-21
IPCA	0.73	0.70	0.03	10.7	10.1
Food and beverage	0.84	0.75	0.02	8.9	7.9
Food-at-home	0.79	0.75	0.01	9.7	8.2
Food service	0.98	0.75	0.01	6.9	7.2
Housing	0.74	1.00	-0.04	15.4	13.0
Electrical energy	0.50	1.42	-0.05	31.9	21.2
Household articles	1.37	1.13	0.01	12.5	12.1
Apparel	2.06	1.25	0.03	8.7	10.3
Transportation	0.58	0.74	-0.04	22.0	21.0
Airline tickets	10.28	10.07	0.00	36.6	17.6
Gasoline	-0.67	-0.60	0.00	50.8	47.5
Health and personal care	0.75	0.54	0.03	3.3	3.7
Personal spending	0.56	0.52	0.00	4.8	4.7
Education	0.05	0.03	0.00	3.3	2.8
Communication	0.34	0.06	0.01	1.4	1.4
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Administered	0.05	0.28	-0.06	19.2	16.9
Free	0.99	0.85	0.10	7.8	7.7
Food-at-home	0.79	0.75	0.01	9.7	8.2
Industrial goods	1.41	1.00	0.10	11.4	12.0
Services	0.79	0.80	-0.01	4.8	4.8
EX3 Core	1.22	0.94	0.10	6.5	7.1
Average of cores	0.90	-	-	-	-

Sources: IBGE and Santander.



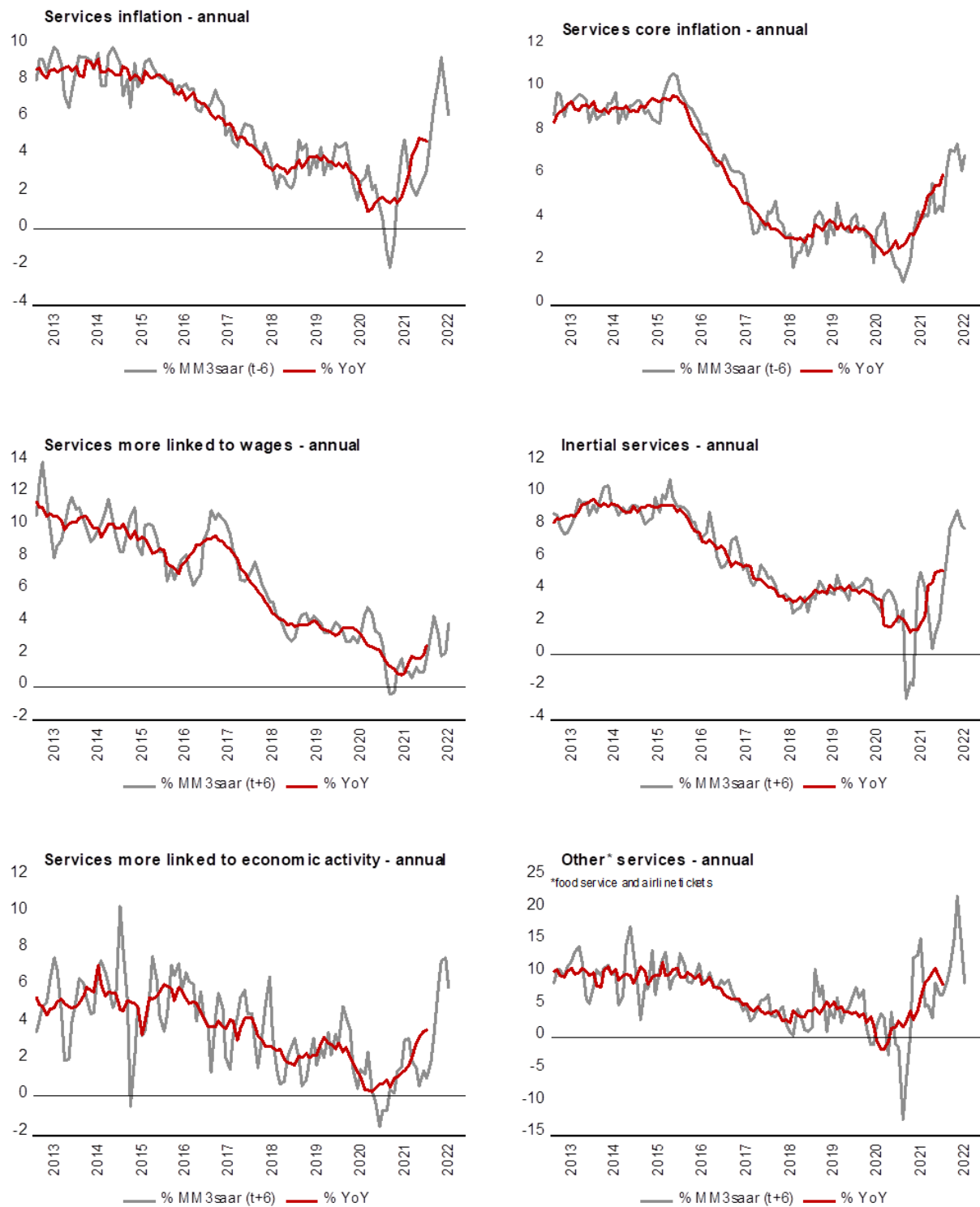
Figure 2. IPCA, Groups and Qualitative Measures



Sources for all charts: IBGE and Santander.



