

# Ahead of the Curve

## Industry weakness in October driven by the auto sector

- Monthly inflation report (November).** We estimate headline inflation at +0.85% m/m and core inflation at 0.23%, remembering that period dynamics are seasonally high due to the reversal of electricity tariffs' subsidies in some states, which would contribute +40bps. Moreover, we see an additional uptick in LP gas, while both fruits and vegetables, and meat and egg, would also be relatively pressured. The core component would contribute 17bps, with 11bps corresponding to services and 6bps in goods. The latter would be benefitted in part by discounts during *El Buen Fin* (equivalent to Mexico's Black Friday), although more modest than in previous years. With these results, annual inflation would be at 3.02%, in line with the previous month. The non-core component would stay low at 1.14%, and core inflation would marginally improve to 3.66%
- Industrial production (October).** We anticipate a 3.1% yoy decline, below the -1.8% of September and which would mark a full-year in contraction. With seasonally-adjusted figures we estimate a 1.2% m/m decline. The month was likely impacted by adverse and temporary events in both mining and manufacturing –specifically, in the auto sector–. Moreover, construction likely stayed limited. Our forecast implies that industry would face an uphill battle in 4Q19, challenging our already modest estimate of a full-year 1.7% contraction. In particular, we are concerned by the signal sent by the IMEF manufacturing index in November, which did not rebound even as operations normalized in the auto sector

December 6, 2019

www.banorte.com  
@analisis\_fundam

**Juan Carlos Alderete, CFA**  
Senior Economist, Mexico  
juan.alderete.macal@banorte.com

**Francisco Flores**  
Economist, Mexico  
francisco.flores.serrano@banorte.com

Document for distribution among the general public

### Mexico weekly calendar

DATE	TIME (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 9-Dec	7:00am	CPI inflation	November	% m/m	<u>0.85</u>	0.83	0.54
				% yoy	<u>3.02</u>	3.01	3.02
		Core		% m/m	<u>0.23</u>	0.23	0.25
				% yoy	<u>3.66</u>	--	3.68
Mon 9-Dec	12:30pm	Government weekly auction: 1-, 3-, and 6-month Cetes; 3y MBono (Mar'23); 3y Udibono (Jun'22)					
Tue 10-Dec		Wage negotiations	November	%	<u>5.9</u>	--	4.0
Tue 10-Dec	10:00am	International reserves	Dec-7	US\$ bn	--	--	180.6
Thu 12-Dec	7:00am	Industrial production	October	% yoy	<u>-3.1</u>	-1.6	-1.8
		(sa)		% m/m	<u>-1.2</u>	--	0.0
		Mining		% yoy	<u>-3.9</u>	--	-2.8
		Utilities		% yoy	<u>1.9</u>	--	3.4
		Construction		% yoy	<u>-7.2</u>	--	-8.3
		Manufactures		% yoy	<u>-1.5</u>	--	0.8
Fri 13-Dec	10:00am	Banxico's survey of economic expectations	December				

Source: Banorte; Bloomberg

## Proceeding in chronological order...

**Annual inflation to remain stable and close to 3% despite higher agricultural goods' prices.** We estimate headline inflation at +0.85% m/m, above the 0.54% of the previous month. Core inflation is expected at 0.23% (previous: 0.25%). As already observed in the first half of the period, dynamics will be highly influenced by the reversal of electricity tariffs' subsidies in some states, contributing with +40bps. Regarding other energy goods, we expect an additional increase in LP gas (+3bps). Gasoline would remain relatively stable, despite upward adjustments in both the MXN and the reference price in the US, in a context of a slight decrease in the tax subsidy. In agricultural goods, fruits and vegetables would add 15bps. Our price monitoring showed relevant increases in onions and husk tomatoes, extending pressures already seen since the start of the month. In addition, we expect higher prices of poultry and eggs, with an +8bps contribution.

