

IPCA December: Some Negative Surprises

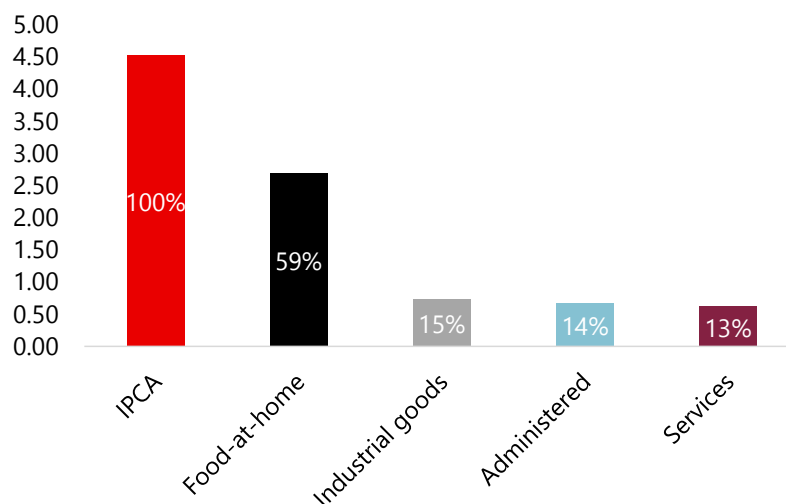
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- IPCA 2020 ended at 4.52%, above the Brazil Central Bank's (BCB) 4.00% target. However, the number is not as bad as the headline could suggest, because the food shock accounted for 60% of the yearly variation, while the average of cores ended at 2.80%.
- Nonetheless, we cannot deny that the monthly print was not great in qualitative terms, as there was an upside surprise concentrated in items related to the core measures—particularly, industrial goods.
- This upside surprise, alongside rising commodity prices and a weak BRL, made us revise the short-term forecasts to 0.36% MoM in January (from 0.19%) and 0.29% MoM in February (from 0.28%); the year-end tracking went to 3.2% (from 3.0%, the official forecast). We still believe in a benign scenario for inflation, but see the risks tilted to the upside.

IPCA 2020 was not as bad as the headline would suggest

The 2020 IPCA inflation closed at 4.52%, above the 4.00% target of the BCB. However, it is worth highlighting that the food shock (+18.2% YoY) was impressive, accounting for 60% of the total variation for the year. In other words, the IPCA ex-food finished the year just at 2.4%—and the official average of cores ended at 2.8%—that is, at very low levels. It is also worth noticing that services inflation was very low, ending 2020 at 1.7%, while industrial goods inflation ended a bit higher, but still below the target, at 3.2%. All in all, despite the high headline, 2020's IPCA inflation was qualitatively good.

Figure 1. IPCA 2020 decomposition



Sources: IBGE and Santander Brazil.

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But the monthly print was not great in qualitative terms

Analyzing at the margin, December's IPCA was higher than expected: 1.35% MoM vs. our forecast of 1.18% and the market's median expectation of 1.21%. For the month, the reading was qualitatively worse: the biggest surprise came in industrial goods (+10 bps of surprise), with cars, clothes and hygiene products being the main deviations. Services also surprised (+6 bps), with food-service and some personal services being the highlights. Food-at-home showed a lower surprise (+2 bps) and continued to decelerate in MoM terms. The average of cores registered +0.65% MoM change, while we expected a milder variation of +0.44%.

Looking ahead, in terms of trend (3mma-saar), services inflation continued to accelerate, but the services' core decelerated a bit. Food-at-home also decelerated a bit in 3mma-saar terms and should be close to marking the peak in YoY terms. On the negative side, industrial goods 3mma-saar inflation keeps accelerating and the YoY change is above the 2017-2019 average. Finally, the average of cores also accelerated mildly in 3mma-saar terms and diffusion was high.

Figure 2. IPCA inflation by groups

IPCA					
Groups	MoM			YoY	
	dec/20	Santander	Dev.	nov/20	dec/20
IPCA	1.35	1.18	0.17	4.3	4.5
Food and beverage	1.74	1.56	0.04	16.0	14.1
Food-at-home	2.12	1.96	0.02	21.1	18.2
Food service	0.77	0.58	0.01	5.1	4.8
Housing	2.88	2.88	0.00	1.5	5.3
Electrical energy	9.34	9.16	0.01	-4.4	9.1
Household articles	1.76	1.24	0.02	3.7	6.0
Apparel	0.59	0.00	0.03	-1.7	-1.1
Transportation	1.36	1.24	0.02	1.2	1.0
Airline tickets	28.05	28.31	0.00	-25.2	-17.2
Gasoline	1.54	2.00	-0.02	1.6	-0.2
Health and personal care	0.40	0.18	0.03	1.5	1.5
Personal spending	0.65	0.43	0.02	1.3	1.0
Education	0.48	0.38	0.01	0.9	1.1
Communication	0.39	0.35	0.00	3.7	3.4
Administered prices	2.04	2.09	-0.01	0.9	2.6
Free prices	1.11	0.86	0.19	5.5	5.2
Food-at-home	2.12	1.96	0.02	21.1	18.2
Industrial goods	0.91	0.46	0.10	2.6	3.2
Services	0.83	0.67	0.06	1.6	1.7
EX3 core	0.60	0.36	0.24	2.4	2.4
Average of cores	0.65	0.44	0.21	2.6	2.8

