1H-April inflation – Pressures continue despite a seasonal moderation in energy

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- **Headline inflation (1H-April): 0.16% 2w/2w; Banorte: 0.11%; consensus: 0.07% (range: -0.19% to 0.13%); previous: 0.59%**
- **Core inflation (1H-April): 0.44% 2w/2w; Banorte: 0.38%; consensus: 0.37% (range: 0.24% to 0.44%); previous: 0.40%**
- **Inflation was above consensus again. Energy (-2.4%) benefitted from the start of summer discounts to electricity tariffs (-12.3%), along with a decline in LP gas (-1.8%). Nevertheless, this was partially compensated by low-grade gasoline (0.8%). On the other hand, agricultural goods (0.7%) remained up. At the core, goods (0.5%) were still affected by processed foods (0.6%), while others (0.5%) showed an adverse seasonality. Services (0.3%) stayed relatively more modest**
- **Annual inflation picked up to 7.72% from 7.45% on average in March, with the core at 7.16% from 6.78% in the same period**
- **We reiterate our view of a 50bps hike by Banxico in its next decision, with special focus on price dynamics and the Fed**
- **The market is pricing-in 50bps hikes in the next meetings**

Inflation at 0.16% 2w/2w in 1H-April, surprising to the upside. The non-core fell for the first time this year, benefitted by energy (-2.4%) due to the start of summer discounts to electricity tariffs (-12.3%). LP gas (-1.8%) also helped, despite remaining volatile due to the war in Ukraine, among other factors. Low grade gasoline grew 0.8% given a decrease in excise tax subsidies. Agricultural goods picked up for a fourth consecutive fortnight (0.7%), both because of fruits and vegetables and meat & egg. At the core, goods (0.5%) maintain a difficult trend, especially processed foods (0.6%). In the latter, we highlight once again corn tortillas (1.1%). Services are still more modest (0.3%), with tourism still adjusting due to the holidays –especially tourism services (9.4%)– while in non-tourism we noted higher prices in dining away from home (0.4%).

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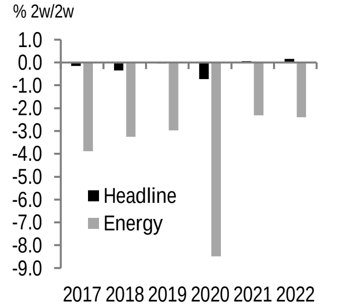
STARMINE AWARDS FOR REUTERS POLLS FROM REFINITIV

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

	INEGI	Banorte	Difference
Total	0.16	0.11	0.05
Core	0.33	0.28	0.05
Goods	0.22	0.20	0.02
Processed foods	0.12	0.13	0.00
Other goods	0.09	0.08	0.02
Services	0.11	0.08	0.03
Housing	0.01	0.02	0.00
Education	0.00	0.00	0.00
Other services	0.10	0.07	0.03
Non-core	-0.17	-0.17	0.00
Agriculture	0.07	0.11	-0.03
Fruits & vegetables	0.02	0.06	-0.04
Meat & egg	0.06	0.05	0.00
Energy & government tariffs	-0.24	-0.28	0.03
Energy	-0.25	-0.28	0.03
Government tariffs	0.00	0.00	0.00

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

Headline inflation and energy prices in 1H-April
% 2w/2w



Source: INEGI

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1H-April 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
Tomatoes	7.9	16.7
Low-grade gasoline	4.1	0.8
Tourism services	3.2	9.4
Chicken	3.1	1.7
Corn tortillas	2.3	1.1
Goods and services with the largest negative contribution		
Electricity tariffs	-25.3	-12.3
Onions	-5.0	-13.5
Lemons	-4.9	-17.3
LP gas	-4.1	-1.8
Bananas	-2.0	-7.1

Source: INEGI|

Annual core inflation above 7% for the first time since January 2001. Annual headline inflation increased from 7.45% on average in March to 7.72%. Meanwhile, the core stood at 7.16% from 6.78% in the same period. In bi-weekly frequency, the latter has moved up in 22 out of the last 23 prints (since the beginning of May last year). We still believe that commodity price dynamics remain key for the short-term outlook. Broadly speaking, news remain negative, both for energy and food. This suggests that the peak in annual inflation could be delayed further than expected (in the next fortnight for the headline, and by the end of June for the core), even with some government efforts to limit price pressures. Locally, we have started to notice a more sizable deterioration in drought conditions in some states (*e.g.* Sonora, Coahuila, Nuevo León) that are relevant to agricultural production. Hence, this suggests a lower probability of a rapid improvement.

Banxico will remain cautious given high inflation and global monetary policy. We expect the central bank to hike by 50bp in the decision to be held on May 12th, to 7.00%. First, inflation has not yielded yet, with results for the headline in 1H22 and the abovementioned risks probably translating into a new upward adjustment in inflation forecasts in said meeting. Secondly, we believe the Fed will raise by the same magnitude on May 4th, narrowing the options available to Banxico given its effect on the relative stance. More importantly, it is quite reasonable to keep seeing a hawkish bias, with further risks of a 50bps hike again at least in the meeting on June 23rd.

From our fixed income and FX strategy team

The market is pricing-in 50bps hikes in the next meetings. After Banxico's latest decision, the market has been consolidating the view of a more restrictive stance, incorporating a high probability of 50bps moves in the next four decisions –May, June, August and September–. In this sense, the short-end is pricing-in cumulative hikes of +260bps for the rest of the year. Inflation data has validated this scenario given renewed pressures on sovereign rates, led by Treasuries –after more hawkish comments from Fed members–. In this way, both Treasuries' and Mbonos' yield curves have shown a strong flattening bias this week, with the greatest pressures in the short-end. Meanwhile, CPI-linked bonds (Udibonos) remain expensive despite a modest compression in breakevens after hitting all-time highs. Specifically, the 3-year reading stands at 5.10%, above the 12-month average of 4.56%.

We do not open new trade ideas in these instruments despite recognizing that these securities could remain bid given ongoing appetite for inflation hedges. Moreover, we also see more relative attractiveness in the belly of the nominal curve given the high probability that short-term inflation pressures keep inverting the US curve, and therefore, in Mexico. Nonetheless, the global backdrop for inflation and rates keeps us out of directional positions.

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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, David Alejandro Arenas Sánchez, Leslie Thalía Orozco Vélez, Hugo Armando Gómez Solís, Yazmín Selene Pérez Enríquez, Miguel Alejandro Calvo Domínguez, Daniela Olea Suárez, Gerardo Daniel Valle Trujillo, Luis Leopoldo López Salinas, Isaías Rodríguez Sobrino, Paola Soto Leal and Daniel Sebastián Sosa Aguilar 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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