

Economic Analysis

Inflation remains subdued

Javier Amador Díaz

Headline: actual: -0.45% FoF (BBVAe: -0.22%; consensus: -0.21%)**Core: actual: 0.03% FoF (BBVAe: 0.10%; consensus: 0.11%)**

- **We revise downwards our year-end inflation forecasts to 2.8% for headline inflation and 2.6% for core inflation, from 2.9% and 2.8% respectively**

Headline inflation came in significantly below expectations in the first fortnight of April, decreasing 0.45% FoF (BBVAe: -0.22%, consensus: -0.21%). In annual terms, headline inflation decreased to 3.03% from 3.30% in the previous fortnight. The inflation print was primarily driven as expected by the seasonal adjustment of electricity tariffs and a reduction in tourism services. The surprise to our forecast came from a larger reduction in tourism services (we thought that the decline would be distributed more evenly between the two fortnights of the month) and declines of perishable food prices driven by a fall in vegetable prices (as opposed to the mild increase we were expecting). Core inflation was 0.03% FoF, much lower than our below-consensus forecast (BBVAe: 0.10%, consensus: 0.11%). In annual terms, core inflation decreased to 2.23% from 2.47% in the previous fortnight. Today's print pushes down our monthly inflation forecasts to -0.19% MoM for headline inflation and 0.13% MoM for core inflation, which leads us to revise down our year-end forecasts to 2.80% for headline inflation and 2.6% for core inflation, from 2.9% and 2.8% respectively. Notably, if our forecasts of headline inflation for April and May are correct (-0.19% and -0.33% MoM, respectively), cumulative inflation to May will be around 0.0% (-0.01%), by far the record low. Even after revising down our year-end forecasts, they leave room to absorb possible pass-through and supply-shocks related pressures in coming months.

The subdued core inflation increase was mainly led by other services prices whose fall more than offset a somewhat higher than anticipated increase in core goods inflation. The core inflation print was mainly driven by the decline in services inflation (-0.15% FoF) on the back of the seasonal reduction in tourism services (-12.2% FoF) and air fares (-15.2%) following the Easter holiday season related increase. Annual services inflation stands at 1.9%, reflecting the reduction in telecommunication services at the beginning of the year but also the weak demand. Meanwhile, core goods inflation increased somewhat more than we were expecting (0.24% FoF) as other core goods inflation showed a 0.30% FoF increase. The limited pass-through seen so far is behind the acceleration in other core goods inflation to 2.5% YoY from 1.8% in the second fortnight of January. Core inflation will likely remain well below 3.0% for the rest of the year.

The drop in vegetable prices and the seasonal adjustment of electricity tariffs are behind the low non-core inflation print. Non-core inflation was -1.89% FoF, pushed down by a 14.1% FoF decrease of electricity tariffs and a 12.2% drop in tomato prices. Additionally, natural gas prices showed a -1.9% FoF decline. Lower natural gas prices contributed to a somewhat larger than expected adjustment of electricity tariffs. May's decline is likely to resemble this larger drop. After surging in March, gasoline prices at the border must have fallen to explain the 0.89% FoF drop in average low-octane gasoline prices.

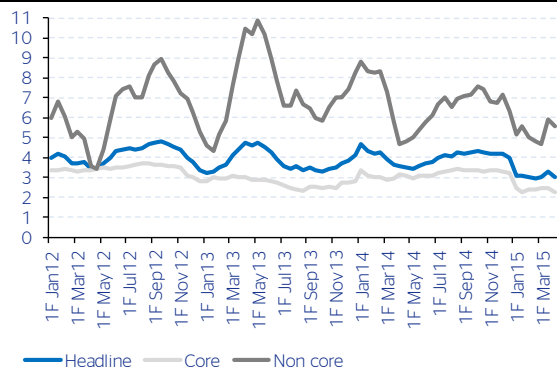
Bottom line: Today's print supports our view that annual inflation is likely to remain close to Banxico's target (3.0%) throughout 2015, and seems to confirm that core inflation will remain subdued despite the weak peso in a context of weak domestic demand.

Table 1
Inflation (FoF and YoY % change)

CPI Inflation						
	Bi-weekly % change			Annual % change		
	1F Apr 2015	BBVAe	Consensus	1F Apr 2015	BBVAe	Consensus
Headline	-0.45	-0.22	-0.21	3.03	3.26	3.28
Core	0.03	0.10	0.11	2.23	2.30	2.32
Non Core	-1.89	-1.33	-1.31	5.57	6.17	6.20

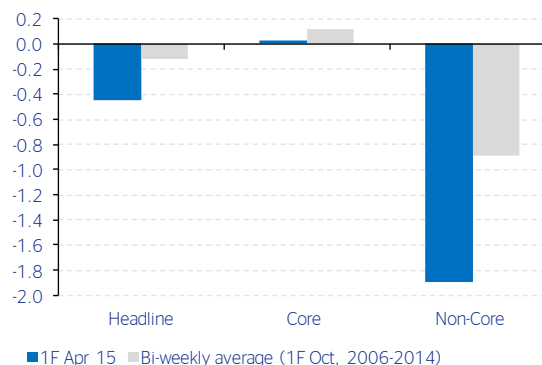
Source: BBVA Research, INEGI

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.