

Deflation in the 1st half of May explained by summer discounts on electricity tariffs

- **INEGI just published its inflation report for the first half of May**
- **Headline inflation (May): -0.48% 2w/2w (Banorte-Ixe: -0.53% 2w/2w; consensus: -0.34% 2w/2w)**
- **Core inflation (May): 0.08% 2w/2w (Banorte-Ixe: 0.12% 2w/2w; consensus: 0.11% 2w/2w)**
- **Deflation in the first half of May was mainly explained by the summer discounts on electricity tariffs**
- **With these numbers, annual inflation remains at 2.53%**

Consumer prices decreased 048% 2w/2w in in the first half of May, below consensus. Core inflation was 0.08% vs. our 0.12% estimate. The main deviation from our forecast comes from: (1) A lower than expected contribution of government tariffs prices (0.1bps vs. our 2.4bps); (2) a lower than expected contribution of goods prices (2.6bps vs. our 4.7bps); (3) an overestimation of agriculture prices (-2.7bps vs. our -1bps); and (4) a larger than expected contribution of energy prices (-55.6bps vs. our -63.6bps), as shown in the table below.

May's 1H inflation by components

% bi-weekly incidence

	INEGI	Banorte-Ixe	Difference
Total	-0.48	-0.53	0.05
Core	0.06	0.09	-0.03
Goods	0.03	0.05	-0.02
Processed foods	0.04	0.02	0.02
Other goods	-0.02	0.03	-0.05
Services	0.04	0.04	0.00
Housing	0.02	0.01	0.01
Education	0.00	0.00	0.00
Other services	0.02	0.03	-0.01
Non-core	-0.57	-0.62	0.06
Agriculture	-0.03	-0.01	-0.02
Fruits & vegetables	-0.05	0.02	-0.07
Meat & eggs	0.02	-0.03	0.05
Energy & government tariffs	-0.55	-0.61	0.07
Energy	-0.56	-0.64	0.08
Government tariffs	0.00	0.02	-0.02

Source: Banorte-Ixe with data from INEGI and Banco de México.

Note: Contributions might not add due to the number of decimals allowed in the table. Previous to year 2011, contributions might not add because of the change in CPI-calculation methodology.

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Deflation in the first half of May was explained by the summer discounts on electricity tariffs. These came down 23.94% subtracting 52.7bps to inflation during the period in question. Meanwhile, agricultural prices were down 0.28% 2w/2w on the back of a 1.34% decline in the prices of fruits and vegetables, due to sharp falls in the prices of tomatoes (-7.04%) and lemons (-7.31%), among others. Similarly, in the core index, merchandise prices increased 0.07% 2w/2w on the back of higher prices of processed foods (0.28%) and a 0.1% reduction in “other merchandises” prices. Moreover, services prices rose 0.09% on the back of higher housing costs (+0.11%), while education costs increased only 0.01%. Finally, other services prices expanded 0.10% due to increases in the cost of restaurants (0.34%), which more than made up for the drop in mobile phone services (-1.31%).

With these numbers, annual inflation stands at 2.53% from 2.54% in the previous month. Meanwhile, core inflation edged up to 2.92% from 2.83% in April.

From our fixed income and FX strategy team

Modest relief rally in local rates as a favorable CPI in Mexico is counterbalancing stronger U.S. data. Local bonds are trading with a modest 3bps rally, benefited by well-anchored inflation dynamics in Mexico, despite stronger U.S. data this morning supporting the hawkish view from several Fed speakers depicted in recent days. Despite today’s relief rally, we remain cautious in terms of Mexican securities. We suggest waiting for better entry levels in the long belly of the Mbonos curve. It is our take that the short-end will remain pressured in tandem with deteriorated dynamics in the FX market since the end of April. In terms of CPI-linked Udibonos, we expect them to continue underperforming Mbonos in the following weeks despite an attractive breakeven, but with a negative carry that will lower the demand for this type of assets.

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