

## Deflation in April was explained by lower electricity and agricultural prices

- **INEGI just published its inflation report for April**
- **Headline inflation (Apr): -0.32%/m/m (Banorte-Ixe: -0.26%/m/m; consensus: -0.25%/m/m)**
- **Core inflation (Apr): 0.22%/m/m (Banorte-Ixe: 0.21%/m/m; consensus: 0.19%/m/m)**
- **Deflation in April was explained by summer discounts on electricity tariffs along with lower agricultural prices**
- **With these numbers, annual inflation is at 2.54% vs. 2.6% in previous month**
- **Local rates rallying in tandem with their U.S. counterparts and benefited by today's CPI report**

**Consumer prices declined more than expected (-0.32%/m/m) in April.** Core inflation was 0.22% vs. our 0.21% estimate. The main deviation from our forecast comes from: (1) A larger than expected reduction in agricultural prices (-13.3bps vs. our -10bps); (2) a lower than expected contribution of government tariffs (-6.5bps vs. our -3.4bps); (3) an overestimation of services prices (2.2bps vs. our 2.8bps); and (4) a larger than expected contribution of merchandise prices (14.4bps vs. our 13.3bps), as shown in the table below.

**April's inflation by components**  
% monthly incidence

	INEGI	Banorte-Ixe	Difference
Total	-0.32	-0.26	-0.054
Core	0.16	0.16	0.006
Goods	0.14	0.13	0.011
Processed foods	0.06	0.06	0.003
Other goods	0.08	0.08	0.009
Services	0.02	0.03	-0.005
Housing	0.03	0.03	0.000
Education	0.00	0.00	0.000
Other services	-0.01	-0.01	-0.006
Non-core	-0.49	-0.43	-0.064
Agriculture	-0.13	-0.10	-0.033
Fruits & vegetables	-0.17	-0.15	-0.022
Meat & eggs	0.04	0.05	-0.014
Energy & government tariffs	-0.36	-0.34	-0.028
Energy	-0.30	-0.31	0.004
Government tariffs	-0.06	-0.03	-0.031

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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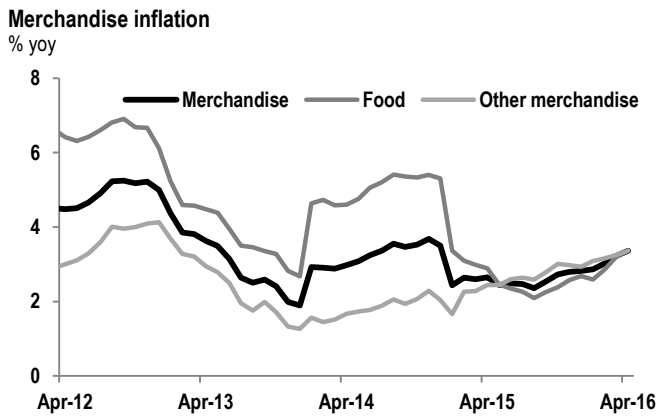
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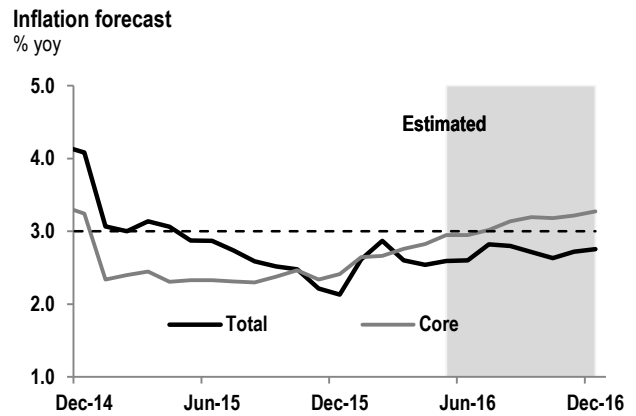
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**Deflation in April was explained by summer discounts on electricity tariffs along with lower agricultural prices.** Energy prices declined 2.94% m/m on the back of a 13.1% reduction in electricity tariffs, while prices of low grade gasoline increased 1.13% m/m. Meanwhile, agricultural prices fell 1.39% m/m explained by significant declines in the price of tomatoes (-17.8%); onions (-25%), Serrano chilies (-26.5%) and other chilies (-17.6%), which more than compensated for the increase of 62.5% in the price of lemons, in the first half of the month. Meanwhile, in the core index, prices increased 0.42% m/m on the back of a 0.38% increase in the prices of food, while the price of other merchandise increased 0.45% m/m. With regard to services inflation, prices of housing and education were up 0.2% and 0.02% m/m, respectively while prices of other services decreased 0.08%, as a result of lower prices of tourism services (-8.1%) and air transportation (-9.4%). Finally, government tariffs fell 1.2% m/m explained by lower fees of electric transportation (-13.3%) and urban bus (-2.8%).

**With these data, annual inflation is at 2.54% vs. 2.6% in the previous month.** Meanwhile, core inflation is at 2.83% from 2.76% in March. Merchandise inflation shows a rising trend edging up from 2.8% at the end of last year to 3.5% in April (see chart below left), probably explained by a gradual pass-through from exchange rate to prices. Nevertheless, lower prices of energy and agricultural prices are more than compensating for these increases, so we continue to see inflation of around 2.8% at the end of the year (see chart below right).



Source: Banorte-ixe with data from INEGI



Source: Banorte-ixe with data from INEGI

*From our fixed income and FX strategy team*

**Local rates rallying in tandem with their U.S. counterparts and benefited by today's CPI report.** Local bonds are partially recovering from last week's sell-off, following closely the rally in sovereign bonds in the U.S. and Europe, and supported by a better-than-expected CPI report in Mexico. In terms of trade ideas, we hold our view that the Mexican yield curve will continue flattening throughout the year. However, we maintain our profit taking recommendation in mid- and long-term Mbonos as a tactical strategy. The rationale this view lies in a twofold argument: (1) likely adjustment in U.S. Treasuries going forward, and (2) country risk spread compression reaching "fair value" levels. Taking into consideration actual valuation of the Mexican yield curve, we suggest waiting for better entry levels for long positions in the belly of the Mbonos curve.

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