Outline

1. External conditions
2. Current situation of the Mexican economy
3. Inflation
4. Monetary policy
5. Final remarks
The COVID-19 pandemic implied shocks that had a widespread impact on all countries, with repercussions on economic activity, inflation and global financial conditions.

<table>
<thead>
<tr>
<th>Health Dimension</th>
<th>Economic Dimension</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Advanced 1/</strong></td>
<td><strong>Emerging 1/</strong></td>
</tr>
<tr>
<td>Cumulative cases</td>
<td>53,333,794</td>
</tr>
<tr>
<td>Cumulative deaths</td>
<td>1,110,598</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Global economic activity continued to recover at a more moderate rate and heterogeneously across countries and sectors. However, pre-pandemic levels have not been reached yet and risks persist.

**World Economy**

**GDP Growth**
Quarterly % change, s. a.

2008 crisis  
2020 crisis  
Emerging  
Emerging excluding China  
Advanced

Start of the crisis 1/

Quarters since the start of the crisis

-6 -5 -4 -3 -2 -1 0 1 2 3 4 5 6

-12 -8 -4 0 4 8

World  
Advanced  
Emerging  
Emerging exc. China

**GDP Growth Forecast**

%  

World  
Advanced  
Emerging  
Emerging exc. China

-4.4 -3.3 -3.5 -2.4  
-5.8 -5.8 -4.9 -4.6  
5.2 3.9 5.5 4.3  
6.0 4.9 6.3 5.4

Source: International Monetary Fund (IMF), World Economic Outlook January 2021.

1/ The start of the 2008 crisis is considered to be Q4-2007, and the start of the 2020 crisis Q1-2020, according to the NBER. Note: The sample of countries used for the calculations represents 85.6% of world GDP measured by purchasing power parity. Forecasts for some sample countries are used in Q3-2020. Source: Prepared by Banco de México with data from Haver Analytics, J.P. Morgan, International Monetary Fund (IMF) and NBER.
After the significant increase in risk aversion in March and April and the important capital outflows in emerging economies, international financial markets have improved, mainly due to the gradual global economic recovery and the monetary and fiscal measures adopted in the main economies.

Global Risk Aversion Index

Accumulated Capital Flows to Emerging Economies Excluding China

Accumulated Flows of Foreign Investment in Government Securities and Equity to Mexico

Note: The sample covers funds used for the buying-selling of stocks and bonds from emerging countries, recorded in advanced countries. Flows exclude portfolio performance and exchange rate fluctuations.

Source: Emerging Portfolio Fund Research.

Note: Total includes: Equity, Bonds, Cetes, Udibonos and other government securities.

Source: Banco de México with data from Indeval.
The emerging economies have faced lower external income due to the weakness of commodity prices, especially energy, and pressure on their spreads and sovereign risk premia, which have moderated in recent months.

Commodity Prices
Index 2014 = 100

1/ Includes Precious Metals, Food and Beverages and Industrial Inputs Price Indices.
2/ Includes Crude oil (petroleum), Natural Gas, Coal Price and Propane Indices.

Source: International Monetary Fund.

EMBI Spread by Credit Rating
Index

Source: Bloomberg.
Inflation in advanced economies has remained low an below central bank targets, while in emerging economies the behavior has been more heterogeneous.

**Advanced Countries**

**Emerging Latin American Countries**

1/ Refers to the Personal Consumption Expenditure Price Index (PCE). Source: BEA, Eurostat and Bank of Japan (see Box 6 of the April-June 2020 Quarterly Inflation Report).

Source: Prepared by Banco de México with information from Haver Analytics (see Box 6 of the April-June 2020 Quarterly Inflation Report).
Given the economic contraction, a downward adjustment of the yield curve is desirable. In advanced economies, the weakness of the demand and the expectation of low short-term rates for a prolonged period, together with moderate risk premia, have contributed to keep long-term rates at low levels.

Monetary Policy Rates of Advanced Economies 1/

1/ For the U.S., the midpoint of the target range for the federal funds rate is used. Source: Haver Analytics (see Box 7 of the July-September 2020 Quarterly Report).

10-year Government Bonds Interest Rates

30-year Government Bonds Interest Rates

Source: Bloomberg.
Among emerging economies, financing costs in Mexico have decreased considerably and long-term interest rates show a more favorable adjustment compared with other economies, as risk premia have decreased to a greater extent.

