

Mexico Inflation Flash

June's biweekly inflation: Inflation Surprised Downwards Thanks to Lower Than Expected Non Core Inflation

General: Actual: -0.05% f/f vs. BBVA: 0.08% f/f Consensus: 0.08% f/f

Core: Actual: 0.07% f/f, vs. BBVA: 0.07% f/f Consensus: 0.08% f/f

- Thanks to a strong decline in egg prices non core inflation fell more than expected, pushing down general inflation below market consensus.
- Core inflation increased 0.07% f/f in line with the market consensus. Annually it remains below 3% y/y as the inflation of its goods component keeps moderating.
- Inflation is now clearly heading towards 4% y/y, and in the absence of new supply shocks it should fall below that threshold before September, as favorable fundamentals such as lower international commodity prices and the ample availability of resources within the economy prevail. None the less non-core inflation remains the main upwards risk given the very high volatility shown by its components this year.

June's biweekly inflation fell -0.05% f/f, below our forecast (0.08% f/f) and the market consensus (0.08% f/f), falling in annual terms from 4.63% y/y in May to 4.24% y/y. Core inflation increased 0.07% f/f in line with our estimate and market consensus, annually it fell from 2.9% y/y in May to 2.8% y/y. Non-Core inflation fell -0.4% f/f well below our forecast and market consensus, decreasing in annual terms from 10.6% y/y in May to 9% y/y.

Core inflation remains well below 3.0% thanks to the continuous moderation of its goods component. Goods prices increased 0.04% f/f, causing its annual inflation to fall from 3.5% y/y in May to 3.2% y/y. Its processed food component fell from 4.4% y/y in the previous month to 4.1% y/y. Meanwhile, the inflation of the rest of goods component fell from 2.8% y/y in May to 2.6% y/y, thanks to a still feeble domestic demand, the beginning of summer sales and a stronger peso through most of the year. The prices of services increased from 2.4% y/y in May to 2.5% y/y. This increase in services prices is due to a slight acceleration in housing and the rest of services inflation, however this should be short lived as weak demand still doesn't justify price increases right now. Strong fundamentals such as lower international grain prices and persistent economic slack will continue favoring a low core inflation, which in case of further deceleration of the economy could moderate even more, however if the recent peso depreciation continues, this could partially compensate a decrease in core inflation caused by slower economic activity.

Non Core inflation fell more than expected thanks to a biweekly decrease in livestock prices. Agricultural inflation decreased from 15.1% y/y in May to 1.8% y/y thanks to lower green tomato and lemon prices which had been affected in previous months by bad weather and a plague respectively, and to a very favorable base effect. Livestock inflation increased from 15.1% y/y in April to 15.9% y/y as poultry markets remain affected by the avian flu, however this increase turned out lower than expected as egg prices decreased during the fortnight compensating the pressures affecting chicken prices. Energy prices rose from 8.2% y/y in May to 8.5% y/y because the inflation of gasoline and heating gas keeps increasing strongly as the government is subsidizing less the prices of these products this year in order to rein in the high fiscal cost paid in previous years. Finally, the inflation of tariffs set by local governments increased from 6.5% y/y in May to 7.0% y/y, thanks to increases in the prices of public transportation. Agricultural and livestock prices should continue falling in coming weeks and thanks to a favorable base effect non core inflation will fall sharply in coming months, however public prices remain an upwards risk, given the smaller energy subsidies and weak local government finance.

Bottom line: Inflation is now clearly heading towards 4% y/y, and in the absence of new supply shocks it should fall below that threshold before September, as favorable fundamentals such as lower international commodity prices and the ample availability of resources within the economy prevail. None the less non-core inflation remains the main upwards risk given the very high volatility shown by its components this year.

Table 1

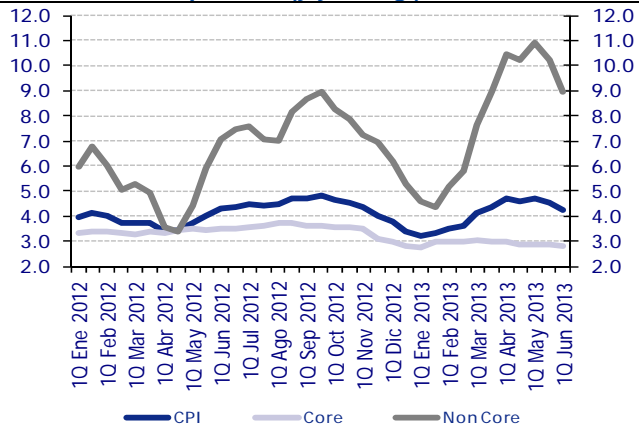
Inflation (y/y and f/f % change)

	Bi-weekly % change			Annual % change		
	1F Jun 2013	Consensus	BBVA Research	1F Jun 2013	Consensus	BBVA Research
CPI	-0.05	0.08	0.08	4.24	4.38	4.38
Core	0.07	0.08	0.07	2.83	2.84	2.83
Non Core	-0.44	0.08	0.11	8.95	9.51	9.55

Source: BBVA Research

Graph 1

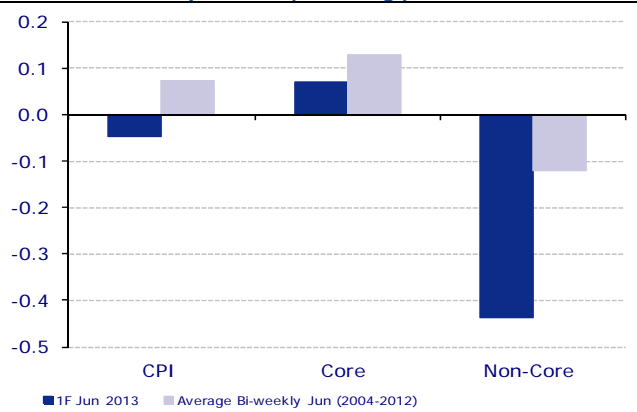
Inflation and components (y/y % chg.)



Source: BBVA Research with INEGI data.

Graph 2

Inflation and components (f/f % chg.)



Source: BBVA Research with INEGI data.

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