Ahead of the Curve

We expect a 11.8% q/q rebound in 3Q20 GDP on strong external demand and the economic reopening

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

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

- **Gross Domestic Product (3Q20 P).** We expect GDP to decline 8.8% y/y on efforts to reopen the economy, after the historical low of -18.7% in 2Q20. July's GDP proxy (IGAE) contracted 9.8% y/y, expecting improvements in August and September. Considering this and with seasonally adjusted figures, we expect GDP to climb 11.8% q/q. By sectors, industry would show a 9.1% y/y contraction (+21.6% q/q), while services could stand at -8.7% y/y (+8.7% q/q). The result would corroborate the beginning of the recovery after the steep contraction because of the strict lockdown –mainly in April and May–. Moreover, we expect this to extend through 4Q20 –albeit at a slower pace, partially due to a base effect–, resulting in a contraction of 9.0% y/y in full-year 2020

- **Trade balance (September).** We expect a high surplus again**,** estimated at US$5,565.0 million, with total exports at -6.3% y/y and imports at -21.6%. In oil, we estimate a US$1,242.2 million deficit, widening despite due to a higher impact of lower prices in shipments abroad relative to its effect on imports. The non-oil balance is expected with a US$6,807.2 million surplus, a new historical high. As in recent months, the contraction over a year ago in exports would be of a much smaller magnitude than in imports. The latter category would remain affected by weakness in domestic demand, along scattered reports of disruptions on increased scrutiny by customs in our country, impacting all sectors

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Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Sun 25-Oct		Daylight savings time ends in Mexico					
Mon 26-Oct	8:00am	Global economic indicator	August	% y/y	-8.7	-8.1	-9.8
		sa		% m/m	1.7	1.9	5.7
		Primary activities		% y/y	3.5	--	11.0
		Industrial production		% y/y	-9.0	--	-11.4
		Services		% y/y	-9.6	--	-10.1
Tue 27-Oct	8:00am	Trade balance	September	US$ mn	5,565.0	3,199.0	6,115.7
		Exports		% y/y	-6.3	--	-7.7
		Imports		% y/y	-21.6	--	-22.2
Tue 27-Oct	11:00am	International reserves	Oct-23	US$ bn	--	--	194.0
Wed 28-Oct	12:00pm	Pemex Quarterly Financial Report 3Q20					
Fri 30-Oct	8:00am	GDP	3Q20 (P)	% y/y	-8.8	-8.9	-18.7
		sa		% q/q	11.8	12.0	-17.1
		Primary activities		% y/y	4.5	--	-0.5
		Industrial production		% y/y	-9.1	--	-25.7
		Services		% y/y	-8.7	--	-16.2
Fri 30-Oct	11:00am	Comercial banking credit	September	% y/y in real terms	-2.0	--	-1.4
		Consumption		% y/y in real terms	-9.8	--	-9.7
		Mortgages		% y/y in real terms	4.1	--	4.4
		Corporates		% y/y in real terms	-0.9	--	0.1
Fri 30-Oct	4:30pm	Budget balance (measured with the PSBR)	September	MXN bn	--	--	-487.9

