Ahead of the Curve

December 18, 2020

Attention in coming weeks on October's GDP-proxy, December's inflation and Banxico minutes

- **Economic activity indicator (October).** We expect IGAE at -5.6% y/y, a tick below the -5.5% of the previous month. This would be mainly explained by a negative calendar effect, with one less working day in the annual comparison (vs. +1 in September). In this sense, sequential figures would show a 1.4% m/m expansion, adding five months in positive territory. Relative to INEGI's forecasts within the *Timely Indicator of Economic Activity*, we are a tad bit more positive, expecting a 5.1% y/y sa decline vs. their -5.4%. As already known, industrial production came in at -3.3% y/y (nsa), much stronger than expected, which implies a 2.0% m/m increase. For services we expect a 6.7% y/y (nsa) contraction, which with seasonally adjusted figures would translate to a 1.0% m/m expansion.

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This is the last publication of the year. We will resume on January 15th. Happy Holidays!

Winners of the award for best economic forecasters for Mexico in 2019, granted by *Refinitiv*

STARMINE AWARDS FOR REUTERS POLLS FROM REFINITIV

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Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 21-Dec	7:00am	Retail sales	October	% y/y	-6.5	--	-7.1
		sa		% m/m	-0.9	--	2.7
Mon 21-Dec		*Citibanamex* survey of expectations					
Tue 22-Dec	10:00am	International reserves	Dec-18	US$ bn	--	--	195.3
Wed 23-Dec	7:00am	CPI inflation	1Q Dec	% 2w/2w	0.30	0.35	-0.10
				% y/y	3.18	3.28	3.23
		Core		% 2w/2w	0.42	0.45	-0.02
				% y/y	3.70	--	3.64
Wed 23-Dec	7:00am	Economic activity indicator	October	% y/y	-5.6	-5.0	-5.5
		sa		% m/m	1.4	1.5	1.0
		Primary activities		% y/y	-10.5	--	6.3
		Industrial production		% y/y	-3.3	--	-6.1
		Services		% y/y	-6.7	--	-5.6
Thu 24-Dec	7:00am	Trade balance	November	US$ mn	5,394.7	4,085.0	-6,223.8
		Exports		% y/y	4.7	--	2.9
		Imports		% y/y	-7.8	--	-13.8
Thu 24-Dec	7:00am	Unemployment rate	November	%	4.42	4.44	4.70
Tue 29-Dec	10:00am	International reserves	Dec-25	US$ bn	--	--	--
Wed 30-Dec	4:00pm	Budget balance	November	MXN bn	--	--	-556.1
Thu 31-Dec	10:00am	Comercial banking credit	November	% y/y	-2.1	--	-2.5
		Consumption		% y/y	-9.3	--	-10.9
		Mortgage		% y/y	4.9	--	4.7
		Corporates		% y/y	-1.5	--	-1.2
Mon 4-Jan	10:00am	Family remmittances	November	US$ mn	3,229.1	--	3,598.3
Mon 4-Jan	1:00pm	PMI's survey (IMEF)	December				
		Manufacturing		index	48.9	--	48.5
		Non-manufactruing		index	48.7	--	49.5
Tue 5-Jan	10:00am	International reserves	Dec-31	US$ bn	--	--	--
Thu 7-Jan	7:00am	CPI inflation	December	% m/m	0.35	--	0.08
				% y/y	3.12	--	3.33
		Core		% m/m	0.47	--	-0.08
				% y/y	3.72	--	3.66
Thu 7-Jan	10:00am	Banxico's minutes	Dec-17				
Fri 8-Jan	7:00am	Consumer confidence (sa)	December	index	35.9	--	36.7

