Economic Analysis

In July, annual inflation resumed its downward trend, standing at 6.9%

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Food inflation remained stable, while non-food inflation declined again, but more sharply

In July, monthly inflation was 0.20% and annual inflation was 6.86%, slightly below market analysts' expectations according to Banco de la República's survey (0.28%) and our forecast (0.24%). With this, the result is 32 bps below the previous month's figure and ends 3 months of stability of total inflation at around 7.2%. In this month, upward pressures from food inflation moderated, resulting in an annual change of 5.26%. Non-food inflation continued to decline, registering an annual change of 7.24%, 40 bps lower than the previous month's figure.

Food inflation remained stable, registering an annual change of 5.26% in July. Upward pressures were driven by the perishable and processed food auctions. In the case of the former, annual inflation rose 26 bps to 10.5%. This result was explained by significant increases in some subclasses such as potatoes and onions. In the case of processed products, annual inflation reached a variation of 4.4%, 21 bps above the previous month's figure, which is mainly explained by base effects, with specific pressures in subclasses such as chocolates. In the case of meats, the annual change was reduced by 62 bps, with an annual inflation of 1.3%, where most of the reduction is due to a base effect.

In general, perishables continue to be guided by harvest cycles, slightly disrupted by weather factors and high volatility, as usual for this sub-basket, generating upward pressures on the basket. Meanwhile, base effects continue to play a prominent role in this basket. In August and September, food inflation is expected to experience some relief from base effects, thanks to high records in the monthly change in these months for 2023. Although the effects of the La Niña phenomenon are yet to be defined, they can be expected to be moderate, with no relevant impact on inflation.

Annual non-food inflation, meanwhile, declined by 40 bps in July, falling to 7.24%. This is a greater moderation than that reported in the last two months (28 bps on average). This result comes with the lowest monthly change for this basket since October 2021 (0.20%), which supports the expectation of gradual moderation of inflationary pressures. The largest adjustment within this basket came from administered prices, with an annual change that decreased by 112 bps compared to the figure presented in June, standing at 12.17%. Despite the significant decrease, this remains the basket with the highest inflation within the total, almost doubling it. The adjustment was due to reductions in electricity tariffs, implemented by energy trading companies, possibly in response to the government's proposal to pay the tariff option for a segment of the population. Added to this is an important base effect, which may be largely associated with fuel prices, as no increases in gasoline prices have been implemented in these months, while several adjustments were made in the second part of 2023.

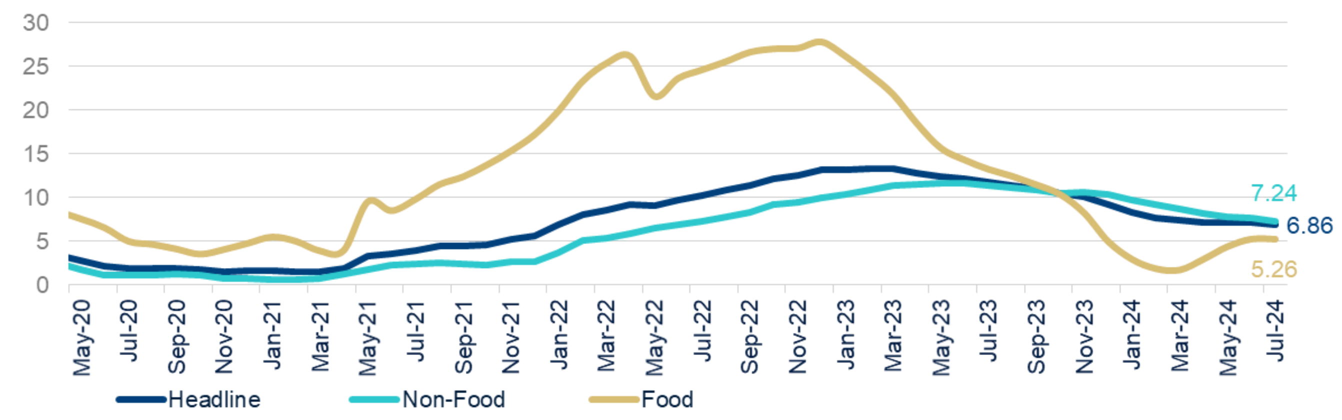
The second basket with the largest adjustment was that of goods. This basket registered an annual change of 1.20%, 23 bps lower than in June. Within it, there were strong base effects in subclasses such as mobile telephone equipment and men's clothing. This dynamic has been sustained for several consecutive months, leading to inflation well below that of the rest of the baskets and of total inflation.

