Quarterly Report
October – December 2020

March 3, 2021

BANCO DE MÉXICO

Outline

1	**External conditions**
2	Current situation of the Mexican economy
3	Inflation
4	Monetary policy
5	Forecasts and final remarks

The COVID-19 pandemic implied shocks that affected countries in a generalized manner, with repercussions in economic activity, inflation and on global financial conditions.

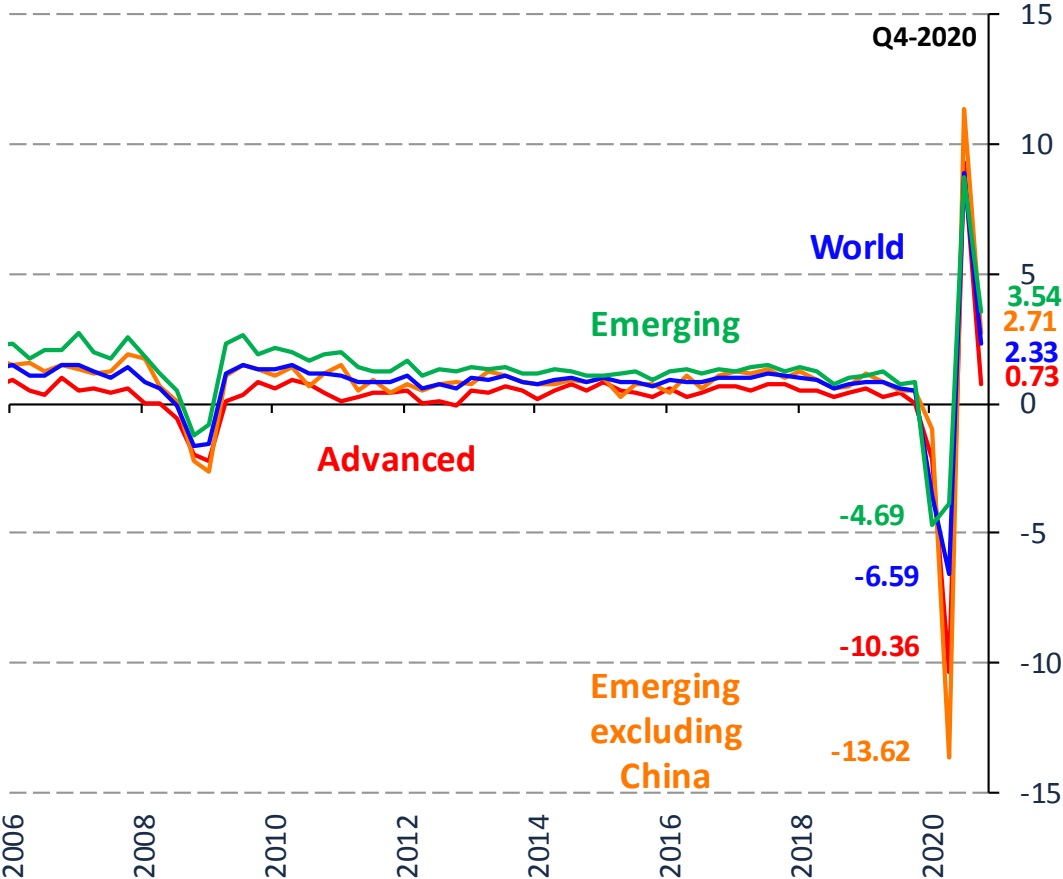| Health Dimension				Economic Dimension		
	Advanced [1]	Emerging [1]	Mexico [2]	Financial shock	Supply shock	Demand shock
Cumulative cases	54,554,193	59,585,911	2,291,883	• Increased global risk aversion. • Capital outflows. • Exchange rate depreciation. • Interest rate increase. • Increased sovereign risk.	• Suspension of productive activities. • Impact: – Global value chains. – In-person services.	• Lower household and business income. • Recomposition of household expenditure.
Cumulative deaths	1,140,298	1,395,222	187,187			

1/ Data as of March 02, 2021. Source: World Health Organization.
2/ Data as of March 02, 2021. Source: Health Ministry of Mexico.