Source: Banorte; Bloomberg

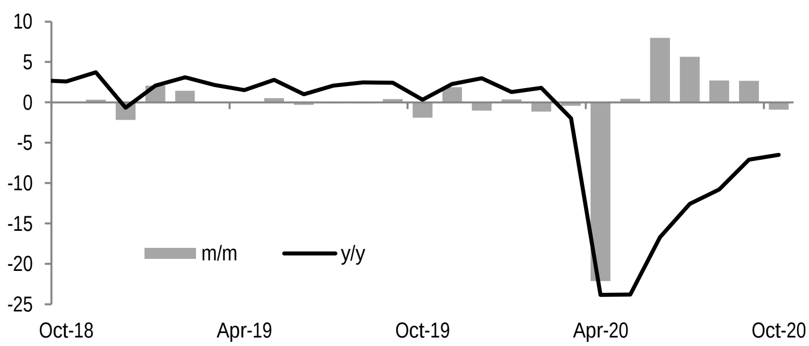
Proceeding in chronological order…

Retail sales to contract for the first time since the reopening in October. We anticipate a 6.5% y/y decline. With seasonally adjusted figures we see a 0.9% m/m contraction after five consecutive months on the upside. In our view, two main factors would explain this: (1) The stagnation of mobility indicators and worse epidemiological conditions by the end of the period; and (2) a likely delay in purchases in anticipation of discounts in November, mainly in durable goods. If we are right, sales would accumulate a 10.1% y/y reduction in the first ten months of the year.

Available indicators have been mixed. On the positive side, ANTAD's total sales grew 1.4% y/y in real terms, above the -1.4% of the previous month. Supermarkets and specialized stores strengthened, while departmental stores fell 4.8%. In our view, the latter supports the possibility of an impact from the second driver mentioned above. Remittances kept growing at a brisk pace. On the contrary, auto sales declined 21.3% y/y (previous: -22.8%), suggesting that weakness persists in durable goods. In addition, imports of non-oil consumption goods were also weaker at -31.0% y/y (-2.7% m/m). Inflation reached a maximum since May 2019 at 4.0% y/y, impacted by higher agricultural goods' prices, among others.

Going forward, we will focus on November's results because of *El Buen Fin*. Total sales by ANTAD members in the period picked up 1.8% y/y in real terms, accelerating only modestly at the margin. Nevertheless, departmental stores surged 5.1% from -3.5% in October. The latter is much better, although with figures skewed to the upside as discounts were available from November 9th to 20th, with some stores even extending them until the 22nd. Given the deterioration of economic conditions and the winter, the holiday shopping season will be key to assess accumulated results with December (and the whole quarter) to have a stronger and more trustworthy signal of the degree of recovery of domestic demand heading into 2021.

Retail sales
% y/y nsa, % m/m sa



Source: INEGI, Banorte

Weekly international reserves report. Last week, net international reserves increased by US$982 million, closing at US$195.3 billion. According to Banxico's report, this was explained by: (1) Dollar sales from the Federal Government to the central bank amounting to US$880 million; and (2) a positive valuation effect in institutional assets of US$102 million. The central bank's international reserves have expanded US$14.5 billion so far in 2020 (please refer to the following table).

Banxico's foreign reserve accumulation details
US$, million

	2019	Dec 11, 2020	Dec 11, 2020	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	180,877	195,341	982	14,463
(B) Gross international reserve	183,028	202,665	1,083	19,638
Pemex	--	--	0	5,149
Federal government	--	--	910	9,053
Market operations	--	--	0	0
Other	--	--	172	5,435
(C) Short-term government's liabilities	2,151	7,325	101	5,174

Source: Banco de México

Lower than average inflation again in 1H-December on lower pressures in fresh fruits, with some distortions at the core. We expect headline inflation at 0.30% 2w/2w, above the -0.10% of the previous fortnight. Nevertheless, this would still be low relative to recent years, with the 5-year average at 0.40%. The non-core component would explain a large part of the moderation, estimated at -0.07%, with core prices up 0.42%. If our forecast materializes, annual inflation would decline further, to 3.18% from 3.33% in November. Meanwhile, the non-core would plunge to 1.61% from 2.33%, lowest since May. Lastly, the core would edge-up to 3.70% from 3.64%, partly because of a slightly more adverse base effect.

Specifically, the non-core component would subtract 2bps. This decline would be driven by fresh fruits and vegetables, down 2.2% 2w/2w. Our monitoring showed a sizeable fall in tomatoes –after increasing slightly in the second half of November–, avocadoes, and onions, among others. On the contrary, meat and egg would extend its increase, up 0.9% and adding four fortnights to the upside. Inside, we expect both chicken and eggs to stay pressured, also impacted by a negative seasonality. Going to energy, we anticipate a 0.4% expansion, with all components rising, albeit modestly. We expect some pressures in gasolines, with low-grade up 0.3% and high-grade at 0.5%. Reference prices abroad showed a relevant upward adjustment while the MXN was just marginally stronger, in a context in which subsidies are still absent. Lastly, LP gas would rise again, at +0.9%, also driven by international prices.

