November 23, 2023

Inflation 1H-November – Pressures in meat and egg, along with an unfavorable seasonality

- **Headline inflation (1H-Nov): 0.63% 2w/2w; Banorte: 0.62%; consensus: 0.63% (range: 0.46% to 0.69%); previous: 0.13%**
- **Core inflation (1H-Nov): 0.20% 2w/2w; Banorte: 0.23%; consensus: 0.21% (range: 0.12% to 0.28%); previous: 0.18%**
- **As is usual, performance was determined by the end of summer discounts to electricity tariffs, resulting in a 22.3% 2w/2w increase. In addition, we noted rises in other categories at the non-core, particularly agricultural items (1.0%) –with relevant pressures in some goods inside. Going to the core, goods (0.3%) had some distortions, especially in 'other goods' (0.0%), which we associate to *El Buen Fin* discounts (Mexico's Black Friday). Finally, services climbed 0.3%, driven by 'others' (0.4%)**
- **In bi-weekly terms, annual inflation climbed to 4.32% from 4.25%, its first increase in 12 fortnights. The core fell to 5.31% from 5.46%, still helped by a positive base effect, which will end this month**
- **Considering the performance in the last couple of months and despite the rebound in agricultural goods, risks for our year-end inflation estimate at 5.0% are tilted to the downside**
- **Attention on Banxico's minutes later today, expecting additional information on changes to the forward guidance and other factors behind the less hawkish tone**

Prices up 0.63% 2w/2w in the 1st half of November. This period is mainly impacted by the end of summer discounts on electricity tariffs –in its second and last tranche–, driving electricity up 22.3%. In other energy items, both LP gas (-0.3%) and low-grade gasoline (-0.2%) moderated, helped by a stronger MXN along with lower international benchmark prices. Also relevant, agricultural goods climbed 1.0%, driven by fruits and vegetables (0.7%) –with large increases in husk tomatoes, tomatoes, and chilies– and in meat and egg –pushed by eggs and chicken, consistent with reports of problems in the sector. At the core (0.20%), goods expanded by 0.1%. We noted the null increase in 'other goods' (0.0%), with its performance skewed by some discounts along with upward adjustments ahead of *El Buen Fin* (Mexico's Black Friday) –which this year was held between November 17th to the 20th. In processed foods (0.3%) sugar was pressured once again. In services (0.3%), the push came again from 'others' (0.4%), both from tourism (*e.g.* air fares) and non-tourism categories (*e.g.* professional services and 'dinning away from home'). Finally, housing rose 0.2%, accelerating at the margin.

1H-November 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
Electricity	37.3	22.3
Eggs	7.2	7.8
Air fares	3.0	11.6
Husk tomatoes	2.7	18.8
Tomatoes	2.2	3.7
Goods and services with the largest negative contribution		
Lemons	-2.8	-15.9
Onions	-1.0	-3.9
Hotels	-0.9	-3.8
Low-grade gasoline	-0.8	-0.2
Avocadoes	-0.6	-2.7

Source: INEGI

Alejandro Padilla Santana
Chief Economist and Head of Research
alejandro.padilla@banorte.com

Juan Carlos Alderete Macal, CFA
Executive Director of Economic Research and Market Strategy
juan.alderete.macal@banorte.com

Francisco José Flores Serrano
Director of Economic Research, Mexico
francisco.flores.serrano@banorte.com

Yazmín Selene Pérez Enríquez
Senior Economist, Mexico
yazmin.perez.enriquez@banorte.com

Cintia Gisela Nava Roa
Senior Economist, Mexico
cintia.nava.roa@banorte.com

www.banorte.com/analisiseconomico
@analisis_fundam

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Performance in previous fortnights implies downside risks to our year-end estimate, despite the rebound in the agricultural sector. With these results, headline inflation rose to 4.32% from 4.25% in the second half of October, breaking with 12 fortnights lower. The adjustment was mainly driven by the non-core, which accelerated to 1.41% from 0.64%. This impulse comes from the agricultural sector, consistent with the rebound in this fortnight. As mentioned in previous posts, we anticipated a stronger push from this category due to more challenging drought conditions through the summer and early autumn. However, and partly based on the performance in today's report, these increases will likely materialize in coming months. In this respect, the risks of additional shocks are relevant, particularly from *El Niño*. According to *NOAA*'s *Climate Prediction Center*, the probability of a 'historically strong' event of this phenomenon increased to 35% in November from 30% in October. The effects stemming from it would probably also extend to energy, where a more severe winter would boost demand for gas and other fuels, pushing prices up. At the core –which in the fortnight moderated to 5.31% from 5.46%, still with a positive base effect–, short-term dynamics will be dominated by the *El Buen Fin* discount period. However, once these distortions are over, goods could remain supported by a strong MXN and further normalization in supply chains. However, we stay cautious on services, where education and 'others' maintain very high rates. All things considered, recent dynamics have inserted relevant downside risks to our year-end inflation estimate of 5%. Nonetheless, we still think the bias is skewed towards higher levels on a longer time horizon, actually anticipating relevant pressures in coming months.

