

Inflation in August explained by higher gasoline prices

September 8, 2016

www.banorte.com
www.ixe.com.mx
@analisis_fundam

- **INEGI just published its inflation report for August**
- **Headline inflation (Aug): 0.28%/m/m (Banorte-Ixe: 0.35%/m/m; consensus: 0.31%/m/m)**
- **Core inflation (Aug): 0.19%/m/m (Banorte-Ixe: 0.18%/m/m; consensus: 0.19%/m/m)**
- **Inflation August was explained by pressures on the prices of low-grade gasoline prices other merchandise prices**
- **With these numbers, annual inflation is at 2.73% vs. 2.65% in previous month**
- **Local rates trading defensively as CPI monthly figure lower than market consensus for a third straight month**

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

Alejandro Cervantes
Senior Economist, Mexico
alejandro.cervantes@banorte.com

Fixed income and FX Strategy

Alejandro Padilla
Director de Estrategia
Renta Fija y Tipo de Cambio
alejandro.padilla@banorte.com

Juan Carlos Alderete, CFA
FX Strategist
juan.alderete.macal@banorte.com

Santiago Leal
Analyst Fixed Income and FX
santiago.leal@banorte.com

Consumer prices increased 0.28%/m/m in August, below expectations. Core inflation was 0.19% in line with our estimates. The main deviation from our forecast comes from: (1) A lower than expected contribution of energy prices (10.7bps vs. our 21.2bps); (2) a lower than expected contribution of services prices (0.8bps vs. our 2bps); and (3) a larger than expected contribution of agricultural prices (3.3bps vs. our -0.9bps), as shown in the table below.

Inflation by components in August
%/monthly incidence

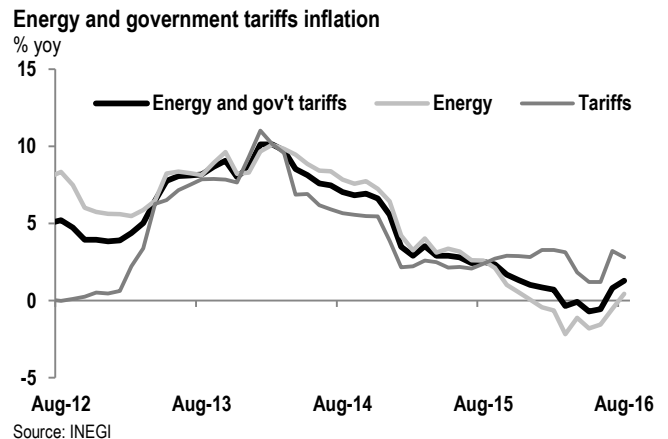
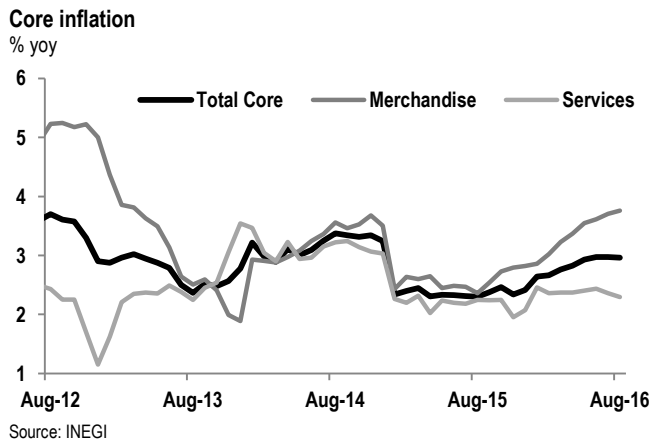
	INEGI	Banorte-Ixe	Difference
Total	0.28	0.35	-0.068
Core	0.14	0.15	-0.012
Goods	0.14	0.14	0.001
Processed foods	0.01	0.01	-0.001
Other goods	0.12	0.12	0.002
Services	0.01	0.02	-0.012
Housing	0.03	0.03	-0.001
Education	0.05	0.05	-0.003
Other services	-0.07	-0.06	-0.009
Non-core	0.14	0.20	-0.058
Agriculture	0.03	-0.01	0.042
Fruits & vegetables	0.04	0.00	0.036
Meat & eggs	-0.01	-0.01	0.007
Energy & government tariffs	0.11	0.21	-0.104
Energy	0.11	0.21	-0.105
Government tariffs	0.00	0.00	-0.001

