

Economic Analysis

Strong inflation driven by the summer vacation season

Javier Amador Diaz

Headline: actual: 0.20% FoF (BBVAe: 0.22%; consensus: 0.16%)

Core: actual: 0.14% MoM (BBVAe: 0.15%; consensus: 0.10%)

- **Both headline and core inflation were broadly in line with our above-consensus forecasts**
- **Annual inflation will hover around 4.0% from July to September due to base effects, before decreasing towards 3.7% at the end of the year**

Both headline and core inflation came in broadly in line with our above-consensus forecasts. Headline CPI increased 0.20% FoF in the first fortnight of July (BBVAe: 0.22%; consensus: 0.16%). Annual inflation accelerated to 4.0% (BBVAe: 4.02%; consensus: 3.96%). Core inflation was 0.14% FoF, in line with our forecast (BBVAe: 0.15%, consensus: 0.10%). This print surprised the market and was driven as we expected by the summer vacation season: tourism services and airfares rose strongly. In annual terms, core inflation accelerated to 3.20% (BBVAe: 3.21%, consensus: 3.16%) from 3.09% in the previous fortnight.

Non-core inflation was driven by strong increases in fruits and vegetable prices. Non-core inflation was 0.38% FoF, mostly driven by a strong increase in fruits and vegetable prices (2.1% FoF) as our daily price monitoring suggested. This was partially offset by significant drops in poultry and eggs prices, which decreased 1.8% FoF and 1.7% FoF, respectively.

Core inflation came in line with our above-consensus forecast, mainly driven by strong services inflation. The strong print was mainly driven by core services inflation (0.28% FoF). The increase was driven by the seasonal increase in tourism services prices (8.57% FoF) and airfares (10.15% FoF), as we expected. In contrast, seasonal summer discounts are behind the core goods deflation (-0.02% FoF) which partially offset the strong services inflation. In annual terms, core inflation accelerated to 3.2% from 3.09% in the previous fortnight.

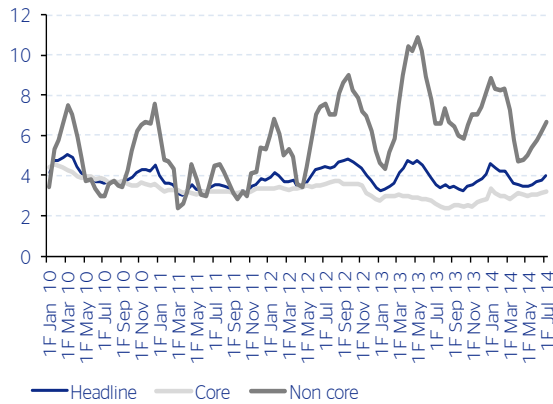
Bottom line: As we expected, due to core inflation seasonality and because of base effects, annual headline inflation to continued to accelerate and reached the upper bound of the inflation target in the first fortnight of July. We expect inflation to remain slightly above 4.0% on average from July to September before decreasing towards 3.7% at the end of the year. Core inflation should remain under control the rest of the year but is likely to accelerate slightly in H2 2014 (to 3.28% on average vs. 3.05% on average during H1 2014) if as expected the economy recovers.

Table 1
Inflation (MoM and YoY % change)

| CPI Inflation | | | | | | |
|---------------|--------------------|-------|-----------|-----------------|-------|-----------|
| | Bi-weekly % change | | | Annual % change | | |
| | 1F Jul 2014 | BBVAe | Consensus | 1F Jul 2014 | BBVAe | Consensus |
| Headline | 0.20 | 0.22 | 0.16 | 4.00 | 4.02 | 3.96 |
| Core | 0.14 | 0.15 | 0.10 | 3.20 | 3.16 | 3.21 |
| Non Core | 0.38 | 0.46 | 0.37 | 6.68 | 6.76 | 6.66 |

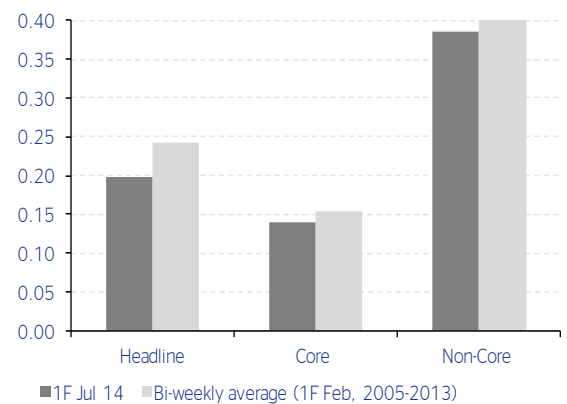
Source: BBVA Research, INEGI

Graph 1
Inflation and components (YoY % change)



Source: BBVA Research, INEGI

Graph 2
Inflation and components (FoF % change)



Source: BBVA Research, INEGI

Disclaimer

This document was prepared by Banco Bilbao Vizcaya Argentaria's (BBVA) BBVA Research and BBVA Bancomer S. A., Institución de Banca Múltiple, Grupo Financiero BBVA Bancomer on behalf of itself and is provided for information purposes only. The information, opinions, estimates and forecasts contained herein refer to the specific date and are subject to changes without notice due to market fluctuations. The information, opinions, estimates and forecasts contained in this document are based upon information available to the public that has been obtained from sources considered to be reliable. However, such information has not been independently verified by BBVA Bancomer, and therefore no warranty, either express or implicit, is given regarding its accuracy, integrity or correctness. This document is not an offer to sell or a solicitation to acquire or dispose of an interest in securities.