Ahead of the Curve

December 17, 2021

Packed schedule at the end of the year, highlighting October's GDP-proxy and 1H-December's inflation

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This is the last publication of the year. We will resume on January 3rd. Happy Holidays!

- **GDP-proxy IGAE (October).** We expect the *Global Economic Activity Indicator* (IGAE) at 1.0% y/y, which translates into a 1.9% y/y advance with seasonally adjusted figures. The latter is in line with the mid-point of the first estimation of INEGI's *Timely Indicator of Economic Activity*. Sequentially, we expect the economy to rebound 1.2% m/m after two months of notable weakness. A key driver would be a relevant improvement in virus conditions, with cases trending lower while mobility kept recovering, reaching pre-pandemic levels. As such, restrictions lessened, allowing for a broader reopening. This has already been reflected in fundamentals, such as employment. By sectors, industry grew 0.6% m/m (+0.7% y/y), better than expected on manufacturing strength. For services, we anticipate a 0.9% m/m expansion (+1.3% y/y), being the sector most benefited by improving virus conditions and with a positive spillover in other metrics.

Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 20-Dec	7:00am	Timely Indicator of Economic Activity (sa)	November	% y/y	--	--	1.9
Tue 21-Dec	7:00am	Aggregate supply and demand	3Q21	% y/y	9.5	9.5	23.3
		Private consumption		% y/y	10.4	--	22.6
		Investment		% y/y	12.6	--	34.1
		Government spending		% y/y	-0.8	--	3.9
		Exports		% y/y	5.3	--	41.9
		Imports		% y/y	23.2	--	35.1
Tue 21-Dec	10:00am	International reserves	Dec-17	US$ bn	--	--	201.4
Tue 21-Dec	3:30pm	Citibanamex bi-weekly survey of economic expectations					
Wed 22-Dec	7:00am	Retail sales	October	%	5.6	5.9	5.9
		sa		%	0.4	0.4	0.2
Thu 23-Dec	7:00am	CPI inflation	1H Dec	% 2w/2w	0.36	0.33	0.51
				% y/y	7.73	7.69	7.70
		Core		% 2w/2w	0.49	0.46	0.23
				% y/y	5.77	--	5.80
Thu 23-Dec	7:00am	Unemployment rate	November	%	3.72	3.72	3.95
		sa		%	3.87	--	3.89
Fri 24-Dec	7:00am	Economic activity indicator	October	% y/y	1.0	0.9	0.9
		sa		% m/m	1.2	0.5	-0.4
		Primary activities		% y/y	0.5	--	-1.1
		Industrial production		% y/y	0.7	--	1.5
		Services		% y/y	1.3	--	0.7
Fri 24-Dec	7:00am	Trade balance	November	US$ mn	-2,261.4	-2,144.1	-2,701.0
		Exports		% y/y	4.8	--	0.0
		Imports		% y/y	20.1	--	25.1
Tue 28-Dec	10:00am	International reserves	Dec-24	US$ bn	--	--	--
Thu 30-Dec		Budget balance (measured with PSBR)	November	MX$ bn	--	--	-560.9
Fri 31-Dec	10:00am	Commercial banking credit	November	% y/y in real terms	-4.8	--	-6.1
		Consumption		% y/y in real terms	-5.0	--	-4.5
		Mortgages		% y/y in real terms	2.8	--	3.2
		Corporates		% y/y in real terms	-7.2	--	-9.4

