

Inflation 1H-September – Additional declines in fruits and vegetables drag the headline down

- **Headline inflation (1H-September): 0.09% 2w/2w; Banorte: 0.16%; consensus: 0.13% (range: 0.04% to 0.32%); previous: -0.06%**
- **Core inflation (1H-September): 0.21% 2w/2w; Banorte: 0.23%; consensus: 0.21% (range: 0.16% to 0.33%); previous: 0.10%**
- The period is impacted by some relevant seasonal effects, which are more evident in the core. As such, we highlight the 2.6% 2w/2w uptick in education due to the return to classes. Continuing with services, housing remained somewhat pressured (0.2%), although with 'others' (0.0%) benefiting from some discounts in the professional category. In goods (0.2%), 'others' also increased (0.3%), in line with the seasonality of the period. Moving to the non-core (-0.31%), agricultural items kept declining –with fruits and vegetables adding a fourth fortnight down at -1.5%. In energy (0.0%), decreases in electricity (-0.8%) and low-grade gasoline (-0.2%) stand out
- In bi-weekly terms, annual inflation moderated to 4.66% from 4.83% in the second half of August. The core declined once again, now at 3.95% (previous: 4.01%)
- We believe that this result, as well as other factors, support our view of a 25bps cut by Banxico this Thursday

Inflation at 0.09% 2w/2w in the 1st half of September. Similar to the previous month, the period is impacted by different seasonal effects, with the main one being the return to classes. These are more evident within the core (0.21%), where the 2.6% increase in education –now driven by elementary and middle school tuitions– stands out. Continuing with services, housing was somewhat high again at 0.2%. 'Others' (0.0%) benefited from some discounts in the professional category (-14.8%), although with some pressures continuing in 'dining away from home'. In goods (0.2%), processed foods moderated 0.0%. However, 'others' accelerated (0.3%) also in line with the period's seasonality. Turning to the non-core (-0.31%), agricultural items continued to decline, now by -0.8%. This reduction was again explained by fruits and vegetables (-1.5%) –with contractions in tomatoes, oranges and bananas–, which now adds four fortnights lower. Meat and egg was more limited at -0.3%. In energy (0.0%), decreases in electricity (-0.8%) and low-grade gasoline (-0.2%) stood out –recognizing a moderation in international references in recent weeks. However, LP gas increased 1.2%. Finally, government tariffs were slightly higher again at 0.3%.

1H-September 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
Elementary school	2.4	5.5
Housing	2.2	0.2
LP gas	1.7	1.2
Lemons	1.6	12.8
Dining away from home	1.4	0.3
Goods and services with the largest negative contribution		
Tomatoes	-6.1	-9.5
Professional services	-3.6	-14.8
Oranges	-2.2	-13.6
Bananas	-1.3	-5.2
Avocadoes	-1.2	-6.0

Source: INEGI



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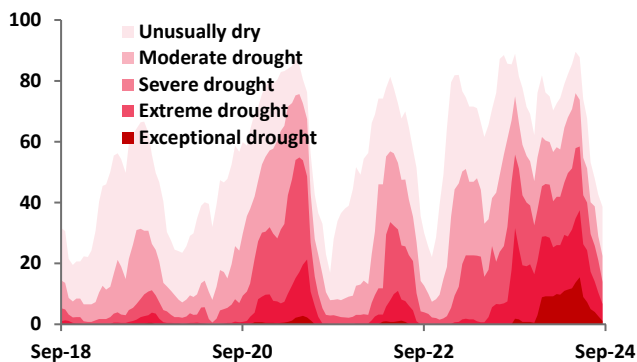
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Headline inflation continues to moderate, with the core also declining, albeit more modestly.

The former came in at 4.66% y/y from 4.83% in the second half of August, lower for a fourth consecutive fortnight. As we have mentioned on previous occasions, this is mainly due to the reduction in the non-core (at 6.73% from 7.27%), which is explained by two factors: (1) The fading of an adverse base effect in energy products, especially LP gas; and (2) the downward reversal in fruits and vegetables after shocks in previous months. Going forward, we believe that conditions could be better, although some challenges remain. Starting with agriculture, drought levels have declined strongly (see chart below, left), due to a season of heavy rains. This will help harvests in general, although we are still waiting for some time to pass for the positive effects to materialize. Nevertheless, some flooding problems have been reported in some regions, which could impact crops. On the other hand, reference prices for energy have shown a downward trend in recent months, a situation that can also be seen in the futures curves of some hydrocarbons such as gasoline (see graph below, right). The reason lies in the expectation of slower global growth, with pessimism in China being one of the main drivers. However, as seen in some recent sessions, their prices remain highly sensitive to geopolitical tensions in the Middle East. In the meantime, core inflation adjusted downwards to 3.95% (previous: 4.01%). This component has hovered around the 4% threshold since the second half of June, which we believe is relatively positive. As we have explained on other occasions, the performance of goods has been key in explaining this (currently at 2.9%). In services –which remain above 5%, at 5.2%–, some mixed results stand out, with improvements in education and in some items within ‘others’, but with increases in housing, as well as continued gains in ‘dining away from home’. In this sense, we believe that the declines for the entire category could continue, although the magnitude of the movements will probably be more limited.

Drought monitor

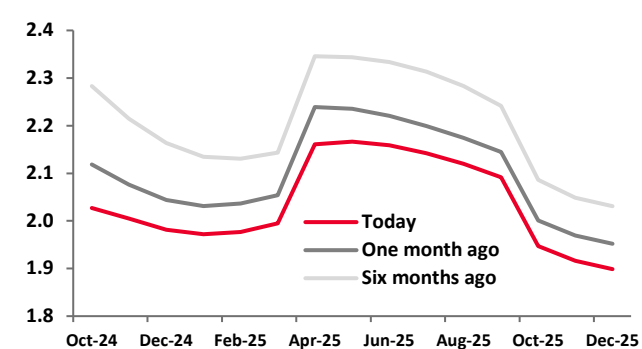
% of the country's territory with some level of impact



Source: Banorte with data from CONAGUA

Gasoline futures (RBOB)

US\$ per gallon



Source: Banorte with data from Bloomberg

Banxico will continue easing with a 25bps cut this Thursday. We believe today's results support the arguments made by dovish members –Governor Victoria Rodríguez, Galia Borja, and Omar Mejía– in recent publications, where they highlighted their expectations that the shock in the non-core would reverse without causing relevant distortions in other items. In addition, and as we mentioned in our [View from the Top](#), there are other factors such as a more challenging economic outlook and the beginning of the Fed cuts that will help the easing cycle to continue in our country. Thus, we anticipate a 25bps reduction to the reference rate in this week's decision, taking it to 10.50%.

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