Ahead of the Curve

Inflation would continue to be impacted by food items at the beginning of September

- **Inflation (1H-September).** We expect headline inflation at 0.37% 2w/2w. As has been a constant in recent periods, dynamics would continue to be mostly unfavorable, with additional pressures on goods –particularly on food items–, although with a moderation in energy, which we expect to have positive effects in the price formation process in coming months. In this context, we anticipate the core at +0.43% 2w/2w (contribution: +32bps), with the non-core more modest at 0.17% (+5bps). With these estimates, annual inflation would stand at 8.71% from 8.70% on average in August. The core would continue to extend its upward trend to 8.27% (previous: 8.05%), while the non-core would moderate to 10.05% (previous: 10.65%)

- ***Timely Indicator of Economic Activity* (August).** This release will include the first estimate for August, as well as revised figures for July. For the latter month, industrial production surprised to the upside relative to the first estimate. Moreover, timely signals for services –especially retail sales– leads us to believe that the adjustment will be to the upside. Hence, we could see a sequential expansion in the month. Turning to August, signals are relatively more negative. Despite an additional decrease in contagions, challenges related to inflationary pressures remained, dampening dynamism of domestic demand. On top of this, we must consider more adverse conditions abroad, with additional evidence of a US deceleration. As such, timely indicators such as IMEF's PMIs and ANTAD sales moderated at the margin

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www.banorte.com
@analisis_fundam

Juan Carlos Alderete, CFA
Executive Director of Economic Research and Financial Markets Strategy
juan.alderete.macal@banorte.com

Francisco Flores
Director of Economic Research, Mexico
francisco.flores.serrano@banorte.com

Yazmín Pérez
Senior Economist, Mexico
yazmin.perez.enriquez@banorte.com

Cintia Nava
Senior Economist, Mexico
cintia.nava.roa@banorte.com

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Mexico weekly calendar

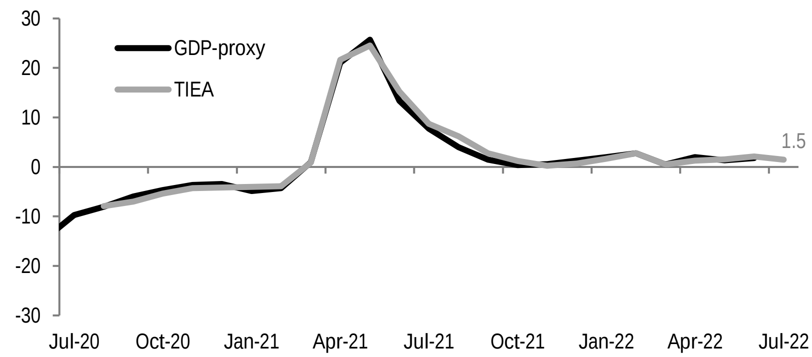
DATE	TIME (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Tue 20-Sep	7:00am	Timely Indicator of Economic Activity (sa)	August	% y/y	--	--	1.5
Tue 20-Sep	10:00am	International reserves	Sep-15	US$ bn	--	--	198.3
Tue 20-Sep	4:30pm	Citibanamex bi-weekly survey of economic expectations					
Wed 21-Sep	8:00am	Aggregate supply and demand	2Q22	% y/y	3.6	--	2.9
		Private consumption		% y/y	5.6	--	7.2
		Investment		% y/y	7.0	--	5.6
		Government spending		% y/y	0.8	--	0.8
		Exports		% y/y	9.8	--	10.1
		Imports		% y/y	7.9	--	5.8
Wed 21-Sep	7:00am	Retail Sales	July	% y/y	4.2	--	4.0
		sa		% m/m	0.5	--	-0.3
Thu 22-Sep	7:00am	CPI inflation	1H September	% 2w/2w	0.37	--	0.32
				%y/y	8.71	--	8.77
		Core		%2w/2w	0.43	--	0.32
				%y/y	8.27	--	8.13

Source: Banorte; Bloomberg

Proceeding in chronological order…

The *Timely Indicator of Economic Activity* will probably point to some weakness in August. This release will include the first estimate for August, as well as revised figures for July. We recall that June's mid-point forecast stood at 2.1% y/y (using sa figures), higher than the 1.8% in the GDP-proxy (IGAE). For the latter month, industrial production surprised to the upside relative to the first estimate. Moreover, timely signals for services –especially retail sales– leads us to believe that the adjustment will be to the upside. Hence, we could see a sequential expansion in the month. Turning to August, signals are relatively more negative. Despite an additional decrease in contagions, challenges related to inflationary pressures remained, dampening dynamism of domestic demand. On top of this, we must consider more adverse conditions abroad, with additional evidence of a US deceleration. As such, timely indicators such as IMEF's PMIs and ANTAD sales moderated at the margin

Monthly GDP-proxy and the Timely Indicator of Economic Activity (TIEA)
% y/y sa



Source: INEGI

Weekly international reserves report. Last week, net international reserves decreased by US$180 million, closing at US$198.3 billion (please refer to the following table). This was mainly explained by a positive valuation effect in institutional assets. Year-to-date, the central bank's international reserves have fallen by US$4.1 billion.

