

Inflation in the 1H of March explained by the higher prices of tourism services

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- **INEGI just published its inflation report for the first half of March**
- **Headline inflation (1H-Mar): 0.29% 2w/2w; Banorte: 0.35% 2w/2w; consensus: 0.25% 2w/2w; (range of estimates: 0.08% to 0.35%); previous: 0.04% 2w/2w**
- **Core inflation (1H-Mar): 0.24% 2w/2w; Banorte: 0.24% 2w/2w; consensus: 0.24% 2w/2w (range of estimates 0.2% to 0.31%); previous: 0.14% 2w/2w**
- **Inflation in the first half of March was explained by pressures on other services, particularly tourism services and air fares**
- **With these results annual inflation stands at 5.17%, below the 5.34% seen in February**
- **Gains in local rates on risk aversion in spite of slightly higher inflation**

Consumer prices increased 0.29% 2w/2w in the first half of March, standing below our forecast (0.35% 2w/2w) but above consensus (0.25% 2w/2w). Core inflation was up 0.24% 2w/2w, in line with our estimate. The main deviation from our forecast comes from a lower than expected contribution from fresh fruits and vegetables, which turned out to be 2bps, below our 7.5bps estimate, as shown in the table below.

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1H-March inflation by major subcomponent

Bi-weekly incidence, %

	Observed	Banorte forecast	Difference
Headline	0.29	0.35	-0.05
Core	0.17	0.18	0.00
Goods	0.05	0.06	-0.01
Processed foods	0.02	0.03	-0.01
Other goods	0.03	0.04	0.00
Services	0.12	0.12	0.01
Housing	0.02	0.03	0.00
Education	0.00	0.00	0.00
Other services	0.10	0.09	0.01
Non-core	0.12	0.17	-0.05
Agricultural	0.05	0.10	-0.04
Fresh fruits and vegetables	0.02	0.08	-0.05
Meat and egg	0.03	0.02	0.01
Energy and government regulated	0.07	0.07	0.00
Energy	0.06	0.07	-0.01
Government regulated	0.01	0.00	0.01

Source: INEGI, Banorte

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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Inflation in the first half of March was explained by pressures on the prices of other services, particularly tourism services and air fares. In particular, the cost of other services increased 0.61% 2w/2w on the back of higher prices of tourism services (9.62% 2w/2w), air fares (13.81% 2w/2w), and restaurants (0.25% 2w/2w). Additionally, processed food prices increased 0.10% 2w/2w. Moreover, prices of other goods edged up 0.19% 2w/2w while housing costs increased 0.12% 2w/2w on the back of a similar increase in home ownership costs.

Regarding the non-core index, energy prices increased 0.55% 2w/2w on the back of and higher prices low-grade (0.91% 2w/2w) and electricity (0.75% 2w/2w), while LP gas costs decreased 0.6% 2w/2w. Moreover, prices of fruits and vegetables edged up 0.68% 2w/2w, driven by higher prices of tomatoes (19.85% 2w/2w) and lemons (31.75% 2w/2w). However, these were offset by the fall in the price of potatoes (-4.13% 2w/2w), and chayotes (-17.99% 2w/2w), among others.

With these figures, annual inflation continued edging down to 5.17% vs. 5.34% in February. Additionally, core inflation came down to 4.15% from 4.27% in the previous month. We continue expecting inflation to show a downward trend to finish 2018 at 4.3%. In the coming months, we will focus on the evolution of energy prices, considering the possible increase in the international reference price –given the start of the US driving season–, as well as the behavior of agricultural prices, and the impact they might have in Mexico’s CPI.

From our fixed income and FX strategy team

Gains in local rates on risk aversion in spite of slightly higher inflation. Today’s CPI report came slightly above market consensus but below our forecast, with a fortnightly reading of 0.29% 2w/2w, with the annual print from 3.34% to 5.17%. The effect on rates was modest, with local bonds benefitting from the strong rally in global rates in a context of lower risk appetite. Mbonos are gaining 2-3bps along the curve and TIE swaps by 1-3bps, with longer tenors even extending gains relative to trading levels before the release. CPI-linked Udibonos are gaining around 2bps, benefiting our short-term tactical trade idea of long positions in the Jun’19 security opened earlier this week (for details, see: “*Fixed-Income and FX Weekly*”, <pdf>, March 20, 2018). Although we acknowledge an attractive valuation in the belly of MBonos, we recommended on Thursday reducing exposure ahead of yesterday’s FOMC decision and today’s inflation report. In spite of the latter, we hold a positive view in these assets for investment strategies with a mid-term horizon. Lastly, we highlight more attractive relative valuations in real rates according to breakevens, with the 3- and 5-year at 3.57% and 3.63%, respectively, while mid- and long-term inflation expectations have cheapened, with the 10-year at 3.64% from 3.72% in the previous week and the 30-year at 3.76% from 3.77%.

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