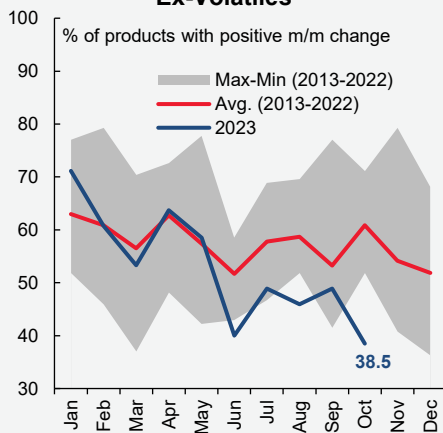


Contributors

Aníbal Alarcón, Senior Economist
 +56.2.2619.5465 (Chile)
anibal.alarcon@scotiabank.cl

Chart 1

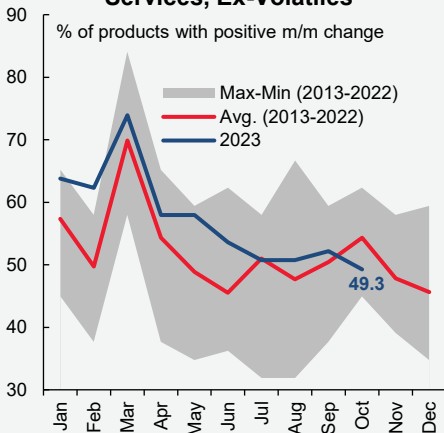
CPI Inflationary Diffusion of Goods, Ex-Volatiles



Sources: Scotiabank Economics, INE.

Chart 2

CPI Inflationary Diffusion of Services, Ex-Volatiles



Sources: Scotiabank Economics, INE.

Chile—October CPI of 0.4% m/m (5% y/y) with Diffusion at Record Lows

- Annual inflation decelerates faster than expected by the central bank and consensus: four products explain 90% of the monthly rise. Some of them could see price reversals in the near term.
- November CPI is expected to be around 0% m/m. We reaffirm our inflation projection of 3.7% y/y in December, reaching sub-3% in March 2024. Watch out for the new CPI basket base 2023=100.
- After the November CPI data, we expect the BCCh to resume rate decreases at a pace of no less than 75 bps.

This morning, the statistical agency (INE) released October CPI data, showing a prices rise of 0.4% m/m, surprising the most inflationary expectations that anticipated a generalized exchange rate pass-through. In our view, this did not occur for two reasons. (1) the exchange rate pass-through is asymmetric to the economic cycle not to its direction, as the central bank (BCCh) highlighted and which explained the delay in the process of rate cuts, consequently placing Chile’s rate among the highest in the world. Excess inventories in commerce and the weakness of the labour market have been sufficient to contain exchange rate pass-throughs. (2) A large part of the depreciation of the CLP has been bilateral with respect to the dollar. That is to say, the CLP has not depreciated sharply with respect to its other trading partners, which implies exchange rate pass-throughs of no more than 10%.

The inflation reading of 0.4% m/m in October (5.0% y/y) is exclusively explained by increases in volatile products, especially food and energy, since inflation ex-volatiles had a 0.0% monthly variation. As a result, inflation ex-volatiles decelerated again in y/y terms, standing at 6.5%. In fact, only four products explained 90% of the m/m inflation increase: gasoline, tourism packages, wine, and soft drinks. The increases in tourism packages and gasoline are mainly explained by the depreciation of the CLP, which should reverse in the coming months.

The inflationary diffusion of the total CPI stood at 43.9% (the share of goods with m/m price increases), the lowest value for an October reading on record (at least since 2009), showing that the downward adjustment of inflation is still strong and is even accentuated at the margin, especially at the level of the core basket. The low level of the indicator is due not only to the low diffusion of goods (38.5%), which also recorded its minimum for the month, but also to the fact that the diffusion of services (49.3%) was at the low end of its range for the first time this year (charts 1 and 2).

Some considerations for monetary policy:

- The exchange rate pass-through of the recent CLP depreciation is very low and limited to some specific products, such as tourism packages and fuels. Contrary to the BCCh’s estimates, the exchange rate pass-through is not being asymmetric with respect to the ups and downs of the exchange rate, but rather the asymmetry is due to the cyclical phase of the economy. CLP depreciations are less inflationary at times of weak domestic demand, while peso appreciations put more downward pressure on prices at times of economic weakness.
- The central bank projected inflation of 4.3% y/y for December, which would be achieved by accumulating 0.6 ppts of inflation between November and December. The BCCh acknowledged a surprise in the August CPI and, certainly, this October CPI should be a surprise for its base projections. Moreover, history shows us that between 2014 and 2020, CPI has not accumulated more than 0.2 ppts in both months.

November 8, 2023

- Regarding the CPI ex-volatiles, the BCCh projected inflation of 6.3% y/y for December, which would be achieved by accumulating 1.1 ppts of inflation between November and December. As in the case of the total CPI, history shows us that between 2013 and 2020, both months have not accumulated inflation above 0.3 ppts.
- Inflation would return to the 3% target (or below) in March 2024. March monthly inflation will also be lower thanks to the new CPI basket. As we pointed out in a previous note regarding the new CPI basket base 2023=100, the March CPI could show a lower incidence of the Education division given the lower participation (of at least 2.5 ppts) in the expenditure captured by the Household Budget Survey, which should be reflected in the new CPI (effect of the free university education). This is important given that historically about 70% of the March CPI is explained by Education.
- We raise the risk of negative inflation in November and/or December. Some emblematic volatile products that injected inflation in the last couple of months are likely to subtract inflation in the last part of the year (gasoline, some vegetables and tourist package). Additionally, the price of new automobiles could resume declines in November considering the low level of sales and the discounts applied to all events in the last few days.

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

™ Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including: Scotiabank Europe plc; Scotiabank (Ireland) Designated Activity Company; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorized by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, and Scotia Inverlat Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.