Available information to Q4-2020 suggests that world economic activity continued to recover, albeit moderately and heterogeneously across countries and sectors. Forecasts by multilateral organizations continue to anticipate that the global economy will rebound in 2021. However, this outlook is still subject to high uncertainty.

World Economy

GDP Growth
Quarterly % change, s. a.

Q4-2020

World
Emerging
Advanced
Emerging excluding China

3.54
2.71
2.33
0.73

-4.69
-6.59
-10.36
-13.62

15
10
5
0
-5
-10
-15

2006 2008 2010 2012 2014 2016 2018 2020

s. a. / Seasonally adjusted figures.
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 the fourth quarter.
Source: Prepared by Banco de México with data from Haver Analytics, J.P. Morgan and International Monetary Fund (IMF).

GDP Growth Forecast
Annual % change

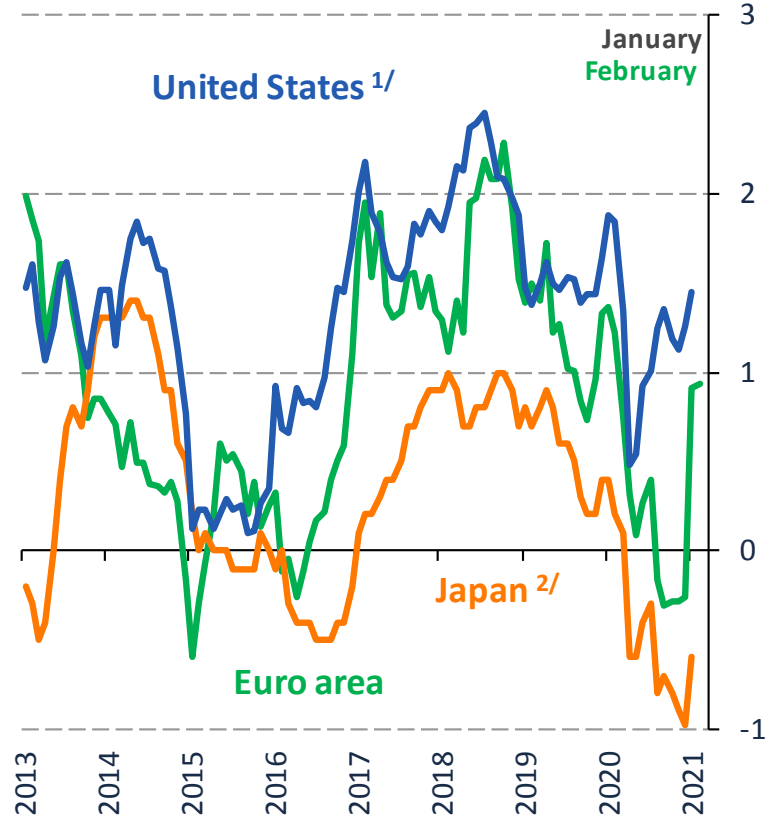|	WEO Update			Change from		
	January 2021			October 2020		
	2020	2021	2022	2020	2021	2022
World	**-3.5**	**5.5**	**4.2**	**0.9**	**0.3**	**0.0**
Advanced	**-4.9**	**4.3**	**3.1**	**0.9**	**0.4**	**0.2**
United States	-3.4	5.1	2.5	0.9	2.0	-0.4
Euro area	-7.2	4.2	3.6	1.1	-1.0	0.5
Japan	-5.1	3.1	2.4	0.2	0.8	0.7
United Kingdom	-10.0	4.5	5.0	-0.2	-1.4	1.8
Emerging	**-2.4**	**6.3**	**5.0**	**0.9**	**0.3**	**-0.1**
Excl. China	-4.6	5.4	4.7	1.1	0.5	-0.1
Mexico	**-8.5**	**4.3**	**2.5**	**0.5**	**0.8**	**0.2**
China	2.3	8.1	5.6	0.4	-0.1	-0.2
India	-8.0	11.5	6.8	2.3	2.7	-1.2
Brazil	-4.5	3.6	2.6	1.3	0.8	0.3

Source: International Monetary Fund (IMF), World Economic Outlook October 2020 and January 2021.

