Ahead of the Curve

Hard landing expected in March PMI manufacturing and confidence

March 27, 2020

www.banorte.com
@analisis_fundam

Juan Carlos Alderete, CFA
Director of Economic Research
juan.alderete.macal@banorte.com

Francisco Flores
Senior Economist, Mexico
francisco.flores.serrano@banorte.com

- **IMEF's PMI indices (March).** We estimate important retracements on the back of a very challenging global backdrop, with basically all regions' outlook darkening on disruptions and restrictions imposed to fight COVID-19. Manufacturing would be most impacted, anticipating a decline to 44.3pts from 49.1pts in February. US indicators available suggest supply-chain disruptions have built-up quite rapidly, with new export orders plunging as global supply chains are more interconnected and just-in-time logistics more widespread than before. In non-manufacturing, we anticipate 47.1pts from 48.8pts. In our view, the A(H1N1) pandemic in April 2009 provides relevant information about possible dynamics in the latter, at least in the short term. In that occasion the indicator fell until May, when restrictions to public life were more heavily imposed
- **Consumer confidence (March).** We expect the index at 41.5pts, below the 43.9pts of the previous month. The fall would be mainly explained by the loss of optimism due to the coronavirus, which has already started to show in other indicators such as inflation and trade balance. We estimate a generalized retracement, with an impact both at the national level and per-household basis. Additional variables pointing in this direction include the FX exchange rate, levels of presidential approval, and the recent behavior of some components within inflation, among others

Mexico weekly calendar

DATE	TIME (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 30-Mar	**5:00pm**	**Budget balance (measured with PSBR)**	February	MX$ bn	--	--	9.1
Tue 31-Mar	**11:00am**	**Commercial banking credit**	February	% y/y real	1.7	--	1.9
		Consumption		% y/y real	1.3	--	1.6
		Housing		% y/y real	6.7	--	7.0
		Non-banking private firms		% y/y real	0.8	--	0.6
Tue 31-Mar	**11:00am**	**International reserves**	Mar-27	US$ bn	--	--	184.2
Wed 1-Apr	**11:00am**	**Family remittances**	February	US$ mn	2,636.1	--	2,582.8
Wed 1-Apr	**11:00am**	**Banxico's monthly survey of economic expectations**	March				
Wed 1-Apr	**2:00pm**	**PMI's survey (IMEF)**	March				
		Manufacturing		index	44.3	--	49.1
		Non-manufacturing		index	47.1	--	48.8
Fri 3-Apr	**8:00am**	**Consumer confidence**	March	index	41.5	--	43.9
Fri 3-Apr	**5:00pm**	**Citibanamex bi-weekly survey of economic expectations**					

Source: Banorte; Bloomberg

Proceeding in chronological order...

MoF's public finance report (February). Attention in the second report of the year will center on the Public Balance and Public Sector Borrowing Requirements (PSBR) –with the latter standing at +$9.1 billion in January–, and comparing them to the forecasts outlined in the *2020 Budget.* We will also be looking into the primary balance, which we expect to post a surplus. Regarding revenue and spending, we will also be on watch for the performance in the annual comparison, particularly the former, as these could offer additional information on economic activity. Finally, we will also analyze public debt, which as of January stood at MXN$10.8tn (as measured by the HBPSBRs).

We expect banking credit to grow 1.7% y/y. It is our take that credit to the non-financial sector kept expanding in the second month of the year. We estimate a 1.7% yoy expansion in real terms, slightly lower than the 1.9% growth observed in January. This would be driven by a 1.3% increase in consumer credit, coupled with a 6.7% and 0.8% expansion in mortgages and corporates, in the same order. The deceleration in annual terms would be mainly driven by an uptick in inflation as it stood at 3.70%, 46bps above the previous month's print.

Weekly international reserves report. Last week, net international reserves decreased by US$445 million, closing at US$184.2 billion. According to Banxico's report, this was mainly due to a negative valuation effect in institutional assets. In this context, the central bank's international reserves have increased by US$3.3 billion during 2020 (please refer to the following table).

