



Inflation Observatory

August 24, 2009

Inflation in the first half of August (0.11% core and general) included the low growth cycle and, for the second consecutive two-week period, reached a level lower than expected

- General and core inflation in the first half of August (0.11%) was below the expected level (general: market and BBVA at 0.23 and 0.31%; core: market and BBVA at 0.19 and 0.14%), and therefore year over year inflation dropped from 5.44% in July to 5.12 in the first half (core from 5.32 to 5.19). These results highlight the impact of the low economic growth cycle and the downward trend of previous supply shocks (e.g., foreign exchange costs), bringing the inflationary trend in line with that announced by Banxico for the quarter (range between 4.75 and 5.25%). With regard to our estimates, the main difference can be seen in agricultural prices (non-core), owing to the fact that the price increases in the wholesale markets were not reflected in the two-week period.
- Core inflation was in line with our forecasts and shows positive signals for the services and non-food goods sub-indexes. Although certain pressures remain in processed foodstuffs, they are easing. The main components of core inflation show bimonthly variations lower than those registered one year ago. In particular, the bimonthly performance of service prices should be pointed out: bimonthly inflation for housing (0.05%) and "other services" (-0.19) reached the lowest level in the history of these sectors for a similar period, with education (0.39) being the second lowest record. The price of goods, in turn, registered variations similar to its historical average, which might suggest that the previous supply shocks in tradable goods (following the exchange rate collapse in late 2008) are reversing and further reductions in its year over year inflation are to be expected.
- Non-core inflation was much better than expected thanks to its more volatile components (agricultural prices) and the adjustment in some controlled prices (telephony) owing to increased competition. Although increases in agricultural prices were registered in supply centers during the first half of the month, they did not affect the end consumers to the same extent, although this situation might change in the second half of the month should the increases in wholesale markets persist.
- Outlook: the inflationary trend is in line with our forecasts, and thus the possibility of 2009 closing under 4% in annual terms, close to our central estimate of 3.85%, cannot be ruled out. However, the risk is biased upwards given the volatility of agricultural prices and the upward evolution of international energy prices, which may give rise to accelerated increases in the prices of gasoline for 2010. In addition, the introduction of new taxes for 2010 owing to fiscal weakness may bring forward the CPI reviews at the end of 2009.

Mexico: Bi-Weekly Inflation

	avg bi-week			
	2001-2008	1Q Ago 2007	1Q Ago 2008	1Q Ago 2009
CPI-Mx	0.25	0.20	0.31	0.11
Core-Mx	0.21	0.18	0.23	0.11
Goods	0.22	0.17	0.34	0.21
Food products	0.19	0.27	0.36	0.18
Other Goods	0.24	0.09	0.32	0.24
Services	0.19	0.19	0.14	0.01
Rent	0.13	0.12	0.09	0.05
Education	0.89	0.93	0.93	0.39
Other serv.	0.00	-0.03	-0.13	-0.19
Non Core-Mx	0.39	0.27	0.52	0.11
Farm products	0.65	0.23	0.15	-0.51
Fruits//Vegetables	0.39	-0.19	-0.99	-0.62
Meat//Eggs	0.84	0.49	0.88	-0.44
Public managed	0.25	0.29	0.70	0.45
Energy	0.36	0.48	1.17	0.64
Controlled prices	0.12	0.11	0.23	0.27

Inflation: Short term deviations (% mom)

	Ago-09		Change
	Forecast -1 month	bi-weekle revision	pp
CPI-Mx	0.31	0.27	-0.04
Core-Mx	0.30	0.28	-0.02
Goods	0.38	0.39	0.01
Food products	0.15	0.34	0.19
Other Goods	0.53	0.43	-0.10
Services	0.22	0.18	-0.05
Rent	0.20	0.15	-0.05
Education	0.69	0.66	-0.03
Other serv.	0.08	0.03	-0.05
Non Core-Mx	0.34	0.24	-0.11
Farm products	0.90	0.07	-0.84
Fruits//Vegetab	2.10	0.90	-1.20
Meat//Eggs	0.09	-0.50	-0.59
Public managed	0.08	0.32	0.24
Energy	0.13	0.57	0.44
Controlled price	0.04	0.11	0.07