Attention on Banxico's minutes, particularly on the factors behind the shift towards a less hawkish tone. We will focus with special care on the forward guidance, adjusted to reflect that the rate will remain at its current level "for some time" and no longer "for an extended period". Considering recent comments from Governor Victoria Rodriguez in the press which seem to have ruled out a first cut in December, mentions from other members, along with her view in the document, may give us more color as to the desired timing and/or the conditions that need to materialize for this to happen.

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Directory

Research and Strategy

Alejandro Padilla Santana
Chief Economist and Head of Research
alejandro.padilla@banorte.com
(55) 1103 - 4043

Raquel Vázquez Godinez
Assistant
raquel.vazquez@banorte.com
(55) 1670 – 2967

Itzel Martínez Rojas
Analyst
itzel.martinez.rojas@banorte.com
(55) 1670 - 2251

Lourdes Calvo Fernández
Analyst (Edition)
lourdes.calvo@banorte.com
(55) 1103 - 4000 x 2611

María Fernanda Vargas Santoyo
Analyst
maria.vargas.santoyo@banorte.com
(55) 1103 - 4000 x 2586

Economic Research

Juan Carlos Alderete Macal, CFA
Executive Director of Economic Research and Market Strategy
juan.alderete.macal@banorte.com
(55) 1103 - 4046

Francisco José Flores Serrano
Director of Economic Research, Mexico
francisco.flores.serrano@banorte.com
(55) 1670 - 2957

Katia Celina Goya Ostos
Director of Economic Research, Global
katia.goya@banorte.com
(55) 1670 - 1821

Yazmín Selene Pérez Enríquez
Senior Economist, Mexico
yazmin.perez.enriquez@banorte.com
(55) 5268 - 1694

Cintia Gisela Nava Roa
Senior Economist, Mexico
cintia.nava.roa@banorte.com
(55) 1103 - 4000

Luis Leopoldo López Salinas
Economist, Global Internacional
luis.lopez.salinas@banorte.com
(55) 1103 - 4000 x 2707

Market Strategy

Manuel Jiménez Zaldívar
Director of Market Strategy
manuel.jimenez@banorte.com
(55) 5268 - 1671

Marissa Garza Ostos
Director of Equity Strategy
marissa.garza@banorte.com
(55) 1670 - 1719

Víctor Hugo Cortes Castro
Senior Strategist, Technical
victorh.cortes@banorte.com
(55) 1670 - 1800

José Itzamna Espitia Hernández
Senior Strategist, Equity
jose.espitia@banorte.com
(55) 1670 - 2249

Carlos Hernández García
Senior Strategist, Equity
carlos.hernandez.garcia@banorte.com (55) 1670 - 2250

Hugo Armando Gómez Solís
Senior Analyst, Corporate Debt
hugoa.gomez@banorte.com
(55) 1670 - 2247

Leslie Thalía Orozco Vélez
Senior Strategist, Fixed Income and FX
leslie.orozco.velez@banorte.com
(55) 5268 - 1698

Isaías Rodríguez Sobrino
Analyst, Fixed Income, FX and Commodities
isaias.rodriguez.sobrino@banorte.com
(55) 1670 - 2144

Gerardo Daniel Valle Trujillo
Analyst, Corporate Debt
gerardo.valle.trujillo@banorte.com
(55) 1670 - 2248

Juan Carlos Mercado Garduño
Strategist, Equity
juan.mercado.garduno@banorte.com
(55) 1103 - 4000 x 1746

Paula Lozoya Valadez
Analyst, Equity
paula.lozoya.valadez@banorte.com
(55) 1103 - 4000

Quantitative Analysis

Alejandro Cervantes Llamas Executive Director of Quantitative Analysis
alejandro.cervantes@banorte.com
(55) 1670 - 2972

José Luis García Casales
Director of Quantitative Analysis
jose.garcia.casales@banorte.com
(55) 8510 - 4608

Miguel Alejandro Calvo Domínguez
Senior Analyst, Quantitative Analysis
miguel.calvo@banorte.com
(55) 1670 - 2220

José De Jesús Ramírez Martínez
Senior Analyst, Quantitative Analysis
jose.ramirez.martinez@banorte.com
(55) 1103 - 4000

Daniel Sebastián Sosa Aguilar
Senior Analyst, Quantitative Analysis
daniel.sosa@banorte.com
(55) 1103 - 4000 x 2124

Jazmin Daniela Cuautencos Mora
Strategist, Quantitative Analysis
jazmin.cuautencos.mora@banorte.com
(55) 1103 - 4000

Andrea Muñoz Sánchez
Analyst, Quantitative Analysis
andrea.muñoz.sanchez@banorte.com
(55) 1103 - 4000

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