Ahead of the Curve

Banxico will continue with its hiking cycle

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- **Banxico's monetary policy decision (March 30th).** We expect a 25bps hike by the central bank, pushing the reference rate to 11.25%, in line with consensus. We expect a unanimous decision, fulfilling the guidance of the previous statement that "*…for its next policy meeting, the upward adjustment to the reference rate could be of a lower magnitude…*". In our view, conditions have improved enough at the margin to justify this, especially inflation dynamics. Nevertheless, we do not rule out one or two dissents from hawkish members, Deputy Governors Espinosa or Heath. We believe the tone of the statement could be less hawkish, awaiting evidence to decide upcoming actions and the possible terminal point of the hiking cycle, which we think is very close

- **2024 Preliminary Policy Criteria.** In line with the Budget and Fiscal Responsibility Law, the Ministry of Finance will present the *Preliminary Economic Policy Criteria* for fiscal-year 2024. The law sets April 1st as the deadline for submission. The document must contain: (1) Main objectives of the Revenue Law and the Spending Budget proposal; (2) scenarios for the main macroeconomic variables fin the upcoming year –including GDP, inflation, interest rate and oil price; (3) scenarios about the total amount of the Spending Budget and its balance –whether it presents a surplus or a deficit–; and (4) a list of priority programs and the amounts expected to be allocated to them. In addition, the MoF includes a detailed analysis of the global and domestic economy, as well as on public finances. Along the presentation of next year's estimates, they will also adjust their expectations for the current year, both for macroeconomic and fiscal variables, including projections for revenues and outlays

Mexico weekly calendar

DATE	TIME (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 27-Mar	8:00am	Trade balance	February	US$ mn	1,520.3	1,099.0	-4,125.1
		Exports		% y/y	2.9	--	25.6
		Imports		% y/y	2.5	--	16.3
Tue 28-Mar	11:00am	International reserves	Mar-24	US$ bn	--	--	202.0
Thu 30-Mar	3:00pm	Banxico's monetary policy decision	Mar-30		11.25	11.25	11.00
Thu 30-Mar		Budget balance (measured with PSBR)	February	MX$ bn	--	--	-15.9
Fri 31-Mar	8:00am	Unemployment rate	February	%	3.02	3.07	3.00
		sa		%	2.95	--	2.92
Fri 31-Mar	11:00am	Commercial banking credit	February	% y/y in real terms	4.7	--	4.8
		Consumption		% y/y in real terms	8.9	--	9.0
		Mortgages		% y/y in real terms	3.5	--	3.2
		Corporates		% y/y in real terms	3.5	--	3.2
Sat 1-Apr		Deadline for the submission of the 2024 Preliminary Policy Criteria					

Source: Banorte; Bloomberg

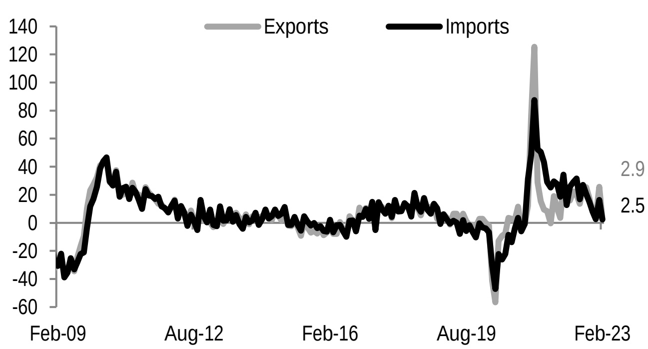
Proceeding in chronological order…

Trade surplus in February, in line with historical patterns. We estimate a US$1,520.3 million surplus in the second month of the year. This would be broadly in line with seasonal patterns, as flows are affected by various effects, including: (1) A normalization in growth rates due to lower price distortions and a more challenging base effect; (2) signs of resilience in domestic consumption; and (3) and adjustment in flows, with the Lunar New Year's seasonality reducing inflows into our country. In annual terms we expect higher exports (+2.9%) and imports (+2.5%), showing an additional normalization in supply chains.

