Ahead of the Curve

Moderate increase in 1H-March inflation

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- **Inflation (1H-March).** We forecast headline inflation at 0.18% 2w/2w, lower than its five-year average of 0.33%, which would be positive. Several factors would have contributed to a more favorable performance, noting: (1) Recent MXN strength; (2) stable energy prices; and (3) a moderation in some cost increases. On the other hand, some risks prevail, including the potential passthrough from higher wages and price increases in some categories that had not adjusted previously. As such, we expect the core at 0.25% (contribution: +18bps) and the non-core unchanged at 0.0% (0bps). If our forecast materializes, annual headline inflation would stand at 7.16% from 7.48% in the previous fortnight, adding four consecutive declines. Similarly, the core would moderate to 8.09% from 8.21%, with the non-core at 4.48% from 5.37%

- **Economic Activity Indicator (January).** We expect the print at 3.8% y/y, higher than the 2.6% from December, even despite a slightly more challenging base. More importantly, this implies +0.2% m/m, coming after the +0.3% of the previous month. This would suggest that 2023 started on the right track despite new headwinds –which will likely have differentiated effects across sectors

Mexico weekly calendar

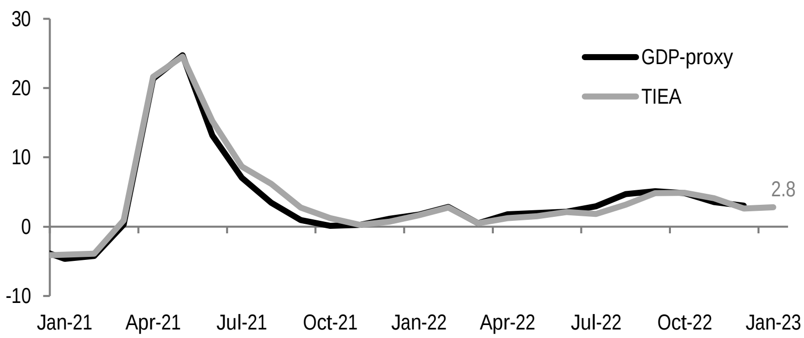
DATE	TIME (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 20-Mar		Markets closed in remembrance of the birth of Benito Juárez					
Tue 21-Mar	4:30pm	Citibanamex bi-weekly survey of economic expectations					
Wed 22-Mar	8:00am	Timely Indicator of Economic Activity (sa)	February	% y/y	--	--	2.8
Wed 22-Mar	8:00am	Aggregate supply and demand	4Q22	% y/y	4.5	--	6.4
		Private consumption		% y/y	4.4	--	6.4
		Investment		% y/y	7.8	--	3.8
		Government spending		% y/y	1.7	--	2.3
		Exports		% y/y	4.4	--	11.6
		Imports		% y/y	6.8	--	11.5
Wed 22-Mar	11:00am	International reserves	Mar-17	US$ bn	--	--	200.6
Thu 23-Mar	8:00am	CPI inflation	1H March	% 2w/2w	0.18	0.28	0.16
				%y/y	7.16	7.26	7.48
		Core		%2w/2w	0.25	0.29	0.16
				%y/y	8.09	8.14	8.21
Thu 23-Mar	8:00am	Retail Sales	January	% y/y	4.4	--	2.5
		sa		% m/m	1.2	--	0.1
Fri 24-Mar	8:00am	Economic activity indicator	January	% a/a	3.8	--	2.6
		sa		% m/m	0.2	--	0.3
		Primary activities		% y/y	6.1	--	8.0
		Industrial production		% y/y	2.8	--	3.0
		Services		% y/y	4.2	--	2.1

