Strong surprise of higher than expected CPI of October (0.7%)

Behind the price increases is the acceleration of consumption due to the injection of liquidity that households have received and the process of opening up the economy.

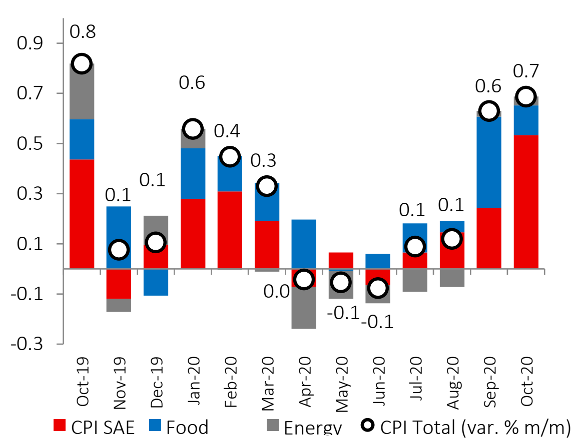
The October CPI variation was well above expectations (Santander: 0.3%; Bloomberg: 0.3%; EEE: 0.3%; EOF: 0.3%; forwards: 0.2%), with a strong incidence of food, housing, durable goods and clothing. The month also saw the reversal of the reduction of the stamp and stamp tax -decreted in April as a measure to face the pandemic-, which contributed almost one tenth to the CPI. With this, after the significant increase in prices in September, annual inflation was just at the 3% goal. While core inflation rose to 2.4%.

Behind the increase in prices are two phenomena whose impact should be transitory. First, there is the injection of liquidity that households received with the withdrawal of pension funds and the Emergency Family Income. Second, the deconfinement process made it easier for people to purchase goods and services. Both events raised consumption very substantially and put pressure on prices. Also the reopening of some services had an impact -such as restaurants-, as price adjustments were made to reflect the higher costs involved in operating under social distancing measures.

We estimate that the factors that have influenced the acceleration of prices in the last two months would have a rather transitory impact. In the case of food prices, where we expected some reversals after the increases in September, we believe that they will remain higher, but we do not anticipate significant increases going forward. Meanwhile, the price of gasoline will continue to decline due to the international drop in oil and the appreciation of the exchange rate. With this, we project that in the last two months of the year the CPI will have zero or slightly negative variations and will close at around 2.7%.

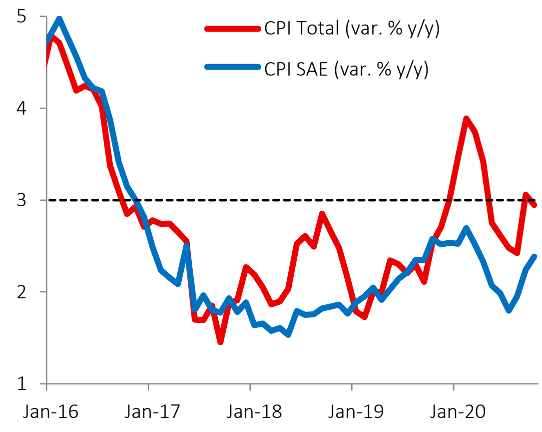
Going forward, the capacity slack in the economy will keep the pressures on prices limited, so inflation is expected to decline to below 3% in the first part of next year. However, a possible second withdrawal of pension funds could generate new pressures for a few months.

