September inflation –We adjust our year-end estimate up to 6.6% as pressures persist

- **Headline inflation (September): 0.62% m/m; Banorte: 0.71%; consensus: 0.61% (range: 0.55% to 0.71%); previous: 0.19%**
- **Core inflation (September): 0.46% m/m; Banorte: 0.52%; consensus: 0.47% (range: 0.45% to 0.52%); previous: 0.43%**
- **In the core, goods picked up 0.7% m/m, with an adverse seasonality in 'other' from school supplies. Services were mixed (0.2%). In the latter, we highlight energy prices (1.1%), especially LP gas (4.7%). Agricultural goods also grind higher (1.4%), with fresh fruits and vegetables (3.2%) likely still affected by weather conditions**
- **Annual inflation picked up to 6.00% from 5.59% in August. The core was higher for a tenth consecutive month, to 4.92% from 4.78%**
- **Given component dynamics and a difficult global backdrop –particularly in energy commodities–, we adjust higher our year-end forecast, to 6.6% from 6.1% previously**
- **Inflationary pressures validate the recent increase in the curve's pricing for Banxico**

Inflation at 0.62% m/m in September. This print was in line with consensus (0.61%) but lower than our 0.71%. This happened after strong pressures in the first half. At the core, goods (0.7% m/m) remain the most affected, with both processed foods and 'others' up by the same magnitude for second month in a row. There's an adverse seasonality in school-related items, recalling the return to in-person classes. Services (0.2%) were more mixed, with education higher (1.3%) but tourism and non-tourism helping at the margin. The non-core increased 1.10%, driven by energy (1.1%). We highlight LP gas (4.7%) despite the price ceiling, as well as natural gas (3.2%) on higher global benchmarks. This was partially compensated by low-grade gasoline (-0.2%). Moreover, agricultural goods (1.4%) also added to the upside, with bad weather (hurricanes, US drought) and supply chain issues likely explaining a good part of the move.

September inflation by components
%, monthly incidence

	INEGI	Banorte	Difference
Total	0.62	0.71	-0.09
Core	0.34	0.39	-0.04
Goods	0.27	0.29	-0.02
Processed foods	0.14	0.16	-0.01
Other goods	0.13	0.14	-0.01
Services	0.07	0.09	-0.02
Housing	0.03	0.03	0.00
Education	0.05	0.05	0.00
Other services	0.00	0.02	-0.02
Non-core	0.27	0.32	-0.05
Agriculture	0.15	0.17	-0.02
Fruits & vegetables	0.16	0.18	-0.02
Meat & egg	-0.01	-0.01	0.00
Energy & government tariffs	0.12	0.15	-0.03
Energy	0.11	0.13	-0.02
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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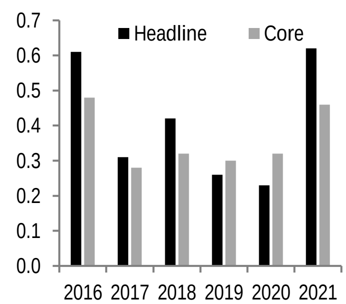
Headline and core inflation in September
% m/m



Source: INEGI

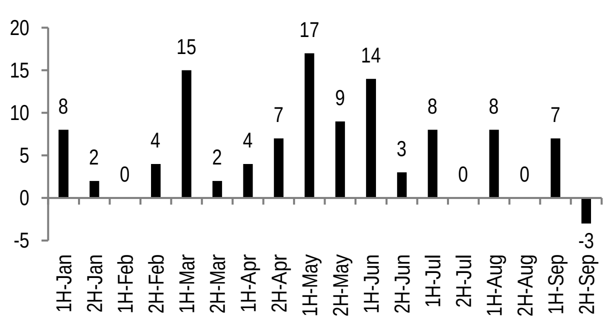
September inflation: Goods and services with the largest contributions
% m/m; monthly incidence in basis points

Goods and services with the largest positive contribution	Incidence	% m/m
LP gas	10.5	4.7
Tomatoes	8.7	13.1
Onions	5.8	27.1
Cooking oil	2.6	5.3
Beef	2.4	1.1
Goods and services with the largest negative contribution		
Chicken	-4.1	-2.4
Professional services	-3.0	-13.8
Bananas	-2.6	-10.0
Avocadoes	-2.0	-6.7
Oranges	-1.9	-9.6