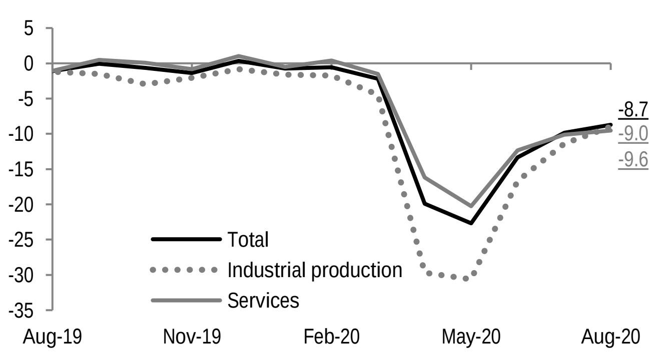
Source: Banorte; Bloomberg

Proceeding in chronological order…

August's IGAE to show that the rebound continued. We expect the *Global Economic Activity Indicator* (IGAE) at -8.7% y/y, stronger in annual terms for a fourth consecutive time. With seasonally adjusted figures, we estimate a sequential recovery of 1.7% m/m, decelerating relative to the 5.7% in July, consistent with signals of a moderation in the pace of the recovery. If we are right, activity would be around 5.7% lower than in February, before the pandemic hit. In contrast to recent months, there is evidence of an added boost from domestic demand, seemingly benefiting from additional reopening efforts and improving epidemiological conditions. On the latter, the traffic-light indicator showed that, by late July, 18 states were in 'red' and the remaining 14 in 'orange'. By the end of August only one was 'red', 21 in 'orange', and 10 in 'yellow'. As already known, industrial production came in at -9.0% y/y, stronger than expected. In monthly terms it rose 3.3%, mainly due to the 11.2% expansion in construction, albeit with all other sectors also positive. Manufacturing performance was somewhat disappointing, growing only 0.8% despite signals of continued dynamism from abroad.

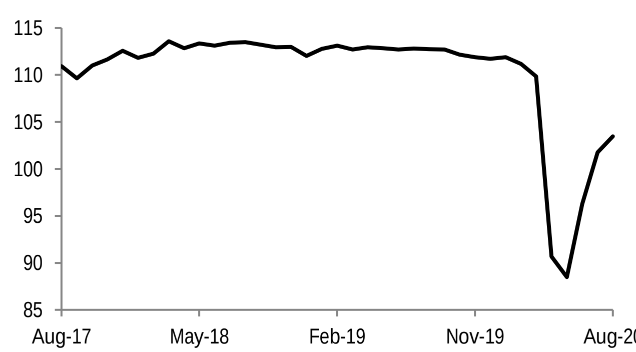
For services we expect -9.6% y/y, which with seasonally adjusted figures would translate to a 0.8% m/m expansion. Some signals were negative, such as IMEF's non-manufacturing indicator slightly declining, and employment losses of around 1.5 million jobs in the sector (both formal and informal). On the other hand, other indicators were more favorable. Among them, the aggregate trend indicator for non-financial services (excluding commerce) improved 1.7pts, with positive figures in three of four components. Moreover, retail sales edged-up 2.5% m/m, below expectations. Hotel occupancy rates were better by 3.8%-pts to 18.7%, even with historically adverse seasonality. Similarly, air passenger traffic for all airports stood at -61.5% y/y (previous: -71.5%). Consistent with epidemiological conditions, other businesses resumed activities. At least in Mexico City, these included cinemas, museums, and bars operating as restaurants, probably boosting performance in entertainment services. Pivoting to more essential sectors, we expect some resiliency in healthcare and education. The former would have been aided by improving conditions, drawing back patients that had postponed non-urgent procedures; the latter might have benefited at the margin from returning to school. Finally, we expect financial and professional services to be somewhat more stable after their recent volatility,

IGAE
% y/y (nsa)



Source: INEGI, Banorte

IGAE
Index (sa)



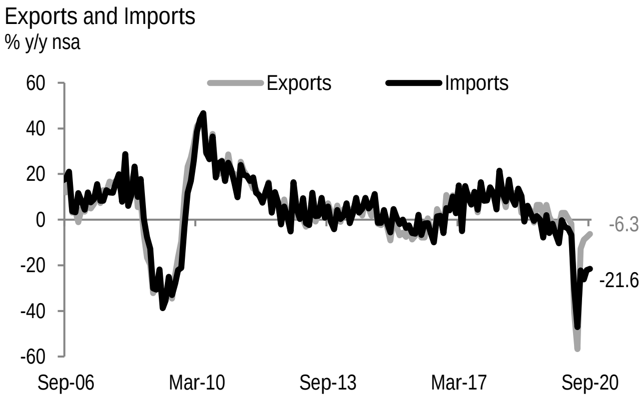
Source: INEGI, Banorte

Trade balance to maintain a wide surplus in September for a fourth month in a row. We estimate a US$5,565.0 million surplus, lower than the historical high of +US$6,115.7 million in August, but still very high. Total trade (exports + imports) would continue recovering, albeit at a slower pace. The latter would come in at US$64.1 billion, 13.9% lower than in the same period of 2019. Total exports would come at -6.3% y/y, while imports would stand at -21.6%.