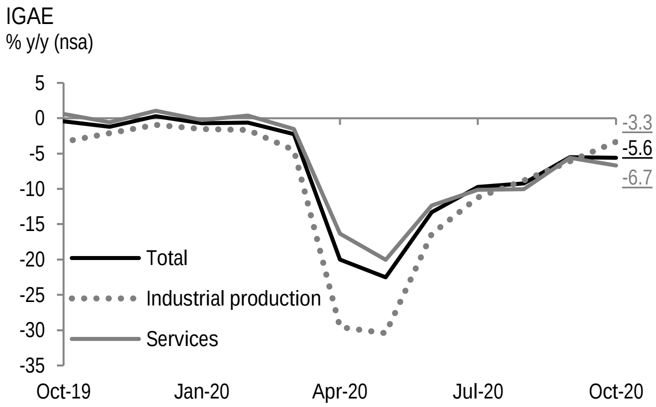
Meanwhile, the core component would add 32bps, with a mixed performance inside. Goods would rise significantly at 0.6%, with other goods bringing the bulk of the increase at 0.9%. This would be a result of the rebound after discounts from *El Buen Fin* and other programs which drove prices sharply down in November. Although an increase is typical, the magnitude is not, as the decline in the previous two fortnights has been the largest for the period since the series is available. Nevertheless, services would be much more modest relative to history, at 0.3%.

Contrasting with the seasonality, tourism related categories (*e.g.* airfares, hotels, and tourism services) would be rather modest, impacted by low demand due to the pandemic. Finally, and similar to previous fortnights, housing should remain relatively low, rising only 0.1%, still pushed down by wide slack.

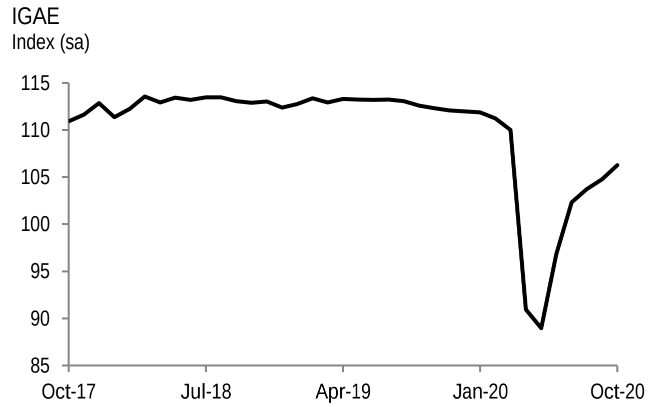
With this result, we expect inflation at +0.35% m/m for December, with the core at 0.47%. Regarding information that we can anticipate by now, we expect energy to continue trending higher, mainly due to an extension in reference prices, although with the exchange rate helping slightly to the downside. Meanwhile, we believe pressures at the core would be more moderate relative to the first fortnight, with goods taking on a similar trend relative to their historical average. Contrary to this, we do not expect significant declines in tourism-related categories, given that they would not rise as much at the start of the period. With this, headline inflation would close the year at 3.12%, below expectations and at its lowest since May. Meanwhile, the core component would stand at 3.72%, still maintaining some resistance to the downside.

October's IGAE to continue the upward trend. We expect the *Global Economic Activity Indicator* (IGAE) at -5.6% y/y, a tick below the -5.5% of the previous month. This would be mainly explained by a negative calendar effect, with one less working day in the annual comparison (vs. +1 in September). In this sense, sequential figures would show a 1.4% m/m expansion, adding five months in positive territory. Relative to INEGI's forecasts within the *Timely Indicator of Economic Activity*, we are a tad bit more positive, expecting a 5.1% y/y sa decline vs. their -5.4%.