Source: INEGI

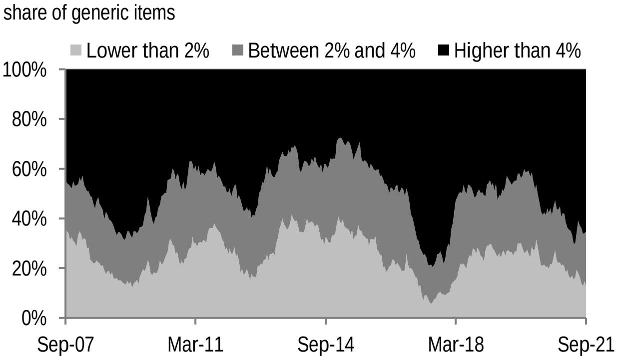
Annual inflation increases again, seeing more short-term pressures. With today's print, annual inflation stands at 6.00% from 5.59% in August, with the core up for a tenth month in a row, to 4.92% from 4.78%, respectively. The latter has consistently surprised to the upside this year (chart below, left) and in our view is more concerning in terms of overall price dynamics. Unfortunately, we believe pressures will continue at least in the short term, because of: (1) More disruptive and persistent supply chain issues than expected; (2) the increase in input costs, especially energy; and (3) a more difficult base effect in both components into December. Regarding the second factor, we highlight that *Bloomberg*'s commodity index (comprised of futures prices for energy, metals and food items) reached a new high since 2015 this week. Attention has been centered on natural gas (with US prices at an almost 13-year maximum), albeit with relevant increases also in LP gas and crude oil, among others. To this we add bets that the winter season will be harsher so demand for heating in the Northern Hemisphere could pick up. Moreover, we have had: (1) Crop failures in several regions impacting food prices; (2) strong moves higher in other commodities such as copper, aluminum and cotton, pressuring input costs for manufacturers; and (3) recent peso weakness against the dollar. In this respect, we have seen clearer signs of price pressures gradually picking up, influenced by strong demand –mostly globally– and limits for an increase in supply. In our view, the diversity and amplitude of recent shocks will be reflected in both components, due to direct (mostly at the non-core) and indirect channels (with second round effects affecting particularly goods at the core, but also some services). In this respect, the share of generic products within CPI that are currently at least 4% y/y higher has been increasing gradually (chart below, right), in our view signaling the wider scope of price adjustments in addition to base effects.

Core inflation surprises
Bps, bi-weekly frequency



*Note: Relative to Bloomberg consensus.
Source: Banorte with data from INEGI and Blloomberg

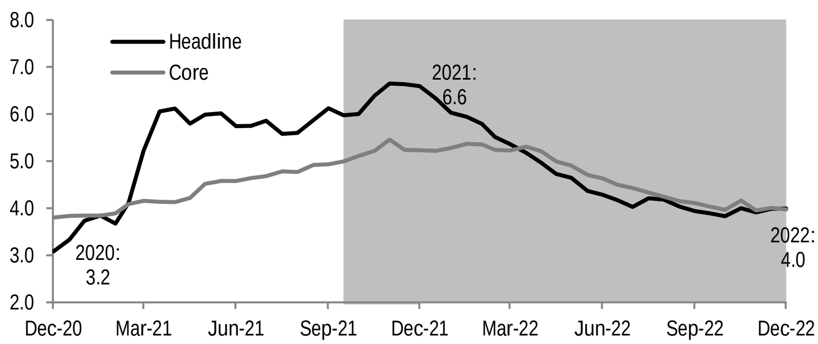
Distribution of annual inflation
% share of generic items



Source: Banorte with data from INEGI

We revise our year-end forecast to 6.6% given recent surprises, stronger commodities and signals of more generalized price pressures. Given this complex backdrop, we adjust our forecasts for headline and core inflation for the end of this year, to 6.6% from 6.1% and to 5.2% from 4.7%, respectively (see chart below). For 2022, we maintain both at 4.0% y/y, higher than analysts' consensus at around 3.8% and 3.7%, in the same order. These estimates already consider additional persistence from current disruptions, both from the supply and the demand side. Nevertheless, we are also waiting for the resolution of some local issues. Among them, we note: (1) Adjustments regarding the *Budget Proposal* for 2022, including in items such as excise taxes, zero tax rate for female hygiene products, VAT to digital platforms and changes to fiscal incentives in some industries, among others; and (2) minimum wage negotiations, with reports about a potential increase of up to 21%, but with the resolution by the *National Minimum Wages Commission* (Comisión Nacional de los Salarios Mínimos or CONASAMI) likely until mid-December.

Inflation forecasts
% y/y, bi-weekly frequency



Source: INEGI, Banorte

From our fixed income and FX strategy team

Inflationary pressures validate the recent increase in the curve's pricing for Banxico. Since its last monetary policy decision, the market has increased bets of a more restrictive stance by Banxico, currently pricing in hikes of +59bps by year-end and +173bps until 1H22. Both are more aggressive than our estimates for 2021 and 2022. The local CPI backdrop context has coupled with sovereign rates' sell-off led by US Treasuries. In this sense, Mbonos have adjusted ~+50bps on average since September, with the 10-year benchmark reaching its highest since April 2020 at 7.61% on Tuesday. We believe the release of Banxico's minutes next Thursday will play a key role to calibrate market expectations. In terms of strategy, we see current Mbono levels as becoming attractive for short-term long tactical positions in long-term tenors; however, the volatility scene and the US jobs report due tomorrow make us lean for a more cautious bias. In Udibonos, we hold a view of greater value in mid-term tenors, specifically the Nov'28 and Nov'31 maturities, in a context of remarkably high inflation breakevens.

Analyst Certification

We, Alejandro Padilla Santana, Delia María Paredes Mier, Juan Carlos Alderete Macal, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Francisco José Flores Serrano, Katia Celina Goya Ostos, Santiago Leal Singer, José Itzamna Espitia Hernández, Alik Daniel García Alvarez, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo 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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	Reference
BUY	When the share expected performance is greater than the MEXBOL estimated performance.
HOLD	When the share expected performance is similar to the MEXBOL estimated performance.
SELL	When the share expected performance is lower than the MEXBOL estimated performance.

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