



May inflation better than expected due to non-core factors: electricity, telephony and agriculture. Core inflation continues its downward trend.

- Headline inflation for May was -0.29% (BBVA forecast -0.26%, market forecast -0.27%) and core inflation 0.26% (BBVA forecast 0.22%, market forecast 0.26%). Yoy inflation for the month therefore rose from 6.17% (April) to 5.98% (May), and core inflation from 5.81 to 5.56%.
- All of the core annual inflation components, except non-food goods, continued their downward trend. May goods inflation (0.54%) is relatively higher than usually recorded this month, which is due to still-high upturns in processed food and heavy increases in “other goods”, caused by commercial goods. In spite of this and with an absence of shocks in food raw materials, the goods category is expected to exert less pressure on general inflation. Monthly services inflation (0.01%) recorded this indicator’s all-time low, due to the heavy decline in prices of services other than education and housing. This could be explained by the downturn in demand for services in light of the low economic growth cycle, which was made worse by the swine flu epidemic (e.g. general tourist services).
- Non-core prices accounted for most of the inflation downturn due to administered prices (electricity) and to a lesser extent to controlled prices (telephone). Although the monthly fall in non-core prices was expected, its scope (-1.79%) was narrower than usually recorded in May (-1.91% average for 2003-08). As regards administered prices, the drop in electricity rates was not as significant as we estimated, although it is worth pointing out that the fall in controlled prices (-0.43%) was the greatest fall for May in the track record of these categories. One explanation is the building competition in some markets such as telephony.
- Outlook: we still think that the extent of the slowing economy should become clear in annual inflation downturns for the rest of 2009. We believe that inflation could end 2009 at 3.8% in yoy terms, although there are some upward risks linked to a possible increase in exchange rate volatility and non-core prices, as well as the lack of flexibility on local markets (which take a long time to respond to the economic cycle with price cuts).

Mexico: Inflation 2009

	Monthly change (%)		Annual change (%)		Dif. (pp)
	Avg. May 2003-08	May-09	Abr-09	May-09	
CPI-Mx	-0.31	-0.29	6.17	5.98	-0.19
Core-Mx	0.26	0.26	5.81	5.56	-0.25
Goods	0.30	0.54	7.17	7.02	-0.14
Food products	0.46	0.57	9.07	8.42	-0.65
Other Goods	0.17	0.52	5.63	5.89	0.26
Services	0.23	-0.01	4.55	4.20	-0.35
Rent	0.30	0.14	3.66	3.38	-0.28
Education	0.10	0.10	5.76	5.77	0.01
Other serv.	0.20	-0.23	5.08	4.50	-0.58
Non Core-Mx	-1.91	-1.79	7.18	7.17	-0.01
Farm products	-0.55	-0.03	11.97	13.39	1.42
Fruits//Vegetables	-1.38	-0.15	8.39	13.03	4.63
Meat//Eggs	0.02	0.04	14.34	13.62	-0.72
Public managed	-2.56	-2.74	4.77	4.01	-0.76
Energy	-5.23	-4.98	4.04	2.99	-1.05
Controlled prices	0.07	-0.43	5.53	5.03	-0.50