As already known, industrial production came in at -3.3% y/y (nsa), much stronger than expected. In monthly terms it rose 2.0%, with a strong rebound in construction (+3.6%), albeit with all other sectors also positive. Manufacturing was resilient, growing 1.8% with a broad recovery, highlighting to the upside machinery and equipment and metallic goods. For services we expect a 6.7% y/y (nsa) contraction, which with seasonally adjusted figures would translate to a 1.0% m/m expansion. We should remember that epidemiological conditions started to deteriorate by the end of the period, albeit probably only with a modest effect on activity. In this context, hotel occupancy rates edged-up to 27.3%, higher than the previous 22.4%, driven by both a positive seasonal effect but also to higher dynamism. In a similar manner, air passenger traffic stood at -45.7% y/y (previous: -50.0%). On a more downbeat note, retail sales indicators were mixed, as outlined in the section above. However, total employment was better, with 1.9 million jobs created. Out of these, 1.6 million were in services, suggesting more dynamism. Pivoting to more essential sectors, we expect some resiliency in healthcare, with rising cases possibly supporting activity in this sector. Education will probably remain stable, with a similar performance expected in financial and professional services.



Source: INEGI, Banorte



Source: INEGI, Banorte

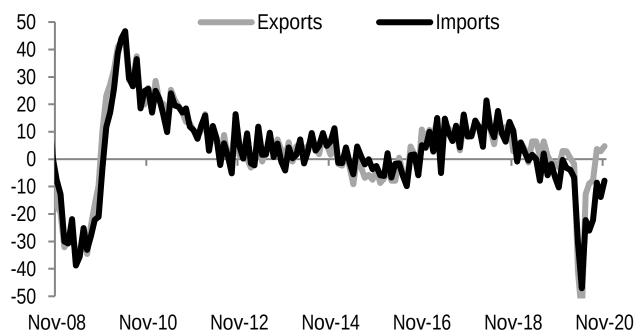
November's trade balance to stay in surplus despite a record high in the previous month. We estimate a US$5,394.7 million surplus, lower than the new historical high of +US$6,223.8 million in October, albeit still very high. Logistics issues continued, including in the Lázaro Cardenas port, due to railway blockades in Michoacán, in place for the full period. According to reports, the oil, steel and auto industries were among the most affected. Apart from these, issues have also been previously reported due to changes in Mexico's customs administration and new labeling regulations. We do not rule out that these factors are exacerbating weakness in imports relative to exports, with this month possibly shedding further light in this regard. We expect total exports and imports at 4.7% and -7.8%, in the same order.

In oil, we estimate a US$1,366.8 million deficit, slightly up from October. We see a recovery in volumes with the normalization of activities in the Gulf of Mexico after a very active hurricane season, with relevant impacts in the previous month. Moreover, prices recovered, particularly on crude oil exports, with the Mexican oil mix at 38.73 from 36.46 US$/bbl. Going to imports, US gasoline prices were also stronger at the margin, albeit more modestly. We anticipate shipments and purchases from abroad to have declined 22.1% and 21.5% y/y, respectively.

We expect the non-oil balance with a US$6,761.4 million surplus. We continue seeing a better performance in exports (6.1% y/y) than imports (-6.3%). In the former, we expect good results in every major component. Agricultural goods (10.8%) would recover after climate disruptions in the previous month, while non-oil mining (53.9%) would also be favorable despite surging in October, benefitted by the uptrend in commodity prices. In addition, we estimate manufacturing at 5.1% from 3.5% in the previous month. In autos, AMIA data and the sector's production in the US were still favorable, with the annual rate still partially distorted by a base effect because of last year's GM strike in the US. Other sectors would also be resilient, pulled by dynamism in said country, including food, electronics, and aerospace, among others. In imports, a positive signal came from Chinese exports to Mexico in October, accelerating after plunging in September (we consider a one-month lag more relevant due to transportation times). Consumption goods (-25.6%) are expected to improve at the margin, albeit mainly because of a base effect.

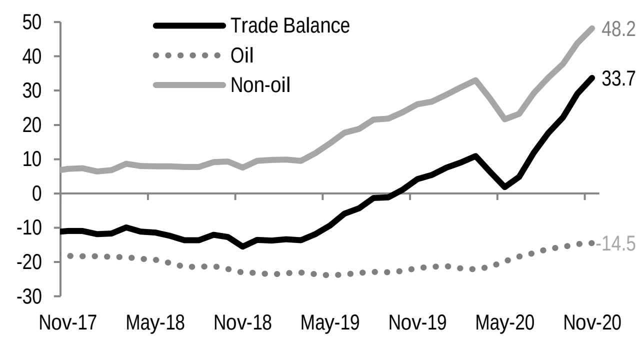
Capital goods should stay dampened at -15.6% y/y, only slightly higher than in the previous month as most business confidence sub-indexes about the 'adequate moment to invest' moved up and the peso strengthened after the US election. In intermediate goods, we expect a rebound to -2.1% from -7.8%, albeit mostly because of a more benign base effect, and still limited when compared to manufacturing exports. In this sense, we believe This component is likely to remain be significantly affected by the bottlenecks mentioned above.