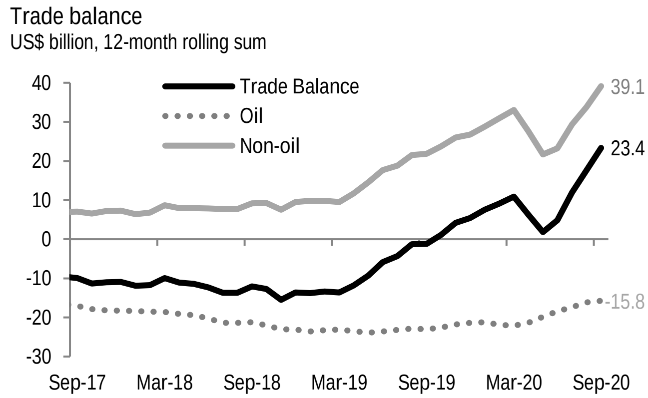
In oil, we estimate a US$1,242.2 million deficit, widening despite a decline in volumes, at levels closer to those seen before the pandemic. On exports, we anticipate a 29.7% y/y drop, decelerating relative to August. Specifically, the price of the Mexican oil mix averaged 37.56 US$/bbl, worse both sequentially (from 40.31 in the previous month) as well as in the annual comparison (-35.5% from -19.7%). This is mainly due to the lack of any significant meteorological phenomena in the period, considering that in August these had an impact as Hurricane Laura passed over the US. Data points to a marginal improvement in volumes, but not enough to compensate for the effect on prices. On imports, we anticipate a 26.7% contraction, also impacted by prices, albeit at a much lesser extent, along signals of an additional moderation in volumes. Specifically, consumption goods would come in at -20.4%, with some stagnation in mobility indicators, while intermediate goods could stand at -29.9%.

The non-oil balance is estimated at a US$6,807.2 million surplus, a new historical high. We expect exports at -5.0% y/y but imports at -21.0%. In the former, agricultural goods could improve marginally to -3.2%, while non-oil mining should remain strong (+38.0%). Within manufacturing, while signals from autos are somewhat mixed and even to the downside, we expect favorable base effect, forecasting a 9.5% contraction. AMIA figures showed a 13.1% y/y decline in exports, worsening relative to the previous month. Nevertheless, the auto sector within US IP rose to 3.6% from 2.3%. On other manufacturing, we anticipate a 3.4% fall, also benefited by a base effect and with other signals of resiliency, mainly in the 'imports' component within the US ISM index (which correspond to our exports).

On imports, there are scattered reports of disruptions on increased scrutiny by customs in our country, impacting all sectors. Despite this, we expect intermediate goods to continue outperforming at -19.3%, also aided by the need to use them on the production process. Consumption goods would remain subdued at -38.5%, still dragged by weakness in domestic demand. Finally, capital goods would come in at -14.4%, marginally better than the previous month due to an extension of MXN strength in the first half of the period, but still very weak, with uncertainty still a key driver for this category.



Source: INEGI, Banorte



Source: INEGI, Banorte

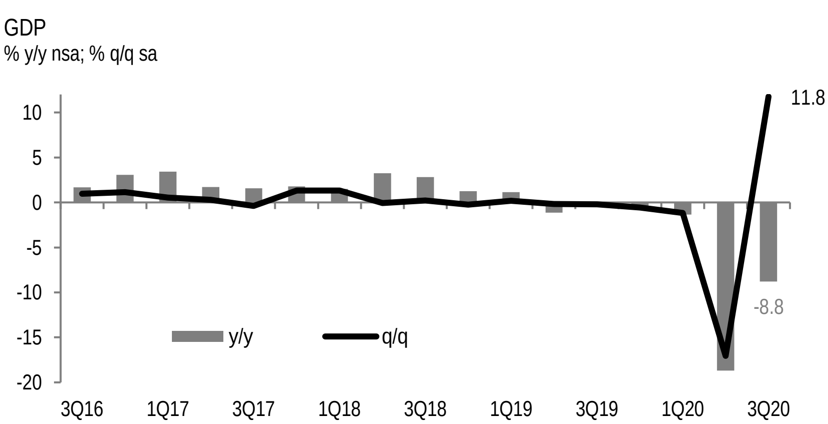
Weekly international reserves report. Last week, net international reserves increased by US$3 million, closing at US$194.0 billion. According to Banxico's report, this was mainly explained by a positive valuation effect in institutional assets. The central bank's international reserves have expanded by US$13.2 billion so far in 2020 (please refer to the following table).