As usual, the basket with the smallest reduction was services, with a decrease of 20 bps compared to June, presenting an annual change of 7.69%. However, the size of the reduction is larger than that observed in the last 3 months, which also points to some additional easing. The adjustments were due to base effects, mainly in subclasses such as meals in table service establishments and services related to co-ownership. This is in addition to reductions in inflation in subclasses such as inter-municipal transport.

Overall, the evolution of non-food inflation continues to be closely affected by base effects, although the monthly change is starting to approach its historical averages. This is present in differential levels between the main baskets with that of the tightest goods and that of the most persistent services. For the remainder of the year the trend will continue to be downward and we expect to see the decline both due to base effects and a gradual dissolution of persistence. Despite this, we still consider that there is high uncertainty due to factors such as the weather (La Niña phenomenon) and its possible impact on transport infrastructure; the timing and speed of the diesel price adjustment; and inflationary inertia factors.

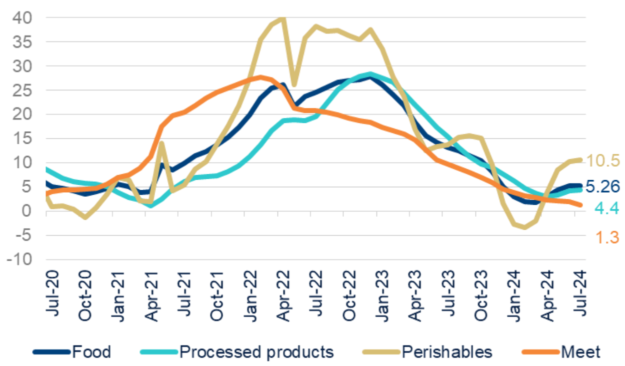
Thus, BBVA Research expects total inflation to continue to fall in the remainder of the year, to around 5.4% in December.

Figure 1. **HEADLINE, NON-FOOD AND FOOD INFLATION** (ANNUAL CHANGE, %)



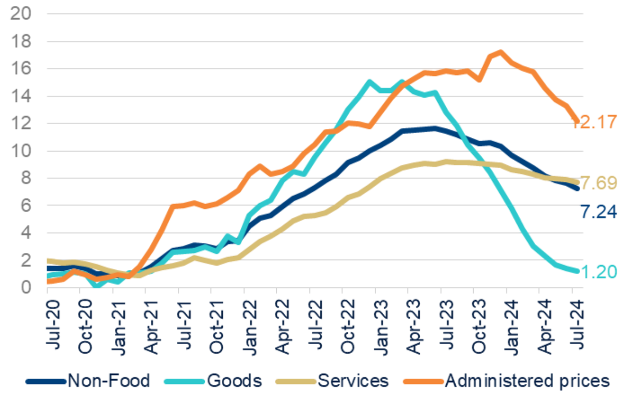
Source: BBVA Research with data from DANE

Figure 2. **FOOD INFLATION MAIN SUB-BASKETS** (ANNUAL CHANGE, %)



Source: BBVA Research with data from DANE

Figure 3. **NON-FOOD INFLATION MAIN BASKETS** (ANNUAL CHANGE, %)



Source: BBVA Research with data from DANE

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