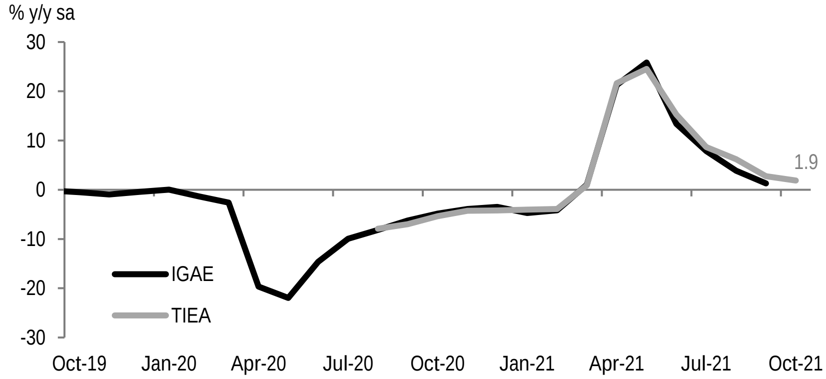
Source: Banorte; Bloomberg

Proceeding in chronological order…

***Timely Indicator of Economic Activity* (November).** This release will include the first estimate for November, as well as revised figures for October. We recall that September's mid-point forecast stood at 2.8% y/y (using sa figures), higher than the 1.3% seen in the GDP-proxy (IGAE). In this backdrop, we believe there is some upside to October's estimate, currently at 1.9% y/y. In particular, industrial production came in above expectations, while signals for services were also better. Sequentially, the period will very likely show an improvement. For November, signals are somewhat mixed, with better conditions surrounding the virus and greater mobility, driving confidence higher. Nevertheless, IMEF's PMIs showed a sequential decline –albeit remaining above the 50.0pts threshold–, which suggests lower dynamism at the margin. Therefore, we believe the monthly metric for the period could show a slight expansion.

Monthly GDP-proxy (IGAE) and the Timely Indicator of Economic Activity (TIEA)

% y/y sa



Source: INEGI

Aggregate demand in 3Q21 to slow down despite relatively resilient consumption. We expect both aggregate supply and demand to expand 9.5% y/y. As in other measures, annual figures will moderate on base effects. Apart from this, activity decelerated more than we had expected as the 'delta' variant hit confidence and supply chain issues remained as a strong headwind.

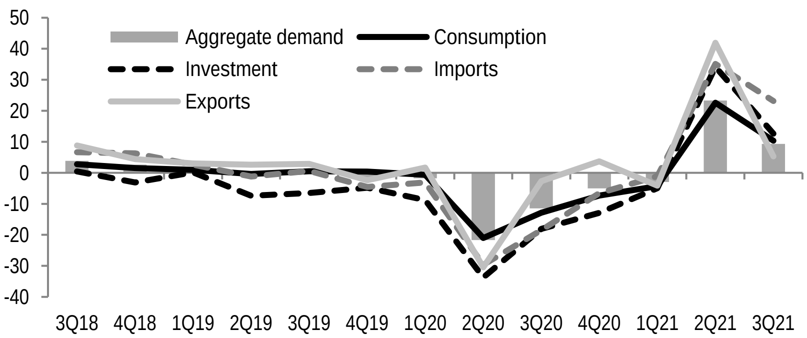
From the supply side, and as already published, GDP surprised to the downside at 4.5% y/y, with a weaker performance in industry and services. Nonetheless, we expect imports at 23.2%, better than initially projected. Converting trade balance figures to MXN at current prices, inbound shipments in the trade balance –which only considers goods– picked up 27.5% y/y, with the current account –also including services– at 26.7%. This is below the 40.5% and 42.0% when expressed in USD, respectively. In this sense, the Mexican peso appreciated 9.3% on average in annual terms. On the other hand, we are more cautious given ongoing inflationary pressures, which tend to widen the gap between figures in nominal and real terms.

In demand, the relative strength in imports would be matched by a stronger consumption, estimated at 10.4%. Consistent with the latter, the monthly indicator showed that imported goods were up 24.9%, while domestic ones were at 8.6%. When adding services to the latter, the result was 12.3%, with base effects due to the pandemic last year still influencing heavily.

If we are correct, this would help confirm increasing signs of more modest domestic demand, affected by the factors above but increasingly by high inflation, in our view. Investment has already been released, at 12.6% y/y (see link above), with an upward surprise in non-residential construction, as well as machinery and equipment. Government spending would fall 0.8%, with a setback after an acceleration in 2Q21. Moreover, current spending by the federal government decelerated to 6.2% from 7.7% previously. Nevertheless, the correlation is relatively weak, which may be related to accounting method differences. Lastly, we estimate exports at 5.3%, significantly below our previous expectations. These have remained affected by supply issues –especially auto manufacturing–, as well as crude oil. Coupled with imports' dynamics, this has shifted the trade balance towards a deficit more clearly since the start of the quarter.

