

Inflation in August explained by pressures on fresh fruits and vegetables as well as energy

- **INEGI just published its inflation report for August**
- **Headline inflation (Aug): 0.49% m/m; Banorte-Ixe: 0.54% m/m; consensus: 0.5% m/m; (range of estimates: 0.43% to 0.58%); previous: 0.38% m/m**
- **Core inflation (Aug): 0.25% m/m; Banorte-Ixe: 0.3% m/m; consensus: 0.29% m/m (range of estimates 0.25% to 0.32%); previous: 0.27% m/m**
- **Inflation in August was explained by pressures on the prices of fruits and vegetables as well as energy**
- **With these numbers, annual inflation is at 6.66% vs. 6.44% in the previous month**
- **Inflation dynamics positive four our trade idea regarding the 3-year CPI-linked Udibono**

Consumer prices increased 0.49% m/m in in August. Core inflation was 0.25% vs. our 0.3% estimate. The main deviation from our forecast comes from: (1) A lower than expected contribution of other services prices (5.6bps vs. our 7.6bps); and (2) a lower than expected contribution of other goods prices (10.6bps vs. our 12.2bps), as shown in the table below.

August inflation by major subcomponent

Monthly incidence, %

	Observed	Banorte-Ixe forecast	Difference
Headline	0.49	0.54	-0.05
Core	0.19	0.23	-0.04
Goods	0.17	0.19	-0.02
Processed foods	0.06	0.07	-0.01
Other goods	0.11	0.12	-0.02
Services	0.03	0.04	-0.01
Housing	0.04	0.03	0.00
Education	0.06	0.06	0.00
Other services	-0.08	-0.06	-0.02
Non-core	0.30	0.31	-0.01
Agricultural	0.20	0.21	-0.02
Fresh fruits and vegetables	0.16	0.17	-0.01
Meat and egg	0.03	0.04	-0.01
Energy and government regulated	0.10	0.10	0.00
Energy	0.08	0.08	0.00
Government regulated	0.02	0.02	0.00

Source: INEGI, Banorte-Ixe

Note: Contributions might not add due to the number of decimals allowed in the table. Previous to year 2011, contributions might not add because of the change in CPI-calculation methodology

September 7, 2017

www.banorte.com
www.ixc.com.mx
@analisis_fundam

Gabriel Casillas

Chief Economist and Head of Research
gabriel.casillas@banorte.com

Delia Paredes

Executive Director of Economic Analysis
delia.paredes@banorte.com

Alejandro Cervantes

Senior Economist, Mexico
Alejandro.cervantes@banorte.com

Francisco Flores

Economist, Mexico
francisco.flores.serrano@banorte.com

Fixed income and FX Strategy

Alejandro Padilla

Head Strategist – Fixed-Income and FX
alejandro.padilla@banorte.com

Juan Carlos Alderete, CFA

FX Senior Strategist
juan.alderete.macal@banorte.com

Santiago Leal Singer

Fixed-Income and FX Strategist
santiago.leal@banorte.com

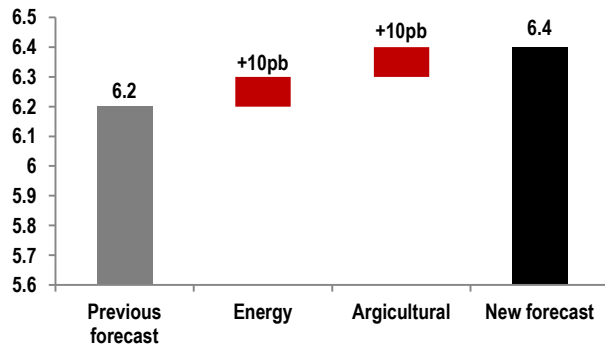
Document for distribution among public

Inflation in August was explained by pressures on the prices of fresh fruits and vegetables, as well as energy. In the first case, prices climbed 4.5% m/m, on the back of the 54.6% m/m rise in the price of onions, as well as increases in the prices of tomatoes (8.4% m/m), potatoes (8.9% m/m), and husk tomatoes (15.7% m/m). However, these increases were offset by the fall in the prices of squash (-26.6% m/m), bananas (-6.5% m/m), avocados (-5.2% m/m) and chilies (-7.2% m/m). Moreover, energy prices rose 0.8% m/m, due to the 3% increase of LP gas and 0.4% m/m in low grade gasoline.

