

## Economic Analysis

# Annual headline inflation is at a record low; we lower our year-end forecast to 2.65%

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**Headline: actual: -0.50% MoM (BBVAe: -0.42%; consensus: -0.47%)****Core: actual: 0.12% MoM (BBVAe: 0.14%; consensus: 0.12%)**

- **Headline inflation declined to 2.9% (an historical low); will most likely remain below 3.0% for the rest of the year**

Headline inflation was -0.50% MoM in May, driven by lower-than-expected inflation in the second half of the month (0.04% FoF). In annual terms, inflation declined to 2.88% from 3.06% in April. The downside surprise to our forecast came mainly from a larger than expected decrease in the fruits and vegetables and meat and eggs components. Core inflation was 0.12% MoM, in line with consensus expectations (BBVAe: 0.14%, consensus: 0.12%). In annual terms, core inflation edged up to 2.33% from 2.31% in the previous month. Compared to our forecast, all core components increased in line with our expectations with the exception of the core other goods component which surprised to the downside. After today's print we expect headline inflation to remain below 3.0% the rest of the year and we lower our year-end forecast to 2.65% from 2.75%. The subdued inflation pressures are likely to reflect into lower core inflation than we previously expected. We now expect core inflation to close the year at 2.5% (2.6% previously). These forecasts leave room to absorb possible pass-through and supply-shocks' related pressures in coming months (e.g., the possible reversal of perishable food prices).

**The lower core inflation print was mainly led by low other core goods prices.** The core inflation print was mainly driven by a low increase in goods inflation (0.08% MoM), which was much lower than we anticipated (BBVAe: 0.16%). FX pass-through remains modest: other core goods annual inflation remained stable in May (2.44% vs 2.45% in April). Core services inflation increased broadly in line with our expectation (0.13% MoM, BBVAe: 0.14%) and continues to reflect the soft demand. Core inflation will likely remain below 2.5% for the rest of the year and will increase until January next year due to base effects and then gradually as economic growth firms up and core inflation returns to its long-term trend.

**The large drop in perishable food prices and the seasonal adjustment of electricity tariffs are behind the low non-core inflation print.** Non-core inflation was -2.40% MoM (BBVAe: -2.27%), pushed down by a 23.3% MoM decrease of electricity tariffs as a result of the start of warm season tariffs in 10 additional cities. Declines in meat and eggs prices (-1.64% MoM) surprised us to the downside (BBVAe: -1.18%), mainly due to the larger than expected decrease in eggs prices (-12.3% MoM). Fruits and vegetables prices also declined more than we anticipated (-0.84% MoM vs BBVAe: -0.24%), mainly driven by the large decline in tomato prices (-12.6% MoM).

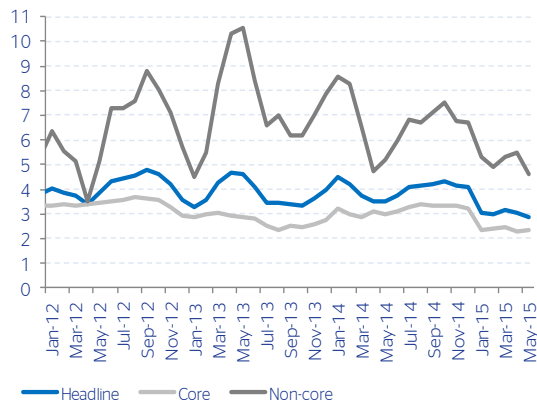
**Bottom line: Today's print supports our view that core inflation will remain subdued despite the weak peso in a context of weak domestic demand.**

Table 1  
**Inflation (MoM and YoY % change)**

Inflation					
	MoM % change			YoY % change	
	May-15	BBVAe	consensus	May-15	Apr-15
Headline	-0.50	-0.42	-0.47	2.88	3.06
Core	0.12	0.14	0.12	2.33	2.31
Non Core	-2.40	-2.27	-2.42	4.64	5.46

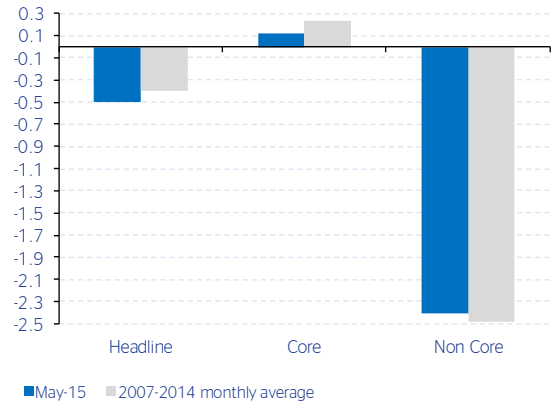
Source: BBVA Research, INEGI

Graph 1  
**Inflation and components (YoY % change)**



Source: BBVA Research, INEGI

Graph 2  
**Inflation and components (MoM % change)**



Source: BBVA Research, INEGI

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