October 20, 2023

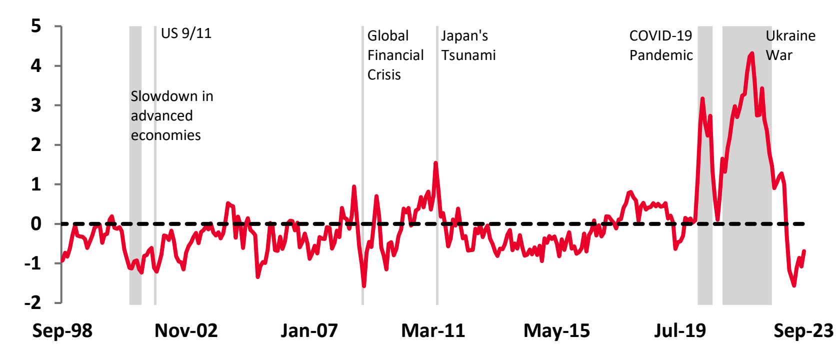
Mexico Economics – View from the Top

- **Structural and cyclical factors could influence negatively international trade dynamics and Mexico's trade balance in coming months**
- **On the weekly agenda, October's 1st half inflation, September's employment, and August's GDP-proxy**

Key factors for international trade… Trade flows have been recovering after the strong pandemic shock, which in Mexico was seen in a much larger imports' contraction. In this context, a series of structural and temporary factors will likely remain as an influence for the rest of 2023 and in 2024. Among the former, we highlight: (1) Geopolitical issues and the 'deglobalization' process; (2) trade disputes between China and the US; (3) the effects from nearshoring; and (4) climate change, with sizable effects on the prices of some goods and even on freight costs (*e.g.* extreme droughts in the Northern Hemisphere that have caused restrictions on crossing points such as the Panama Canal, with estimates that the restrictions will be binding at least until June 2024). On the latter, we can mention: (1) The cyclical divergence among regions, with greater strength in the US vs the Eurozone and China; (2) commodity price volatility, with increases in energy recently, but with declines in some agricultural goods; and (3) inflation, distorting signals about underlying strength in flows when nominal figures are used. In this backdrop, the World Trade Organization revised its 2023 growth forecast for global goods trade lower this month, to barely 0.8% y/y from 1.7% (April's estimate). For 2024, they forecast +3.3%. However, this assumes higher global growth that will trigger demand for durable goods, as well as machinery and equipment.

…and for supply chains. We believe that the normalization of inputs' supply and freight costs has supported trade. According to the New York Fed's *Global Supply Chain Pressure Index*, conditions have improved sharply since the beginning of 2022. However, towards the end of 2023 they could be more challenging, as warned by a potential trend change since last May (see chart below). Specifically, we do not rule out that some events may cause immediate pressure, such as: (1) The UAW's strike in the US, now in its 35th day, and expanding to more assembly plants; (2) an escalation of the Israel-Hamas conflict; and (3) a greater economic impact in China due to financial instability in the real estate sector.

New York Fed's Global Supply Chain Pressure Index
Standard deviation for average value