The core component would contribute 17bps, with 11bps corresponding to services. We expect housing to keep growing at a relatively steady pace (+3bps), with most pressures centered in other services (+8bps). Goods would add around 6bps, evenly divided between processed foods and other goods. On the latter, we did observe a benefit due to discounts during *El Buen Fin* (equivalent to Mexico's Black Friday), although less so than in previous years, remembering that the first day with discounts fell during the first half of the month.

With these results, annual inflation would be at 3.02%, in line with the previous month. The non-core component would stay low at 1.14%, increasing relative to the 1.01% of October. Core inflation would marginally improve to 3.66%, (previous: 3.68%). In this context, we still expect inflation to close the year at 3.0%, remembering that there will be a favorable base effect during the first half of December, which could help mitigate arising pressures in agricultural goods.

**Weekly government bond auction.** The Ministry of Finance (MoF) –via Banco de Mexico as its financial agent, will offer 3-year fixed-rate Mbonos (Mar'23), 3-year inflation-linked Udibonos (Jun'22), in addition to the 1-, 3-, and 6-month zero-coupon Cetes (see following table). As usual, results will be released at 12:30pm (ET).

### Auction specifics (Monday, December 9<sup>th</sup>, 2019)

	Maturity	Coupon rate, %	To be auctioned <sup>1</sup>	Previous yield <sup>2</sup>
<b>Cetes</b>				
1m	09-Jan-20	--	5,000	7.40
3m	14-Mar-20	--	15,000	7.44
6m	04-Jun-20	--	15,000	7.35
<b>M Bono</b>				
3y	09-Mar-23	6.75	10,500	6.62
<b>Udibonos</b>				
3y	09-Jun-22	2.00	UDIS 875	3.40

Source: Banorte with data from Banco de México 1. Except for Udibonos, which are expressed in UDI million, everything else is expressed in MXN million. 2. Yield-to-maturity reported for Cetes, Mbonos and Udibonos

**Wage negotiations to climb 5.9% in November.** This would be considerably higher than 4.0% previously. This increase would be explained by a change in the composition of workers benefited, with the private sector recovering share relative to public employees. In this context, revisions within the first group have averaged 6.3% so far this year, reaching only 3.4% in the second one. Going forward, attention will turn to the minimum wage increase for 2020, with our expectation for a 10-15% hike, which we believe will continue to be the main driver of wage dynamics.

**Weekly international reserves report.** Last week, net international reserves increased US\$40 million, closing at US\$180.6 billion. According to Banxico's report, this comes from a positive valuation effect in central bank assets. In this context, the central bank's international reserves have increased US\$5.8 billion during 2019 (please refer to the following table).

**Banxico's foreign reserve accumulation detail**

US\$, million

	2018	Nov 29, 2019	Nov 29, 2019	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	174,793	180,597	40	5,805
(B) Gross international reserve	176,384	185,289	525	8,905
Pemex	--	--	32	97
Federal government	--	--	325	3,116
Market operations	--	--	0	0
Other	--	--	168	5,693
(C) Short-term government's liabilities	1,592	4,692	485	3,100

Source: Banco de México

**Industrial production weakness in October, because of autos.** We anticipate a 3.1% yoy decline, which would mark a full-year in contraction and its weakest print in this period. With seasonally-adjusted figures we anticipate a 1.2% m/m decline. The month was likely impacted by adverse and temporary events in both mining –particularly oil services– and manufacturing –specifically, in the auto sector–. Moreover, construction likely stayed limited. On a supply-side point of view, industry remains as the most relevant drag to GDP growth.

We estimate mining at -3.9% yoy, below the -2.8% observed in August. According to Pemex, oil production averaged 1,681kbpd, representing a 4.9% fall in annual terms. Gas was slightly better at 1.6%. It should be mentioned that according to the company's CEO, Octavio Romero, scheduled maintenance works were already anticipated to impact production of oil-based products, likely affecting services provided to the industry. In terms of employment, job creation seems to be stabilizing but has stayed below levels during the same period of the previous year (-1.0% yoy). Overall, we continue anticipating that stabilization in oil production is likely to add to growth in 2020, sector which has been a persistent drag for industry during a prolonged period.