Banxico's foreign reserve accumulation details
US$, million

	2019	Oct 16, 2020	Oct 16, 2020	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	180,877	194,029	3	13,152
(B) Gross international reserve	183,028	200,054	374	17,026
Pemex	--	--	50	4,749
Federal government	--	--	582	7,040
Market operations	--	--	0	0
Other	--	--	-258	5,237
(C) Short-term government's liabilities	2,151	6,025	370	3,874

Source: Banco de México

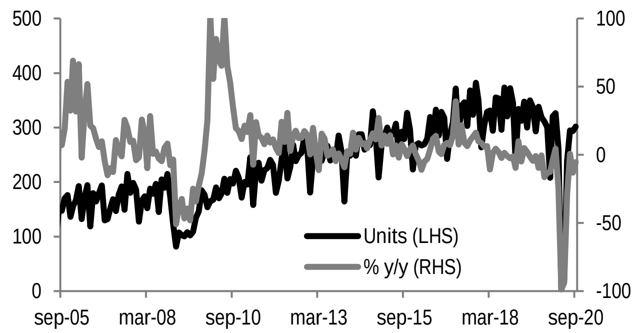
Sequential recovery in 3Q20 GDP as the economy started recovering from the lockdown. We expect GDP to decline 8.8% y/y, improving relative to the historical low of -18.7% in 2Q20 (see chart below), driven by efforts to reopen the economy. July's GDP proxy (IGAE) contracted 9.8% y/y, expecting additional improvements in August (see section above) and September. Considering this and using seasonally adjusted figures, we expect GDP to climb 11.8% q/q, slightly stronger than in our most recent update.



Source: INEGI, Banorte

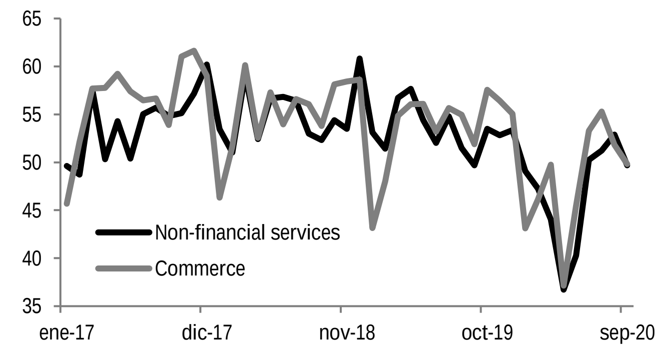
For industry, September's key drivers suggest an additional uptick, probably slower relative to the +3.3% m/m in the previous month. For manufacturing, IMEF's PMI climbed 1.0pt to 46.4pts, with strength in 'production'. Autos were better at -5.5% y/y (previous: -13.2%), with 301,426 total units (see chart below, left). US manufacturing was broadly stable, with no signs yet of a sizable impact from the expiration of several provisions within the CARES act that helped the economy. Considering this, and despite signs of a steeper slowdown in August, we expect some renewed strength in this sector. Turning to mining, we did not identify a relevant impact from hurricanes during the month –which was reflected also on prices (see section above)–, thus expecting a marginal improvement. Meanwhile the non-oil sector would maintain its upward trajectory, possibly turning positive in the annual comparison. For construction, and after a sizable positive surprise in August, we see an additional pick-up as pointed out by both business confidence and the aggregate trend indicator. Another tailwind would have been the announcement of Mexico City's government allowing for works to be carried out one additional day, as it had been limited to five days a week since they were designated as essential. This would be favorable, considering prevailing uncertainty and late signals of a slowdown in government spending in physical investment. Taking all this into account, we expect a 9.1% y/y contraction (+21.6% q/q) in the period.