Banxico's foreign reserve accumulation details
US$, million

	2021	Sep 9, 2022	Sep 9, 2022	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	202,399	198,294	-180	-4,105
(B) Gross international reserve	207,745	204,605	-200	-3,139
Pemex	--	--	0	350
Federal government	--	--	422	2,182
Market operations	--	--	0	0
Other	--	--	-623	-5,671
(C) Short-term government's liabilities	5,346	6,311	-21	965

Source: Banco de México

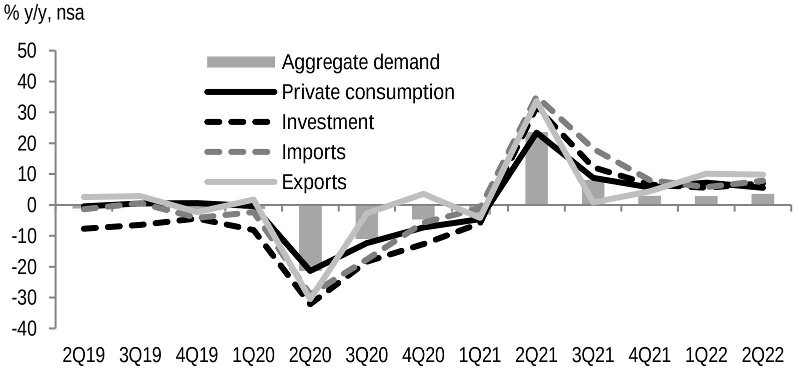
Aggregate demand likely kept climbing in 2Q22, boosted by better domestic conditions. We expect both aggregate supply and demand at 3.6% y/y. From the supply side, we already know that GDP grew 2.0% y/y, extending the recovery trend for a third consecutive quarter. Inside, dynamism was centered in both industry and services.

Meanwhile, we anticipate imports at 7.9% y/y, accelerating from the 5.8% of the previous quarter. Converting trade balance data to MXN at current prices, inbound shipments of goods picked up 29.2% y/y, with the current account –also including services– stronger at 29.7%. This is slightly higher than when figures are expressed in USD as the Mexican peso fell 0.3% on average in annual terms. Nevertheless, we expect overall growth to be impacted once again by inflationary pressures, which accelerated sharply and should widen the gap even further between figures in nominal and real terms.

On demand, private consumption would remain quite strong at 5.6%, with a boost from services and the imported component. The monthly indicator grew 7.1%, with imported goods leading gains (+18.7%), but with services (+9.4%) also benefitting from a further normalization in activity. As such, fundamentals were mostly better throughout the period, with remittances' strength likely key to offset some of the negative effects from the suspension in social programs payments. Investment was more resilient than anticipated, coming in at 7.0%. The boost came mostly from machinery and equipment (+13.6%), especially the imported component, while construction (+1.6%) was supported by non-residential activity. We expect government spending at +0.8%, with relative stability on electoral spending. In this context, while current government expenditures rose 7.4% y/y, we expect a heavy drag from inflation and a continuation of the trend of a lower effect on value added. Lastly, we anticipate exports at 9.8%. Similar to shipments abroad, differences between the trade balance and the balance of payments were tight, suggesting that services broadly grew at the same pace as goods, as shown in the current account report. We consider this would be quite positive given prevailing disruptions to trade in the period.

If we are correct, domestic demand would have continued to strengthen despite prevailing challenges from abroad, mainly domestic consumption. As such, we expect this to continue for the rest of the year, albeit most likely at a slower pace as headwinds seem to have gathered force. Nonetheless, these conditions are still consistent with our view of an expansion of 2.1% in GDP this year.

