

August inflation – Reaching the upper bound of the variability range around the target

- **Headline inflation (August): 0.39% m/m; Banorte: 0.37%; consensus: 0.39% (range of estimates: 0.32% to 0.42%); previous: 0.66%**
- **Core inflation (August): 0.28% m/m; Banorte: 0.30%; consensus: 0.28% (range of estimates: 0.25% to 0.30%); previous: 0.40%**
- **Within the core, we highlight some renewed pressures in goods (0.5% m/m) during the month. Services remain contained (0.2%), with the seasonal decline on airfares and tourism-related services not showing up sizably due to the pandemic. The non-core was slightly up (0.6%), with agricultural goods mixed (0.9%) while energy inched higher (0.3%), mainly on higher gasolines in the latter part of the month**
- **Annual inflation picked up to 4.05% from 3.62% in July, increasing for four months in a row. Core inflation was also higher, at 3.97% from 3.85%. Thus, both measures are virtually at the 4% upper bound of the central bank’s variability range. We reiterate our call of a 25bps cut by Banxico on September 24th**
- **Real-rate Udibonos’ carry is still good, although their valuation remains unattractive in short-term tenors**

Consumer prices up 0.39% m/m, in line with consensus. On the other hand, it was slightly higher than our 0.37%. Nonetheless, the bi-weekly print was above expectations for a fifth consecutive time. Within the core, we highlight some pressures in goods, up 0.5% m/m, virtually in line with our monitoring. Moreover, we note that services remain contained (0.2%), with airfares and tourism-related services mixed but declining less than in recent years. In our view, this is related to distortions because of the pandemic that have affected demand and its typical seasonality. The non-core was up 0.6%, with both components up. Agricultural goods were more mixed, with fresh fruits and vegetables higher more strongly (3.0%) but meat and egg down (-0.9%). Energy inched higher (0.3%), mainly on higher gasolines in the second half –most likely on the impact of hurricane Laura.

August inflation by components
%, monthly incidence

	INEGI	Banorte	Difference
Total	0.39	0.37	0.02
Core	0.24	0.23	0.01
Goods	0.19	0.18	0.01
Processed foods	0.07	0.07	-0.01
Other goods	0.12	0.10	0.02
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	0.15	0.14	0.01
Agriculture	0.09	0.08	0.01
Fruits & vegetables	0.14	0.11	0.03
Meat & egg	-0.05	-0.03	-0.02
Energy & government tariffs	0.06	0.06	0.00
Energy	0.03	0.03	0.00
Government tariffs	0.03	0.03	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



**STARMINE AWARDS
FOR REUTERS POLLS
FROM REFINITIV**

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August 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
Tomatoes	8.2	13.9
Lemons	3.5	32.9
Water supply rights	2.7	2.8
LP gas	2.5	1.3
Onions	1.9	10.2
Goods and services with the largest negative contribution		
Eggs	-3.2	-3.7
Oranges	-2.7	-11.9
Chicken	-2.3	-1.4
Beer	-2.0	-1.4
Bananas	-1.6	-6.0

Source: INEGI

We reiterate our call of a 25bps rate cut by Banxico on September 24th. With today's report, annual inflation picked up to 4.05% from 3.62% in July, with four months in a row higher. Core inflation stands at 3.97% from 3.85%. These are their highest since May 2019 and March 2018, respectively. Moreover, both stand virtually at the 4% upper bound of the central bank's variability range. According to our forecasts, inflation will continue increasing modestly at least until September, influenced in part by the prevalence of a challenging base-effect, especially with the non-core component below 1% y/y one year ago. We note this situation has already been accounted for by Banxico in its latest [Quarterly Report](#), in which short-term inflation forecasts were adjusted upwards. In either case, we see an even more cautious stance by the central bank, given: (1) These price dynamics, particularly in core inflation; (2) our view that the [latest minutes were less dovish](#) at the margin, especially as the dissenter in favor of a 25bps cut was Deputy Governor Irene Espinosa; (3) other geopolitical risks that could push market volatility higher, highlighting the US election on November 3rd; and (4) accumulated rate cuts of 375bps in this easing cycle. Given these, we reiterate our call of a more modest 25bps cut (to 4.25%) on September 24th, where we expect it to end the year. We note consensus has also moved with our view, according to the [latest central bank survey](#). Going forward, there are many unknowns for 2021, leading us to expect Banxico will maintain a prudent approach and leave the rate unchanged. However, considering risks for economic activity and the institution's scenarios for inflation, among other factors, we believe the skew is tilted towards more easing instead of a tighter policy stance.

From our fixed income and FX strategy team

Real-rate Udibonos' carry is still good, although their valuation remains unattractive in short-term tenors. With inflation readings this Wednesday broadly in line with expectations, we hold a view about still attractive carry gains for real-rate securities although with a valuation that remains relatively expensive, especially for short-term tenors. In particular, the 3-year breakeven locates at 3.46%, 31bps higher than its 12-month mean, while the 5-, 10-, and 30-year maturities average a 6bps distance above this reading. In terms of strategy we hold short-term tactical [long positions in Mbonos May'29 and Nov'38](#), in a context of tight valuations in the nominal yield curve. Meanwhile, approached with rate futures the market is currently pricing in accumulated rate cuts for Banxico by -38bps for the remainder of 2020 (Banorte -25pb).

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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HOLD	When the share expected performance is similar to the MEXBOL estimated performance.
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