Strong rise in the CPI exceeds all expectations

This once again puts pressure on the BCCh's monetary strategy, after the more "dovish" tone of the recent IPoM

Although a substantial increase in prices was expected in March, the 1.9% increase was well above expectations (Santander: 1.5%; Bloomberg: 1.2%). With this, annual inflation rose to 9.4%.

The month's variation reflected the second-round effects of previous price rises, seasonal factors (education) and, above all, the impact of the advance in world food values due to the war in Ukraine. When considering the CPI SAE, which excludes food and energy, the increase in prices was much lower (1.2% MoM; 7.4% YoY).

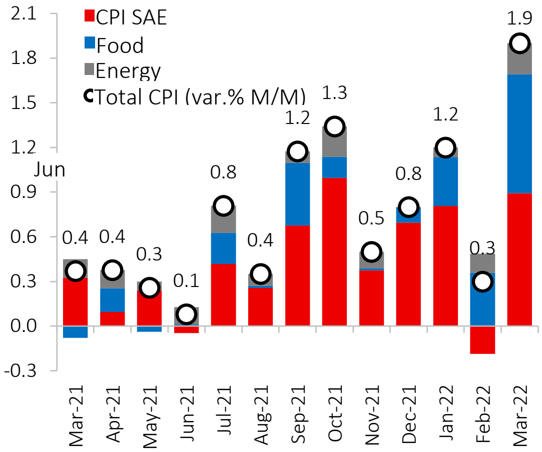
The rise in food prices reported for March "advances" part of what we had considered for April, so we have revised our estimate for this month's CPI downwards marginally, to 0.6%. Still, pressures remain very high. Commodity values have risen sharply and as long as there is no clear resolution to the conflict in Ukraine, they will remain elevated. For its part, the more contractive position of the Fed will lead to a strengthening of the dollar that will also impose increases in imported costs. On the other hand, the moderation in economic activity will put a brake on price increases in the second part of the year. Thus, for the end of the year we estimate that inflation will close at 8%.

This inflationary data for March was certainly above what was projected by the Central Bank in its last Report (1% implicit, when considering the quarterly estimates reported by the issuing institute) and puts pressure again on the conduct of monetary policy, after the more "dovish" tone of the most recent report. In the absence of new inflation data before the next Monetary Policy Meeting to be held in early May, it is likely that the next rate hike will be substantive again, of 100 basis points or more.

Market response

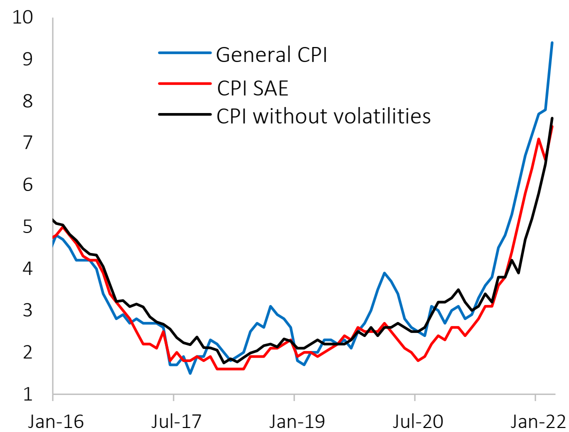
Swap rates reacted with strong increases after publication of the IPC data, in magnitudes between 20 and 40 bp, which will also be reflected in benchmark bond rates. The exchange rate continued with important increases, accumulating a variation of 4.3% in the week, up to $816, in line with the strengthening of the global dollar, even though the price of copper remains at high levels (US$4 .7 per pound).