Regarding core items, education prices rose 1.2% m/m, due to higher prices of universities (2% m/m) and high school (2.2% m/m). Moreover, other services decreased 0.4% m/m, on the back of declines in tourism services (-9.8% m/m) and air fares (-19.4% m/m). Additionally, processed foods increased 0.4% m/m, while other goods rose 0.6% m/m.

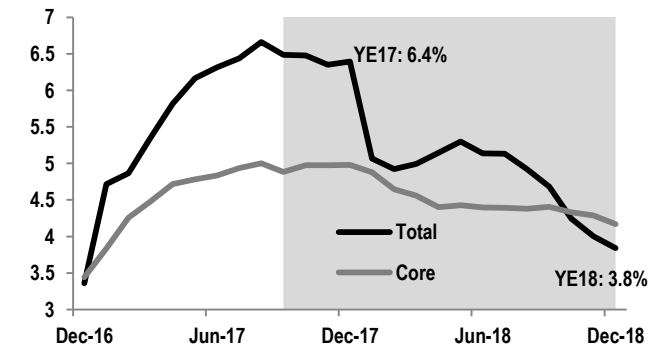
We now expect inflation at 6.4% by year end (vs. our previous 6.2%). The reason behind this change comes mainly from the natural disasters and weather conditions in the US, given the impact of Hurricane Harvey and the implications of Hurricane Irma in Florida. In the first case, we anticipate an impact on the prices of energy, particularly on gas, which is already fully liberalized and can therefore be adjusted without restriction. Additionally, we expect increased pressures on agricultural products. We consider that the adjustment in energy prices will add 10 basis points, while in the agricultural sector these will add 10 basis points. Since we expect the impact of these effects to be transitory, we maintain our inflation estimate for the end of 2018 at 3.8% yoy.

Changes in our inflation forecast
%



Source: Banorte

Inflation trajectory 2017-2018
% yoy



Source: INEGI; Banorte

From our fixed income and FX strategy team

Inflation dynamics positive for our trade idea regarding the 3-year CPI-linked Udibono. Consumer prices continue trending higher, granting an attractive carry in CPI-linked securities (*e.g.* Udibonos). Given the dynamics discussed in the previous section, we hold a positive view in terms of our trade idea on the 3-year Udibono Dec'20. Moreover, the 3-year breakeven is at 3.64%, below the 12-month average of 3.71%, and 1.2σ from its 3-month MA, suggesting an attractive valuation. Based on our inflation forecasts, 12m carry in UDIS is at 4.81%, significantly higher than consensus, one-year forward inflation of 3.87% (median) according to Banxico's latest survey released last Friday. On the other hand, the disruptions in crude oil, gasoline and other energy markets following Hurricane Harvey could result in some inflationary pressures ahead, adding to the positive factors for this trade idea commented in previous publications. Taking into account this scenario, we recommend holding the long positions in the 3-year Udibono Dec'20 with entry level of 3.05%, target of 2.90%, stop-loss of 3.15%, and current level of 3.01%. More details in our research note "*We recommend long positions in the 3-year Udibono Dec'20*" <[pdf](#)>, published on August 9th, 2017.

Disclaimer

The information contained in this document is illustrative and informative so it should not be considered as an advice and/or recommendation of any kind. BANORTE is not part of any party or political trend.

GRUPO FINANCIERO BANORTE S.A.B. de C.V.
Research and Strategy

Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967

Economic Analysis

Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Alejandro Cervantes Llamas	Senior Economist, Mexico	alejandro.cervantes@banorte.com	(55) 1670 - 2972
Katia Celina Goya Ostos	Senior, Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Miguel Alejandro Calvo Domínguez	Economist, Regional & Sectorial	miguel.calvo@banorte.com	(55) 1670 - 2220
Juan Carlos García Viejo	Economist, International	juan.garcia.viejo@banorte.com	(55) 1670 - 2252
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611

Fixed income and FX Strategy

Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Juan Carlos Alderete Macal, CFA	FX Senior Strategist	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Santiago Leal Singer	Strategist Fixed income and FX	santiago.leal@banorte.com	(55) 1670 - 2144

Equity Strategy

Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Victor Hugo Cortes Castro	Technical Analysis	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Equity Research – Conglomerates / Financials/ Mining / Petrochemicals	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research – Airlines / Airports / Cement / Infrastructure / REITs	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251

Corporate Debt

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248

Wholesale Banking

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebillos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
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) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Asset Management	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Victor Antonio Roldan Ferrer	Head of Corporate Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454