

# Economic Watch

## Mexico

May 09, 2011

Economic Analysis

Pedro Uriz Borrás

pedro.uriz2@bbva.bancomer.com

## Expected upturn in annual inflation is underway

### Inflation April 2011

- **Almost no changes, in accordance with CPI expectations in April. On an annual basis, inflation increased from 3.0% in March to 3.4%.**
- **Core inflation increased 0.08% mom, in line with our forecast of 0.09%.**
- **Performance over the next two months will determine the intensity of the upturn in inflation in 2011.**

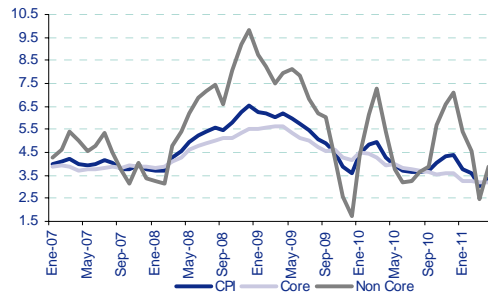
General inflation remained almost unchanged in April, falling -0.01% mom. This is due to downward factors such as the coming into force of summer electricity prices in some cities around the country, the stability of non-food goods prices and a new fall in telephone prices). The year-on-year climb, which will continue for the next two or three months, is the result of a comparison with a few months in 2010 that recorded very low growth rates in prices and the current situation in which, as well as the aforementioned downward factors, there are risks of an upturn due to the performance of commodity prices.

Core inflation rose 0.8% in April, reaching annual stability at 3.2% in March. Food prices continue to be the main upward factor. In April they rose 0.6% mom, 6% yoy since the 5.5% yoy result registered in March, which is much higher than the trend recorded by the other components in the core index. Prices in other goods and services are still performing positively, due to the exchange rate appreciation and the prevailing supply gap to meet growth in domestic consumer demand. This is clear from available estimates of the output gap -with a slow uptrend- or the unemployment rate figures -above levels prior to the 2009 crisis- or moderate real worker income levels. In April, the other services component stood out, falling -0.6% mom due to the fall in mobile telephone prices (-11.4% mom) and Internet service prices (-6.7% mom). This more than offset the increase in vacation packages (4.26% mom) due to the Easter vacation. So far this year, the accumulated fall in telephone services overall is -4.8%.

Non-core inflation fell -0.3% mom, with increases in agricultural prices (7.2% mom) due to tomato prices (55.9% for the month). Energy prices dropped -3.25% mom due to the coming into force of summer electricity prices in several cities. Finally, the trend in government prices continued to be surprisingly positive, falling slightly in April (-0.03% mom). This trend is largely due to the reduction and, in some cases, cancellation of the car owners tax in several states.

Inflation has begun to climb in annual terms, which is determined by the impact on the CPI from main risks such as high oil prices and food *commodity* prices in international markets. However, positive factors limiting inflation such as exchange rate appreciation and the lack of pressure from domestic demand are still around. The intensity of the upturn in inflation in the coming months will determine whether it ends the year within the central bank's variability range (the target is 3% with a variability margin of 1% either way):

Chart 1  
General inflation and components (% yoy change)



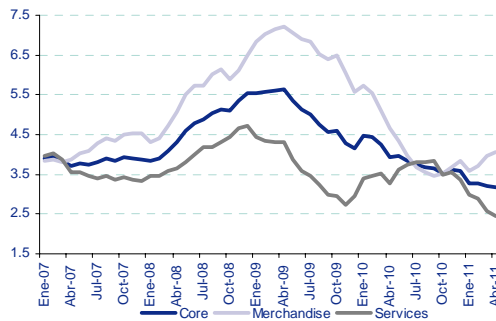
Source: BBVA Research with Banxico data

Table 1  
Inflation breakdown (% yoy and mom change)