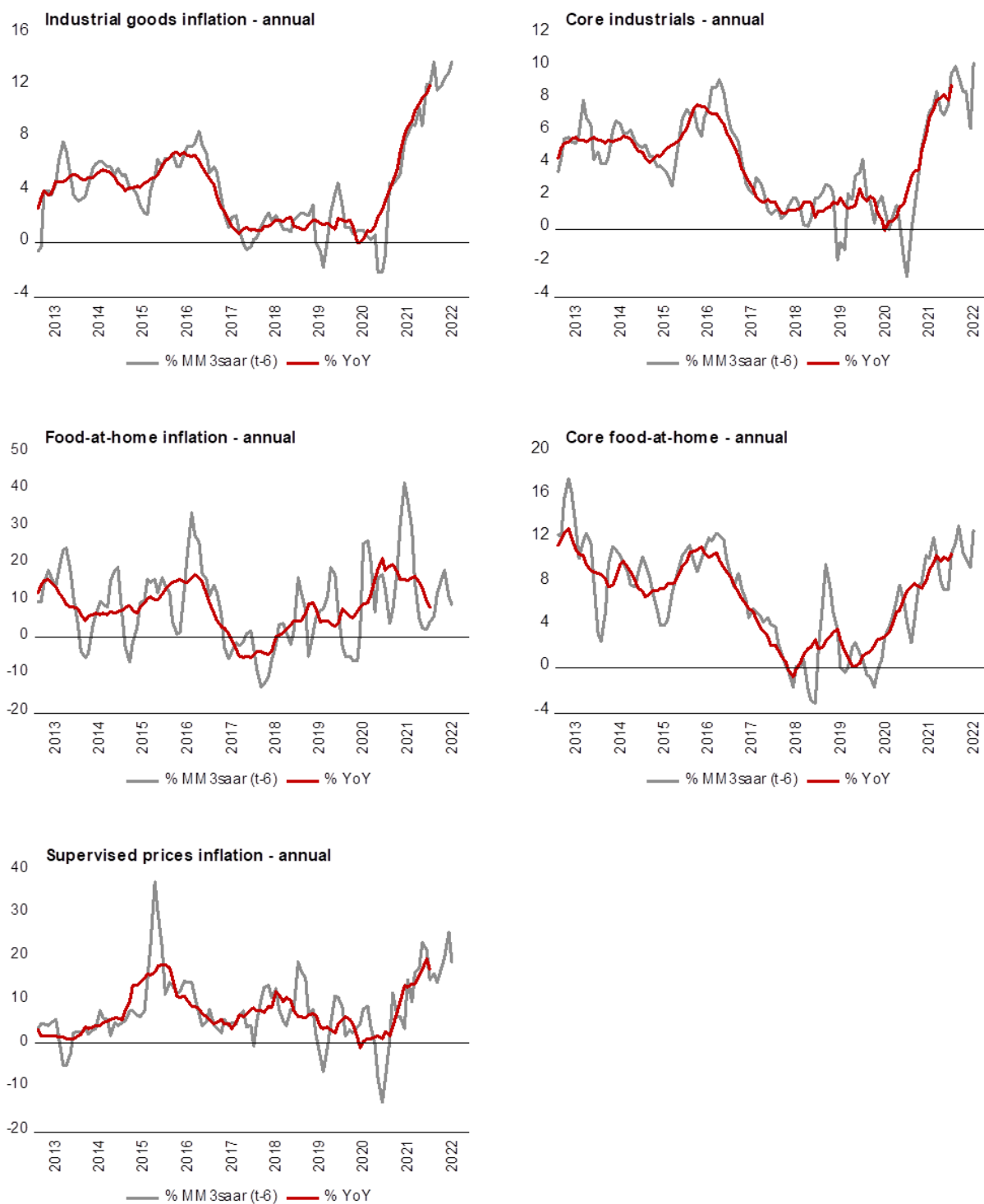
Figure 3. IPCA, Groups and Qualitative Measures (continuation)



Sources for all charts: IBGE and Santander.



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



Sources for all charts: IBGE and Santander.



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