4Q20 GDP – Activity fell 8.3% in the year, on the unprecedented impact of the pandemic

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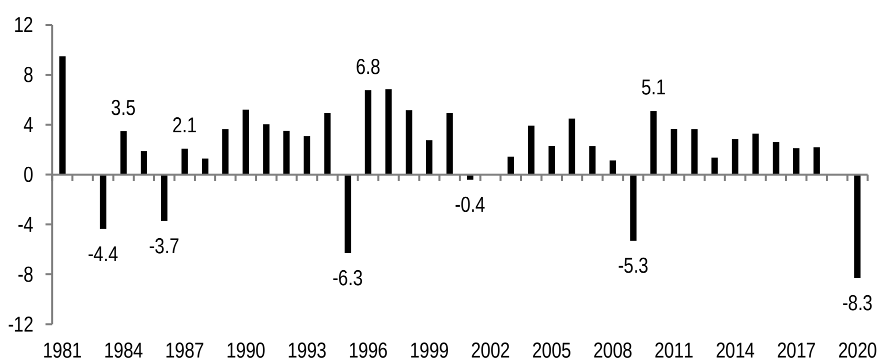
- **Gross Domestic Product (4Q20 P, nsa): -4.5% y/y; Banorte: -5.6%; consensus: -5.2% (range of estimates: -7.6% to -5.0%); previous: -8.6%**
- **Gross Domestic Product (4Q20 P, sa): 3.1% q/q; Banorte: 2.1%; consensus: 3.1% (range of estimates: 2.1% to 3.5%); previous: 12.1%**
- **GDP in 2020 fell 8.3% y/y from -0.1% in 2019. Primary activities increased 2.0%, with industry backtracking 10.0% while services stood at -7.7%**
- **The recovery extended both in industry (+3.3% q/q) and services (+3.0%) continued in the quarter, remembering they remain below pre-pandemic levels. Primary activities showed some payback at -2.6%**
- **Considering that the monthly GDP-proxy (IGAE) fell 4.6% y/y on average in October-November, today's print would imply a contraction of around 3.2% y/y in December, higher than estimated by INEGI's Timely Indicator of Economic Activity**
- **We maintain our 2021 full-year GDP forecast of +4.1% y/y, with external demand strength and a gradual normalization in domestic activity later in the year driving the recovery**
- **Revised figures will be published on February 25th**

GDP falls 8.3% y/y in 2020. This compares to the -0.1% of the previous year and is the largest contraction within INEGI's official series (see chart below). This was mostly explained by the unprecedented shock to activity from the COVID-19 pandemic and the distortions that resulted from efforts to combat it. The largest impact was in April and May, with lockdowns bringing the economy to a halt significantly. Afterwards, we saw a gradual recovery, albeit with persistent weakness in socially-dependent sectors. In this backdrop, industry (-10.0%) and services (-7.7%) were the weakest, with agriculture (+2.0%) staying strong given its essential status. We should recall that there was a marginal boost from the leap-year, which added close to 0.2%-pts. The contraction with seasonally adjusted figures was -8.5% y/y (Table 1).

GDP
% y/y, nsa



Source: INEGI

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

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4Q20 GDP fell 4.5% y/y. This was better than our estimate (-5.6%) but closer to consensus (-5.2%). The period's dynamic was characterized by additional reactivation efforts at the start of the quarter, albeit with a deterioration in epidemiological conditions triggering lockdowns in some states towards the end. Activity was better than the -8.6% of the previous quarter (Chart 1). By sectors, primary activities remain the only ones in positive territory at 4.8%. Unlike 3Q20, industry (-3.3%) surpassed services (-5.1%), as seen in Chart 2. We believe this is related to: (1) Strength from external demand favorably driving manufacturing; (2) a positive base effect in the auto sector, remembering GM's strike last year; (3) the possibility of a faster adaptation of industry to distancing and sanitary measures; and (4) a significant lag in categories that rely on social interaction within services (*e.g.* lodging, entertainment, and transportation).