Exports and Imports
% y/y nsa



Source: INEGI, Banorte

Trade balance
US$ billion, 12-month rolling sum

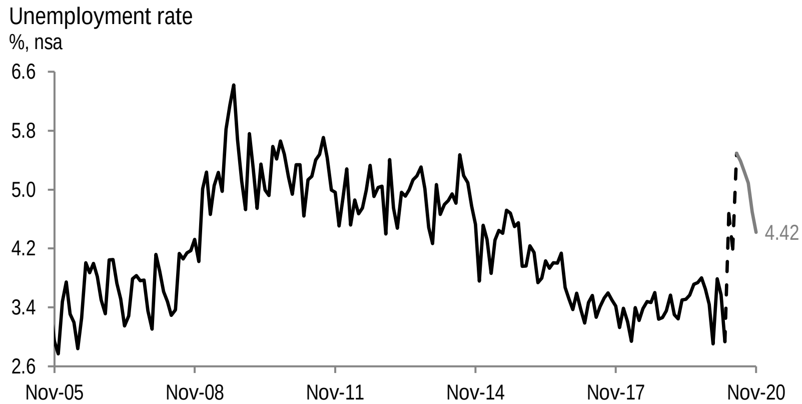


Source: INEGI, Banorte

We expect an additional decline in the unemployment rate in November. We estimate the unemployment rate at 4.42% (original figures), 28bps lower than the previous month's print. We should mention that once again there is a favorable seasonal effect that will skew the figure to the downside. Historically (since 2005), the average decline between October to November is 25bps, with only three out of fifteen years showing an increase. However, we expect a slightly better performance, driven by strength from the previous months along the accumulated economic recovery, with a marginal benefit from temporary jobs related to *El Buen Fin* (Mexico's Black Friday). This would happen despite the deterioration in epidemiological conditions since late October. In this context, IMSS's data showed a creation of 148.7 thousand new positions, moderating relative to the 200.6 thousand from the previous month, albeit consistent with its typical seasonality. Meanwhile, 'employment' components within IMEF's indices were mixed, with a decline in manufacturing and an increase in non-manufacturing, contrasting with signals from the previous month.

Regarding additional data within the report, it is likely that the part-time rate extends its decline, albeit probably with an additional moderation. Meanwhile, we expect the participation rate to extend higher, with most coming from the "available to work" share from those outside it. Finally, informality could keep climbing, continuing its path to normalization.

All in all, we believe that distortions around the pandemic and its economic impact will continue to cloud data. Nevertheless, we still consider that barred any major lockdowns, employment could continue to recover, albeit probably at a much slower pace. In this context we should remember that around 2.8 million jobs are left to be recovered relative to pre-pandemic levels, suggesting that it still could take some time to see a complete rebound. This in turn will probably also result in some additional weakness in domestic demand, dragging relative to the external component.



Source: INEGI, Banorte

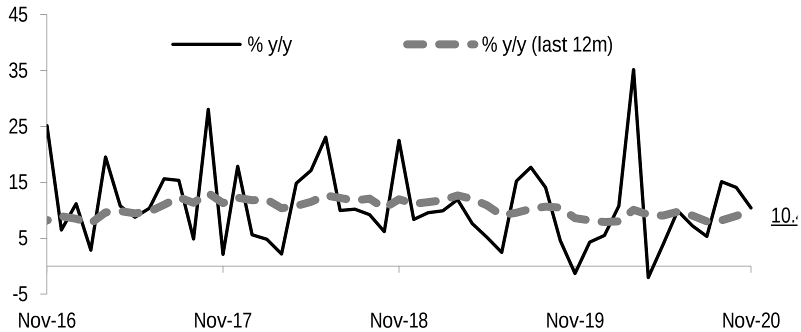
MoF's public finance report (November). Attention will center on the Public Balance and Public Sector Borrowing Requirements (PSBR) –the latter at -$556.1 billion in October– to compare them with updated forecasts in the last quarterly report. We will also look at revenues and spending, particularly 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. We will also analyze public debt, which as of October stood at MXN$12.0tn (as measured by the Historical Balance of the PSBR).

