

## June Inflation Report: Food Pushed Inflation to 3.42%

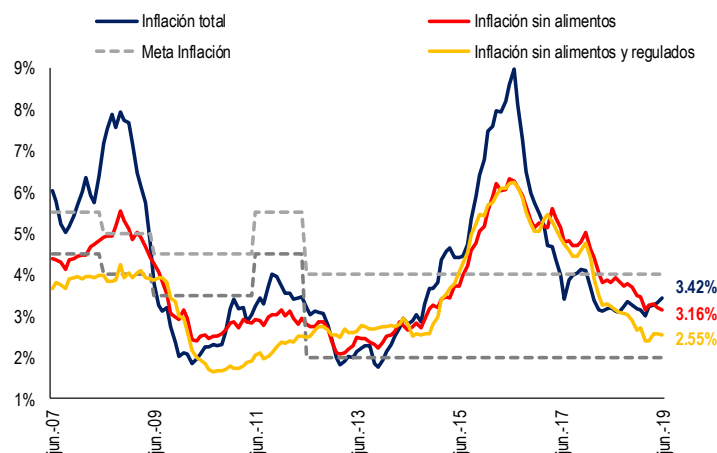
### Main Takeaways

- In June, monthly inflation reached 0.27% and annual inflation 3.42%.
- The monthly result was mostly explained by food inflation (0.57%) and transportation (0.46%), followed by housing (0.07%) and entertainment (0.53%).
- Inflation ex food fell to 3.16% YoY, while the ex food and regulated figure remained stable at 2.55%.
- This report suggests that, against our expectation of inflation of 3.4% by the end of 2019, some upward risks persist.
- We believe that the upward evolution of inflation will not result in an interest rate movement by the Central Bank.

In June, the consumer price index recorded a monthly increase of 0.27%. This reading came below our expectation (0.35%) but was 6-bp higher than the figure expected by economic analysts (0.21%). Similarly, the report was higher than the average recorded for June over the last decade (0.23%) and also higher than June 2018's (0.15%). Again, more than half of the result was explained by the behavior of the food item (0.57%), driven by the rise in prices of vegetables. In addition, the adjustment in prices of housing, entertainment and transport services was also relevant, explaining about 40% of the total result.

Thus, annual inflation advanced to 3.42%. This is the highest level in more than a year and gives continuity to an upward trend that has taken place since last March. Again, this was the result of a greater contribution of food inflation (4.83%), which peaked since February 2017 and continues to respond to short-term factors and the effect of a low comparison base. Conversely, inflation ex food continued to decline (3.16%) and remained close to the 3% target of the Central Bank. Thus, last month's report reaffirmed that the evolution of inflation in the country is favorable and that it takes place in a context of upward pressures due to supply factors and relative stability in expenses associated with demand.

Figure 1. Headline inflation, core inflation measurements and target range (annual % var.)



Source: Grupo Bancolombia, DANE

## Main Inflation Results

### Food Inflation

**Food (0.57%) contributed the most to the monthly inflation result.** During June, this basket was marked by the rise in the price of beef (1.54%), which showed a significant increase in Cucuta and Bogota, and also by the increase in prices of vegetables (3.7%), particularly tomato (7.84%). The advance in the cost of plantain (5.89%) also contributed positively, whose supply was affected by rains, as did the adjustment in the price of potatoes (1.9%). It should be mentioned that, according to the DANE, the closure of the road that connects Bogota with the eastern plains was not a determining factor in the revision of food prices in June.

**Annual food inflation increased to 4.83%.** This implies an acceleration of 57 bps compared to May, and it's the highest since February 2015. This acceleration trend becomes more evident when taking into account that, a year ago, inflation of this item was around 1.74%. This dynamic reflects the fact that climatic conditions are less favorable for supply, and also show the effect of comparing the results against the low variations observed in 2018.

### Inflation – Non-Tradables

**Expenses associated with housing and entertainment services explained the monthly variation of non-tradables (0.23%).** In the first case, the adjustment of rent (0.26%) and housing services (0.27%), which together contributed 15 bps to the aggregate variation of the CPI, was decisive. On the other hand, the indicator that tracks the cost of tour packages showed a monthly increase of 3.22%, in line with the holiday season. On the other hand, the rest of the items in this basket did not show significant variation, and therefore the evolution of the group surprised our expectations (0.29%).