The sequential recovery continued. Using seasonally adjusted figures, GDP rose 3.1% q/q (Banorte: 2.1%; consensus: 3.1%), building up on the +12.1% of the previous period and adding two positive quarters (Chart 3). One part of the deceleration in the pace of the expansion is natural, driven by a more challenging base effect. Notwithstanding, it reflects a relevant improvement in activity. On the other hand, it is not enough to compensate for the accumulated decline in the five quarters ending in 2Q20. Hence, activity remains around 6.1% below its peak in 1Q19, which also corresponds to a historical high.

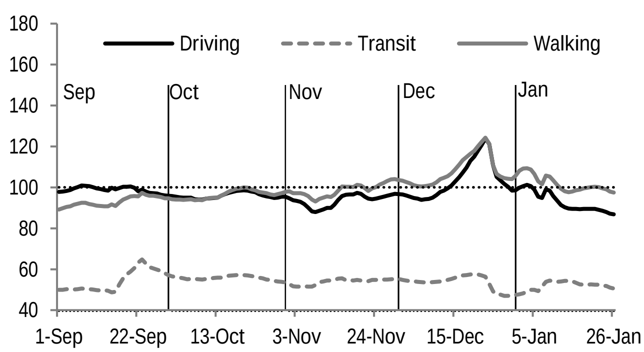
Industry was again the largest mover, at +3.3% q/q (Chart 4), managing to recover some steam and no longer the weakest sector relative to pre-pandemic levels. Using other indicators (as we do not have the breakdown in this release), construction was likely strongest, with manufacturing more modest albeit still relatively good. Mining was somewhat weaker, with a relevant impact from negative meteorological conditions. Services were at +3.0%. We believe that people's fatigue, a relative normalization of supply chains, and the downtrend of COVID-19 cases for most of the period followed by the reopening of several locations –including in the informal sector– helped initially. An additional boost was observed from the extended discount period of *El Buen Fin* (Mexico's Black Friday) in November. Nevertheless, as contagions increased the sector likely started to decelerate, finally impacted again from stricter lockdowns in December. Finally, primary activities declined 2.6% (Table 2), with some payback after the 8.0% expansion of the previous quarter.

The report suggests a sequential contraction in December. Considering that the monthly GDP-proxy (IGAE) averaged -4.6% y/y in October-November, today's estimate implies December at around -3.2% y/y. This month was benefited by a calendar effect, with two additional working days in the annual comparison. Correcting for this (using seasonally adjusted figures), activity would fall around 4.2% y/y. This is more optimistic relative to the -5.4% in INEGI's Timely Indicator of Economic Activity. In this respect, it looks positive when compared with IMEF's indicators and ANTAD sales. Nevertheless, the trade balance also pointed to a strong performance in both exports and imports, possibly exacerbating the divide between industry and services. Finally, mobility decreased marginally when adjusting for holiday-related spikes (24th and 31st). In sequential terms, the economy would have declined around 0.7% m/m, first fall since the recovery started in June.

We maintain our 4.1% y/y GDP forecast for 2021. Despite a more challenging base effect because of the performance in 2020, we reaffirm our call of a 4.1% y/y rebound this year (see Table 3 and Table 4). We believe risks for activity in the short-term have increased, with the possibility that lockdowns in the ten states currently in 'red' could extend further into 1Q21, also not ruling out more of them impose additional restrictions. On a more positive note, those currently in 'red' could relax these measures as the harsher days of winter passes by and the rate of contagion moderates. In addition, industry is seemingly not affected as much as we originally thought. There are structural factors favoring this (*e.g.* not much need for social interaction, some sectors catalogued as essential), but we still consider that most of the support comes from external demand, mainly by the US. This is clearly portrayed by *Markit*'s PMI indicators, particularly in manufacturing.