We maintain our full-year GDP forecast at 5.7%, albeit recognizing some downside risks. Our main concern currently is the effect of high inflation, which in our view is increasingly challenging demand, both domestically and abroad. As price pressures linger around, real consumption going into 2022 may be an additional headwind for GDP, acting in opposite direction to the improvement that it would have from higher employment levels and record remittances.

Aggregate demand
% y/y, nsa



Source: INEGI, Banorte

Weekly international reserves report. Last week, net international reserves increased by US$1,448 million, closing at US$201.4 billion (please refer to the following table). According to Banxico's report, this was explained by: (1) US dollar sales from Pemex to the central bank amounting US$100 million; (2) US dollar sales from the Federal Government to Banxico amounting US$1,500 million; and (2) a negative valuation effect in institutional assets of US$152 million. So far this year, the central bank's international reserves have increased by US$5.8 billion.

Banxico's foreign reserve accumulation details
US$, million

	2020	Dec 10, 2021	Dec 10, 2021	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	195,667	201,441	1,448	5,773
(B) Gross international reserve	199,056	212,855	-602	13,799
Pemex	--	--	0	1,158
Federal government	--	--	-127	-1,635
Market operations	--	--	0	0
Other	--	--	-475	14,276
(C) Short-term government's liabilities	3,389	11,415	-2,050	8,026

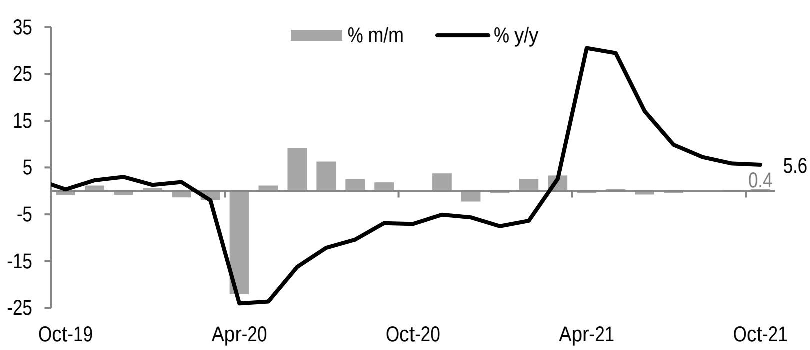
Source: Banco de México

Retail sales to maintain an upward trend in October. We expect a 5.6% y/y increase (previous: 5.9%). On sequential terms, this would translate to 0.4%, accelerating after two months of modest expansions. In our view, the main driver would be a further improvement on virus conditions, with cases trending lower and the 'traffic light' indicator allowing for higher mobility, benefiting consumer confidence. Nevertheless, price pressures remain as a relevant drag, among possible hesitancy ahead of *El Buen Fin* (Mexico's Black Friday) discounts in November.

Available information is mostly stronger. ANTAD's same-store sales accelerated (despite a more challenging base effect) to 5.0% y/y in real terms from +3.9% previously. Gasoline sales (in volume) rose both sequentially and in annual terms, consistent with improving mobility, which neared pre-pandemic levels. Non-oil consumption goods imports expanded 3.2% m/m, building up on the +1.1% seen in September. However, we are somewhat cautious on these, as they are measured in nominal terms. On the contrary, AMIA sales moderated to 74.4 thousand units, which represents a 6.1% m/m contraction. Turning to fundamentals, signals are quite positive. Remittances surged to a new historical high of US$4,818.6 million, accelerating 7.7% m/m. In addition, employment recovered quite strongly, with around 1.3 million jobs created, along further improvements in other metrics. Lastly, consumer loans showed additional dynamism, despite remaining in negative territory in the annual comparison.

