

## October inflation – Below expectations again on energy and agricultural goods

- **Headline inflation (October): 0.57% m/m; Banorte: 0.60%; consensus: 0.60% (range: 0.56% to 0.67%); previous: 0.62%**
- **Core inflation (October): 0.63% m/m; Banorte: 0.66%; consensus: 0.65% (range: 0.58% to 0.69%); previous: 0.67%**
- **The print was aided by lower pressures at the non-core. Despite the return higher in electricity tariffs (17.5% m/m), LP gas (-7.3%) and agricultural goods (-0.5%) declined. At the core, goods kept increasing (0.9%), particularly processed foods (1.0%). In services (0.3%), advances remain centered in ‘others’ (0.5%)**
- **Annual headline inflation moderated to 8.41% from 8.70% in the previous month. Nevertheless, the core accelerated for 23<sup>rd</sup> straight month, climbing to 8.42% (previous: 8.28%)**
- **We restate our call of +75bps by Banxico tomorrow, with the reference rate closing the year at 10.50%**
- **Market widely expects a 75bps hike tomorrow**

**October’s inflation climbs 0.57% m/m, helped by the non-core.** The core remained high at 0.63%. The second half of the month showed an extension of several of the trends seen in the [first fortnight](#). Goods were high at 0.9%, driven both by processed foods (1.0%) –highlighting increases in key goods such as corn tortillas and milk–, as well as ‘others’ (0.7%), albeit not ruling out that the latter could have started to be affected by preparations ahead of *El Buen Fin* (Mexico’s Black Friday). In services (0.3%), pressures remained in ‘others’ (0.5%), with some adjustments in tourism categories, but with most of the brunt still in ‘dining away from home’. At the non-core (0.38%), and as already known, energy has a negative seasonality due to the end of summer discounts on electricity tariffs (17.5%). Nevertheless, LP gas fell sharply throughout the month (-7.3%), helped by lower prices in the US. On the contrary, gasolines likely started to reflect actions by [OPEC+](#), among other factors, with low-grade fuel up 0.7%. Agricultural goods were mostly positive (-0.5%), especially fruits and vegetables (-1.3%). Meat and egg moved modestly to the upside (0.1%), albeit with slight signs of pressures in the second half on reports of a new bout of bird flu, although still at an early stage.

October 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
Electricity	25.6	17.5
Tomatoes	11.2	18.8
Dinning away from home	4.7	1.0
Corn tortillas	3.5	1.6
Low-grade gasoline	3.3	0.7
Goods and services with the largest negative contribution		
LP gas	-15.0	-7.3
Potatoes	-8.4	-16.1
Onions	-8.0	-18.4
Avocadoes	-4.4	-16.2
Oranges	-4.3	-17.3

Source: INEGI

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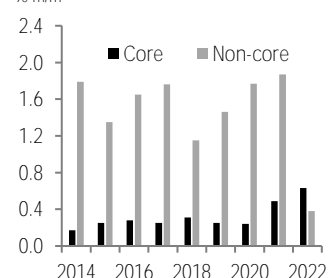
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Core and non-core inflation in  
October  
% m/m



Source: INEGI

**Annual inflation moved lower, but underlying problems persist.** With these results, headline inflation fell to 8.41% from 8.70% y/y, its first monthly decline since May. However, the core accelerated for a 23<sup>rd</sup> month in a row to 8.42% from 8.28%. This is more concerning and implies a challenging backdrop, especially as additional risks seem to be materializing. In our opinion, concerns on energy remain in place, both due to the trend on reference prices in gasolines –with actions by the US government not enough to offset for OPEC+ cuts–, as well as possible sways in gas prices as winter approaches. As already stated, news on chicken prices are negative, with reports of bird flu outbreaks in seven states and US supplies also under pressure because of the same factor. Possibly better, we will be looking into dynamics stemming from *El Buen Fin* discounts –which will take place from November 18<sup>th</sup> to 21<sup>st</sup>– and the possible spillover sales related to the 2022 *FIFA World Cup* –from November 20<sup>th</sup> to December 18<sup>th</sup>. Finally, we will keep monitoring the effects from the [\*Complementary Measures to the Plan Against Inflation\*](#). Considering the balance of risks, we maintain our forecast for year-end inflation at 9.0% –still above consensus–, albeit acknowledging that the final figure could be below our forecast given recent dynamics, particularly at the non-core level.

**Banxico will keep tightening monetary policy given a complex and uncertain backdrop.** In our view, the decision to hike the reference rate by 75bps in tomorrow's decision is quite clear, considering: (1) The adjustment of the same magnitude by the Fed last week; (2) an additional deterioration in core inflation; and (3) the need to maintain caution in an environment of high volatility in global financial markets and capital flows. As several of these factors –if not all– will remain at play in future decisions, we believe the central bank will keep tightening monetary conditions, anticipating the reference rate by year-end at 10.50% and a terminal point for this cycle at 11.00% (to be reached by the end of 1Q23).

*From our fixed income and FX strategy team*

**Market widely expects a 75bps hike tomorrow.** In a complex inflationary backdrop, the market is fully pricing-in a 75bps hike by Banxico tomorrow, in tandem with the last Fed decision. Moreover, market expectations point towards greater conviction about a moderation in the pace of hikes in December (+50bps) –in similar fashion with the US– and a terminal rate of 11.00% next year. In this context, we expect volatility in the fixed-income market to remain high, so we reaffirm our preference for relative value strategies vs directional positions. The latter, despite recognizing an attractive valuation in long-term Mbonos, mainly in tenors Nov'38 and Nov'42, which both ended October at 10.00% and are now trading at the same level of 9.91%. Meanwhile, despite a recent compression of breakevens across all maturities, CPI-linked bonds (Udibonos) continue to reflect an unattractive relative valuation. For example, the 3-year breakeven stands at 5.03% from 5.46% a month ago, well above Banxico's inflation target. Therefore, we do not see enough attractiveness in Udibonos, at least for now.

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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 Thalia 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, 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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