Banking credit to recover slightly in November, albeit remaining negative. We expect a 2.1% y/y contraction in real terms, slightly better than the -2.5% in October. Performance would be mostly explained by a rebound in consumer credit, to -9.3% from -10.9% in the previous month. This would be supported by *El Buen Fin* and other discounts and offers made in the period. So far, forward looking indicators have been positive regarding sales, which we believe will also translate to credit. Meanwhile, mortgages would remain on an upward trend (+4.9%), benefited by the characteristics of this type of loans. Lastly, corporate credit would extend its decline, coming in at -1.5%. In the month, the effect from inflation would help the figures, considering that it stood at 3.33%, 76bps lower than in October.

Remittances still strong in November. We expect remittances to increase 10.4% y/y to US$3,229.1 million, below the +14.1% seen in October albeit still favorable, with three consecutive months advancing at a double-digit pace. We highlight that the period's absolute amount is typically among the lowest in the year. In our view, this could be influenced by expenses due to Thanksgiving and the upcoming holiday season, with migrants also trying to take advantage of discount in Black Friday and Cyber Monday. Considering this, we expect inflows to maintain a strong performance despite the pandemic. Nevertheless, the labor market and economic activity in the US decelerated, mostly attributed to the second wave of COVID-19. In turn, this has resulted in new restrictions in several states, although not as strict relative to those between March and May.

Despite of the latter, employment conditions kept improving among Hispanics and Latinos in that country, but at a more modest pace. Specifically, the unemployment rate diminished to 8.4% from 8.8% in October. Working-age Mexican migrants increased by 140.9 thousand, reaching a total of almost 26.8 million. We observed both more employed people and less unemployed, with the highest gains among non-citizens. As mentioned before, we believe this is relevant as it this group is likely to send more resources back to their families given that they could have tighter links with them. For full-year 2020, we maintain our estimate that remittances could be close to US$40.4 billion.

Family remittances
% y/y

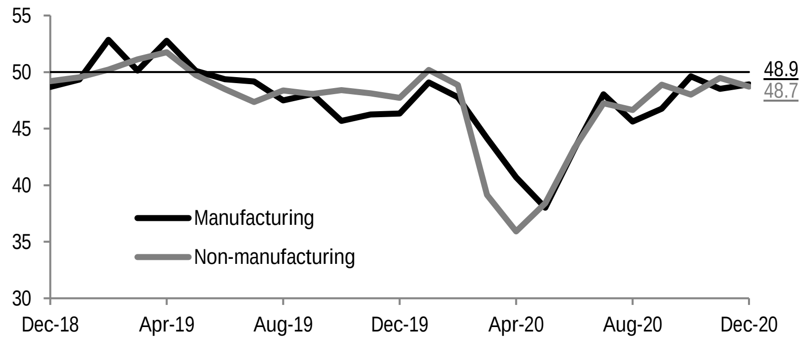


Source: Banxico

IMEF indicators to reverse some of their dynamics in December. We expect them to show a contrary performance relative to the previous month, with manufacturing edging-up, and non-manufacturing erasing some gains. We estimate manufacturing at 48.9pts (+0.4pts). There were some favorable developments locally, including lifted railway blockades in Michoacán at the end of November. Nevertheless, epidemiological conditions kept worsening, which might dampen optimism. Externally, *Markit's* manufacturing PMI in the US showed a slight retracement to 56.5pts, but still very strong. Within the report, new orders and production were positive, which bodes well for activity in our country. In addition, we do not rule out some renewed optimism due to the start of the deployment of the vaccine.

The non-manufacturing indicator would decline to 48.7pts, which implies a 0.8pts sequential contraction. This would be mainly explained by two factors: (1) A loss in optimism after *El Buen Fin* and other discounts in the month –mainly impacting commerce– as forward-looking indicators show performance was slightly positive in November; and (2) additional restrictions in the State and Mexico and Mexico City, among other states, limiting operating hours for non-essential businesses at the beginning of the month but with a lockdown once again being announced today for this two states. Nevertheless, and possibly acting as a counterweight, persistent job gains since the reopening, with signals up to November still suggesting that this trend continued.