Source: Banorte; Bloomberg

Proceeding in chronological order…

INEGI's *Timely Indicator of Economic Activity* to moderate in January, with some uncertainty ahead. This release includes revised figures for January and the first estimate for February. We recall that December's mid-point forecast was 2.6% y/y (with sa figures), in line with the GDP-proxy (IGAE). For the first month of 2023 we envision an upward revision, even after a negative surprise in industrial production. Nevertheless, we see some resiliency in services. Hence, we believe that a sequential expansion is still feasible. For February, information so far has been mixed. IMEF's PMI indicators accelerated slightly –with strength mainly in non-manufacturing. Nevertheless, ANTAD's sales moderated significantly, even after annual inflation was lower in the period. Therefore, we believe that a modest sequential gain is possible, although without ruling out a slight contraction

Monthly GDP-proxy and the Timely Indicator of Economic Activity (TIEA)
% y/y sa



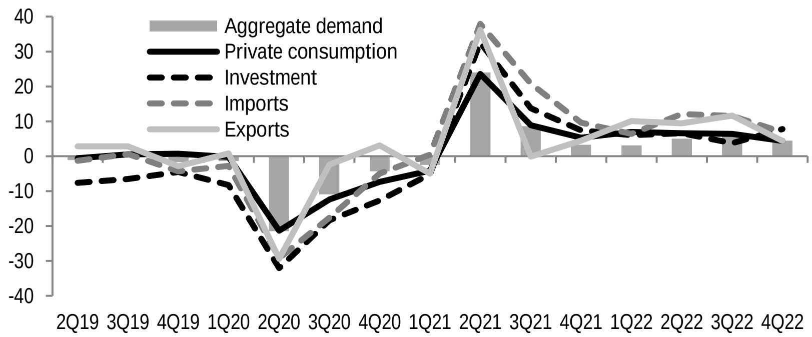
Source: INEGI

Aggregate demand likely maintained a favorable trend in 4Q22. We expect both aggregate supply and demand at 4.5% y/y, moderating from the 6.4% increase of the previous quarter. From the supply side, we already know that GDP grew 3.6% y/y, extending its recovery trend for a fifth consecutive quarter. Dynamism was relatively broad-based, noting the outperformance in construction and some non-essential services. We expect these to have translated favorably into investment and consumption, respectively. We anticipate imports at 6.8% y/y, decelerating from 11.5% in the third quarter. Converting trade balance figures to MXN at current prices, goods entering the country rose 2.8%, with the current account –which also includes services– at 3.4%. This is lower than with data in USD as the Mexican peso appreciated 5.2% y/y on average. Nevertheless, it seems some normalization is starting to show up due to lower price distortions in the period.

On demand, private consumption would remain quite strong at 4.4%, with a boost from services and imported goods. The monthly indicator grew 4.2%, with services leading (+6.8%), but with imported goods (+6.7%) probably benefitting from MXN strength. We believe fundamentals were key for dynamism, with employment showing broad gains –despite its negative seasonality– and with remittances still strong. Investment would accelerate at 7.8%, particularly because of machinery and equipment (13.5%). On the other hand, construction (3.0%) gathered pace, in our view because of appetite in industry.

We forecast government spending at +1.7%. Current spending by the Federal Government rose 13.9% y/y. albeit remembering that there are relevant differences in accounting practices at the end of the year. Lastly, we anticipate a deceleration in exports, to 4.4%. Similar to shipments from abroad, differences between the trade balance and the balance of payments widened, (with outflows in MXN at +3.7% and 4.7%, respectively), pointing to stronger relative growth in services.

Aggregate demand
% y/y, nsa



Source: INEGI, Banorte

Weekly international reserves report. Last week, net international reserves increased by US$299 million, closing at US$200.6 billion (see table below). This was mainly due to a positive valuation effect in institutional assets. Year-to-date, the central bank's reserves have increased by US$1.5 billion.