While still modest, the result would be positive as it would signal that consumption remained on a favorable track towards the end of the year. Early information from retailers suggests favorable results from *El Buen Fin*, with reports of up to a 10% y/y increase in sales (in nominal terms). However, we still remain cautious over two risks: (1) An upward extension in price pressures, with notable sequential increases during October and November, especially on key staples; and (2) possible effects from supply constraints ahead of the holiday season, albeit with the latter possibly affecting only some goods (*e.g.* mobile phones, computers, videogame consoles, etc.).

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



Source: INEGI, Banorte

Inflation in 1H-December to be swayed by seasonal trends, along other shocks. We expect inflation at 0.36% 2w/2w (previous: 0.51%), low relative to its 5-year average of 0.42%. However, we must recall that the latter figure tends to be skewed higher by the rollback of *El Buen Fin* discounts (Mexico's Black Friday). Nevertheless, this would not be of the same magnitude in this occasion, considering that part of the rebound was already seen in 2H-November due to the timing in which discounts took place this year. In addition, we noted an important decline in energy, mainly LP gas, which would help offset the recent increase in agricultural goods. By components, the core would be highest at +0.49% (contribution: +37bps), with the non-core barely at -0.01% (0bps). With these results, annual inflation would climb to 7.73%, accelerating from the 7.38% on average seen in November and its highest since January 2001. The core would climb to 5.77% (previous: 5.67%), continuing with an upward trend. The non-core would come in at 13.80% (previous: 12.61%).

Within the core, goods would remain pressured (0.5%; 15bps). Processed foods are estimated to climb 0.3% (+7bps), with reports suggesting that increases continued. Overall, these items will still be impacted by cost pressures and shocks to supply chains. Meanwhile, other goods would climb 0.4% (+8bps), still with a slight rebound after the extension of some discounts in the last weeks of November, albeit moderate relative to previous years. Services are likely to be high (0.6%; 22bps). A large part of this would correspond to other services, up 1.2% (+20bps), impacted by both an adverse seasonality in tourism –ahead of the winter holidays– as well as additional pressures in other categories. Lastly, housing would maintain a slight acceleration at 0.1% (+2bps).

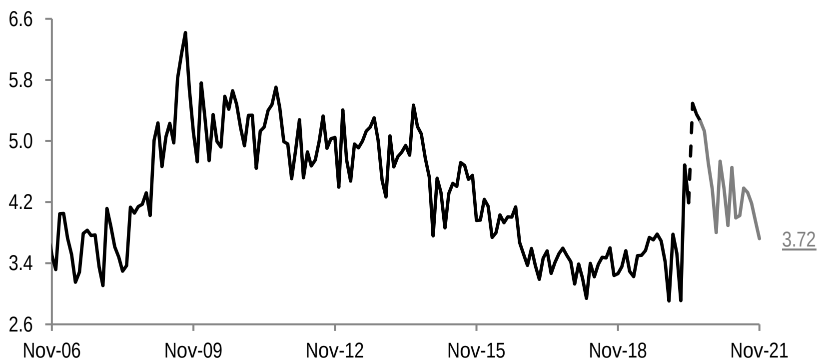
Going to the non-core, the behavior should be highly differenced. Energy would fall sharply, down 0.8% (-8bps) due to a strong improvement in LP gas. Specifically, we anticipate this category at -4.9% (-12bps), benefiting from an important fall in international references, even despite a modest depreciation of the exchange rate. On the contrary, gasolines are projected to increase at the margin, highlighting low-grade at +0.4% (+2bps). Despite an improvement in foreign prices, the subsidy to excise taxes has decreased, which we believe will offset for the former. Meanwhile, electricity tariffs are expected to advance 0.5% (+1bps). On the other hand, government tariffs would remain contained at 0.1%. On agricultural goods, we expect pressures to continue, albeit at a lower pace than in the previous month, at 0.7% (+8bps). These would be centered in fruits and vegetables (1.0%; +5bps), with our monitoring showing mixed signals across different goods, especially with uncertainty surrounding tomatoes and chilies. On meat and egg (0.5%; +3bps) we expect a moderation after the acceleration in the previous two months, helped by better signals on beef and eggs.