Source: Banorte with data from New York Fed

In Mexico, the exchange rate, inflation, and weather conditions will influence the non-oil balance. In addition to what has already been described, trade flows could be affected in the short-term by: (1) Mexican peso strength, driving imports higher; (2) relatively high inflation, which tends to increase trade growth rates in nominal terms; and (3) adverse weather conditions.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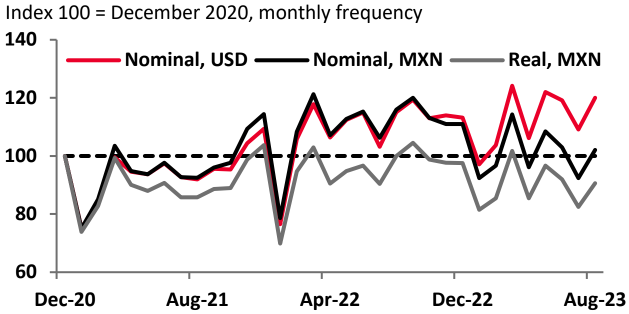
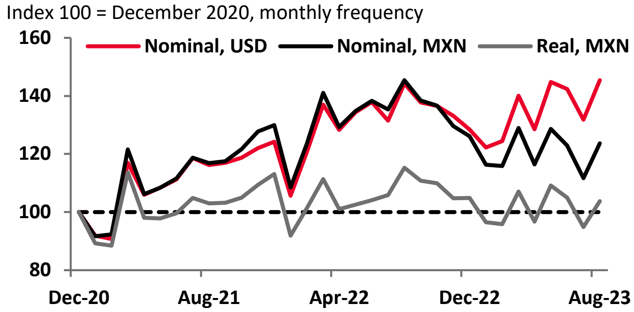
To illustrate the first two, the charts below show the effect of the exchange rate and inflation on exports and imports. When we convert flows to Mexican pesos, a more moderate increase is seen in the former and somewhat more stability in the latter. If we also deflate them, shipments abroad are lower than at the end of 2020, while purchases from the rest of the world continue to show an increase, albeit modest. This suggests that inflation is biasing growth of both flows upwards, while exchange rate appreciation is giving some support to imports –with stronger gains in consumer and capital goods. Auto exports also stand out, with dynamism despite US industrial weakness and high interest rates, although the strike will probably slow down this category in the short-term. Regarding climatological factors, *El Niño* began in June, causing high temperatures in the summer with repercussions on agricultural production –and, therefore, on exports. To this, we must add the possible effects of the hurricane and winter seasons.

Mexico's non-oil exports
Index 100 = December 2020, monthly frequency



Source: Banorte with data from INEGI, Banxico and FRED

Mexico's non-oil imports
Index 100 = December 2020, monthly frequency



Source: Banorte with data from INEGI, Banxico and FRED

Logistic problems in ports, customs, and railways can also be headwinds. Representatives of the auto sector have pointed out obstacles due to the saturation and lack of logistics infrastructure, delaying the transit of goods by one month on average (mainly in the Lázaro Cárdenas port). Land transportation was affected by the closure of the Córdova-Américas customs, with losses of US$1.7 billion in 23 days according to Chihuahua's state government. Meanwhile, the Texas Department of Public Safety intensified inspections of cargo transportation in Chihuahua and Nuevo León, triggering higher freight costs –up to ten times more– and transit times –in Ciudad Juárez, up to 19 thousand cargo vehicles were queuing, with an estimated 2 or 3 weeks to normalize flows. This is key since most goods are transported by land, with 61% of the total in 2022. Finally, *Ferromex* had a temporary stoppage of 40% of its freight trains, with an estimated daily loss of $40 million.

Calendar of economic events

Date	Time (ET)	Event or indicator	Period	Unit	Banorte	Consensus	Previous
Mon 23-Oct	8:00am	Monthly GDP-proxy IGAE	August	% a/a	3.5	3.5	3.2
		Monthly GDP-proxy IGAE*		% m/m	0.3	0.3	0.2
		Primary activities*		% m/m	0.9	--	-0.2
		Industrial production*		% m/m	0.3	--	0.5
		Services*		% m/m	0.2	--	-0.1
Tue 24-Oct	8:00am	CPI inflation	1Q-Oct	% 2w/2w	0.32	0.31	0.13
		CPI inflation		%y/y	4.35	4.34	4.47
		Core		%2w/2w	0.19	0.19	0.11
		Core		%y/y	5.49	5.49	5.74
Tue 24-Oct	11:00am	International reserves	Oct-20	US$ bn	--	--	204.1
Tue 24-Oct	11:00am	Government weekly auction: 1-, 3-, 6-, and 24-month Cetes; 5-year Mbono (Mar'29); 30-year Udibono (Nov'50) and 1-, 3-, 7-year Bondes F					
Thu 26-Oct	8:00am	Unemployment rate	September	%	2.93	--	2.96
		Unemployment rate*		%	2.74	--	2.72
Fri 27-Oct	8:00am	Trade balance	September	US$ mn	-223.8	-371.9	-1377.1
		Exports		% y/y	0.6	--	3.8
		Imports		% y/y	-0.7	--	-4.3

*Seasonally adjusted figures. Source: Banorte with figures from INEGI, Banxico, and Bloomberg

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, Juan Carlos Mercado Garduño, Daniel Sebastián Sosa Aguilar, Jazmin Daniela Cuautencos Mora 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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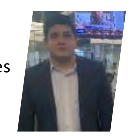

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