In the major advanced economies, inflation remains below their central banks' targets, although inflation expectations have been revised upwards in some countries mainly due to prospects of a greater fiscal stimulus and a more vigorous economic recovery.
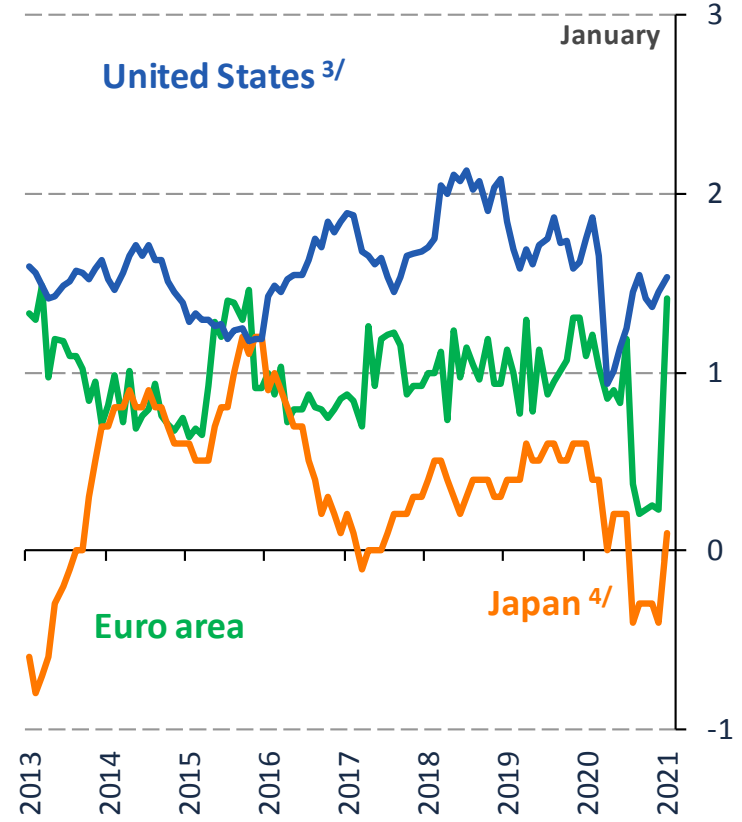
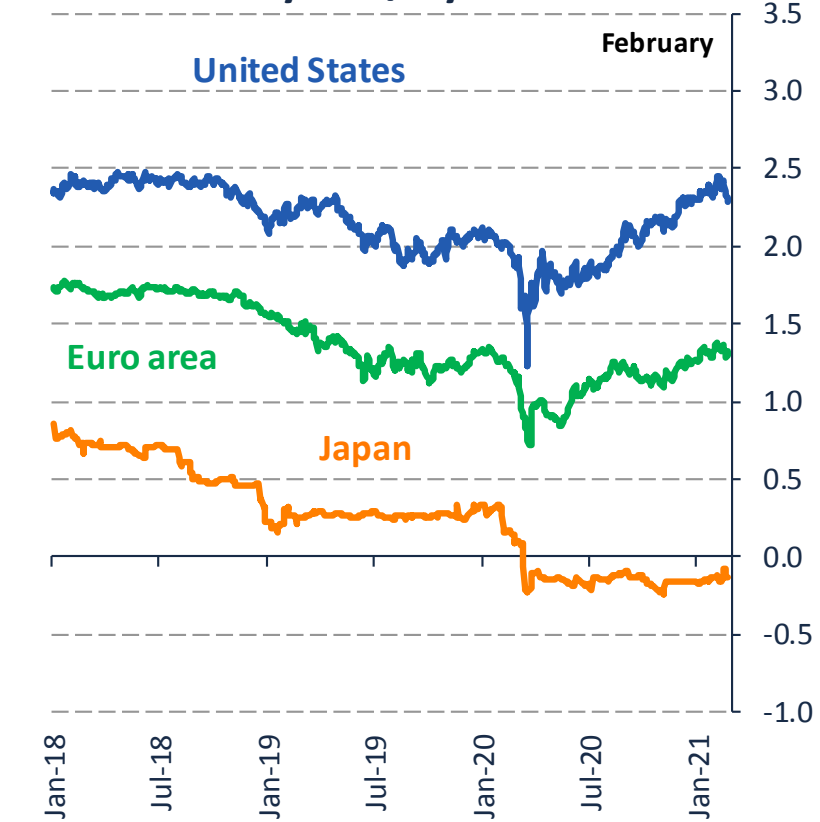## Advanced Economies
Annual % change

