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Uruguay Strategy Flash

Uruguay's Monthly Inflation Prints +0.61%mom

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September CPI prints +0.61%mom, coming in 8bp over the +0.53%mom expectations portrayed in the BCU's survey. Monthly inflation printed +0.61%mom, — now accelerating relative to the recent prints, which saw a whole trimester of negative prints (May's -0.01%mom, June's -0.46%mom, and July's -0.36%mom), followed by a timid +0.17% rise in August. In addition, food prices, the largest contributor to CPI deacceleration in recent months, finally printed a positive variation in September. In this context, the inflationary process continues to gain momentum, even demonstrating a slight acceleration relative to the recent trimester of negative prints. After posting an average +1.9% monthly print in the first four months of the year, followed by four back-to-back negative variations (-0.74%mom in August, and -0.54%mom, -1.31%mom and -1.27%mom in May, June, and July, respectively), the Food & Non-Alcoholic Beverages segment posted a positive monthly print, clocking in at +1.01%mom. The segment was the main driver behind the monthly increase in the headline gauge. However, an increase in Transport (+1.27%mom), and Hotels&Restaurants (+0.68%mom) also contributed positively to the rise. On the yearly gauge, consumer prices rose by +3.87%, being slashed by nearly 0.24pp relative to an already low +4.11%yoy print in August and clocking in at the lowest mark in 2023. The yearly index in September was aided by the tailwind provided by the baseline effect, as Sep-22's print came in at +0.8%mom, nudging the headline trend down. In this context, the yoy variation now sits comfortably inside of the BCU's target, coming under the +6%yoy upper bound for the fourth month running after standing over the mark for two full years. With September's inflation clocking in at +0.61%mom, YTD inflation currently stands at +4.21%, increasing relative to August.