Banxico's foreign reserve accumulation details
US$, million

	2019	Mar 20, 2020	Mar 20, 2020	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	180,877	184,174	-445	3,297
(B) Gross international reserve	183,028	188,939	185	5,912
Pemex	--	--	757	2,225
Federal government	--	--	-58	1,918
Market operations	--	--	0	0
Other	--	--	-515	1,769
(C) Short-term government's liabilities	2,151	4,765	629	2,614

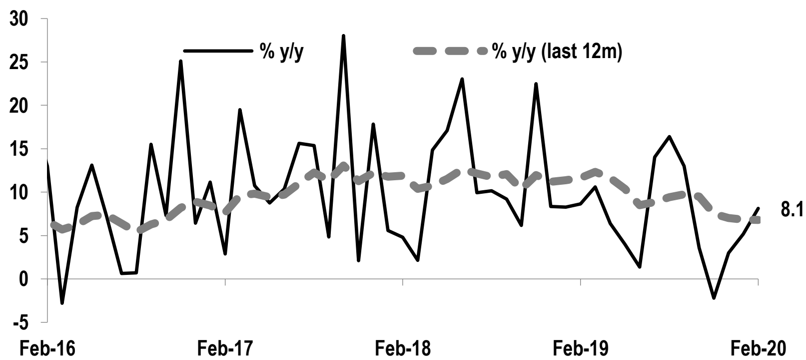
Source: Banco de México

Strong remittances in February. We expect remittances at US$2,636.1 million, up 8.1% y/y, which would be its largest since September. Similar to January, the period is typically skewed to the downside due to a seasonal effect at the start of the year. If this materializes, it would be highly positive as employment conditions in the US for Mexican migrants kept worsening. Specifically, employment for non-native migrants 'with citizenship' and 'without citizenship' exhibit growth at multi-year lows. On the contrary 'natives' improved. However, it is our take that the latter group is less likely to send remittances, as they are more established in the US.

News about migration in the period were relatively muted, leading us to believe that they might not have had a relevant impact. Going to other variables, the Mexican peso depreciated slightly, averaging USD/MXN 18.84 (previous: 18.80). The path was of a slight appreciation in the first half of the month, climbing steeply in the latter part. In this sense, we believe the impact could be positive, albeit marginally.

Going forward, we expect a sizable downward shock to remittances due to COVID-19. We believe Mexican workers might be more highly exposed to lay-offs or work suspension without pay, which on top of the health crisis, will surely impact their economic well-being. This could exacerbate as a result of travel restrictions at the Northern Border, which will be temporary in place and at least from March 21st to April 20th. Despite of them, the US Embassy in Mexico provided guidelines that only "essential travel" will be allowed, which includes workers crossing the border (*e.g.* in the agricultural sector). Under these conditions, we believe it is likely that they could increase their propensity to save, thus reducing the amount sent over to their families.

Family remittances
% y/y



Source: Banxico

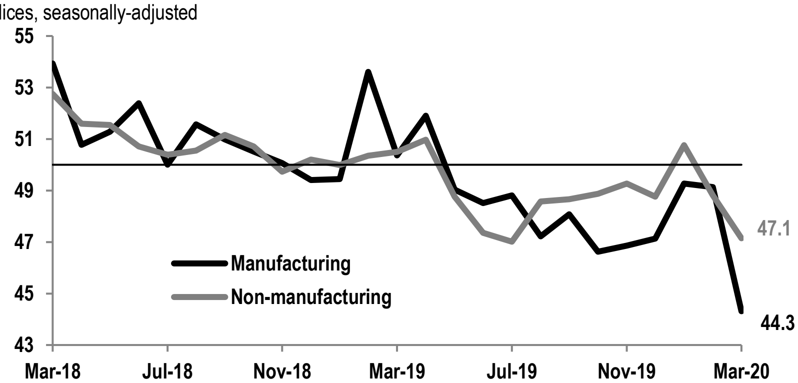
Banxico's survey of economic expectations. As usual, market participants will focus on inflation, growth, reference rate, and exchange rate forecasts. Regarding the first, analysts expect 2020 year-end inflation at 3.53%, below our 3.6% estimate. Medium and long-term expectations could remain unchanged, still above target. On growth, the estimate for this year is at 0.9%, However, given recent shocks we will likely see sizable revisions to the downside, closer to our -3.5% forecast. The current view on the reference rate by YE20 is 6.50%, which we also expect to be cut meaningfully on current conditions (Banorte: 5.50%). Finally, the exchange rate for year-end 2020 stands at USD/MXN 19.50, also in line for get major upward revisions (Banorte: 22.00).