Aggregate demand
% y/y, nsa



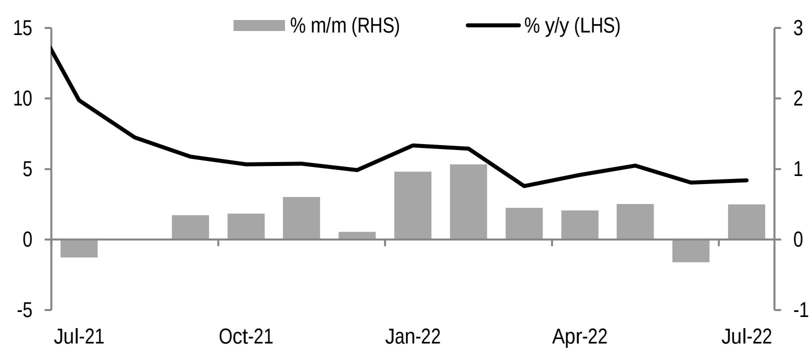
Source: INEGI, Banorte

Retail sales to rebound in July, boosted by a better backdrop. We estimate them at +4.2% y/y, better than the 4.0% of the previous month. Sequentially, sales would return to expansion at +0.5% m/m, erasing the 0.3% loss from the previous month, which in our view would be positive. Specifically, some of the factors that would have contributed to additional dynamism include: (1) The resumption of payments from social programs after the electoral ban; (2) a moderation in COVID-19 cases in the latter part of the month; and (3) no disruptions from sales campaigns in the previous month.

So far, available data is mixed. ANTAD sales gathered pace, with total stores up to 5.6% y/y in real terms (previous: 2.1%) and same-stores at 3.3% (previous: -0.1%), even despite additional price pressures. Gasoline sales decelerated to 700kbpd from 721kbpd in the previous month. However, we attribute this mostly to a seasonal effect, considering less trips as kids did not go to school because of the summer holiday. On a more negative note, auto sales moderated to 90.0 thousand units, which translates to a 6.8% m/m contraction. Lastly, non-oil consumption goods imports fell 0.2% m/m, its first decline in 10 months. One thing we should factor-in is that these figures are measured in nominal terms, which given the decline in the price of commodities and transportation costs, might not be as negative as it seems. On fundamentals, news were more favorable. Remittances maintained remarkable strength, adding a third month above $100 billion and reaching a new historical high. Employment was relatively favorable with +8.6 thousand new positions, albeit with notable seasonal drivers distorting figures. Lastly, consumer loans kept gathering pace, which might be a useful tool for families to smooth-out consumption.

We believe this result supports our view that June was only a bump in the road to recovery, with growth likely resuming from here onwards. However, risks remain, including persistent price pressures and a possible slowdown in the pace of the recovery of economic activity.

Retail sales
% y/y nsa, % m/m sa



Source: INEGI, Banorte

Core inflation for the 1st half of September still pressured by food, but with slowdown in energy. We expect headline inflation at 0.37% 2w/2w. As has been a constant in recent periods, dynamics would continue to be mostly unfavorable, with additional pressures on goods –particularly on food items–, although with a moderation in energy, which we expect to have positive effects in the price formation process in coming months.

In this context, we anticipate the core at +0.43% 2w/2w (contribution: +32bps), with the non-core more modest at 0.17% (+5bps). With these estimates, annual inflation would stand at 8.71% from 8.70% on average in August. The core would continue to extend its upward trend to 8.27% (previous: 8.05%), while the non-core would moderate to 10.05% (previous: 10.65%).

At the core, and as we already mentioned, goods would be the highest at 0.5% 2w/2w (+20bps), highlighting processed foods at +0.7% (+15bps). We think that these continue to adjust to accumulated increases in input prices, on top of the fact that some of the retail stores could be gradually applying the increases announced by producers in previous periods (*e.g.* Coca-Cola Femsa, Bimbo, Lala, etc.). On other goods (+0.3%; +5bps), seasonality is more favorable, with adjustments in school supplies probably left behind. Regarding services (+0.4%: +12bps), education would climb 2.4%, considering that tuition fees in basic education are usually adjusted in this period. On others (+0.1%; +2bps) dynamics would be more mixed, with stability on tourism categories, but with the effect related to last wills' discounts being offset by additional pressures on other items, highlighting restaurants. Lastly, housing would be more modest at +0.2% (+2bps).

In the non-core, agricultural prices would remain under pressure at +0.8% (+9bps). On this occasion, the expansion would be concentrated in meat and egg (+0.9%; +6bps), with reports of rises in the price of chicken and eggs after a moderation in the previous fortnights. Meanwhile, fruits and vegetables are expected to climb more modestly by +0.6% (+3bps), with our monitoring showing declines in bananas and avocados, although with signs of increases in tomatoes. In energy (-0.5%; -5bps), we expect declines in LP gas (-1.4%; -3bps) and in low-grade gasoline (-0.4%; -2bps). Although we saw decreases in reference prices of both, the adjustment in the latter would be limited by the reduction in the government stimulus. Electricity would also be lower (-0.2%; 0bps), although moderate after a more substantial decrease in the first half of August. Finally, government tariffs would rise 0.1% (+1bps).