	Weight	MoM % Chg.			YoY % Chg.		
		Abr-10	Abr-11	Promedio Abr 03-09	Feb-11	Mar-11	Abr-11
<b>CPI</b>	<b>100.00</b>	<b>-0.32</b>	<b>-0.01</b>	<b>0.11</b>	<b>3.57</b>	<b>3.04</b>	<b>3.36</b>
<b>Core</b>	<b>74.77</b>	<b>0.11</b>	<b>0.08</b>	<b>0.27</b>	<b>3.26</b>	<b>3.21</b>	<b>3.18</b>
<b>Merchandise</b>	<b>37.03</b>	<b>0.25</b>	<b>0.35</b>	<b>0.33</b>	<b>3.71</b>	<b>3.97</b>	<b>4.07</b>
Processed Food	14.67	0.17	0.58	0.42	4.78	5.55	5.98
Other Merchandis	22.35	0.32	0.17	0.25	2.86	2.75	2.60
<b>Services</b>	<b>37.74</b>	<b>-0.02</b>	<b>-0.15</b>	<b>0.21</b>	<b>2.89</b>	<b>2.57</b>	<b>2.44</b>
Housing	17.86	0.11	0.20	0.28	2.12	2.10	2.19
Education	5.20	0.06	0.07	0.11	4.49	4.46	4.47
Other Services	14.68	-0.17	-0.56	0.18	3.07	2.34	1.93
<b>Non-Core</b>	<b>25.23</b>	<b>-1.66</b>	<b>-0.28</b>	<b>-0.39</b>	<b>4.53</b>	<b>2.46</b>	<b>3.90</b>
Farm Produce	8.07	-2.29	3.06	0.56	3.09	-1.69	3.70
Fruits/Vegetables	3.27	-5.01	7.22	1.48	4.76	-6.36	5.71
Meats	4.80	-0.30	0.16	0.04	2.04	1.86	2.33
<b>Energy &amp; Govt.</b>	<b>17.17</b>	<b>-1.24</b>	<b>-2.11</b>	<b>-0.95</b>	<b>5.32</b>	<b>4.96</b>	<b>4.04</b>
Energy	7.77	-2.37	-3.25	-1.72	5.88	5.96	5.00
Govt. Fees	9.39	0.61	-0.03	0.36	4.38	3.27	2.62

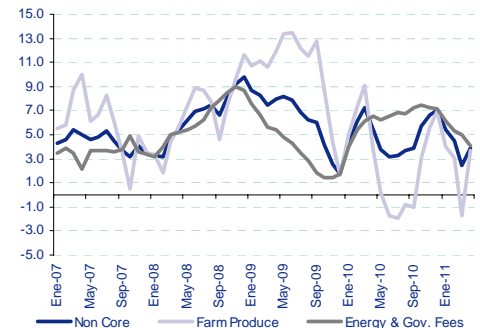
Source: BBVA Research with Banxico data

Chart 1  
Core inflation and components (% yoy change)



Source: BBVA Research with Banxico data

Chart 2  
Non core inflation and components (% yoy change)



Source: BBVA Research with Banxico data

Chart 1  
Inflation forecast for May (% yoy and mom change)

	Peso (%)	Monthly change (%)				Annual change (%)		
		2003- 2009	Mar-11	Abr-11	May-11	Mar-11	Abr-11	May-11
<b>CPI-Mx</b>	<b>100.0</b>	<b>-0.31</b>	<b>0.19</b>	<b>-0.01</b>	<b>-0.39</b>	<b>3.04</b>	<b>3.36</b>	<b>3.61</b>
<b>Core-Mx</b>	<b>74.8</b>	<b>0.24</b>	<b>0.30</b>	<b>0.08</b>	<b>0.18</b>	<b>3.21</b>	<b>3.18</b>	<b>3.12</b>
Goods	37.0	0.33	0.48	0.35	0.33	3.97	4.07	4.17
Food products	14.7	0.48	0.90	0.58	0.60	5.55	5.98	6.34
Other Goods	22.4	0.22	0.17	0.17	0.14	2.75	2.60	2.51
Services	37.7	0.16	0.15	-0.15	0.06	2.57	2.44	2.26
Rent	17.9	0.28	0.21	0.20	0.20	2.10	2.19	2.14
Education	5.2	0.10	0.04	0.07	0.10	4.46	4.47	4.49
Other serv.	14.7	0.07	0.11	-0.56	-0.10	2.34	1.93	1.57
<b>Non Core-Mx</b>	<b>25.2</b>	<b>-2.18</b>	<b>-0.16</b>	<b>-0.28</b>	<b>-2.27</b>	<b>2.46</b>	<b>3.90</b>	<b>5.10</b>
Farm products	8.1	-0.48	-1.25	3.06	-0.29	-1.69	3.70	7.10
Fruits//Vegetables	3.3	-1.21	-3.05	7.22	-0.90	-6.36	5.71	14.32
Meat//Eggs	4.8	0.02	0.05	0.16	0.18	1.86	2.33	2.54
Public managed	17.2	-3.21	0.44	-2.11	-3.40	4.96	4.04	3.98
Energy	7.8	-5.20	0.76	-3.25	-5.40	5.96	5.00	5.15
Controlled prices	9.4	0.10	-0.15	-0.03	0.11	3.27	2.62	2.59
					<i>Monthly Revision</i>			<i>Monthly Revision</i>

Source: BBVA Research with Banxico data

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