We forecast a US$1,695.7 million deficit in the oil balance, moderating relative to January. Exports (-2.2% y/y) would reflect slightly stronger volumes –at least according to US timely data–, offsetting for a lower price of the Mexican oil mix, averaging 67.27 US$/bbl (-22.6% y/y). On imports (2.8%), price variations were also negative in LP gas, gasolines, and natural gas. Nevertheless, this would have been compensated by strong volumes, explained by an additional normalization in economic conditions.

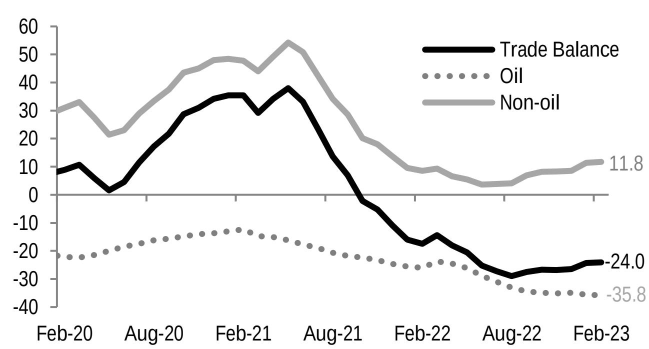
The non-oil balance would post a US$3,216.0 million surplus. Within exports (3.3%), we expect resilience to remain in manufacturing (3.5%), particularly in autos at 9.1%. AMIA figures point to an acceleration in flows from light and heavy vehicles. On 'others' (0.4%), we note an adverse base effect, albeit with some support due to stability in US manufacturing. Agricultural outflows would decelerate to 4.9%, in our opinion on less favorable prices. Turning to imports (2.5%), we anticipate mixed results. Strength would remain in consumption (21.3%) on the back of resilient fundamentals and an additional MXN appreciation. Meanwhile, intermediate goods would be affected by lower dynamism in exports at -1.3%. Lastly, capital goods (17.3%) would likely remain supported by nearshoring efforts.

Exports and imports
% y/y



Source: INEGI, Banorte

Trade Balance
US$ billion, 12-month rolling sum



Source: INEGI, Banorte

Weekly international reserves report. Last week, net international reserves increased by US$1.4 billion, closing at US$202.0 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$2.9 billion.

Banxico's foreign reserve accumulation details
US$, million

	2022	Mar 17, 2023	Mar 17, 2023	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	199,094	201,972	1,405	2,878
(B) Gross international reserve	201,143	205,761	1,153	4,618
Pemex	--	--	0	0
Federal government	--	--	-267	2,274
Market operations	--	--	0	0
Other	--	--	1,420	2,344
(C) Short-term government's liabilities	2,049	3,789	-253	1,740

Source: Banco de México

Banxico to slow down the pace, taking the reference rate to 11.25%. We expect a 25bps hike by the central bank, pushing the reference rate to 11.25%, in line with consensus. We expect a unanimous decision, fulfilling the guidance of the previous statement that "*…for its next policy meeting, the upward adjustment to the reference rate could be of a lower magnitude…*". In our view, conditions have improved enough at the margin to justify this, especially inflation dynamics. Nevertheless, we do not rule out one or two dissents from hawkish members, Deputy Governors Espinosa or Heath. We believe the tone of the statement could be less hawkish, awaiting evidence to decide upcoming actions and the possible terminal point of the hiking cycle, which we think is very close.

The outlook on prices seems to have improved, including the latest print in which annual inflation moderated to 7.12%, adding four consecutive fortnights lower. Some of this is explained by a more favorable base. Nevertheless, some positive developments have also started to materialize, with the main one being the effect of MXN strength. As such, headline inflation so far in the quarter has averaged 7.6%, already lower than the central bank's 7.7% forecast. However, optimism might be dampened somewhat by the core, with lingering effects in processed foods and with services showing additional pressures –in our view with a relevant push from higher labor costs. This is consistent with some concerns recently expressed by Deputy Governor Espinosa. In an interview with *Bloomberg,* she stated that "*…core inflation has been very resistant to decline…*", while also adding that "*…we are in a very complex and uncertain environment…*". In this sense, this component has averaged 8.3% so far in the quarter vs. their 8.2% forecast. In this context, revisions to short-term estimates will likely be mixed and modest, expecting a downward adjustment for the headline of around 20bps, with the core stable at best. Currently, the central bank considers that the balance of risks remains tilted to the upside. We would not be surprised if it is modified to stable based on our year-end forecast of 4.8%. Nevertheless, some caution could very well remain as the core is more likely to be revised upwards, especially when compared against our 5.6% estimate relative to the one made by the central bank (see table below).