**The annual change in prices of non-tradables was 3.36%.** That is, the reading remained close to May's record (3.34%) and was 90-bp lower than in June 2018. In this group, the increase in prices continued to be mainly explained by the item of education (5.07%) and hotels (4.13%), which nonetheless showed a moderate advance YoY. In this regard, it is important to mention that the latest reports suggest that the adjustment of prices on this front, which are of low frequency, seem to be incorporating lower records and lower inflation expectations.

### Inflation – Tradables

**Monthly inflation of tradables (0.24%) was pressured by transport.** On the one hand, prices of vehicles increased 0.49% with respect to May, and contributed 4 bps to the variation of the total CPI. In addition, there's the adjustment in air tickets, which according to the holiday season showed a monthly increase of 3.71%. On the other hand, the rise in the price of alcoholic beverages (0.25%), garments (0.09%), and some personal hygiene, cleaning and pharmaceutical products also contributed positively.

**Annual inflation of tradables is yet to show greater reactions to FX movements.** In fact, in June this was 1.17%, yielding 5 bps compared to the reading of May and 66 bps compared to a year ago. Meanwhile, the annual depreciation of the COP averaged 12.5% in the same period. This reveals that a context of low transfer of these movements to consumer prices prevails, which could be explained by the fact that the economy still operates below potential. In this way, although this is an element to be considered in the future, for the moment the report of last month mitigates part of the risks on this front.

## Inflation – Regulated Group

**Thanks to the fall in electricity, the regulated group (-0.09%) came below expectations.** In particular, this service showed a decrease of 2.22%, consistent with the higher levels of reservoirs due to rainfall, and subtracted 44 bps from the aggregate variation of the CPI. However, public transport, and particularly inter-municipal transport, in view of the greater demand characteristic of the season, adjusted prices up 6.59%, mitigating part of the bearish pressures of the energy sector. In addition, there's also an increase of 0.26% in the price of fuel, and of 0.14% in fares of urban public transport.

**The annual change in the regulated index lost ground and stood at 5.33%.** In this way, there was a 20-bp deceleration compared to May, and was 48-bp lower compared to June 2018. Again, this was due to the fact that the adjustment of the price of energy (electricity, natural gas and fuels) of 5.61%, was less pronounced than a year ago, when it reached near 6%. This is partly explained by a context of lower oil prices, and that is something that we believe may prevail for the rest of the year. However, the uncertainty regarding adjustments in energy tariffs means that this item continues to be one of the risk factors for the convergence of headline inflation to the Central Bank's target.

## Core Inflation

**In June, core inflation lost ground.** Specifically, the index that excludes the price of food went from 3.2% YoY in May to 3.16%, thanks to the correction of tradable and regulated indexes. Meanwhile, the measurement that excludes the price of food and also of regulated items remained stable at 2.55%. For purposes of monetary policy, the reports on this front are favorable and continue to justify the decision to maintain, for one of the most prolonged periods, an expansive policy stance, since at the moment there are no signs that pressures are being generated in prices from the demand side.

### Main inflation results in Colombia – Expenditure divisions

| División                           | Ponderación   | jun.-19      |              |              | jun.-18      |              |              |
|------------------------------------|---------------|--------------|--------------|--------------|--------------|--------------|--------------|
|                                    |               | Mes          | 12 meses     | Año corrido  | Mes          | 12 meses     | Año corrido  |
| <b>Total</b>                       | <b>100.0%</b> | <b>0.27%</b> | <b>3.42%</b> | <b>2.71%</b> | <b>0.15%</b> | <b>3.20%</b> | <b>2.47%</b> |
| Alimentos Y Bebidas No Alcoholicas | 15.05%        | 0.85%        | 4.99%        | 5.27%        | -0.04%       | 1.11%        | 2.14%        |
| Bebidas Alcohólicas y Tabaco       | 1.70%         | 0.25%        | 5.23%        | 4.42%        | 0.15%        | 5.08%        | 3.53%        |
| Prendas De Vestir Y Calzado        | 3.98%         | 0.09%        | 0.57%        | 0.35%        | 0.07%        | 0.25%        | 0.08%        |
| Alojamiento y Servicios Públicos   | 33.12%        | 0.07%        | 4.13%        | 2.18%        | 0.06%        | 4.21%        | 2.60%        |
| Muebles y Articulos Para El Hogar  | 4.19%         | 0.21%        | 2.52%        | 2.22%        | 0.11%        | 1.82%        | 1.58%        |
| Salud                              | 1.71%         | 0.28%        | 2.06%        | 1.35%        | 0.23%        | 4.31%        | 3.14%        |
| Transporte                         | 12.93%        | 0.46%        | 3.07%        | 2.25%        | 0.33%        | 4.23%        | 2.90%        |
| Información Y Comunicación         | 4.33%         | -0.12%       | 0.07%        | 1.73%        | 1.69%        | 3.30%        | 1.95%        |
| Recreación Y Cultura               | 3.79%         | 0.53%        | 2.02%        | 1.57%        | 0.04%        | 2.54%        | -0.74%       |
| Educación                          | 4.41%         | 0.00%        | 5.07%        | 4.66%        | 0.00%        | 6.91%        | 6.47%        |
| Restaurantes Y Hoteles             | 9.43%         | 0.10%        | 3.76%        | 2.64%        | 0.17%        | 3.14%        | 2.56%        |
| Bienes Y Servicios Diversos        | 5.36%         | 0.14%        | 2.40%        | 2.19%        | 0.14%        | 2.70%        | 1.95%        |