CPI surprises again in October



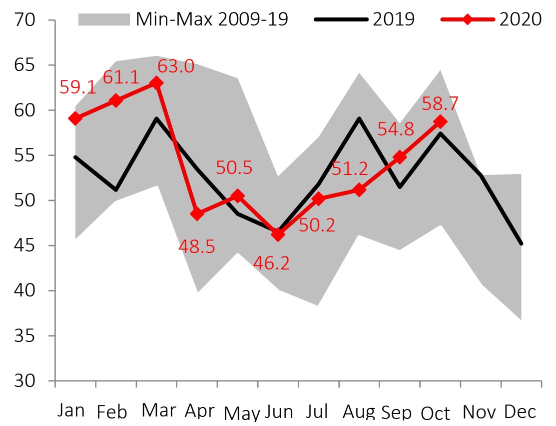
Source: INE and Santander

Inflation returned to the 3% target



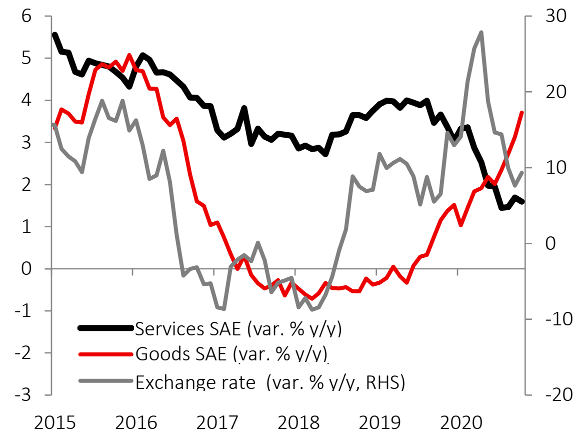
Source: INE and Santander

Price increases were generalized



Diffusion index: percentage of products with an increase in price in the month.
Source: INE and Santander

Prices of godos SAE continue to accelerate, despite moderation in the exchange rate



Source: INE and Santander

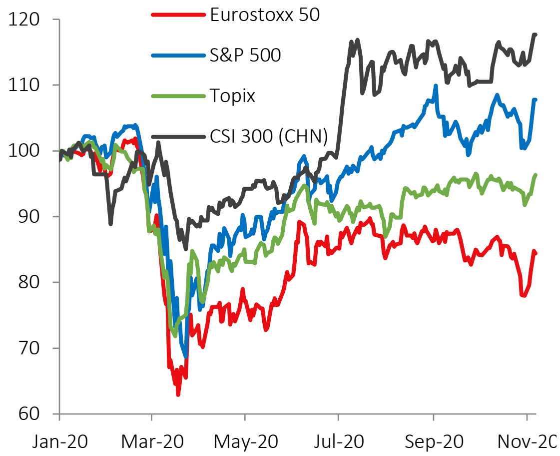
Preliminary results of the elections in the US generate realignment of the markets

As of the closing of this report, the final results of the election were not known. Still, trends are that Democrat Joseph Biden would rise to the presidency while the Senate would remain in the hands of Republicans. Democrats would maintain control of the House of Representatives, but with less slack. If this scenario occurs, the eventual Biden government would have serious difficulties in implementing its ambitious plan, in particular, the tax reform. In the short term, the chances of a strong fiscal package to counter the pandemic are reduced.

After the election, markets tended to retreat, although they have recovered on the prospect that there will be no major changes in economic policy in the coming years. For its part, the slope of the yield curve has flattened, due to the fact that the eventual stimulus package would be less ambitious, and the dollar has weakened almost 2% in the week.

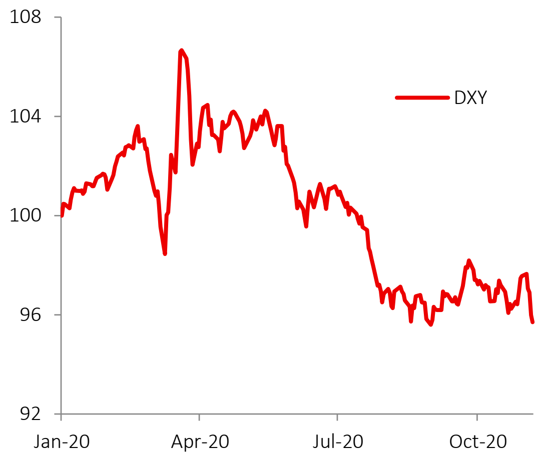
This occurs in a context where the pandemic continues to escalate in advanced economies. In Europe, infections have increased again and a number of countries are adopting containment measures. Meanwhile, in the United States, daily cases have risen above 100,000, the highest figures since the pandemic broke out. The US elections have distracted markets from these developments, but impacts on asset valuations may be seen over the next week.

The main global markets increase after the US elections.



Source: Reuters and Santander

The dollar has tended to weaken globally



Source: Reuters and Santander

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