Monetary Policy Rates of Emerging Economies

10-year Government Bonds Interest Rates

Source: Haver Analytics (see Box 7 of the July-September 2020 Quarterly Report).

Source: Bloomberg (see Box 7 of the July-September 2020 Quarterly Report).
Outline

1. External conditions
2. Current situation of the Mexican economy
3. Inflation
4. Monetary policy
5. Final remarks
Economic activity in Mexico improved during the Q4-2020 at a slightly higher-than-foreseen rate, although it remains below the levels prior to the pandemic.
<table>
<thead>
<tr>
<th>Sectors that have recovered their pre-pandemic levels (20.7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services:</td>
</tr>
<tr>
<td>70</td>
</tr>
<tr>
<td>Non-manufacturing industrial services:</td>
</tr>
<tr>
<td>100</td>
</tr>
<tr>
<td>Primary:</td>
</tr>
<tr>
<td>110</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Sectors that remain less than 5% below their pre-pandemic levels (57.3%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services:</td>
</tr>
<tr>
<td>110</td>
</tr>
<tr>
<td>Non-manufacturing industrial services:</td>
</tr>
<tr>
<td>100</td>
</tr>
<tr>
<td>Primary:</td>
</tr>
<tr>
<td>70</td>
</tr>
</tbody>
</table>