Banxico's foreign reserve accumulation details
US$, million

	2022	Mar 10, 2023	Mar 10, 2023	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	199,094	200,567	299	1,472
(B) Gross international reserve	201,143	204,608	149	3,465
Pemex	--	--	0	0
Federal government	--	--	-42	2,541
Market operations	--	--	0	0
Other	--	--	191	924
(C) Short-term government's liabilities	2,049	4,042	-149	1,992

Source: Banco de México

Favorable trends will help keep inflation low in 1H-March. We forecast headline inflation at 0.18% 2w/2w, lower than its five-year average of 0.33%, which would be positive. Several factors would have contributed to a more favorable performance, noting: (1) Recent MXN strength (albeit with notable pressures in the last days of the fortnight); (2) stable energy prices; and (3) a moderation in some cost increases. On the other hand, some risks prevail, including the potential passthrough from higher wages and price increases in some categories that had not adjusted previously. As such, we expect the core at 0.25% (contribution: +18bps) and the non-core unchanged at 0.0% (0bps). If our forecast materializes, annual headline inflation would stand at 7.16% from 7.48% in the previous fortnight, adding four consecutive declines. Similarly, the core would moderate to 8.09% from 8.21%, with the non-core at 4.48% from 5.37%.

Within the core, goods would climb 0.3% 2w/2w (+11bps), once again leading upwards. Processed foods would remain somewhat pressured at +0.3% (+7bps), with our monitoring suggesting important adjustments higher in milk and soda. 'Other goods' would rise 0.2% (+4bps), in our view more supported by MXN gains. Services would accelerate marginally (0.2%; +7bps), highlighting some larger-than-usual pressures in housing. 'Other services' (0.3%; +5bps) would be impacted by slight advances in tourism categories –due to the start of *Spring Break*–, albeit with 'dining away from home' still moving up due to accumulated cost pressures –including on labor.

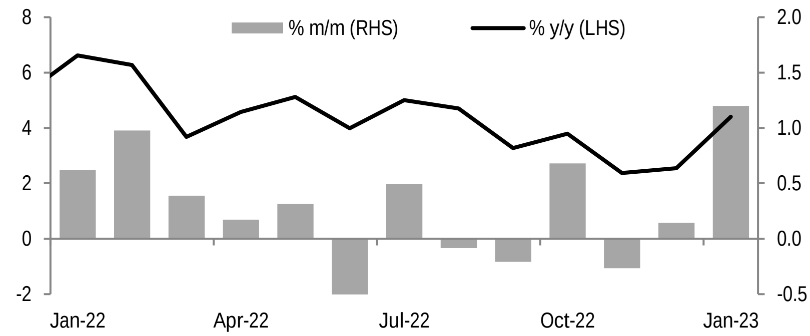
At the non-core, energy would fall 0.1% (-1bp). We highlight LP gas (-0.8%; -1bp), helped both by the exchange rate and international references. In electricity tariffs (-0.2%; 0bps) we expect a marginal decline after the announcement of a decline in high-consumption tariffs in the period. Gasolines would be more stable, even despite a seasonal increase in US futures. As such, we expect low-grade fuel at 0.1% (+1bp). In agricultural, signs are mostly positive, expecting -0.1% (-1bp). This would have centered in meat and egg (-0.4%; -3bps), with our monitoring showing declines in beef and chicken. Fruits and vegetables would climb 0.4% (+2bps), mostly on potatoes and onions. Finally, we expect higher government tariffs, noting the coming into force of a 7.8% increase in some federal highways' tolls starting on March 6th.

Retail sales probably gained pace in January. We forecast sales at 4.4% y/y, stronger at the margin despite a negative base effect, in turn suggesting renewed strength. It implies a sequential gain of 1.2% m/m, adding up to December's +0.1%. This would be favorable and consistent with other tailwinds, including resilient fundamentals and the new 20% increase in the minimum wage.