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We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Katia Celina Goya Ostos, Francisco José Flores Serrano, José Luis García Casales, Víctor Hugo Cortes Castro, José Itzamna Espitia Hernández, Carlos Hernández García, Leslie Thalía Orozco Vélez, Hugo Armando Gómez Solís, Yazmín Selene Pérez Enríquez, Cintia Gisela Nava Roa, Miguel Alejandro Calvo Domínguez, Daniela Olea Suárez, José De Jesús Ramírez Martínez, Gerardo Daniel Valle Trujillo, Luis Leopoldo López Salinas, Isaías Rodríguez Sobrino, Paola Soto Leal, Oscar Rodolfo Olivos Ortiz, Daniel Sebastián Sosa Aguilar and Salvador Austria Valencia 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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GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Alejandro Padilla Santana	Chief Economist and Head of Research	alejandro.padilla@banorte.com	(55) 1103 - 4043
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
María Fernanda Vargas Santoyo	Analyst	maria.vargas.santoyo@banorte.com	(55) 1103 - 4000
Economic Research			
Juan Carlos Alderete Macal, CFA	Executive Director of Economic Research and Financial Markets Strategy	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Director of Economic Research, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Director of Economic Research, Global	katia.goya@banorte.com	(55) 1670 - 1821
Yazmín Selene Pérez Enríquez	Senior Economist, Mexico	yazmin.perez.enriquez@banorte.com	(55) 5268 - 1694
Cintia Gisela Nava Roa	Senior Economist, Mexico	cintia.nava.roa@banorte.com	(55) 1103 - 4000
Luis Leopoldo López Salinas	Manager Global Economist	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Market Strategy			
Manuel Jiménez Zaldívar	Director of Market Strategy	manuel.jimenez@banorte.com	(55) 5268 - 1671
Fixed income and FX Strategy			
Leslie Thalía Orozco Vélez	Senior Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Isaías Rodríguez Sobrino	Strategist, Fixed Income, FX and Commodities	isaias.rodriguez.sobrino@banorte.com	(55) 1670 - 2144
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Carlos Hernández García	Senior Strategist, Equity	carlos.hernandez.garcia@banorte.com	(55) 1670 - 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Paola Soto Leal	Analyst	paola.soto.leal@banorte.com	(55) 1103 - 4000 x 1746
Oscar Rodolfo Olivos Ortiz	Analyst	oscar.olivos@banorte.com	(55) 1103 - 4000
Corporate Debt			
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Quantitative Analysis			
Alejandro Cervantes Llamas	Executive Director of Quantitative Analysis	alejandro.cervantes@banorte.com	(55) 1670 - 2972
José Luis García Casales	Director of Quantitative Analysis	jose.garcia.casales@banorte.com	(55) 8510 - 4608
Daniela Olea Suárez	Senior Analyst, Quantitative Analysis	daniela.olea.suarez@banorte.com	55) 1103 - 4000
Miguel Alejandro Calvo Domínguez	Senior Analyst, Quantitative Analysis	miguel.calvo@banorte.com	(55) 1670 - 2220
José De Jesús Ramírez Martínez	Senior Analyst, Quantitative Analysis	jose.ramirez.martinez@banorte.com	(55) 1103 - 4000
Daniel Sebastián Sosa Aguilar	Analyst, Quantitative Analysis	daniel.sosa@banorte.com	(55) 1103 - 4000
Salvador Austria Valencia	Analyst, Quantitative Analysis	salvador.austria.valencia@banorte.com	(55) 1103 - 4000
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5004 - 1282
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Frigolet Vázquez Vela	Head of Sólida Banorte	alejandro.frigolet.vazquezvela@banorte.com	(55) 5268 - 1656
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 5140
Carlos Alberto Arciniega Navarro	Head of Treasury Services	carlos.arciniega@banorte.com	(81) 1103 - 4091
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8173 - 9127
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5249 - 6423
Lizza Velarde Torres	Executive Director of Wholesale Banking	lizza.velarde@banorte.com	(55) 4433 - 4676
Osvaldo Brondo Menchaca	Head of Specialized Banking Services	osvaldo.brondo@banorte.com	(55) 5004 - 1423
Raúl Alejandro Arauzo Romero	Head of Transactional Banking	alejandro.arauzo@banorte.com	(55) 5261 - 4910
René Gerardo Pimentel Ibarrola	Head of Corporate Banking	pimentelr@banorte.com	(55) 5004 - 1051
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.roldan.ferrer@banorte.com	(55) 1670 - 1899