

# 1H-September inflation – Modest on lower pressures at the core

- **Headline inflation (1H-Sep): 0.16% 2w/2w; Banorte: 0.11%; consensus: 0.10% (range of estimates: -0.05% to 0.33%); previous: 0.17%**
- **Core inflation (1H-Sep): 0.17% 2w/2w; Banorte: 0.16%; consensus: 0.18% (range of estimates: 0.05% to 0.26%); previous: 0.18%**
- **The core component was relatively low (contribution: 13bps), with an unusually modest contribution in education (+1.1% 2w/2w). On the other hand, goods seem to have taken a breather, at 0.2%. Within the non-core, agricultural prices increased 0.2% while energy was mixed, with gasolines and electricity up but LP gas lower**
- **Annual inflation picked up modestly, reaching 4.10% from 4.05% in August. Core inflation was more stable, at 3.99% from 3.97%. Non-core prices inched to 4.44% from 4.30%, partially on a difficult base effect that has not yet started to fade away**
- **Today’s print keeps showing distortions in prices due to the pandemic, albeit with some positive news at the core level. We expect Banxico to cut the reference rate by 25bps later today, to 4.25%**
- **We still see value in Udibonos, although we assess better entry levels**

**Consumer prices up 0.16% 2w/2w in the first half of September.** This was above our 0.11% forecast, in a context of a wide range of estimates. The core increased 0.17% (Banorte: 0.16%), low relative to its 0.26% five-year average. The main driver was education (1.1% 2w/2w), lowest since the series is available (1995) and even though this print is usually high due to the return to school. In our view, this is another consequence of the pandemic. Other services (0.1%) surprised slightly higher. More positive though, goods seem to have taken a breather, with both processed foods and other goods at 0.2% and the latter quite low despite an unfavorable seasonality. Non-core prices stood at 0.15%, with pressures in meat and egg. Energy was modest (0.1%), with LP gas decelerating (-0.6%) which helped to compensate for electricity and gasolines, with the latter still impacted by recent disruptions due to Hurricane Laura in August.

1H-September inflation by components  
%, bi-weekly incidence

	INEGI	Banorte	Difference
Total	0.16	0.11	0.06
Core	0.13	0.12	0.01
Goods	0.06	0.10	-0.04
Processed foods	0.03	0.04	0.00
Other goods	0.03	0.07	-0.03
Services	0.06	0.02	0.04
Housing	0.01	0.01	0.00
Education	0.04	0.02	0.03
Other services	0.01	-0.01	0.02
Non-core	0.04	-0.01	0.05
Agriculture	0.02	0.00	0.02
Fruits & vegetables	0.00	-0.01	0.01
Meat & eggs	0.01	0.01	0.00
Energy & government tariffs	0.02	-0.01	0.03
Energy	0.01	-0.02	0.02
Government tariffs	0.01	0.00	0.01

Source: INEGI, Banorte.

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

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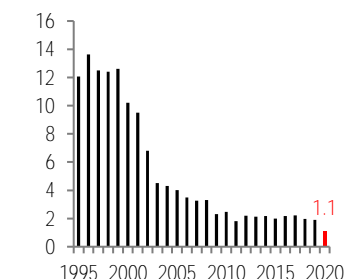
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Winners of the award for best economic forecasters for Mexico in 2019, granted by *Refinitiv*



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Education (school tuition) inflation in Sep-1H  
% 2w/2w



Source: INEGI

1H-September inflation: Goods and services with the largest contributions  
 % 2w/2w; bi-weekly incidence in basis points

Goods and services with the largest positive contribution	Incidence	% 2w/2w
Onions	5.2	23.6
Chicken	3.1	2.0
Dining away from home	1.5	0.3
Autos	1.4	0.7
Elementary school tuition	1.4	2.4
Goods and services with the largest negative contribution		
Tomatoes	-5.3	-7.9
Professional services	-3.1	-13.8
Eggs	-1.8	-2.3
Avocados	-1.3	-5.0
Oranges	-1.3	-6.6

Source: INEGI

**Marginal increase in annual inflation, to 4.1%.** Annual inflation picked up modestly, reaching 4.10% from 4.05% in August. Core inflation was more stable, at 3.99% from 3.97%. On the other hand, non-core prices inched to 4.44% from 4.30%, partially on a difficult base effect. Although headline inflation is slightly above the upper bound of Banxico’s variability range, we maintain our estimate that inflation will finish the year at 3.7%, in our view still with broadly balanced risks. In this respect and on a more positive note, headline inflation has likely already reached its high for this year and it will fall gradually in the fourth quarter, mainly as a challenging base effect at the non-core level starts to fade away.

**We expect a 25bps rate cut by Banxico today, to 4.25%.** Today, at 2:00pm (ET), Banxico will hold its seventh policy decision of the year. We anticipate a 25bps rate cut to 4.25%, in line with market expectations. We believe it will be a majority decision, with at least one but even possibly two members favoring -50bps. This is based on: (1) Our assessment of the [latest minutes](#), in which one member was markedly dovish, other two more neutral, and the remaining two definitely hawkish; and (2) financial market dynamics since the last decision. We expect the tone of the statement to lean towards a less accommodative stance given accumulated rate cuts and short-term inflation pressures (with both measures virtually at the upper bound of Banxico’s variability range). For further details, see our weekly document, [Ahead of the Curve](#). Regarding the latter, we believe today’s print was favorable, especially in dynamics within core goods. Nevertheless, it is too early judge if pressures have waned and some of this is to a great extent because of additional distortions due to the pandemic. Considering this, we see most members remaining cautious on inflation, which has not declined despite the high degree of slack and even with a relevant moderation in services. On the other hand, we should highlight that this was already expected to a great extent by the central bank in its latest [Quarterly Report](#). Specifically, the estimate for average headline and core inflation for 3Q20 (with only one fortnight left) stands at 3.9% in both cases, in line with their performance so far.

*From our fixed income and FX strategy team*

**We still see value in Udibonos, although we assess better entry levels.** The risk-off mode has triggered sharp pressures in EM currencies, where the Mexican peso has sold-off 7% in the last 5 days. Under this context, the Udibonos' curve has experienced a better relative performance than Mbonos registering a modestly positive weekly balance, contrary to the nominal yield curve steepening. This has resulted in a brake for recent breakeven compression, where the 3- and 5-year readings still trade at a greater span from their 12-month mean (~25bps) when compared to the 10- and 30-year marks (~6bps). Considering the bi-weekly CPI dynamics and its possible short-term performance, we see carry attractiveness in Udibonos, although we evaluate better opportunities to position in these securities. Meanwhile, ahead of Banxico's decision today the market prices in accumulated rate cuts for 2020 by -32bps.

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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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