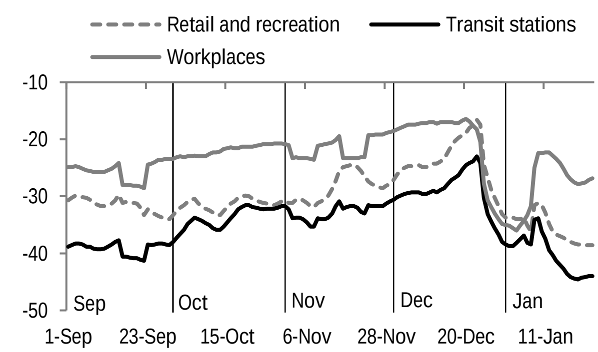
We still see with more concern the impact on services, much more susceptible to lockdowns, especially considering that: (1) Some of the most populated regions in our country are also among those more impacted; and (2) relief measures haven been very limited, which could result in a higher amount of definitive business closures. Mobility reports so far have shown a slight –but steady– downward trend in January, with detailed data from *Google* pointing to sharp declines in retail and recreation (chart below, right).

Apple Maps queries
Index 100 = Feb-13-2020, 7-day average



Source: Apple

Google mobility indicators
Percentage deviation to pre-pandemic levels, 7-day average



Source: Google

Despite of this, we still think several factors that will help activity along the year. Firstly, stimulus from abroad will be larger than originally forecasted, with the Biden administration in the US pushing for a US$1.9 billion package, with some other targeted actions also expected. This comes on top of accommodation efforts from the Federal Reserve which will extend into the foreseeable future. These, on top of significant advances in the vaccination process, will probably drive the US economy higher, thus having a positive spill-over on Mexico. The most benefitted would be manufacturing on supply and exports on the demand side. In turn, this could also have an indirect and positive effect in other sectors. Specifically, this could boost domestic demand, at least consumption. However, overall dynamism will remain limited in the short-term and will depend on the accumulated number of vaccinated people. In this context, another relevant factor will be the evolution of employment conditions, with some uncertainty about when we could see a full recovery of jobs, but likely taking more time.

On investment, signals are mixed, with the possibility of businesses implementing 'nearshoring' practices, on top of a potential benefit from tensions between the US and China. Nevertheless, other headwinds prevail, mainly related to idiosyncratic factors such as concerns about the rule of law, low productivity growth, and controversial law reforms, among others. In this sense, we believe that sector will remain as the weakest, requiring a sizable boost in confidence levels that depend on more factors other than the vaccination process.

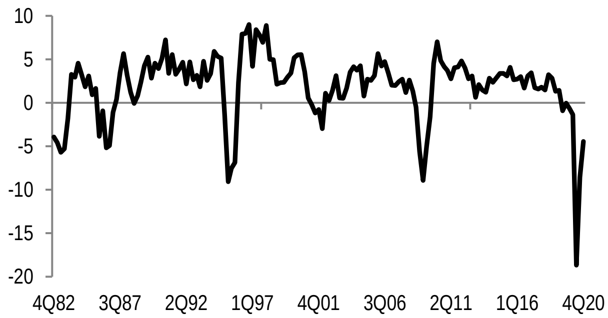
Considering the factors mentioned above and a more difficult base effect after today's print, we expect a more subdued pace of recovery in the first half of the year. Hence, we estimate a 0.3% q/q contraction in 1Q21. On the other hand, we still expect a more visible acceleration starting in 3Q21, with vaccinations and other reactivation efforts having a more sizable impact in a backdrop in which contagion rates are likely to be lower as we pass the winter months.

Table 1: GDP
% y/y nsa, % y/y sa

	nsa						sa					
	4Q20	3Q20	4Q19	4Q19	2020	2019	4Q20	3Q20	4Q19	3Q19	2020	2019
Total	-4.5	-8.6	-0.6	0.0	-8.3	-0.1	-4.6	-8.6	-0.7	-0.1	-8.5	0.0
Agricultural	4.8	7.7	-1.5	2.0	2.0	0.3	4.9	7.4	-1.7	1.8	2.0	0.5
Industrial Production	-3.3	-8.8	-2.2	-1.4	-10.0	-1.7	-3.4	-8.8	-2.0	-1.6	-10.2	-1.7
Services	-5.1	-8.8	0.1	0.6	-7.7	0.7	-5.3	-8.9	0.0	0.5	-7.9	0.7