The variation in March (1.9%) is mainly explained by food



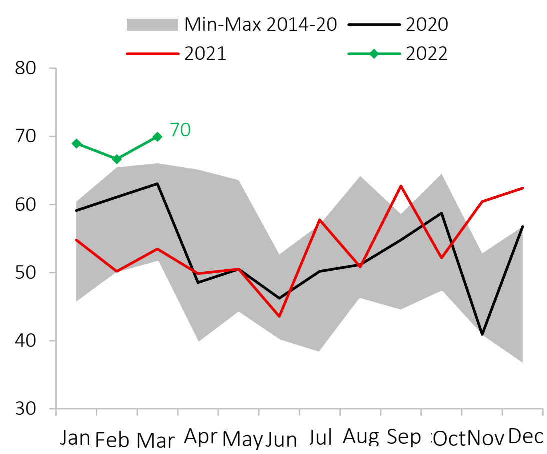
Source: INE and Santander

Twelve-month inflations reaches 9.4% for the first time since 2008



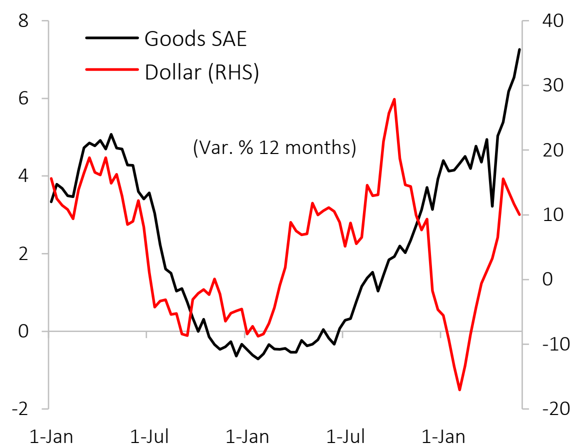
Source: INE and Santander

Price rise was generalized within the basket



Source: INE and Santander

The increase in the prices of goods is accentuated



Source: INE and Santander

International markets close with falls and adjust to a more restrictive Fed

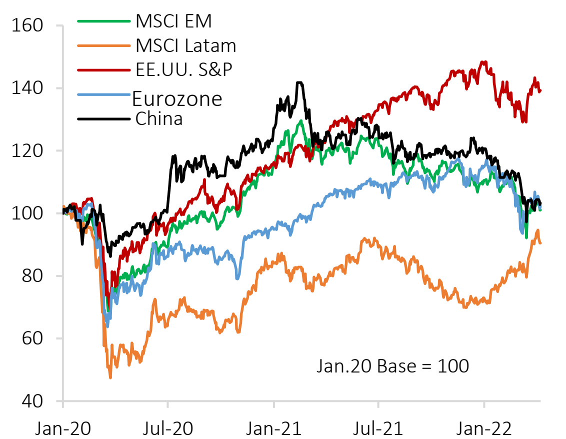
At the international level, the main stock markets registered widespread declines (global MSCI: -1.4%) affected by the concern that persists over the development of the war in Ukraine and the prospect of further tightening of monetary policy in the US, along with a more aggressive approach to shrinking the Fed's balance sheet, as noted in the March meeting minutes. This led to a significant increase in long-term rates (+22 bps on average), with the US T10 at 2.7% (+33 bps) and a strengthening of the global dollar that brought the DXY index to levels close to 100 points -its highest level in two years-, amid an increase in risk aversion (VIX: +2 points).

Despite the challenges and lower growth expectations after the Russian invasion, the activity observed in services in the Euro Zone (PMI: from 54.8 to 55.6) and the US (ISM: from 56.5 to 58.3) rebounded in March, thanks to the economic reopening that occurred after the wave of the Omicron variant. Still, markets remain cautious as accusations of massive war crimes in Ukraine led to further sanctions being imposed, including a European Union ban on oil and coal imports and Russia's expulsion from the United Nations.

For their part, the prices of the main raw materials reflected mixed movements (copper: +1%; WTI oil: -3%; wheat: +5%). The value of WTI oil closes around US$97 a barrel after announcements of the release of strategic reserves by the International Energy Agency (IEA) in addition to those of the US - totaling 240 million barrels- and in the face of an unexpected weekly rise in US inventories.

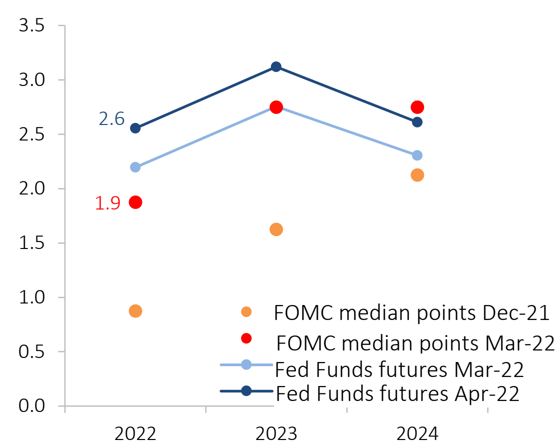
Finally, a strong impact was felt by services activity in China in March, according to the Caixin PMI, which experienced its biggest contraction in two years (42.0 vs. 50.2 previously), affected by mobility restrictions due to outbreaks of coronavirus.

International stock indices show widespread declines at the end of the week



Source: Bloomberg and Santander

The market is positioning itself for a further tightening of monetary policy in the US.



Source: Bloomberg and Santander