Inflation forecasts
% y/y, quarterly average

	4Q22	1Q23	2Q23	3Q23	4Q23	1Q24	2Q24	3Q24	4Q24
Headline	8.0*	7.7	6.4	5.3	4.9	4.2	3.7	3.4	3.1
Core	8.4*	8.2	7.3	6.2	5.0	4.1	3.5	3.2	3.1

Source: Banco de México. * Observed data. In 4Q22, averages were 8.0% and 8.4% for the headline and core, respectively

The Board's reaction function seems to be putting less weight to the Fed's actions –especially when looked through the lens of the previous decision surprise. Notwithstanding this, it is our take that the latest 25bps hike from said institution will also help Banxico to reduce the pace. In our view, the high rate spread between Mexico and the US has been key to avoid a more significant MXN depreciation –outperforming most EM currencies– in an environment of increased risk aversion triggered by concerns about the US and European banking sectors. Despite its recent slide –from a low of 17.96 pesos per dollar on March 3rd– to 18.45 per dollar, it remains quite resilient and stronger than its average level in 2022 of 20.11. In this backdrop, Governor Rodriguez mentioned in the *Banking Convention* that "*...we'll take into account the Fed's decision and many other factors, to the extent they affect the inflation outlook...*". On the domestic banking sector, she stated that "*...at this time, we do not see any risk for our financial system...*". Meanwhile, Deputy Governor Borja –at the same event– echoed some of these comments, stating that Banxico will follow its own pace in upcoming decisions.

All in all, and considering all available information, it is our take that the central bank will avoid another surprise, especially as data supports a moderation in the hiking pace. Currently, we think this will not be the last increase. However, additional guidance in the statement and the related minutes –to be published on April 13th– regarding further actions would be most welcomed, particularly as the monetary policy outlook has become more uncertain worldwide.

MoF's public finance report (February). Attention will center on the Public Balance and Public Sector Borrowing Requirements (PSBR) in the second month of 2023 after a $15.9 billion deficit in January. Oil-related revenues will probably decline considering a lower price of the Mexican oil mix (in annual terms). Meanwhile, we await income taxes and VAT collection, trying to get clues about economic dynamism. In addition, we will pay attention to excise taxes, considering changes in international reference prices for fuels. On spending, we will follow financial costs and programmable spending –especially in autonomous and administrative branches–, along with outlays by Pemex and CFE. Finally, we will also analyze public debt, which amounted to $14.0 trillion in January (as measured by the Historical Balance of the PSBR).

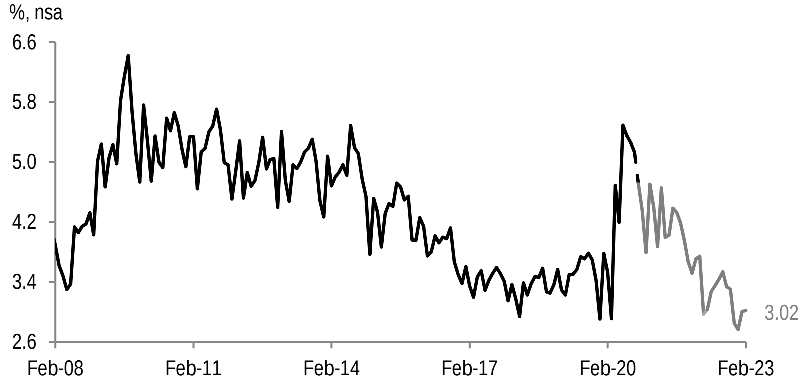
Unemployment to tick higher in February, with job gains continuing. We expect the unemployment rate at 3.02% (original figures), barely up from the 3.00% seen in January. The increase would be partly explained by seasonal factors, remembering that the figure tends to revert higher in the first few months of the year. With seasonally adjusted figures we expect a similar increase, to 2.95% from 2.92%. Timely data shows mostly positive signs, albeit with a more challenging backdrop. Back to original figures, we expect a higher level of employment, albeit not ruling out a moderation relative to those seen in the last three years given January's unusual uptick. We also anticipate gains in the labor force, albeit slightly stronger, explaining the adjustment in the unemployment rate. As such, we expect a modest increase in the participation rate, while the part-time rate could be more stable.