Auto production
Thousand units, % y/y



Source: INEGI; AMIA

Aggregate trend indicators
Index



Source: INEGI

In services we anticipate an 8.7% y/y contraction (+8.7% q/q). In particular, the overall trend has been more positive than we originally anticipated, aided by a faster recovery in mobility. However, and consistent with broader signals of a more modest rebound, figures from both *Apple* and *Google* suggest some stagnation in September, still below pre-pandemic levels. In addition, aggregate trend indicators for both commerce and non-financial services backtracked some gains (chart below, right), consistent with the latter. Despite of this, most other signals continue to be favorable, starting with IMEF's non-manufacturing PMI, up 2.6pts to 49.3pts, closer to the expansion threshold. On a sector basis, tourism- and entertainment-related indicators improved further, with air passenger traffic in privately operated airports at -43.6% y/y (previous: -56.8%) and hotel occupancy rates in the first week of September at 20.8% (vs. the 18.7% average through August). Some leisure and entertainment services continued to open, probably boosting activity in this sub sector.

On retail, ANTAD's same-store sales ticked-up 2.6%-pts to -4.1% y/y in real terms, highlighting additional strength within departmental stores, albeit with supermarkets slightly slowing down, suggesting some normalization. On the contrary, auto sales stayed weak at -22.8%. Finally, and similar to our view for August, we believe healthcare, education and financial services will remain resilient, especially as their downturn during the lockdown was very modest and, in some cases, negligible.

In a relevant side note, INEGI released during the week a brand-new *nowcasting* indicator to approximate economic activity in a timelier fashion. Using estimates for August and September, July's IGAE, along other assumptions, we calculated that these forecasts would be consistent with a GDP decline of around -8.5% y/y. This is slightly stronger than our -8.8% estimate, mainly as we see a less vigorous rebound in services. Despite of this, the result would corroborate the beginning of the recovery after the steep contraction seen in the lockdown period –mainly April and May–. We expect this to extend through 4Q20 –albeit at a slower pace, partially due to a base effect–, resulting in a contraction of 9.0% y/y in full-year 2020.

Banking credit to remain negative in September, with weakness in consumer and business loans. We expect a 2.0% y/y contraction in real terms, below the -1.4% in August. Performance would be mostly explained by the 9.8% decline in consumer credit, but also by the 0.9% downfall in corporates. The first has been highly impacted by the deterioration in fundamentals, mainly employment, but also from relevant changes in consumption patterns. Meanwhile, in the latter, the trend has been downwards after strong increases during the lockdown months, suggesting that businesses' liquidity needs might already be covered or that the outlook is still somewhat negative. Finally, we expect mortgages more stable at +4.1%, benefited by the specific characteristics of this type of loans. Unlike previous months, the effect from inflation would be marginal, given that it stood at 4.01% y/y in September, 3bps below the previous month's print.

MoF's public finance report (September). Attention will center on the Public Balance and Public Sector Borrowing Requirements (PSBR) –with the latter at -$487.9 billion in August– to compare them with updated forecasts in the *2021 Budget Proposal*. We will also look to revenues and spending, particularly the annual comparison. The former could offer additional insights on activity, while the latter will give further light on spending in key sectors, considering austerity efforts coupled with higher spending to combat COVID-19 and its economic effects. We will also analyze public debt, which as of August stood at MXN$12.0tn (as measured by the Historical Balance of the PSBR). Finally, we will also look at the expanded report as these are quarterly figures, which might include updates to macroeconomic forecasts, as well as the analysts' call that will probably take place until Tuesday, November 3rd.

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, Eridani Ruibal Ortega and Juan Barbier Arizmendi, 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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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.

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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	katia.goya@banorte.com	(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
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Juan Barbier Arizmendi, CFA	Analyst	juan.barbier@banorte.com	(55) 1670 - 1746
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 Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5268 - 9996
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Frigolet Vázquez Vela	Head of Sólida Banorte	alejandro.frigolet.vazquezvela@banorte.com	(55) 5268 - 1656
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Carlos Alberto Arciniega Navarro	Head of Treasury Services	carlos.arciniega@banorte.com	(81) 1103 - 4091
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
Lizza Velarde Torres	Executive Director of Wholesale Banking	lizza.velarde@banorte.com	(55) 4433 - 4676
Osvaldo Brondo Menchaca	Head of Specialized Banking Services	osvaldo.brondo@banorte.com	(55) 5004 - 1423
Raúl Alejandro Arauzo Romero	Head of Transactional Banking	alejandro.arauzo@banorte.com	(55) 5261 - 4910
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