

The Cloudy Year Has Just Begun

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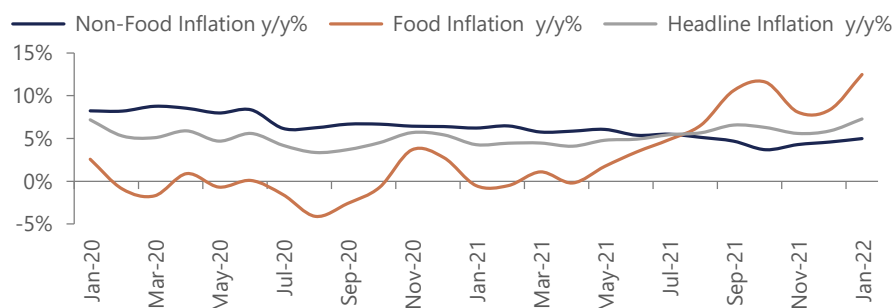
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The highest reading in two years, January's annual urban headline inflation above our expectations: Fueled by the unfavorable base-year effect, upward adjustment in some of subsidized food items, in addition to the last cold wave effect on vegetable prices, annual urban headline inflation surged to +7.3% y/y in January 2022 (vs. our expectations of +6.9% y/y) from +5.9% in December 2021. **The acceleration in inflation came to reflect the continued increase in both food basket inflation at +12.4% y/y (vs. +8.4% y/y in December) and non-food inflation at +5% y/y (vs. +4.6% y/y in December).** The increase in annual food prices was driven by inflation in: (1) bread and cereals (+7.2% y/y vs. +5.5 % y/y in December); (2) dairy and eggs (+12.9% y/y vs. +11.3% y/y in December); (3) vegetables (+17% y/y vs. -6.9% y/y in December); and (4) sugar and related products (+17.7% y/y vs. +5% y/y in December). Non-food inflation also remained on an upward trajectory, driven mainly by the higher contributions of housing and utility baskets and clothing baskets.

On a monthly basis, inflation also accelerated to +0.9% m/m from -0.1% in December: After two months of deflation, food prices reverted to +0.9% m/m (vs. -0.1% m/m in December). The unfavorable weather conditions and subsidized food card price adjustments drove food inflation to reach +2.1% m/m (vs. -1% m/m in December), the highest reading since September 2021. Most of food basket components' inflation was on an upward trend, mainly meat and poultry (+2.1% y/y vs. -1.4% y/y in December); vegetables (+3.5% y/y vs. -7.1% y/y in December); dairy and eggs (+2% y/y vs. +0.5% y/y in December); and sugar and related products (+0.4% y/y vs. +12.1% y/y in December). Monthly non-food inflation rose to +0.36% m/m (vs. +0.32% m/m in December), with clothing and footwear, furniture and household equipment, and the medical basket driving the increase.

Global conditions and an unfavorable base will continue to cloud the inflation outlook for 2022: The CBE's next meeting on 24 March will likely have another close to mid-point target reading in February (7.2% in our estimates). Thus, we do not expect any shift in its monetary stance, at least in March. **Global commodity headwinds remain key upward risks, and the spillover effect of a hawkish Fed policy is expected to become more pronounced by Q2 2022. Thus, an extended hold-rate decision should be enough for now to rein in inflation expectations.**

Figure 1: Food Inflation at its highest level in more than two years



Source: CAPMAS, Prime Research.

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