Significant increase in the CPI in July (0.8%) reflects strong increase in consumption

prices opens the door for a more accelerated withdrawal of the monetary impulse by the Central Bank

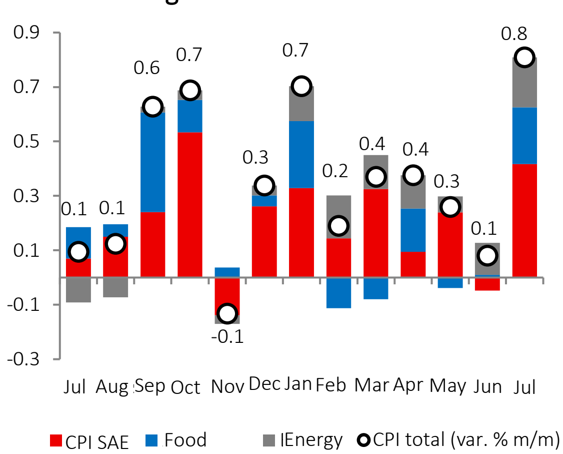
The July CPI was well above market expectations (Santander: 0.4%; Bloomberg: 0.4%), driven by the transportation (0.22 pp) and food (0.21 pp) components. The SAE CPI grew 0.6%, explaining half of the variation in the total index. Considering the low comparison bases - in July 2020 the CPI was 0.1% - annual inflation reached 4.5%, its highest record in five years.

In addition to the price of gasoline, the transportation component was driven by new cars that increased, in a month where there are usually price drops. In the case of food, the increases are generalized among the different products, highlighting the increase in beef. Beyond the products with the highest incidence, 58% of the basket had an advance in the month, placing the price diffusion index at maximum levels for the month of July.

These results reflect the substantial expansion of consumption - as shown by the record trade figures - influenced by the withdrawals of pension funds and fiscal aid, and they occur in a context where international prices have also risen. Given the above, it is possible that the pressures will continue for several months, which will impact inflation by the end of the year. On the other hand, although gasoline will fall in August due to the adjustments to the MEPCO parameters, going forward they will rise again, incorporating the increases in international fuel values observed so far and a more depreciated exchange rate.

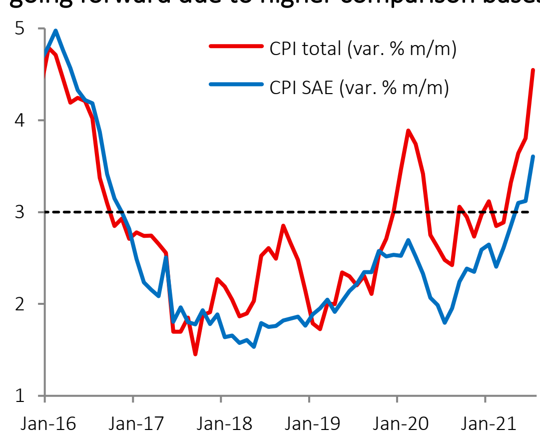
On the other hand, the rapid deconfinement from July will allow the return to operation of non-essential services -such as cinemas and gyms-, which will probably lead to the rise in their values in the first months of operation. Going forward, higher comparison bases will cause the annual variation of the CPI to moderate. All in all, we estimate that inflation will close the year somewhat above 4%.

Inflationary surprise in July is distributed among different categories



Source: INE and Santander

Annual inflation reaches 4.5%, but will descend going forward due to higher comparison bases



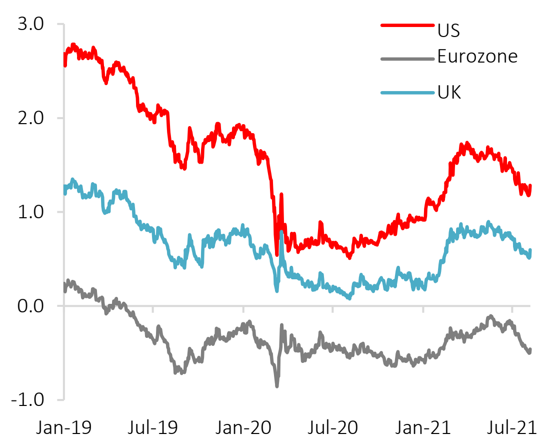
Source: INE and Santander

Global financial markets recover during the week

The stock indices advanced between 1% and 2%, partially recovering the losses of the previous week, especially the Chinese stock market (+ 2% vs -5%). Investor sentiment is torn between the optimism generated by the good quarterly results of large companies and the concern about the increase in infections worldwide. At the close of this report, after positive employment data in the US, long rates in the main economies reversed the downward trend and exhibited significant increases (+ 4bp on average compared to the previous week). In this context, the dollar, which had remained stable, ended up strengthening on the margin (DXY: -0.7%).