We still forecast some relative consistency in informality, with current levels in line with long-term averages. Regarding wages, we still see increases, with the lighthouse effect from the minimum wage hike likely starting to materialize.

On timely data, IMSS reported 175.9 thousand new jobs. Nevertheless, with seasonally adjusted figures it stood only at 73.1 thousand. Meanwhile, employment components within IMEF indicators were favorable for both sectors, with both above the 50pts threshold. Within aggregate trend indicators, employment categories for construction, manufacturing, and commerce improved, with non-financial services as the only one lower. Finally, signals within *S&P Global*'s manufacturing PMI showed stability, albeit with larger challenges for the labor market, noting that "*A high churn rate negatively influenced headcounts at goods producers in February…*".

Despite an outlook mired with relevant risks, in our view the labor market remains strong, giving signs of little slack. This is very favorable for consumption in the year, expecting the latter to be an important driver for growth in 2023.

Unemployment rate
%, nsa



Source: INEGI, Banorte

Slight deceleration in banking credit in February, impacted by a challenging base. We anticipate growth in loans of 4.7% y/y in real terms, adding 11 months in positive territory. The moderation in the pace would be explained by a more difficult base effect, particularly for consumer loans, with dynamism persisting. Specifically, we believe resilience in economic activity, along with interest in investment related to nearshoring, would have kept pushing credit higher despite interest rate hikes. In addition, the arithmetic effect from inflation is positive, with the annual print moderating by 29bps to 7.62%. Nevertheless, families could have continued turning to credit to smooth their consumption patterns. Looking at the details, we expect consumer loans at 8.9% (previous: 9.0%), with corporates gathering pace at 3.5% (previous: 3.2%). Lastly, mortgages would be more stable at 3.7% (previous: 3.6%).

Presentation of the *Preliminary Economic Policy Criteria* for 2024. In line with the Budget and Fiscal Responsibility Law, the Ministry of Finance will present the *Preliminary Economic Policy Criteria* for fiscal-year 2024. The law sets April 1st as the deadline for submission. The document must contain: (1) Main objectives of the Revenue Law and the Spending Budget proposal; (2) scenarios for the main macroeconomic variables fin the upcoming year –including GDP, inflation, interest rate and oil price; (3) scenarios about the total amount of the Spending Budget and its balance –whether it presents a surplus or a deficit–; and (4) a list of priority programs and the amounts expected to be allocated to them. In addition, the MoF includes a detailed analysis of the global and domestic economy, as well as on public finances. Along the presentation of next year's estimates, they will also adjust their expectations for the current year, both for macroeconomic and fiscal variables, including projections for revenues and outlays.

We expect a keen focus in two main issues. First, estimated GDP growth for 2023, with the current forecast at 3.0% y/y. In our view, this could be revised down towards a lever closer to market and foreign institutions expectations. Second, potential adjustments to revenues, expenses, and the projected fiscal deficit Considering this, we do not rule out relevant modifications on Public Sector Borrowing Requirements (PSBR) and their Historical Balance (HBPSBR) –which represent the broadest measures of the public balance and debt–, currently estimated at -4.1% and 49.4% of GDP, in the same order.

Analyst Certification

We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Katia Celina Goya Ostos, Francisco José Flores Serrano, José Luis García Casales, Víctor Hugo Cortes Castro, José Itzamna Espitia Hernández, Carlos Hernández García, Leslie Thalía Orozco Vélez, Hugo Armando Gómez Solís, Yazmín Selene Pérez Enríquez, Cintia Gisela Nava Roa, Miguel Alejandro Calvo Domínguez, José De Jesús Ramírez Martínez, Gerardo Daniel Valle Trujillo, Luis Leopoldo López Salinas, Isaías Rodríguez Sobrino, Paola Soto Leal, Daniel Sebastián Sosa Aguilar and Andrea Muñoz Sánchez, 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.
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