Economic and Financial Markets Research
Economic Research, Mexico

August 22, 2025

Inflation 1H-August – Surprise due to a moderation in goods within the core

- **Headline inflation (1H-August): -0.02% 2w/2w; Banorte: 0.12%; consensus: 0.12% (range: 0.00% to 0.18%); previous: 0.07%**
- **Core inflation (1H-August): 0.09% 2w/2w; Banorte: 0.21%; consensus: 0.14% (range: 0.10% to 0.21%); previous: 0.11%**
- **The result was explained by the 0.41% decline of the non-core, highlighting the positive performance in agriculture (-1.0%). Both fruits and vegetables, and meat and egg, declined. Energy prices (0.0%) were very limited again. In the core, seasonal effects dominated several of the adjustments. In services (0.1%) the impacts are mixed, with the 'back-to-school' period resulting in increases in education (0.7%), but with reductions in tourism within 'others' (0.0%). Housing advanced 0.2%. Finally, in goods (0.1%), 'others' surprised lower as the period used to exhibit increases due to the end of some discounts in clothing**
- **With bi-weekly figures, annual inflation came in at 3.49% from 3.48% in the 2nd half of July, with the positive base effect starting to fade. Core inflation was also broadly unchanged at 4.21% (previous: 4.22%)**
- **Banxico's minutes support the institution's dovish tone and our forecast of -25bps in September, with the interest rate reaching 7.00% by year-end**

Inflation of -0.02% 2w/2w in the 1st half of August. The low print vs. its historical average was driven by the non-core at -0.41%. Inside, the decline was concentrated in agriculture (-1.0%), with contractions in both fruits and vegetables (-1.2%) –with significant reductions in tomatoes, bananas, and squashes– and meat and egg (-0.8%) –with chicken and eggs lower. Energy prices were again very stable at 0.0%, with limited changes in electricity (0.2%). Government tariffs came in at 0.0%. The core (0.09%) was affected by some seasonal distortions. In services (0.1%), changes are linked to the 'back-to-school' period, with education up 0.7% –with university and high school tuitions up– but with tourism down (*e.g.* air fares at -8.4% and packages at -0.9%) within 'others' (0.0%). However, pressures prevail in 'dining away from home' (0.4%) inside the latter. Housing moderated at the margin at 0.2%. In goods (0.1%), 'others' were unchanged (0.0%), contrasting with the historical seasonality that typically exhibits the end of discounts on clothing and shoes. Finally, processed foods increased by 0.2%.

1H-August 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
Dining away from home	2.0	0.4
Housing	1.9	0.1
University	1.3	1.1
Serrano chilies	1.0	12.9
Beef	1.0	0.5
Goods and services with the largest negative contribution		
Tomatoes	-4.6	-8.8
Chicken	-4.5	-2.5
Air fares	-2.2	-8.4
Cinema	-1.5	-10.0
Eggs	-1.4	-1.3

Source: INEGI


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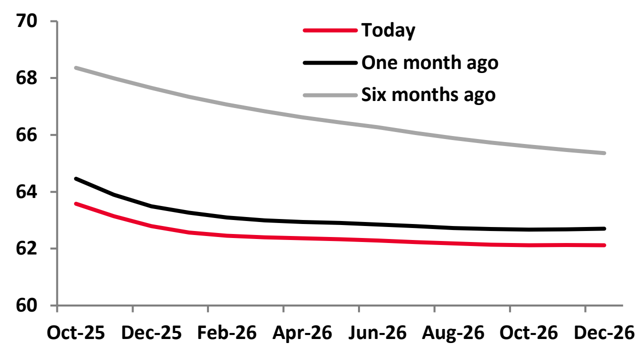
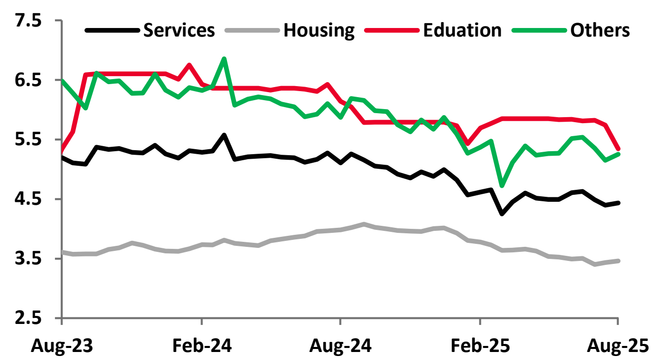
Slight uptick in the annual comparison for the headline, with a positive base effect beginning to fade. With these results, headline inflation stood at 3.49% y/y, up from 3.48% in the 2nd half of July. The increase was explained by the non-core, now at 1.10% (previous: 1.04%), with favorable base effects for agricultural items (0.4%) and energy (0.5%) starting to dissipate. In the former, we continue to closely monitor the rainy season and its effect on crops, with substantial improvements in drought levels and news so far showing no significant losses due to excessive rainfall. In meat and egg, we have no reports of significant disruptions, although global prices remain under some pressure. In the latter, OPEC+ actions and expectations about global economic activity have depressed benchmark prices, with futures showing much more favorable paths (see chart below, left). Meanwhile, the core continued to rise, now at 4.21% (previous: 4.22%). Inside, goods were relatively stable at 4.0%, although with the base effect for both processed foods and 'others' becoming increasingly difficult –reaching its peak in November. MXN strength could help limit further adjustments, but we remain cautious about the impact from some of the trade restrictions announced by our country in various sectors (*e.g.* textiles, shoes, *minimis*). Finally, services moderated at the margin at 4.4% (see chart below). Relevantly, housing has halted its downward trend, accelerating to 3.5%, with more substantial increases in the previous fortnights. Education was lower at 5.3%, still awaiting adjustments in elementary and middle school tuitions next month to assess its level for the coming year. Lastly, 'others' accelerated to 5.3%, with challenges persisting for this category.

WTI futures
US$/bbl



Source: Banorte with data from Bloomberg

Core inflation: Services
% y/y, bi-weekly frequency



Source: Banorte with figures from INEGI

The latest minutes suggest that there is still room for further cuts. The document published yesterday corroborated the members' dovish tone. In this backdrop, we believe that despite some challenges for inflation still in the cards, the limited performance of economic activity, expectations about the Fed's next actions, and Mexican peso dynamics will continue to drive cuts. Thus, we keep our call of -25bps in September and of an interest rate of 7.00% by the end of the year.

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We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Marissa Garza Ostos, Katia Celina Goya Ostos, Francisco José Flores Serrano, José Luis García Casales, Santiago Leal Singer, Víctor Hugo Cortes Castro, Leslie Thalía Orozco Vélez, Hugo Armando Gómez Solís, Carlos Hernández García, Yazmín Selene Pérez Enríquez, Cintia Gisela Nava Roa, José De Jesús Ramírez Martínez, Daniel Sebastián Sosa Aguilar, Gerardo Daniel Valle Trujillo, Luis Leopoldo López Salinas, Marcos Saúl García Hernandez, Juan Carlos Mercado Garduño, Ana Gabriela Martínez Mosqueda, Jazmin Daniela Cuautencos Mora, Andrea Muñoz Sánchez and Paula Lozoya Valadez, 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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