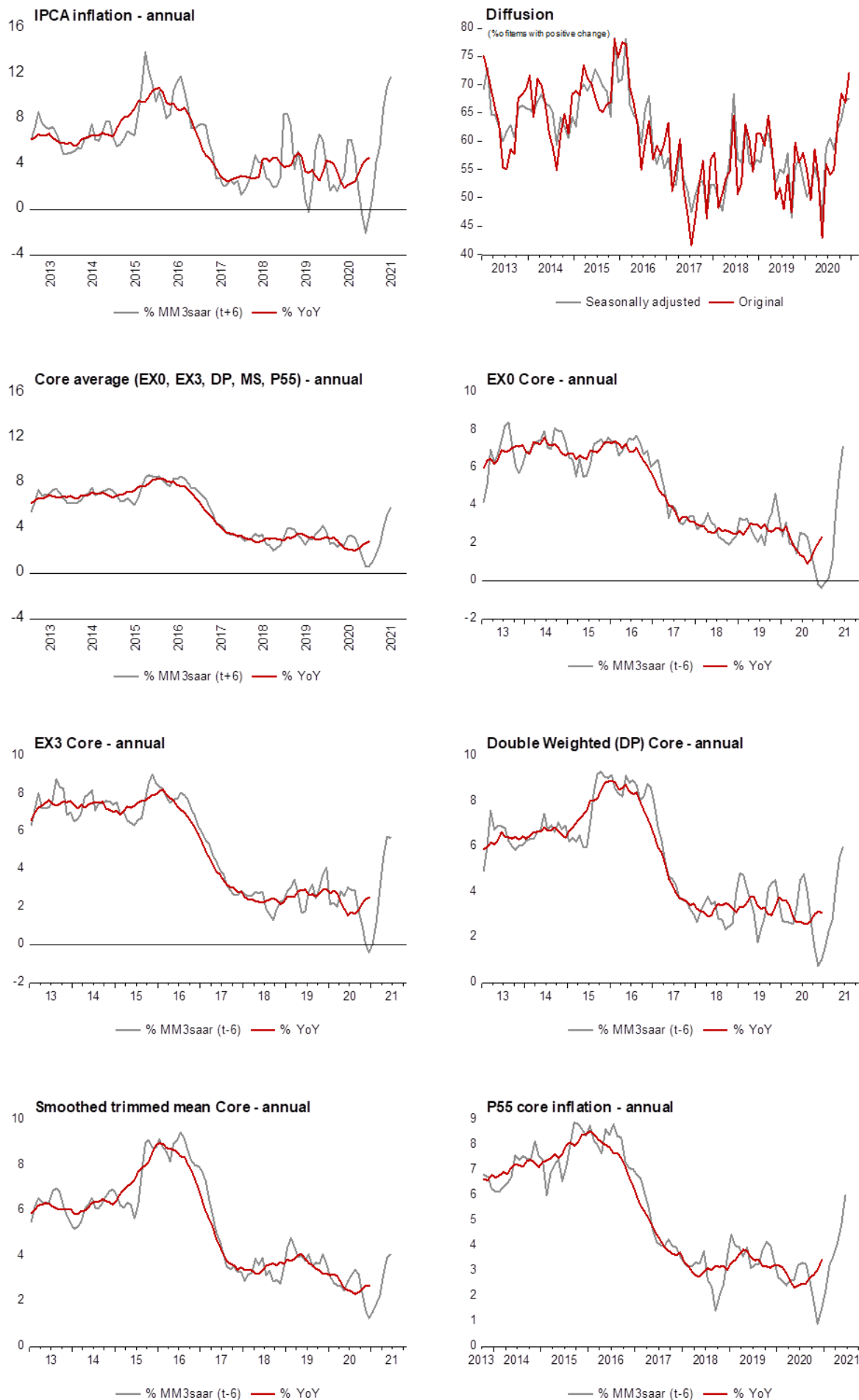
Sources: IBGE, BCB and Santander Brazil.