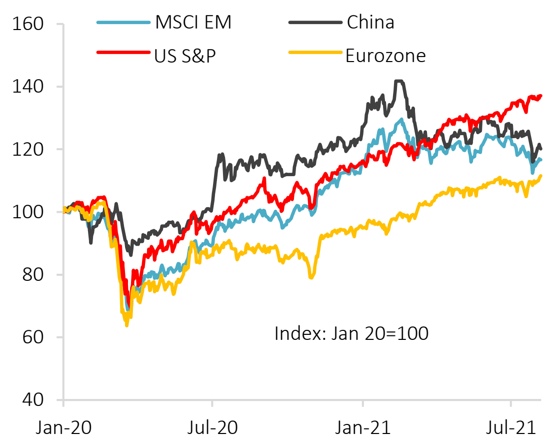
Activity indicators in the US for July, released in the week, remained favorable (Markit manufacturing PMI: 63.4 vs. 63.1 expected; ISM services: 64.1 vs. 60.5 expected). Although the labor market figures, in general, were mixed (ADP jobs: 330,000 vs. 690,000 expected; initial unemployment benefits: 385,000 vs. 383,000 forecast; non-agricultural payrolls: 943,000 vs.-870,000 projected), unemployment surprised with a significant decrease (5.4% vs.-5.7% anticipated). In Europe, with slight surprises, the signs still show optimism in the manufacturing sector and caution in services (manufacturing PMI: 62.8 vs. 62.6 expected; services: 59.8 vs. 60.4 expected), while in China, the manufacturing sector generated concern with a significant slowdown (PMI Caixin: 50.3 vs. 51.0 expected).

10 yr rates reverse trend and close with increases



Source: Bloomberg and Santander

Stock exchanges recover during the week



Source: Bloomberg and Santander

High volatility continues to affect local assets

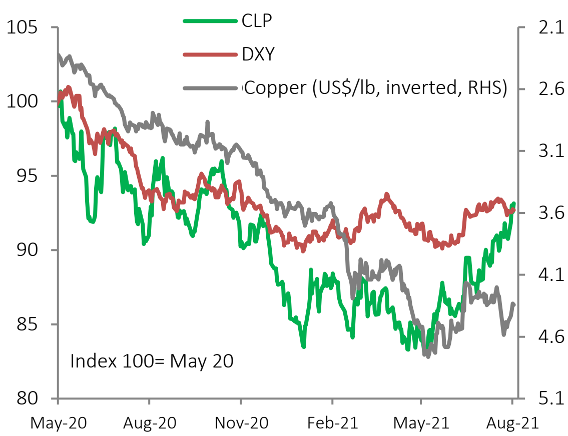
Neither the favorable activity data in June (Imacec: 20.1% y / y) nor the reduction in the number of infections have encouraged local markets. The IPSA closed the week marginally higher, at 4,278 points (0.6%), after good international data. On the other hand, the local currency has continued to weaken, reaching $ 788 per dollar at the end of this report, accumulating a depreciation of almost

4% in the week. This, in a context where, in addition, the price of copper has fallen (-3%) and the dollar has strengthened.

The lower appetite for local assets also affected long-term fixed income instruments. The 10-year benchmark in pesos rose 10bp in the week and exceeded 4.5%. In the opposite direction, the readjustment rates show further falls, around 20 bp so far this day, reflecting expectations of higher inflation going forward after the July CPI was known.

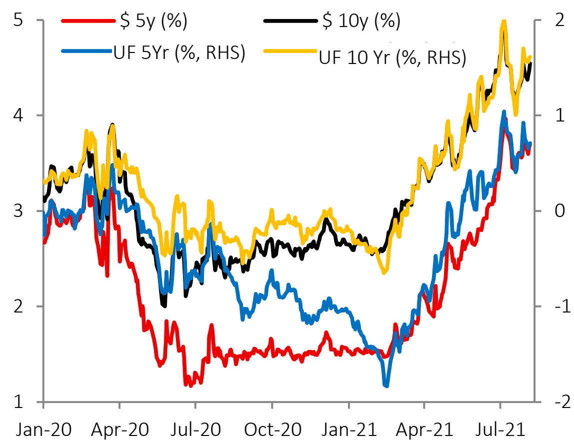
Also, after the inflation record, nominal swap rates rose sharply (+ 25bp on average), pointing to a faster withdrawal of the monetary stimulus. According to the forward curve, the MPR could close the year at around 2%, with a possible 50 bp increase in the next MPR at the end of August.

Depreciation of the Peso associated to the fall in copper, strengthening of the dollar and internal political risk



Source: Bloomberg and Santander

Nominal long-term rates return to an upward trend, while those in UF fall.



Source: RiskAmerica and Santander