Apart from this, our muted forecast is mainly driven by manufacturing, which would contract 1.5% yoy, weakest since June 2013. As already shown in trade balance and AMIA's production figures (with finished vehicles at -16.3% yoy), autos were impacted by GM's strike in the US –resolved until October 25<sup>th</sup>– and the temporary close of two Ford plants and one by VW.

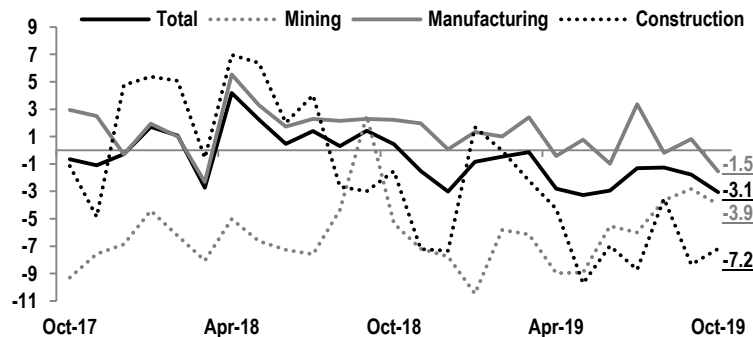
In this respect, manufacturing exports and non-oil intermediate goods imports were very weak, also reflected in US IP which has contracted for four consecutive months in annual terms. Employment data did not signal this performance, albeit not very surprising as temporarily halting operations was not equated with layoffs.

Lastly, disappointing results in construction would extend, estimated at -7.2% yoy. In our view, the fact that the sector's business confidence until November has reversed the uptick observed in September points to prevailing weakness, with the 'adequate moment to invest' component also quite weak. Employment levels seem to be improving slightly but remain lower than in the same period of 2018, falling 2.3% yoy. Overall, available data suggests that challenges for the sector remain high.

All in all, our forecast would imply that industry will face an uphill battle in 4Q19, challenging our already modest estimate of a full-year 1.7% contraction. In particular, we are concerned by the signal sent by the IMEF manufacturing index in November, which did not rebound even as operations in the auto sector normalized, in a context in which trade uncertainty remains in place despite news pointing to a potential resolution in tensions between the US and China.

**Industrial production**

% yoy



Source: INEGI, Banorte

**Banxico's survey of economic expectations.** As usual, market participants will focus on inflation, growth, the reference rate, and exchange rate forecasts. Regarding the first, analysts expect 2019 year-end inflation at 2.95%, practically in line with our 3.00% estimate. Medium and long-term expectations could remain relatively unchanged, still above target. On growth, the estimate for 2019 stood at 0.0% in the previous survey (Banorte: -0.1%), while 2020's print came in at 1.07% (Banorte: 1.4%). The current view on the reference rate by YE19 is 7.25%, in line with our expectations. For 2020, consensus points to 75bps of easing (Banorte: -125bps). Finally, the exchange rate estimate for year-end 2019 stands at USD/MXN 19.48 (Banorte: 20.30). In addition, forecasts for YE20 stand at 20.00, below our 21.30.

**Disclaimer**

The information contained in this document is illustrative and informative so it should not be considered as an advice and/or recommendation of any kind. BANORTE is not part of any party or political trend.

## Analyst Certification

We, Gabriel Casillas Olvera, Delia Maria Paredes Mier, Alejandro Padilla Santana, Manuel Jiménez Zaldívar, Tania Abdul Massih Jacobo, Katia Celina Goya Ostos, Juan Carlos Alderete Macal, Víctor Hugo Cortes Castro, Marissa Garza Ostos, Miguel Alejandro Calvo Domínguez, Hugo Armando Gómez Solís, Gerardo Daniel Valle Trujillo, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Santiago Leal Singer, Francisco José Flores Serrano, Luis Leopoldo López Salinas, Jorge Antonio Izquierdo Lobato, Eridani Ruibal Ortega and Leslie Thalia Orozco Vélez, 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.