Labor market improvement to continue in November. We estimate the unemployment rate at 3.72% (original figures), down 23bps relative to October. This would be mostly on a positive seasonal effect, as this figure tends to improve towards the end of the year. With seasonally adjusted figures we anticipate more stability, with a 2bps improvement to 3.87%. This would be supported by better conditions in the epidemiological front.

Nevertheless, signals on activity are more mixed, with an upward trend in mobility on top of seemingly positive results from *El Buen Fin* (Mexico's Black Friday), albeit with other indicators –such as [IMEF's PMIs]– suggesting lower dynamism. In our opinion, the net effect would be favorable. Nonetheless, gains both on employment and the labor force will likely be more modest than in October. We expect the participation rate to add a second month higher, while the part-time rate could benefit further from a looser 'traffic light' indicator. Despite of this, these should remain far from their pre-pandemic levels. On informality, we do not rule out a modest reversion higher after a relevant decrease in the previous report. Lastly, wages could reestablish their upward trend after a moderation in October, probably responding to larger price pressures. Nevertheless, slack in the labor market may be offsetting some of this, resulting in a lower advance. If the improvement in the labor market continues, conditions for a rebound in activity would be clearer, favoring our current estimate of a 1.6% q/q expansion in 4Q21 GDP.

Advanced data is mixed. Employment affiliated to IMSS rose by 165.5 thousand, extending gains for a fifth month in a row. With seasonally adjusted figures this translates into +34.5 thousand jobs, accelerating at the margin. Employment indices within aggregate trend indicators showed positive signals, with advances in the four major sectors (manufacturing, construction, commerce, and non-financial services), highlighting additional strength in commerce. On a negative note, employment components within IMEF indicators inched lower, with manufacturing even below the 50pts threshold.

Unemployment rate
%, nsa



Source: INEGI, Banorte

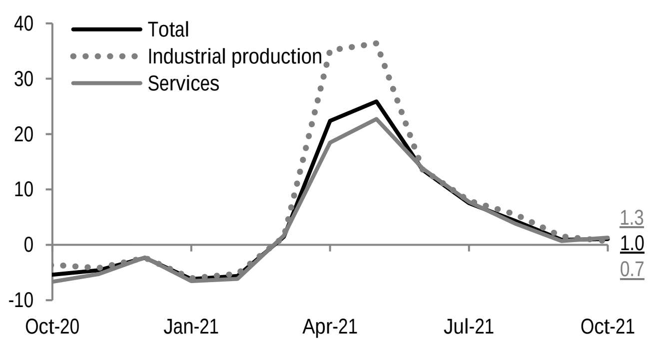
October's GDP-proxy to rebound after recent weakness. We expect the *Global Economic Activity Indicator* (IGAE) at 1.0% y/y, slightly higher than the 0.9% seen in September. With seasonally adjusted figures, this would translate into a 1.9% y/y advance, as there is one less working day in the annual comparison. This is in line with the mid-point of the first estimation of INEGI's *Timely Indicator of Economic Activity*. Sequentially, we expect the economy to rebound 1.2% m/m after two months of notable weakness. A key driver would be a relevant improvement in virus conditions, with cases trending lower while a mobility kept recovering, reaching pre-pandemic levels. As such, restrictions lessened, allowing for a broader reopening. This has already been reflected in fundamentals, such as employment.

By sectors, industry grew 0.6% m/m (+0.7% y/y), better than expected on manufacturing strength (+1.8% m/m), boosted by gains in transportation and electronic equipment. Mining (+0.2%) and utilities (+1.2%) also improved. However, construction remained weak (-1.3%). We see agriculture at +1.2% m/m (0.5% y/y), also rebounding. More stable inflation in this category suggests less supply pressures and increased product availability, even after factoring-in a slowdown in this sector's exports.

