

## July inflation – Annual rate increases to 3.6%, in line with expectations

- **Headline inflation (July): 0.66% m/m; Banorte: 0.71%; consensus: 0.65% (range of estimates: 0.40% to 0.72%); previous: 0.55%**
- **Core inflation (July): 0.40% m/m; Banorte: 0.42%; consensus: 0.40% (range of estimates: 0.26% to 0.43%); previous: 0.37%**
- **Relevant increases were observed in core- and non-core prices, albeit more modest in the second fortnight. In the former, goods increased 0.6% m/m, with pressures in both processed foods (0.6%) and other goods (0.7%). Services remain muted. In the latter, energy ended 3.9% up. In agricultural goods, we highlight that fresh fruits and vegetables reversed partially their previous decline, although ending 1.4% lower**
- **Annual inflation increased to 3.62% from 3.33% in June, reaching a five-month high. Core inflation was also higher, at 3.85% from 3.71% in the same period. We maintain our year-end forecast at 3.7%, above market expectations closer to 3.6%**
- **We maintain long positions in Udibono Dec'25**

**Consumer prices up 0.66% m/m, in line with expectations.** This was virtually in line with consensus at 0.65%, but further away to our 0.71% forecast. With this, there have been four consecutive fortnights with an upward surprise relative to market, albeit more modest recently. We highlight increases in both the core and non-core, albeit more modestly at the margin, adding 30bps and 36bps, respectively. Within the former, increases were observed in both processed foods (0.6% m/m) and other goods (0.7%), in our view influenced by the reopening of the economy. Services stayed muted, at 0.1% (contribution: 5bps). At the non-core, energy was higher again, up 3.9%. Low-grade gasoline increased 5.6% m/m, adding 27bps. Agricultural goods partially reversed their first half decline, ending virtually flat in July.

July inflation by components  
%, monthly incidence

	INEGI	Banorte	Difference
Total	0.66	0.71	-0.05
Core	0.30	0.32	-0.02
Goods	0.25	0.27	-0.01
Processed foods	0.12	0.12	0.00
Other goods	0.13	0.14	-0.01
Services	0.05	0.05	0.00
Housing	0.02	0.02	0.00
Education	0.00	0.00	0.00
Other services	0.03	0.03	0.00
Non-core	0.36	0.39	-0.03
Agriculture	0.00	0.02	-0.03
Fruits & vegetables	-0.07	-0.06	-0.01
Meat & egg	0.07	0.08	-0.01
Energy & government tariffs	0.36	0.37	-0.01
Energy	0.35	0.36	-0.01
Government tariffs	0.01	0.01	0.00

Source: INEGI, Banorte.

Note: Contributions might not add due to the number of decimals allowed in the table.

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Winners of the award for best economic forecasters for Mexico in 2019, granted by *Refinitiv*



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July inflation: Goods and services with the largest contributions

% m/m; monthly incidence in basis points

Goods and services with the largest positive contribution	Incidence	m/m
Low-grade gasoline	26.7	5.6
Chicken	8.7	5.6
LP Gas	4.7	2.3
High-grade gasoline	3.2	5.3
Beer	2.3	1.7
Goods and services with the largest negative contribution		
Serrano chillies	-4.2	-29.2
Eggs	-3.0	-3.4
Tomatoes	-2.8	-4.5
Grape	-2.0	-29.3
Squash	-1.7	-24.1

Source: INEGI

**Despite higher annual inflation, we expect Banxico to continue cutting the reference rate.** Specifically, annual inflation increased to 3.62% from 3.33% in June, reaching a five-month high. core inflation was also higher, at 3.85% from 3.71% in the same period and to the upside April. In our view, the tone of most members within Banxico’s Board remains dovish, particularly on the back of the strong economic decline, which was confirmed [in the 2Q20 GDP report](#). In this backdrop, we expect the central bank to keep cutting the reference rate by 50bps in each of the next two meetings, to be held on August 13<sup>th</sup> and September 24<sup>th</sup>, reaching 4.00%, level where we expect it to end in 2020. On the other hand, we believe they will maintain a cautious stance despite the environment of low prices globally and ample monetary easing in both developed and emerging economies, driven by high uncertainty and recent inflation dynamics. Specifically, we highlight that core inflation has not been able to decline further from 3.5% y/y since late 2016 despite the high degree of economic slack. In this context, we maintain our forecast that headline inflation will close the year at 3.7% and the core at 3.9%, both higher than the 3.6% and 3.7% consensus estimate [in the latest central bank survey](#), in the same order. In our view this factor, along the cautiousness shown by the institution about financial stability risks given unprecedented uncertainty, will remain relevant for a pause in the easing cycle relatively soon and at 4.00% –higher than the 3.00% low observed between mid-2014 and late 2015–, which started in August last year when the rate was at 8.25%

*From our fixed income and FX strategy team*

**We maintain long positions in Udibono Dec’25.** Today’s report continues to validate our view of an attractive carry in real rates for the second half of the year, which according to our inflation estimates, stands at 2.09% (5.22% annualized) for the 146 days remaining in 2020. Implied inflation in the market has depicted a relatively stable performance in the last weeks with greater upward adjustments in short-term readings as a result of a stronger relative performance in real-rate Udibonos with respect to Mbonos in this time frame. In this sense, the 3-year breakeven stands at 3.35%, 35bps above its 12-month median and 32bps higher than a month ago. Meanwhile, the 5-, 10- and 30-year metrics stand at levels 2bps lower than 12-month mean, on average, and 16bps higher than their levels the previous month. Considering these factors, we hold our trade recommendation opened on July 23<sup>rd</sup> consisting on [long positions in Udibono Dec’25](#) with an entry level at 1.78%, target at 1.48%, stop-loss at 2.00% and last close at 1.58%.

## Analyst Certification

We, Gabriel Casillas Olvera, Alejandro Padilla Santana, Delia María Paredes Mier, Juan Carlos Alderete Macal, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Tania Abdul Massih Jacobo, Francisco José Flores Serrano, Katia Celina Goya Ostos, Santiago Leal Singer, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo, Eridani Ruibal Ortega and Juan Barbier Arizmendi, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

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