In this respect, timely data has been positive, highlighting better results in ANTAD's sales. Same-store sales accelerated towards 2.2% Y7Y in real terms (previous: 1.1%), with total sales also higher at 5.5% (previous: 3.8%). Auto sales grew 1.1% m/m (with our in-house seasonal adjustment model), quite good after rising 9.4% in the previous month. Non-oil consumption good imports advanced 19.1% m/m, its second highest print since the series is available (1993), although without ruling out a meaningful distortion because of New Year celebrations in China. Gasoline sales reached 625kbpd, lower by 48kbpd relative to December. Nevertheless, this deceleration is partly justified by seasonal drivers. The unemployment rate reached a new historical low, while wages picked up in annual terms. Moreover, remittances kept growing at a double-digit pace. Lastly, consumer credit was stable at 9.0% y/y in real terms

Going forward, we believe that consumption will keep growing vigorously, supported by labor market strength and more positive economic conditions overall. Nevertheless, some headwinds remain, including persistent price pressures and more significant monetary tightening than anticipated at the beginning of the year.

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



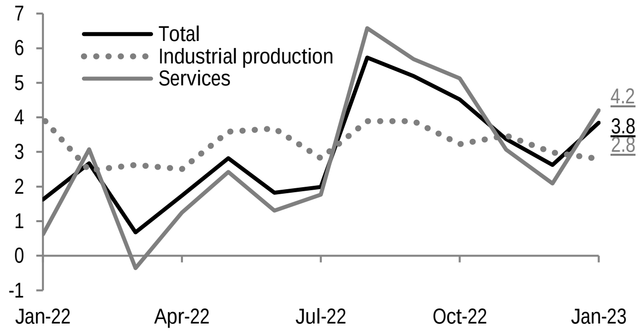
Source: INEGI, Banorte

Upward push in activity at the turn of the year. We expect the monthly GDP-proxy IGAE at 3.8% y/y, higher than the 2.6% from December, even despite a slightly more challenging base. More importantly, this implies +0.2% m/m, coming after the +0.3% of the previous month. This would suggest that 2023 started on the right track despite new headwinds –which will likely have differentiated effects across sectors.

As we already know, industrial production had null growth (0.0% m/m; 2.8% y/y). This was supported by manufacturing (0.7% m/m) and mining (0.2%), albeit mixed in the former. Meanwhile, construction had a relevant setback (-1.0%) after four months of strong gains. On the other hand, we expect -1.5% m/m in primary activities (6.1% y/y), with adverse signs both in prices and the sector's exports.

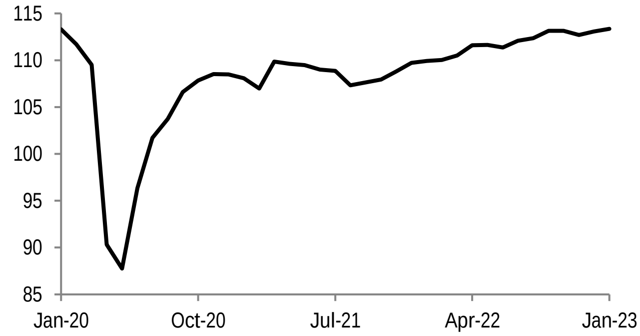
Figures for services are more positive at the margin, expecting +0.4% m/m (4.2% y/y). We believe the boost at the end of 2022 continued, supported by the new minimum wage, more than offsetting an acceleration in inflationary pressures. In addition, employment recovered and remittances maintained dynamism despite a negative seasonality. In this sense, although IMEF's non-manufacturing PMI decelerated at the margin to 52.6pts, it maintained some strength. By sectors, figures on commerce have been positive, with a favorable outlook for retail sales (see section above). On tourism, air passenger traffic accelerated in the annual comparison, albeit moderating in absolute terms (in line with its seasonality). Hotel occupancy rates showed the same behavior. On other categories, we will be looking into education and healthcare, especially given sequential increases in the last four months which set a challenging base effect. Finally, we expect weakness to persist in professional and support services, which have added 6 consecutive periods lower.

GDP-proxy IGAE
% y/y (nsa)



Source: INEGI, Banorte

GDP-proxy IGAE
Index (sa)



Source: INEGI, Banorte

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