For services, we anticipate a 0.9% m/m expansion (+1.3% y/y), being the sector most benefited by improving virus conditions and with a positive spillover in other metrics. However, we remain wary about the possible negative effect of additional price pressures, as evidenced by an acceleration in the month's CPI report. In this backdrop, available data suggests a more favorable backdrop. Among them, IMEF's non-manufacturing PMI climbed 1.7pts to 51.8pts, with gains across all components, especially 'production'. Meanwhile, INEGI's employment report showed slightly more than 1 million jobs gained in the sector, with most of them in commerce and restaurants and lodging. Turning to sector data, retail sales look stronger, as outlined in a previous section. On entertainment and tourism, we believe higher mobility could have provided a boost. Regarding the latter, the hotel occupancy rate climbed to 47.2%, a notch higher than the 39.8% of the previous month –partly on a seasonal effect–, with a similar trend for air passenger traffic (albeit decelerating in annual terms on a more challenging base effect). Pivoting to more essential sectors, we could see modest gains, considering resilience in the previous month in categories such as education and healthcare, as well as government services.

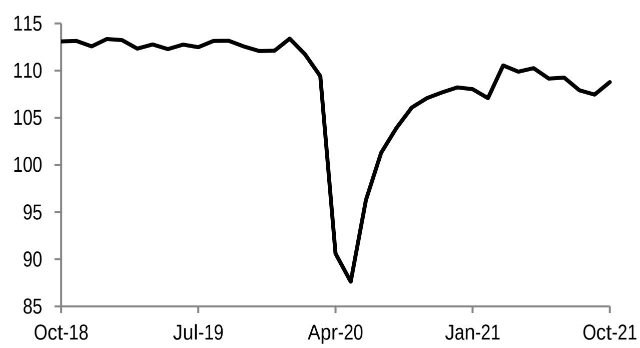
Going forward, timelier signals point to an extension of the recovery, albeit at a slower pace. Although virus conditions improved further, price pressures also exacerbated, with the annual print reaching its highest level since early 2001. In our view, this is the most important risk currently, with the possibility of increasingly affecting demand levels.

IGAE
% y/y (nsa)



Source: INEGI, Banorte

IGAE
Index (sa)



Source: INEGI, Banorte

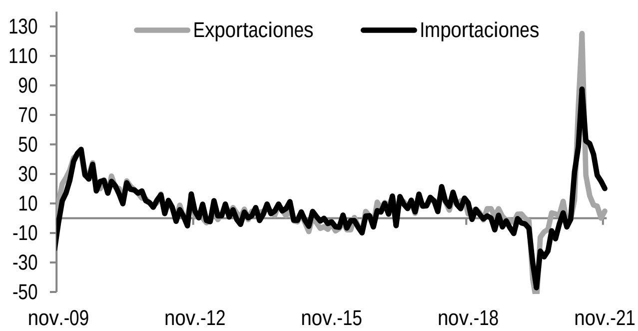
November's trade balance to stay in deficit. We estimate a US$2,261.4 million deficit, with total exports and imports at 4.8% and 20.1% y/y, respectively. Historically, the period has tended towards more modest deficits than in October, as companies have already replenished their inventories in advance to the discount and holiday seasons.

Nevertheless, volatility in flows may be higher given supply bottlenecks and longer delivery times. Moreover, prices add another layer of uncertainty given high upward pressures in a plethora of categories, inflating balances in both shipments and purchases abroad. Hence, increased caution about their implications for economic activity is recommended. The period also had one more working day in the annual comparison.

In oil, we estimate a US$1,766.9 million deficit. This would be more positive than in October, albeit with each component stronger in absolute terms as prices and volumes increased sequentially. We expect exports at 90.2%, with crude-oil up 88.4%. The Mexican oil mix averaged 75.08 US$/bbl from 74.46 previously, up 91.1% y/y. International prices reacted to the downside late in the period after the release of strategic reserves by several countries, although it is likely to be more important for December, especially as this was coupled with increased concerns about the impact of the 'omicron' variant. Available data on volumes is also higher. On purchases, gasoline prices in the US were marginally lower after picking up in October. Nevertheless, flows are more correlated with prices lagged by one month. On the other hand, volumes of US gasoline exports to Mexico rebounded. In our view, this may likely be related to higher mobility levels, in turn influenced by better pandemic conditions domestically.

