

Mexico Inflation Flash

May's first fortnight inflation: annual upturn caused by agricultural prices

General: Actual:-0.48% f/f vs. BBVA:-0.62% f/f Consensus:-0.45% f/f
Core: Actual: 0.14% f/f, vs. BBVA:0.03% f/f Consensus:0.11% f/f

- Inflation fell -0.48% f/f during May's first fortnight, however in annual terms it increased and reached 3.71% y/y.
- Core inflation also raised in annual terms driven by the services index, which has increased from 2.18% y/y during March's second fortnight to 2.66% y/y in this fortnight. This increase was due mainly to the base effect, given the very low inflation during May 2011, since there are no demand pressures affecting core prices.
- Inflation will end the year below 4%, though the possibility of upwards surprises that drive it above this threshold during the following months must not be disregarded.

During May's first fortnight inflation reduced -0.48% f/f, however, in annual terms it rebounded to 3.71% y/y from the 3.41% y/y registered in April. Core inflation raised 0.14% f/f also rebounding in annual terms from 3.39% y/y in April to 3.51% in the fortnight. Non-core inflation reduced -2.55% f/f, however it was the biggest contributor to the annual increase raising from 3.4% in April to 4.4%.

The observed rebound in core inflation was caused mainly by the behavior of the prices of services, which increased from 2.48% y/y in April to 2.66% y/y in May. This behavior was due to annual increases in the prices of education and in the rest of services component, within this last one we highlight the increases suffered by the prices of dinners and restaurants. On the other hand the prices of merchandise increased less from 4.48% y/y in April to 4.53%. **The prices of merchandise have stabilized around 4.5% since March, however we must be vigilant to pressures that may arise caused by the exchange rate pass-through and/or the prices of grains in the world.** We insist that **core inflation is not being affected by demand pressures.**

Non-core inflation picked up due to the increase experienced during the fortnight by agricultural prices that in annual terms meant increasing from 0.86% in April to 3.61% y/y in the fortnight. Despite the favorable behavior in agricultural prices seems to be fading, we believe the increases experimented by this prices in the short term will be moderate given the information from wholesale local markets. Administered prices kept reducing annually during the fortnight from 5% y/y in April to 4.87% y/y in the current fortnight; however within energy prices there are some upwards pressures caused by domestic gas prices. Non-core inflation has absorbed several supply shocks since 2011, even when we consider it will not increase dramatically in the short term, the accumulation of this shocks poses downwards rigidity, which will accentuate during the summer.

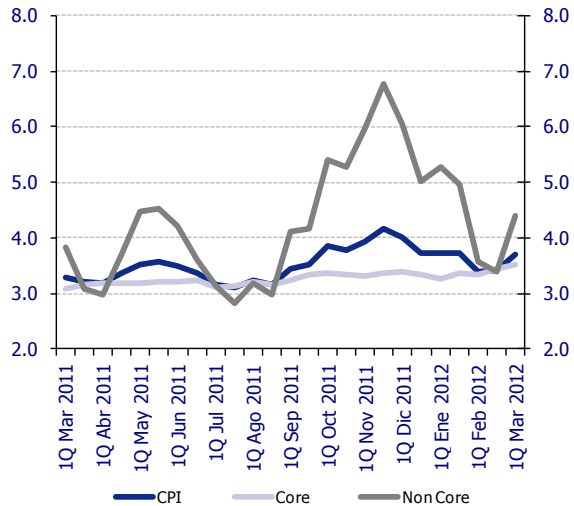
The increase experienced by inflation in annual terms was foreseeable, both because of the surprisingly positive past couple of months, and by the comparison against a relatively low inflation during 2011. We consider that inflation fundamentals remain consistent with inflation below 4% at year's end. However, given the diverse external shocks affecting the exchange rate, if upwards surprises occur in the following months in the non-core component, we can't rule out the possibility that inflation might rise above that threshold transitorily during the 3Q12.

Table 1
Inflation (y/y and ff % change)

Inflation (Bi-weekly and annual % chg.)						
	Bi-weekly % chg.			Annual % chg.		
	1F May 2012	Consensus	BBVA Research	1F May 2012	Consensus	BBVA Research
CPI	-0.48	-0.45	-0.62	3.71	3.74	3.56
Core	0.14	0.11	0.03	3.51	3.47	3.39
Non Core	-2.55	-2.30	-2.76	4.41	4.68	4.18

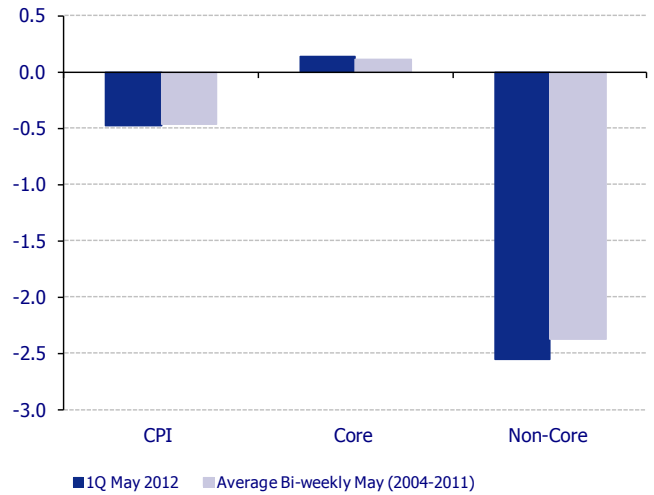
Source: BBVA Research

Graph 1
Inflation and components (y/y % chg.)



Source: BBVA Research

Graph 2
Inflation and components (m/m % chg.)



Source: BBVA Research

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