IMEF indicators to fall strongly in March. We estimate important retracements on the back of a very challenging global backdrop, with basically all regions' outlook darkening on disruptions and restrictions imposed to fight COVID-19. In our view, Mexico will also be affected strongly, despite domestic activity not changing radically most of the period. We believe manufacturing will be most impacted, anticipating a decline to 44.3pts from 49.1pts.

US indicators available suggest supply-chain disruptions have built-up quite rapidly as a result of the pandemic, with Markit's PMI falling to a new low since 2009 of 49.2pts from 50.7pts in February. The indicator was buoyed to some extent by longer supplier delivery times –which typically signal stronger demand–, albeit not the case now as the indicator showed steep contractions in production and new orders. We also take as significant that new export orders declined heavily, with the report stating that key partners shut down operations or limited the size of their orders. This could also have at least something to do with the steep depreciation of the Mexican peso, which affects both indicators. In this respect, on a month-to-date basis the currency has depreciated around 16%, worse than in the height of the 2008 Financial Crisis in October, when it lost 14.7%. The only weaker period in the recent record is December 1994, when the currency plunged 32.2% as the crawling-peg FX regime was abandoned. In our view, the effect in manufacturing will be faster, with global supply chains more interconnected and just-in-time logistics more widespread than before.

Going to the non-manufacturing sector, we anticipate a decrease to 47.1pts from 48.8pts. Although some limitations to public activity have been announced, these have not been as stringent as in other regions. Mexico has still not officially restricted travelling from other countries, schools were officially closed only since the beginning of this week, and the "Phase 2" of the pandemic was activated on March 24th. Nevertheless, mobility in the domestic market has decelerated meaningfully. In this respect, we believe the A(H1N1) pandemic in April 2009 provides relevant information about possible short-term dynamics. In that occasion, the indicator fell until May, when restrictions to public life were more heavily imposed. On the other hand, the economy's weakness since last year suggests the risk of a stronger impact is relatively high, so we adjust our estimates accordingly. Moreover, the unemployment rate in February stood at 3.69% (hovering near highs since 3Q16) and the annual pace of formal job creation is at multi-year lows. In our view, high uncertainty keeps affecting consumer behavior, which will only be exacerbated by the virus. On the contrary, real wages have been advancing, supported in part by minimum wage hikes outpacing inflation.

IMEF indices
Indices, seasonally-adjusted



Source: IMEF

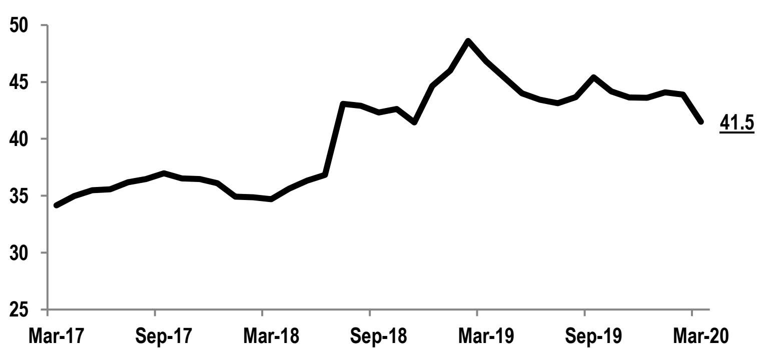
Consumer confidence to fall steeply in March on virus fears. We expect confidence at 41.5pts (seasonally-adjusted). We believe the fall will be mainly explained by the loss of optimism due to the COVID-19 outbreak, which has already started to show in some indicators, such as in the latest inflation and trade balance figures. We estimate the retracement to be generalized, given that there is both an impact at a national level, but also on a per-household basis.

In this context and in our view very relevant, the exchange rate depreciated strongly in the month, from around 18.80 per dollar at the end of the previous survey period (February 20th) to close to 24.40 last week. It should be noted that although this variable reflects to a great extent higher appetite for risk-haven assets by foreign investors, it is virtually a fact, in our view, that it will impact the perception about domestic economic conditions. To the latter we must add a further decrease in presidential approval, indicator that has been correlated to positively with consumer confidence levels. According to the daily poll from *El Economista/Consulta Mitofsky*, approval ratings reached a new low for this administration, hovering around the critical level of 50%.