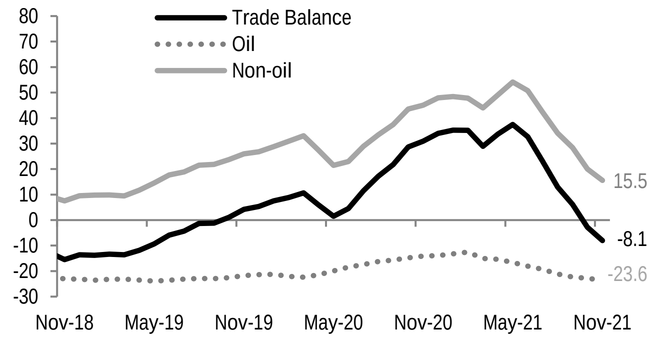
In non-oil, we anticipate a US$494.5 million deficit, with exports and imports at 1.2% and 15.1% y/y, in the same order. In the former, we see an acceleration in agricultural goods to 12.9% y/y. Domestic prices of fruits and vegetables (and to a lesser extent, meat and egg) shot up, which in our view may be related to higher exports (and lower domestic availability) on higher profit margins in the US, especially as drought conditions in the southeast of the country remain difficult, In mining, October's rise in prices extended through November, which may keep providing a boost to annual rates. Nevertheless, signals in manufacturing are more mixed. Autos remain in a difficult spot, with vehicle exports according to AMIA lower at the margin with 211,263 units (-26.6% y/y from -19.9% previously). In contrast, the sector's production in the US kept moving higher, with the imports component within the ISM indicator also increasing and back to expansion territory. Nonetheless, IMEF's manufacturing indicator inched lower, including production, employment and deliveries. In our view, these discrepancies could be a result of bottlenecks and delays in trade, leading to desynchronization. Imports are relatively weak on seasonal patterns. In this respect, Chinese exports to Mexico in October (in our view relevant because of shipping times) moderated to 39.7% y/y, albeit elevated on still favorable base effects. This is consistent with the deceleration in ISM's exports component (to 57.9pts from 62.3pts in the previous month). We do not see a sizable impact from restrictions in some countries due to the 'Omicron' variant, as concerns in this front exacerbated until the end of the month. As in exports, higher prices may boost figures in absolute terms. Lastly, a steeper slowdown is possible in capital goods, affected by higher uncertainty about growth and additional peso weakness, averaging close to 21 per dollar in the month.

Exports and Imports
% y/y nsa



Source: INEGI, Banorte

Trade balance
US$ billion, 12-month rolling sum



Source: INEGI, Banorte

MoF's public finance report (Jan-Nov). Attention will center on the Public Balance and Public Sector Borrowing Requirements (PSBR). Given that this is not a quarterly report, we do not expect updates on the macro framework and other fiscal variables. As such, the comparisons will be made relative to the last quarterly update, which showed modest revisions vs. the estimates outlined in the 2022 General Policy Criteria. Until October, the PSBR deficit amounted to $560.9 billion, with the traditional public deficit at $351.0 billion. We will also pay attention to revenue and spending dynamics in the annual comparison. Lastly, we will analyze public debt, which stood at MXN$12.6tn in the same period (as measured by the Historical Balance of the PSBR).

Banking credit to maintain dynamism in November, despite a negative effect from inflation. We anticipate a 4.8% y/y decline in banking credit to the private non-financial sector, better than the -6.1% seen in the previous month. The improvement would be driven by: (1) A more favorable base effect; and (2) an additional boost from the economic recovery. We believe the latter is being aided by epidemiological conditions, having a positive impact on both consumer and business confidence. However, we must note that the month's figures will be dragged by inflation, with a 114bps increase relative to the previous month to 7.37% y/y. As such, consumer loans would stand at -5.0% –not as benefited by the base effect–, with corporates with a larger improvement at -7.2%. Lastly, mortgages would remain somewhat stable at 2.8%.

Analyst Certification

We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Francisco José Flores Serrano, Katia Celina Goya Ostos, José Itzamna Espitia Hernández, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez and Gerardo Daniel Valle Trujillo, 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
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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			
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