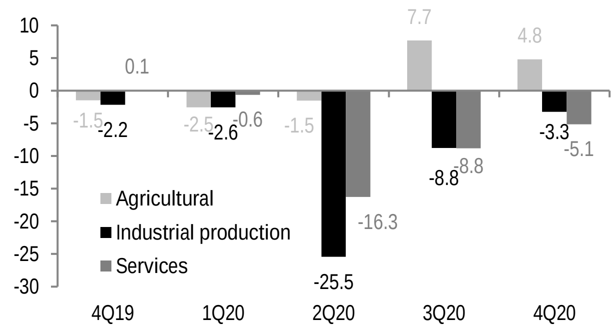
Source: INEGI

Chart 1: GDP
% y/y nsa



Source: INEGI

Chart 2: GDP by sectors
% y/y nsa



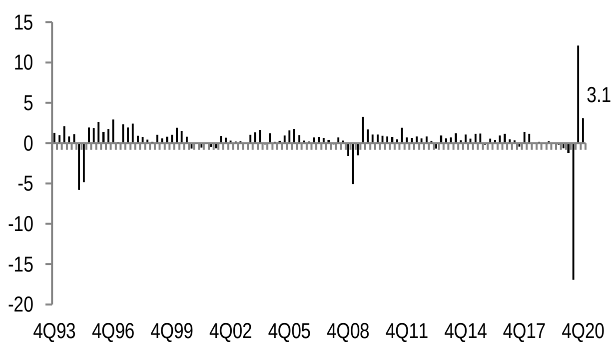
Source: INEGI

Table 2: GDP
% q/q sa, % q/q saar

	% q/q				% q/q saar			
	4Q20	3Q20	2Q20	1Q20	4Q20	3Q20	2Q20	1Q20
Total	3.1	12.1	-17.0	-1.2	12.9	58.0	-52.4	-4.9
Agricultural	-2.6	8.0	0.5	0.2	-10.1	35.8	1.9	0.8
Industrial Production	3.3	21.7	-23.3	-0.9	13.9	119.3	-65.5	-3.5
Services	3.0	8.8	-15.1	-1.0	12.6	39.9	-48.1	-3.8

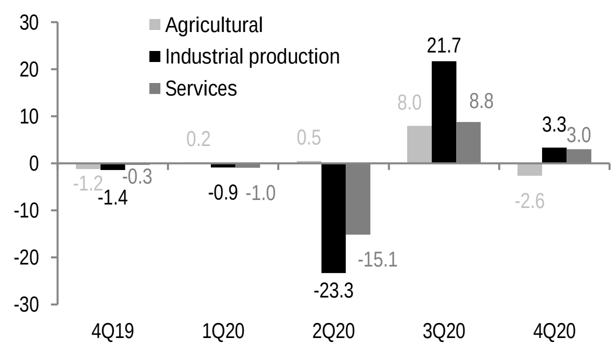
Source: INEGI

Chart 3: GDP
% q/q sa



Source: INEGI

Chart 4: GDP by sectors
% q/q sa



Source: INEGI

Table 3: GDP 2021: Supply
% y/y nsa; % q/q sa

% y/y	1Q21	2Q21	3Q21	4Q21	2021
GDP	-5.5	16.0	4.3	3.4	4.1
Agricultural	1.0	3.8	-3.6	-1.1	0.1
Industrial Production	-6.1	24.5	4.3	2.7	5.2
Services	-5.4	13.0	4.7	3.9	3.7
% q/q					
GDP	-0.3	0.9	1.0	1.4	--

*Note: Underlined figures indicate forecast
Source: INEGI, Banorte

Table 4: GDP 2021: Demand
% y/y nsa; % q/q sa

% y/y	1Q21	2Q21	3Q21	4Q21	2021
GDP	-5.5	16.0	4.3	3.4	4.1
Private consumption	-7.0	19.2	8.5	6.9	6.2
Investment	-12.9	24.1	8.1	3.1	4.0
Government spending	-3.7	-2.3	-3.0	1.3	-2.0
Exports	-2.8	32.9	5.5	3.3	8.0
Imports	-7.0	24.9	17.7	9.0	10.0
% q/q					
GDP	-0.3	0.9	1.0	1.4	--

*Note: Underlined figures indicate forecast
Source: INEGI, Banorte

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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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