### Global Index of Economic Activity and its Components

**Average of Dec 2019 - Feb 2020 = 100, s. a.**

<table>
<thead>
<tr>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
<th>Apr</th>
<th>May</th>
<th>Jun</th>
<th>Jul</th>
<th>Aug</th>
<th>Sep</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oil and coal derivatives</td>
<td>105.1</td>
<td>85.8</td>
<td>99.3</td>
<td>98.2</td>
<td>100.7</td>
<td>100.0</td>
<td>79.7</td>
<td>92.4</td>
<td>113.6</td>
<td>112.9</td>
<td>95.6</td>
</tr>
<tr>
<td>Computer, communication, measurement eq.</td>
<td>100.1</td>
<td>100.5</td>
<td>100.3</td>
<td>78.6</td>
<td>78.3</td>
<td>95.6</td>
<td>104.9</td>
<td>100.8</td>
<td>104.5</td>
<td>104.5</td>
<td>102.4</td>
</tr>
<tr>
<td>Plastic and rubber</td>
<td>98.8</td>
<td>99.8</td>
<td>97.0</td>
<td>65.9</td>
<td>60.2</td>
<td>82.9</td>
<td>93.0</td>
<td>99.5</td>
<td>100.8</td>
<td>102.6</td>
<td>100.6</td>
</tr>
<tr>
<td>Electrical appliances and electrical power eq.</td>
<td>101.7</td>
<td>98.3</td>
<td>101.0</td>
<td>89.2</td>
<td>79.0</td>
<td>82.5</td>
<td>99.1</td>
<td>102.5</td>
<td>106.6</td>
<td>107.1</td>
<td>108.6</td>
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<td>Wholesale trade</td>
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<td>97.8</td>
<td>84.6</td>
<td>71.6</td>
<td>90.4</td>
<td>93.2</td>
<td>96.2</td>
<td>97.0</td>
<td>98.8</td>
<td>107.0</td>
</tr>
<tr>
<td>Metal products</td>
<td>100.2</td>
<td>99.0</td>
<td>98.3</td>
<td>82.6</td>
<td>74.7</td>
<td>78.4</td>
<td>97.6</td>
<td>99.4</td>
<td>100.4</td>
<td>104.1</td>
<td>102.6</td>
</tr>
<tr>
<td>Primary activities</td>
<td>102.5</td>
<td>95.5</td>
<td>106.4</td>
<td>102.8</td>
<td>104.3</td>
<td>98.7</td>
<td>112.4</td>
<td>106.7</td>
<td>107.8</td>
<td>108.3</td>
<td>108.4</td>
</tr>
<tr>
<td>Mining of metallic and non-metallic minerals</td>
<td>99.8</td>
<td>101.2</td>
<td>94.0</td>
<td>68.8</td>
<td>69.2</td>
<td>87.5</td>
<td>96.7</td>
<td>98.7</td>
<td>100.1</td>
<td>102.6</td>
<td>101.9</td>
</tr>
<tr>
<td>Non-metallic mineral based products</td>
<td>99.6</td>
<td>100.4</td>
<td>98.4</td>
<td>60.8</td>
<td>68.6</td>
<td>82.6</td>
<td>91.5</td>
<td>97.7</td>
<td>98.6</td>
<td>99.8</td>
<td>100.5</td>
</tr>
<tr>
<td>Food</td>
<td>99.9</td>
<td>100.0</td>
<td>100.8</td>
<td>99.7</td>
<td>98.4</td>
<td>98.7</td>
<td>99.6</td>
<td>98.8</td>
<td>100.0</td>
<td>100.3</td>
<td>100.1</td>
</tr>
<tr>
<td>Paper</td>
<td>101.4</td>
<td>99.5</td>
<td>98.3</td>
<td>94.5</td>
<td>98.4</td>
<td>92.0</td>
<td>97.7</td>
<td>98.2</td>
<td>97.8</td>
<td>97.8</td>
<td>98.3</td>
</tr>
<tr>
<td>Textile industry and textile finishing</td>
<td>98.3</td>
<td>100.9</td>
<td>98.1</td>
<td>86.1</td>
<td>94.1</td>
<td>71.2</td>
<td>82.9</td>
<td>89.2</td>
<td>89.8</td>
<td>91.1</td>
<td>98.7</td>
</tr>
<tr>
<td>Machine and equipment</td>
<td>103.8</td>
<td>97.5</td>
<td>95.9</td>
<td>79.0</td>
<td>81.5</td>
<td>76.5</td>
<td>82.6</td>
<td>87.8</td>
<td>97.5</td>
<td>98.3</td>
<td>98.3</td>
</tr>
<tr>
<td>Educational; health and social assistance</td>
<td>99.6</td>
<td>99.8</td>
<td>99.0</td>
<td>99.4</td>
<td>99.0</td>
<td>98.9</td>
<td>97.4</td>
<td>99.4</td>
<td>99.4</td>
<td>99.8</td>
<td>99.5</td>
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<tr>
<td>Construction specialized jobs</td>
<td>100.9</td>
<td>99.2</td>
<td>96.9</td>
<td>76.0</td>
<td>69.5</td>
<td>82.0</td>
<td>84.3</td>
<td>90.1</td>
<td>97.3</td>
<td>97.4</td>
<td>96.2</td>
</tr>
<tr>
<td>Utilities</td>
<td>101.9</td>
<td>99.7</td>
<td>98.3</td>
<td>95.7</td>
<td>94.9</td>
<td>96.3</td>
<td>93.8</td>
<td>97.5</td>
<td>98.1</td>
<td>98.5</td>
<td>99.1</td>
</tr>
<tr>
<td>Textile inputs and textile finishing</td>
<td>98.6</td>
<td>100.1</td>
<td>98.4</td>
<td>82.9</td>
<td>87.6</td>
<td>77.3</td>
<td>86.5</td>
<td>92.0</td>
<td>92.8</td>
<td>97.8</td>
<td>98.3</td>
</tr>
<tr>
<td>Basic metal</td>
<td>103.8</td>
<td>97.5</td>
<td>95.9</td>
<td>79.0</td>
<td>81.5</td>
<td>76.5</td>
<td>82.6</td>
<td>87.8</td>
<td>97.5</td>
<td>98.3</td>
<td>98.3</td>
</tr>
<tr>
<td>Other manufacturing industries</td>
<td>99.8</td>
<td>99.9</td>
<td>90.0</td>
<td>73.3</td>
<td>77.3</td>
<td>82.1</td>
<td>90.2</td>
<td>96.5</td>
<td>97.6</td>
<td>97.4</td>
<td>99.3</td>
</tr>
<tr>
<td>Transport equipment</td>
<td>101.4</td>
<td>102.8</td>
<td>82.9</td>
<td>14.1</td>
<td>20.7</td>
<td>75.1</td>
<td>94.0</td>
<td>91.3</td>
<td>96.2</td>
<td>96.1</td>
<td>96.5</td>
</tr>
<tr>
<td>Wood</td>
<td>99.1</td>
<td>99.7</td>
<td>97.9</td>
<td>63.5</td>
<td>57.9</td>
<td>75.6</td>
<td>84.5</td>
<td>91.0</td>
<td>93.9</td>
<td>98.1</td>
<td>100.4</td>
</tr>
<tr>
<td>Retail trade</td>
<td>100.0</td>
<td>99.5</td>
<td>97.2</td>
<td>67.5</td>
<td>67.2</td>
<td>80.0</td>
<td>89.4</td>
<td>92.1</td>
<td>93.1</td>
<td>96.9</td>
<td>99.7</td>
</tr>
<tr>
<td>Textile products, except garments</td>
<td>103.5</td>
<td>99.0</td>
<td>99.5</td>
<td>41.4</td>
<td>54.8</td>
<td>73.2</td>
<td>91.2</td>
<td>93.6</td>
<td>95.4</td>
<td>96.4</td>
<td>95.8</td>
</tr>
<tr>
<td>Chemical</td>
<td>99.7</td>
<td>99.5</td>
<td>101.1</td>
<td>94.4</td>
<td>88.6</td>
<td>91.5</td>
<td>94.8</td>
<td>97.5</td>
<td>97.7</td>
<td>98.8</td>
<td>98.4</td>
</tr>
<tr>
<td>Financial and insurance; real estate and rental services</td>
<td>100.3</td>
<td>100.1</td>
<td>100.3</td>
<td>97.3</td>
<td>99.5</td>
<td>98.8</td>
<td>98.5</td>
<td>98.8</td>
<td>99.0</td>
<td>99.0</td>
<td>98.7</td>
</tr>
<tr>
<td>Production of comp. of. and enterprises</td>
<td>100.2</td>
<td>99.7</td>
<td>99.6</td>
<td>99.1</td>
<td>99.4</td>
<td>99.4</td>
<td>99.6</td>
<td>98.5</td>
<td>98.5</td>
<td>98.1</td>
<td>96.6</td>
</tr>
<tr>
<td>Oil and gas extraction</td>
<td>101.4</td>
<td>100.3</td>
<td>100.1</td>
<td>99.4</td>
<td>99.4</td>
<td>99.4</td>
<td>99.6</td>
<td>98.5</td>
<td>98.5</td>
<td>98.1</td>
<td>96.6</td>
</tr>
<tr>
<td>Oil and coal derivatives</td>
<td>105.1</td>
<td>85.8</td>
<td>99.3</td>
<td>98.2</td>
<td>100.7</td>
<td>100.0</td>
<td>79.7</td>
<td>92.4</td>
<td>113.6</td>
<td>112.9</td>
<td>95.6</td>
</tr>
</tbody>
</table>