Short-term forecasts worsened a bit, but the medium-term scenario did not change

We revised our short-term IPCA forecasts upwards: January went to 0.36% MoM (from 0.19%) and February went to 0.29% MoM (from 0.28%). On top of the December reading's surprise, commodity prices continue to rise, while the BRL is not appreciating (contrary to our expectation). This short-term revision led us to revise our 2021 tracking from 3.0% (still the official forecast) to 3.2%, but we still believe in a benign scenario, with the food shock fading, services accelerating at a slow pace (weak job market), industrial goods decelerating (as the mismatch between supply and demand ends) and administered prices being an upward pressure. However, we see risks tilted to the upside, as commodity prices are rising considerably and BRL is struggling to appreciate; also, this reading increases the risk for industrial goods, in our view, as the pass-through from the wholesale level seems to be bigger than we were expecting.



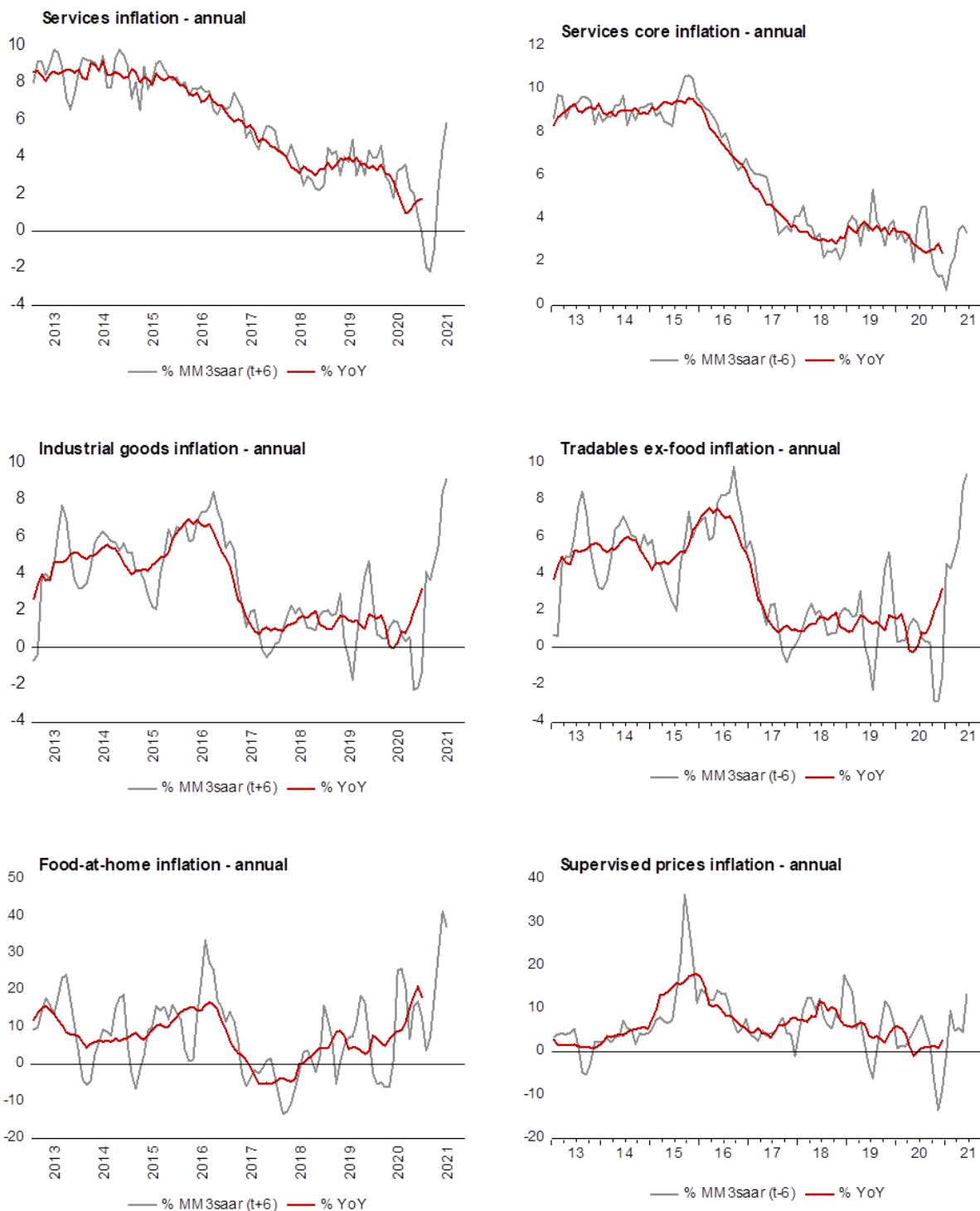
Figure 3. IPCA inflation and qualitative measures



Sources: IBGE, BCB and Santander Brazil.



Figure 4. IPCA inflation by groups



Sources: IBGE, BCB and Santander Brazil.



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