Inflation in the 1st half of March stayed relatively high in the annual comparison at 3.71%. Nevertheless, there was a slight decrease in the energy and agricultural components. Moreover, we have identified a strong fall in low-grade gasoline in the second half of the month, which could somewhat help the purchasing power component) is that. In addition, the unemployment rate in February climbed marginally to 3.69%, which could also add some pressure to household components.

We believe confidence will keep declining, impacted not only by shocks such as lower economic activity and a higher FX rate. Very high uncertainty and social distancing are likely to affect households, with greater risk of facing health issues which our view will almost surely will deteriorate perceptions about the future in an important manner.

Consumer confidence
Index, sa



Source: INEGI

Analyst Certification

We, Gabriel Casillas Olvera, Alejandro Padilla Santana, Delia María Paredes Mier, Juan Carlos Alderete Macal, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Tania Abdul Massih Jacobo, Francisco José Flores Serrano, Katia Celina Goya Ostos, Santiago Leal Singer, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo, Jorge Antonio Izquierdo Lobato and Eridani Ruibal Ortega, 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.

Relevant statements.

In accordance with current laws and internal procedures manuals, analysts are allowed to hold long or short positions in shares or securities issued by companies that are listed on the Mexican Stock Exchange and may be the subject of this report; nonetheless, equity analysts have to adhere to certain rules that regulate their participation in the market in order to prevent, among other things, the use of private information for their benefit and to avoid conflicts of interest. Analysts shall refrain from investing and holding transactions with securities or derivative instruments directly or through an intermediary person, with Securities subject to research reports, from 30 calendar days prior to the issuance date of the report in question, and up to 10 calendar days after its distribution date.

Compensation of Analysts.

Analysts' compensation is based on activities and services that are aimed at benefiting the investment clients of Casa de Bolsa Banorte and its subsidiaries. Such compensation is determined based on the general profitability of the Brokerage House and the Financial Group and on the individual performance of each analyst. However, investors should note that analysts do not receive direct payment or compensation for any specific transaction in investment banking or in other business areas.

Last-twelve-month activities of the business areas.

Grupo Financiero Banorte S.A.B. de C.V., *through its business areas, provides services that include, among others, those corresponding to investment banking and corporate banking, to a large number of companies in Mexico and abroad. It may have provided, is providing or, in the future, will provide a service such as those mentioned to the companies or firms that are the subject of this report. Casa de Bolsa Banorte or its affiliates receive compensation from such corporations in consideration of the aforementioned services.*

Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1 % of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

Guide for investment recommendations.

	Reference
BUY	When the share expected performance is greater than the MEXBOL estimated performance.
HOLD	When the share expected performance is similar to the MEXBOL estimated performance.
SELL	When the share expected performance is lower than the MEXBOL estimated performance.

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V, since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

The information contained hereby has been obtained from sources that we consider to be reliable, but we make no representation as to its accuracy or completeness. The information, estimations and recommendations included in this document are valid as of the issue date, but are subject to modifications and changes without prior notice; Grupo Financiero Banorte S.A.B. of C.V. does not commit to communicate the changes and also to keep the content of this document updated. Grupo Financiero Banorte S.A.B. of C.V. takes no responsibility for any loss arising from the use of this report or its content. This document may not be photocopied, quoted, disclosed, used, or reproduced in whole or in part without prior written authorization from Grupo Financiero Banorte S.A.B. of C.V.

BANORTE

GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Gabriel Casillas Olvera	IRO and Chief Economist	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Economic Research and Financial Market Strategy			
Alejandro Padilla Santana	Executive Director of Economic Research and Financial Markets Strategy	alejandro.padilla@banorte.com	(55) 1103 - 4043
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Economic Research			
Juan Carlos Alderete Macal, CFA	Director of Economic Research	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Senior Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Senior Economist, Global		(55) 1670 - 1821
Luis Leopoldo López Salinas	Economist, Global	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
Fixed income and FX Strategy			
Santiago Leal Singer	Senior Strategist, Fixed Income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Senior Strategist, Equity	valentin.mendoza@banorte.com	(55) 1670 - 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Corporate Debt			
Tania Abdul Massih Jacobo	Director of Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Economic Studies			
Delia María Paredes Mier	Executive Director of Economic Studies	delia.paredes@banorte.com	(55) 5268 - 1694
Miguel Alejandro Calvo Domínguez	Senior Analyst, Economic Studies	miguel.calvo@banorte.com	(55) 1670 - 2220
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
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.ceballos@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 Corporate Banking	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 Commercial Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454