IMEF indicators
Diffusion indicators, sa



Source: IMEF

Banxico's minutes to corroborate the need for a pause given available information. The central bank will release the monetary policy minutes of its decision held on December 17th, in which the reference rate was left at 4.25%. The decision was made by majority vote, with two dissenters supporting a 25bps cut. The tone is likely to be similar to the statement, which we saw as more dovish relative to previous communications.

We expect Deputy Governor Jonathan Heath to have voted again for a cut, this time joined by Deputy Governor Gerardo Esquivel. This is supported by our analysis of the latest minutes, in which we identified him as the most dovish member, after Heath. However, we will also be carefully looking at the views of the other three members, especially Governor Díaz de León and Deputy Governor Irene Espinosa, remembering this was last decision Javier Guzmán. Especially, will be looking for their take on inflation, both actual and expectations, as we think this will be the key factor about when to resume the easing cycle. On prices we will also analyze comments about the balance of risks, with special attention on the impact from *El Buen Fin* and its possible aftermath.

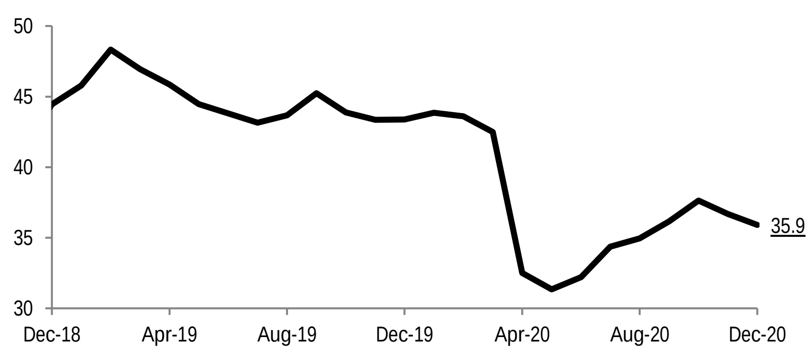
Within the document we noted a slightly more favorable opinion on the global outlook, with comments about the vaccine, additional fiscal stimulus in the US and reduced geopolitical uncertainty. We will be looking to the assessment about its positive impact on our country, as well as on expanded views on activity and risks for it, especially as COVID-19 cases have continued to rise. Finally, we will also watch comments on macro-financial risks, considering recent market performance, rating actions and measures by both the Federal Government and Pemex to improve the latter's financial situation.

All in all, we believe the document will support our view that the easing cycle will resume on February 11th with a 25bps cut, followed by two additional reductions of the same magnitude in back-to-back meetings. As a result, the rate would end 2021 at 3.50%. As mentioned previously, this would be supported by: (1) A more benign inflation outlook; (2) changes to Banxico's Board; (3) short-terms risks for growth; (4) a favorable scenario for financial flows; and (5) greater awareness of the central bank's independence and institutional framework.

Consumer confidence to extend lower in December. We expect confidence at 35.9pts (seasonally adjusted), weaker than the 36.7pts of the previous month and with a second month to the downside. Overall, we believe negative factors will outweigh positive developments in the month. If we are right, the indicator would remain around 7.7pts below its level in February, before the pandemic. The main driver behind the decrease would be the deterioration in the country's epidemiological conditions and its subsequent impact on activity. In this sense, this week, the State of Mexico and Mexico City determined that non-essential businesses should close by 5:00pm. This comes on top of previous restrictions implemented in both states since November 23rd, where hours of service had already been limited. Moreover, today's announcement that both states are now 'red' according to the epidemiological traffic-light indicator. This could have a more relevant impact on current conditions, both for households and the country. Nevertheless, so far mobility indicators have showed a slight recovery relative to November's deceleration, which could partially compensate for this effect.

Meanwhile, the publication of the National Vaccination Plan, as well as the start of the inoculation process might support expectations. The exchange rate has been broadly stable, with a recovery in the last few days, which could also boost sentiment. Nevertheless, available surveys about the Presidential approval so far this month have shown a slight downtick. This could weigh on country's expectations. On purchasing power, we could see a more modest deterioration, similar to the previous month. In this sense, and as detailed in the section on inflation, we expect an additional decline in fruits and vegetables, which should help at the margin. However, energy rose slightly, which could fuel the decline. In this context, we believe the recovery of confidence towards levels seen before the pandemic could take a while. The deployment of the vaccine could be a key factor, without also ruling out possible distortions given next year's elections.

Consumer confidence
Pts, seasonally adjusted



Source: Banorte with data from 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, 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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	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.

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