## Relevant statements

In accordance with current laws and internal procedures manuals, analysts are allowed to hold long or short positions in shares or securities issued by companies that are listed on the Mexican Stock Exchange and may be the subject of this report; nonetheless, equity analysts have to adhere to certain rules that regulate their participation in the market in order to prevent, among other things, the use of private information for their benefit and to avoid conflicts of interest. Analysts shall refrain from investing and holding transactions with securities or derivative instruments directly or through an intermediary person, with Securities subject to research reports, from 30 calendar days prior to the issuance date of the report in question, and up to 10 calendar days after its distribution date.

### Compensation of Analysts.

Analysts' compensation is based on activities and services that are aimed at benefiting the investment clients of Casa de Bolsa Banorte and its subsidiaries. Such compensation is determined based on the general profitability of the Brokerage House and the Financial Group and on the individual performance of each analyst. However, investors should note that analysts do not receive direct payment or compensation for any specific transaction in investment banking or in other business areas.

### Last-twelve-month activities of the business areas.

Grupo Financiero Banorte S.A.B. de C.V., through its business areas, provides services that include, among others, those corresponding to investment banking and corporate banking, to a large number of companies in Mexico and abroad. It may have provided, is providing or, in the future, will provide a service such as those mentioned to the companies or firms that are the subject of this report. Casa de Bolsa Banorte or its affiliates receive compensation from such corporations in consideration of the aforementioned services.

Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

### Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

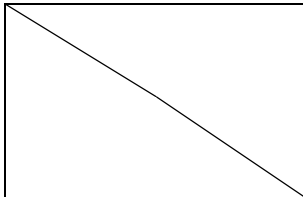
### Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1 % of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

### Guide for investment recommendations.

	<b>Reference</b>
<b>BUY</b> <b>HOLD</b> <b>SELL</b>	When the share expected performance is greater than the MEXBOL estimated performance. When the share expected performance is similar to the MEXBOL estimated performance. When the share expected performance is lower than the MEXBOL estimated performance.

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

### Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V., since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

The information contained hereby has been obtained from sources that we consider to be reliable, but we make no representation as to its accuracy or completeness. The information, estimations and recommendations included in this document are valid as of the issue date, but are subject to modifications and changes without prior notice; Grupo Financiero Banorte S.A.B. of C.V. does not commit to communicate the changes and also to keep the content of this document updated. Grupo Financiero Banorte S.A.B. of C.V. takes no responsibility for any loss arising from the use of this report or its content. This document may not be photocopied, quoted, disclosed, used, or reproduced in whole or in part without prior written authorization from Grupo Financiero Banorte S.A.B. of C.V.

**GRUPO FINANCIERO BANORTE S.A.B. de C.V.**
**Research and Strategy**

Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967

**Economic Analysis**

Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Katia Celina Goya Ostos	Senior, Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Juan Carlos Alderete Macal, CFA	Senior Economist, Mexico	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Miguel Alejandro Calvo Domínguez	Economist, Regional	miguel.calvo@banorte.com	(55) 1670 - 2220
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Luis Leopoldo López Salinas	Analyst, Global Economist	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611

**Fixed income and FX Strategy**

Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Santiago Leal Singer	FX Senior Strategist	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Fixed Income and FX Strategist	leslie.orozco.velez@banorte.com	(55) 5268 - 1698

**Equity Strategy**

Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Víctor Hugo Cortes Castro	Technical Analysis	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Equity Research – Conglomerates / Financials/ Mining / Petrochemicals	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research – Airlines / Airports / Cement / Infrastructure / REITs	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 – 4000 x 2755
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251

**Corporate Debt**

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Manager, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248

**Wholesale Banking**

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebaldos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Corporate Banking	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.rolan.ferrer@banorte.com	(55) 5004 - 1454