Source: Grupo Bancolombia, DANE.

## Main results of inflation in Colombia – Traditional classifications

|                                     | Ponderación   | jun.-19       |              |              | jun.-18      |              |              |
|-------------------------------------|---------------|---------------|--------------|--------------|--------------|--------------|--------------|
|                                     |               | Mes           | 12 meses     | Año corrido  | Mes          | 12 meses     | Año corrido  |
| <b>Total</b>                        | <b>100.0%</b> | <b>0.27%</b>  | <b>3.42%</b> | <b>2.71%</b> | <b>0.15%</b> | <b>3.20%</b> | <b>2.47%</b> |
| <b>Alimentos*</b>                   | 23.8%         | 0.57%         | 4.83%        | 4.66%        | 0.02%        | 1.74%        | 2.27%        |
| <b>Sin alimentos**</b>              | <b>76.2%</b>  | <b>0.17%</b>  | <b>3.16%</b> | <b>2.22%</b> | <b>0.21%</b> | <b>3.81%</b> | <b>2.55%</b> |
| <b>Sin alimentos y regulados***</b> | 60.0%         | 0.23%         | 2.55%        | 2.07%        | 0.24%        | 3.23%        | 2.17%        |
| <b>Regulados***</b>                 | <b>16.2%</b>  | <b>-0.09%</b> | <b>5.33%</b> | <b>2.84%</b> | <b>0.10%</b> | <b>5.82%</b> | <b>3.86%</b> |
| <b>Transables***</b>                | 18.4%         | 0.24%         | 1.17%        | 1.41%        | 0.28%        | 1.83%        | 1.32%        |
| <b>No transables***</b>             | <b>41.6%</b>  | <b>0.23%</b>  | <b>3.36%</b> | <b>2.37%</b> | <b>0.21%</b> | <b>4.27%</b> | <b>2.79%</b> |

\* Incluye restaurantes

\*\* Excluye alimentos y restaurantes

\*\*\* Clasificación provisional

Source: Grupo Bancolombia, DANE.

## Outlook and Implications of Monetary Policy

**This report suggests that, against our expectation of inflation of 3.4% by the end of 2019, some upward risks persist.** Our base estimate results from the balance between rising food inflation, which should not deviate beyond 4.5%, and the stability of core inflation slightly above 3%. However, the last readings of the food basket already impose some pressure on this projection, and from now on this impulse can be aggravated by factors that now look weak but can't be discarded, such as the prolongation of El Niño in what remains of 2019 or a convincing manifestation of the effects of road closures on the prices of agricultural products. Finally, a reactivation of the transfer of the depreciation of the COP towards the basket of tradables would culminate with the stability observed today in core inflation, and would alter one of the factors that keeps today headline inflation from pronouncedly deviating from the 3% target.

**We believe that the upward evolution of inflation will not result in an interest rate movement by the Central Bank.** June's inflation report stated again that the upward pressures on inflation come from elements related to supply, such as food, whose impulses are transitory and therefore should quickly disappear. However, these shocks may result in some upward revision of inflation expectations. That is why we consider that keeping the interest rate at 4.25%, in a slightly expansive area, looks like the most appropriate balance between such upside risks and an evolution of economic activity that sustains a recovery, but that looks paused, and that requires a continuity of the monetary stimulus. In fact, we believe that, at least with respect to prices, the latest information makes a cut in the repo rate less likely. Thus, we expect the repo rate to remain at 4.25% for what is left of 2019.