*Note: Figures in parentheses represent their share in 2013.*

1/ Obtained as the index in each month over its average during the period Dec-2019 to Feb-2020 multiplied by one hundred.

Source: Prepared by Banco de México with data from INEGI.
Private consumption and gross fixed investment have shown some improvement since June, although in recent months the rate of recovery has moderated, remaining significantly below their pre-pandemic levels.
During the second half of 2020, exports showed a relatively faster recovery than imports. For 2020 as a whole, the current account surplus was 2.4% of GDP, the highest surplus reported since 1983.
After having significantly deteriorated as a result of the COVID-19 pandemic, various labor market indicators improved during the second half of 2020, although remaining weak in the last months of the year.

National Unemployment Rate\(^1\)\n\% \(\text{, o. s.}\)

Employed Population by Condition of Occupation\(^2\)
\text{Million people}

IMSS-insured Jobs, Total IGAE and Employed Population
Index 2020=100, s. a.
After having widened significantly in Q2-2020, slack conditions partially reversed this trend in the second half of 2020, although they still remain at historically wide levels.

**Output Gap Estimate**

% of potential output, s. a.

**Monthly Slack Indicators: Main Component by Indicators Frequency**

%
Outline

1. External conditions
2. Current situation of the Mexican economy
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4. Monetary policy
5. Final remarks
Inflation continues to be influenced by the effects of the COVID-19 pandemic. After registering 2.15% in April, it rose to 4.09% in October, but has since decreased to 3.84% in F1-February.

1/ Since 2003, a permanent inflation target of 3%, with a variability interval of +/-1%, was established for headline inflation. Source: Banco de México and INEGI.
Core inflation components were affected by the shocks caused by COVID-19. In the first months of the pandemic, there was an increase in inflation of food merchandise and a decrease in that of services. In November, non-food merchandise inflation registered significant downward pressures mainly associated with the longer duration and greater intensity of the “Buen Fin” discount sales. In F1-February, core inflation increased, largely because the effects of this discounts faded.