Source: Banorte-Ixe with data from INEGI and Banco de México.
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

Document for distribution among public

Inflation August was explained by pressures on the prices of low-grade gasoline prices other merchandise prices. In particular, the low-grade gasoline prices rose 3.16%, adding 15.1bps to total CPI variation during August. On top of this, electricity tariffs were up 0.93% monthly. Such increases were more than offset by the 5% decline in the price of domestic gas. Meanwhile, merchandise prices edged up 0.39% m/m on the back of a 0.07% increase in the prices of food along other merchandise prices, up 0.65%, explaining 44% of inflation in the period in question. Regarding services inflation, education costs were up 0.92% given the start of the new school year, while housing costs rose 0.15%. By contrast, other services came down 0.39% m/m with significant declines in tourism services prices (-9.03%), air transportation fares (-13.78%) and mobile services (-1.12%). Finally, agricultural prices increased 0.35% m/m on the back of significant increases in fruit and vegetables (1.18%) combined with a reduction of “meat & egg” prices (-0.11%).

With these data, annual inflation is at 2.73% vs. 2.65% in the previous month. Meanwhile, the core inflation remained at 2.96% y/y. We continue to see pressures on merchandise prices, on the back of the contagion coming from the depreciation of the Mexican peso, although inflation in the rest of the components of the core sub-index remains relatively stable, as shown in the chart below. In this context, we maintain our expectation that inflation will end the year at around 2.8%, taking into account, among others: (1) Increases in gasoline prices; (2) increases in electricity rates high consumption; and (3) the fact that *INEGI* has delayed the coming year change in CPI methodology.



From our fixed income and FX strategy team

Local rates trading defensively as CPI monthly figure lower than market consensus for a third straight month. Mexican bonds are trading flat today, despite a 2bps sell-off in US Treasuries and 3bps losses in European and Asian bonds, as a lower than expected CPI monthly print has compensated the disappointment of global investors following ECB policy decision today. In our view, annual inflation could end the year around 2.8% (currently at 2.7%), with favorable dynamics in coming months that could result in a well-anchored inflation premium embedded in Mbonos. As of yesterday's close, inflation breakevens are located at 2.99% in the 3-year tenor, 3.05% at 5-year, 3.02% at 10-year and 3.03% at 30-year, hovering around Banxico's inflation target of 3%. This suggests an attractive valuation for CPI-linked Udibonos for the next years; however, demand for these securities remains extremely low as the current inflation scenario poses downside risks for carry gains in real-rate instruments. It is under this rationale that we continue suggesting overweight in Mbonos and underweight in Udibonos, at least until the current scenario reaches an inflection point (possibly until next year). Moreover, taking into account this outline and the pricing of the yield curve, we remain positive in terms of the belly of the Mbonos curve, which continues depicting a more attractive relative valuation *vis-à-vis* other tenors, especially the 5-to-7-year segment for a short-term tactical strategy. Despite this assessment, we are keen to waiting for better market conditions and entry points to start a directional recommendation in these securities, ahead of important risk factors in coming weeks: Fed's decision (Sep 21st), first presidential debate in the US and a possible OPEC non-official meeting (Sep 26th), and Banxico's decision (Sep 29th), among others.

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
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 Strategist	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Santiago Leal Singer	Analyst 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
Víctor Hugo Cortes Castro	Equity Research Analyst	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Senior Equity Research Analyst – Conglomerates / Financials/ Mining / Chemistry	marissa.garza@banorte.com	(55) 1670 - 1719
Marisol Huerta Mondragón	Equity Research Analyst – Food / Beverages / Specialized Commerce	marisol.huerta.mondragon@banorte.com	(55) 1670 - 1746
José Itzamna Espitia Hernández	Equity Research Analyst – Airports / Cement / Infrastructure / Fibras	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research Analyst – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Eugenia Ivonne Arias Medina	Analyst	eugenia.arias.medina@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	Analyst, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Idalia Yanira Céspedes Jaén	Analyst, Corporate Debt	idalia.cespedes@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
Víctor Antonio Roldan Ferrer	Head of Corporate Banking	victor.rolan.ferrer@banorte.com	(55) 5004 - 1454