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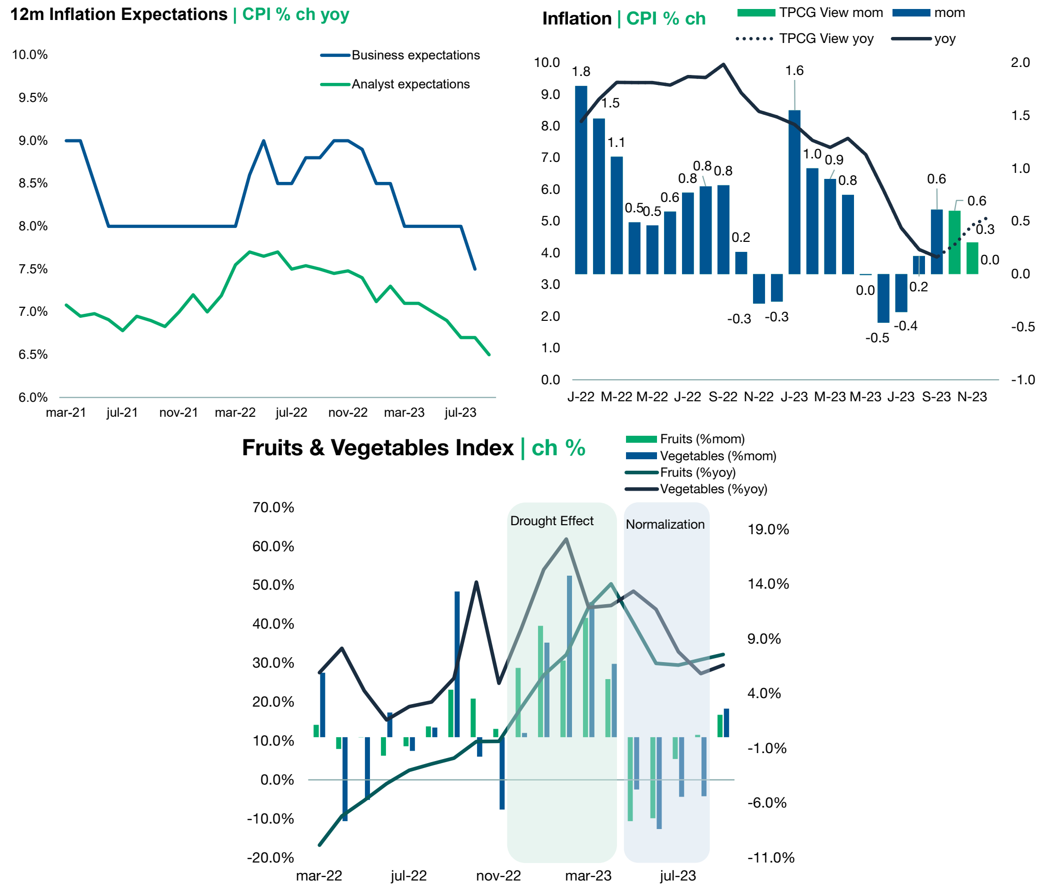
September's CPI print was largely explained by the rise in the Food & Non-Alcoholic Beverages segment, which compounded with rises in Transport and Hotels&Restaurants prices. The Food & Non-Alcoholic Beverages segment finally reverted its negative trend, caused by the normalization of food prices after the drought. Its +1.01%mom print was the first positive variation since April, which suggests the end of the extremely volatile behavior that characterized the segment since its 1Q23 spikes. Still, in September, subsection performance was also marked by volatility, with several sub-indexes experiencing large decreases, deepening most trends relative to July. The always volatile Fruits segment seems to have normalized, experiencing a +2.06%mom rise, as did Vegetables increasing by +2.61%mom. Meat prices experienced a decrease in September, with the subsection printing a -0.72%mom drop, with Fish following suit, as the latter decreased by -1.64%mom. However, the largest contributor inside the segment was Non-Alcoholic Beverages, which experienced a +6.56%mom rise, largely driven by a hike in water prices (+33.15%mom). This came on the back of the government reimposing taxes on bottled water, a measure which was implemented due to the dry climatic conditions causing water shortages all around the country during 2Q23. In this context, Food & Non-Alcoholic Beverages' contribution singlehandedly added 26bp to the monthly print. The other subsections that affected prices significantly were in Transport (+1.27%mom), and Hotels&Restaurants (+0.68%mom). The first rose mainly due to increases in Gasoil (+5.94%mom) and Fuel (+4.55%mom), while the fall in Airplane Ticket prices (-10.68%mom), offset part of the rise. This segment contributed 14bp to the monthly increase of the general index. The second was affected by a rise in Hotel prices (+2.26%mom) nudging the headline index upwards by another 6bp. The rest of the sectors experienced increases mostly in the +0.2%mom — +0.6%mom range, contributing the remainder of the September print.

Figure 1: September's inflation came slightly over expectations



Source: TPCG Research based on INE & CINVE

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We find the print to be credit positive, albeit we believe inflation is poised to reaccelerate during 4Q23 and 1Q24, with the headline index still remaining inside the BCU's target range. As we expected, the end of the drought marked an abrupt correction in Food prices, which tilted the general index strongly to the downside, after being the major cause of the strong increases in monthly inflation at the start of the year. With September's print showcasing an increase in food prices, it seems as if the situation has finally normalized, with both the Fruits and Vegetables subsections posting positive variations. In this context, we now expect prints to converge more clearly to core inflation, which stands near the 0.2%-0.4% level. However, taking a look at the yoy index, it seems that inflation has troughed. The +3.87%yoy mark is artificially low, in the sense that it was aided by a strong baseline tailwind and the negative prints coming out of the drought. In 4Q23, the baseline effect will reverse, starting to push the headline index upwards. In addition, the administration's income and fiscal policies are also consistent with an acceleration of inflation in the medium term. Finally, looking at tomorrow's COPOM meeting, we expect the BCU to lower the policy rates by 50bp. In our view, even if the worse-than-expected performance of the economy and the very low inflation prints could warrant a 75bp reduction, the recent performance of the USDUYU, which widened significantly, advocates for a tighter cut.

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