Core Inflation: Deviation from Monthly Change s.a. Historical Average

Min. and Max. Deviation from Historical Average

F1-Feb-21

Core Merchandise
Food merchandise
Sugar products
Corn products
Sausages
Alcoholic beverages
Wheat products
Soy products
Dairy products
Rest of food merchandise
Non-food merchandise
Transport and cars
Household app. and furniture
Clothing and footwear
Hygiene and care
Medicines
Household cleaning products
Entertainment material
Rest of non-food merchandise
Services
Housing
Education
Rest of services
Tourism services
Other services

s. a. / Seasonally adjusted figures as of the F1-February 2021. The historical average considers the years from 2010 to 2019. For the minimum and maximum, the period from January 2020 to the F1-February 2021 is considered.

Source: Seasonal adjustment prepared by Banco de México with INEGI data.
There has been a noticeable heterogeneity in the annual variation of the core sub-index components.

Standard Deviation of the Annual Variation of the Components that Make Up Each Group of the CPI

Weighted Density Functions of Accumulated Inflation from February 2020 to F1-February 2021 by City

1/ The annual inflation of each item of the CPI is constructed and then the standard deviation of the components of each index and sub-index is obtained. Information as of F1-February 2021. Source: Banco de México (see the Box 5 of the April-June 2020 Quarterly Report).

Source: Banco de México and INEGI.
Outline

1. External conditions
2. Current situation of the Mexican economy
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5. Final remarks
In 2020 Banco de México’s Governing Board lowered the reference rate by 300 basis points. After a pause in the November and December decisions, in February 2021, interest rate was lowered 25pb to a level of 4.00%.

Target for the Overnight Interbank Interest Rate and Headline Inflation

1/ %, annual % change

1/The data shown up to January 20, 2008 corresponds to the overnight interbank interest rate (policy rate). Source: Prepared by Banco de México with INEGI data.

Short-term Ex-Ante Real Rate and Estimated Range for the Short-term Neutral Real Rate in the Long Term

2/ %

2/ The short-term ex-ante real rate is constructed using the Target for the Overnight Interbank Interest Rate and 12-month inflation expectations from Banco de México’s Survey. The dotted line corresponds to the midpoint of the range for the short-term neutral real rate in the long term, which is now between 1.8 and 3.4%. Source: Banco de México.
Short- and medium-term interest rates decreased, partly reflecting Banco de México's monetary policy decisions, while long-term rates have achieved an orderly downward adjustment and are below pre-pandemic levels.

Note: The gray lines refer to the daily yield curves since March 18, 2020.

Source: Proveedor Integral de Precios (PIP).
As a result of improved international financial conditions, a recovery was observed in emerging market foreign currencies and sovereign risk indicators during Q3 and Q4-2020, although an important heterogeneity across this group of economies is observed.

Emerging Economies

Nominal Exchange Rate against USD
Index Jan-01-2020=100

Source: Bloomberg.

CDS of Selected Emerging Economies
Basis points

Source: Bloomberg.
Due to the pandemic, the Mexican economy faced a tightening of financial conditions, although this tightening was less severe than that registered in the crisis of 1994 and 2008.

1/ The index is constructed using an autoregressive vector model with time-varying factors (Koop / Korobilis, 2014). Preliminary information was used for the December timely GDP (IGAE) and for the Q4-2020 credit gap. Source: Prepared by Banco de México with data from Bloomberg, BMV and INEGI (see Box 3 of the Financial Stability Report, December 2020).


3/ It refers to the real exchange rate with respect to a group of 111 countries. Source: Bank of Mexico and INEGI (see Box 3 of the Financial Stability Report, December 2020).
Outline

1. External conditions
2. Current situation of the Mexican economy
3. Inflation
4. Monetary policy
5. Final remarks
Final Remarks

- The Governing Board will take the necessary actions, on the basis of incoming information, so that the reference rate is consistent with the orderly and sustained convergence of headline inflation to the 3% target, during the time frame in which monetary policy operates.

- The risks for inflation, economic activity and financial markets pose major challenges for monetary policy and for the economy. In this regard, it is necessary to enable an orderly adjustment that allows for a change in relative prices, without affecting the price formation process and inflation expectations.

- Monetary policy implementation will depend on the evolution of the factors that affect headline and core inflation, their foreseen trajectories within the forecast horizon and their expectations.

- Perseverance in strengthening the macroeconomic fundamentals and adopting the necessary actions, regarding both monetary and fiscal policies, will contribute to a better adjustment of domestic financial markets and of the economy as a whole.

- It is necessary to contribute to an orderly adjustment of the economy, thus promoting the reactivation of productive activity and employment, enabling flexibility in resource allocation, ensuring proper microeconomic functioning, and addressing institutional and structural problems.