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Uruguay Strategy Flash

Uruguay's Monthly Inflation Prints -0.36%mom

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July CPI prints -0.36%mom, coming in 76bp under the +0.4%mom expectations portrayed in the BCU's survey. Monthly inflation printed -0.36%mom, — competing a whole trimester of negative prints, with May's-0.01%mom print and June's -0.46%mom, which followed a strong +0.75% in April. The collapse of the monthly index continues to be explained by the end of the drought, as it continues to pressure food prices to the downside, allowing them to normalize. In this context, the inflationary process prolonged its abrupt stop in July, which is consistent with the normalization of agricultural prices. After posting an average +1.9% monthly print in the first four months of the year, the Food & Non-Alcoholic Beverages segment presented a negative monthly variation for the third month in a row, coming in at -1.27%mom, which followed prints of -0.54%mom and -1.31%mom in May and June, respectively. The subsection had printed +1.93%mom in April, +2.24%mom in March, +1.84%mom in February, and +1.85%mom in January, accumulating a +8.1% rise in the first four months of the year. The segment nearly singlehandedly spearheaded the decreases, with both Clothing (-2.59%mom) and Transport (-0.57%mom) also deepening the negative trend, while a very timid increase in Restaurants&Hotels (+0.54%mom) partially offset the drop in food and fuel prices. The rest of the segments had little to no influence on the monthly print. On the yearly gauge, consumer prices rose by +4.79%, being slashed by nearly 1pp relative to an already low +5.98%yoy print in June, and clocking in at the lowest mark in 2023. The yearly index in July was aided by the tailwind provided by the baseline effect, as July-22's print came in at +0.77%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 second month running after standing over the mark for two full years. With July's inflation clocking in at -0.36%mom, YTD inflation currently stands at +3.4%, dropping relative to June.

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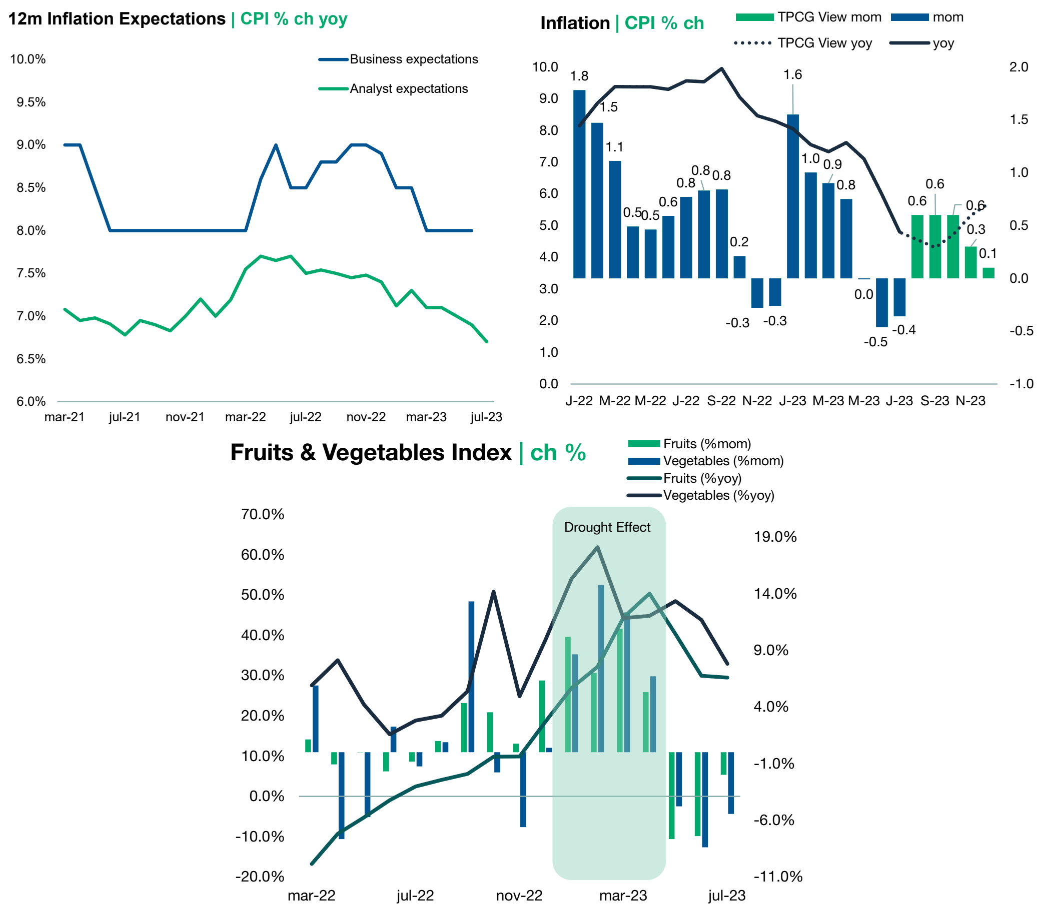
July's CPI print came mostly on the back of the Food & Non-Alcoholic Beverages segment, as the normalization of food and water prices compounded with drops in fuel and clothing prices to deepen the deflationary trend. The Food & Non-Alcoholic Beverages continued its current trend, deepening the reversion of the 1Q23 prints, posting a drop -1.27%mom drop following another negative print in June (-1.31%mom). In July, subsection performance was also marked by volatility, with several sub-indexes experiencing large decreases, deepening most trends relative to May. The always volatile Fruits segment experienced a -1.99%mom drop, as did Vegetables, which fell by -5.44%mom, as the normalization of food prices continues to normalize post-drought. Meat prices also experienced a decrease in July, with the subsection printing a -0.73%mom drop. Dairy products saw their prices increase, by +0.75%mom. Another key drop was observed in the Beverages subsection, which fell by -5.37%mom, mostly explained by the drop in Water prices (-24.16%), as the recent improvement in climatic conditions managed to ease the acute water shortage that was plaguing the country in recent months. In this context, Food & Non-Alcoholic Beverages' contribution singlehandedly contributed 34bp to the monthly print. The only other three subsections that affected prices significantly were Transport (-0.57%mom), Clothing (-2.59%mom), and Restaurants&Hotels (+0.54%mom). The first dropped mainly due to decreases in Gas (-0.31%mom), and Airplane Ticket prices (-5.71%mom), contributing 6bp to the monthly fall of the general index. The second was affected by a drop in Women's Clothes prices (-4.36%mom), which nudged the headline index downwards by another 7bp. Finally, Restaurants and Hotels rose driven by Restaurant Services (+0.55%mom), contributing an extra 5bp to the monthly gauge. Finally, the rest of the sectors experienced increases mostly in the -0.3%mom — +0.4%mom range, contributing the remainder of the July print, with the exception of Health, which clocked in at +0.81%mom, offsetting the monthly fall by 3bp.

Figure 1: July's inflation came way under expectations



Source: TPCG Research based on INE & CINVE

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We find the print to be credit positive, and strongly supportive of our local currency position in nominals. 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. In this context, the drought added volatility to an inflationary process that was not reflecting a strong deacceleration in the core index, which averaged a +0.27% mom print from February to July. This month, the effect of the drought started to wane, as both the Fruits and Vegetables subsection posted reductions of less magnitude than in June. However, this was compensated by the normalization of water prices as the hydric crisis in the main metropolitan areas of the country eased. Still, we continue to believe that the current deflationary process is also transitory. We expect prints to converge to core inflation, which stands near the 0.2%-0.4% level. In addition, a high baseline will probably push the headline yoy index to the downside up until 4Q23. However, the weak prints of the last quarter of 2022 should probably force the yoy gauge slightly upwards.

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