Headline Inflation

United States [1]

January
February

Euro area

Japan [2]

1/ Refers to the Personal Consumption Expenditure Price Index (PCE). 2/ Excludes fresh food and the direct effect of the tax increase on consumption and the free-day care and preschool programs.
Source: BEA, Eurostat and Bank of Japan.

Core Inflation

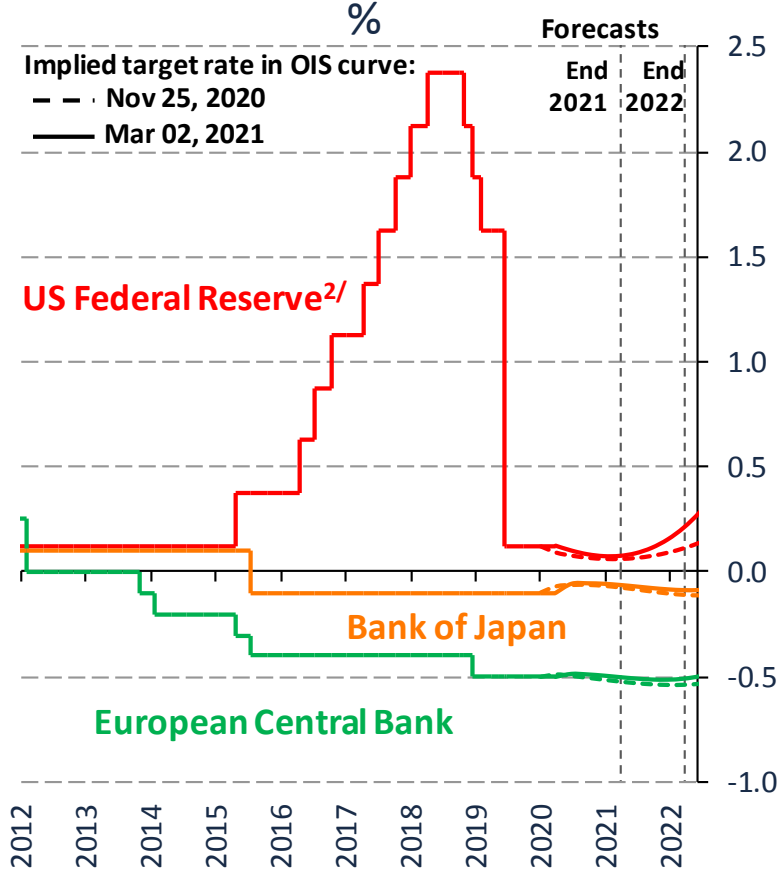United States [3]

January

Euro area

Japan [4]

3/ Refers to the Personal Consumption Expenditure Price Index (PCE). 4/ Excludes energy and fresh food and the direct effect of the tax increase on consumption and the free-day care and preschool programs.
Source: BEA, Eurostat and Bank of Japan.

Headline Inflation Expectations 5 years/5 years

February

United States

Euro area

Japan

Source: JP Morgan.

Central banks in advanced economies underlined their commitment to maintaining accommodative monetary policy stances for an extended period. Meanwhile, recently, long-term interest rates rebounded significantly in the United States due to the expectations of a significant fiscal stimulus.
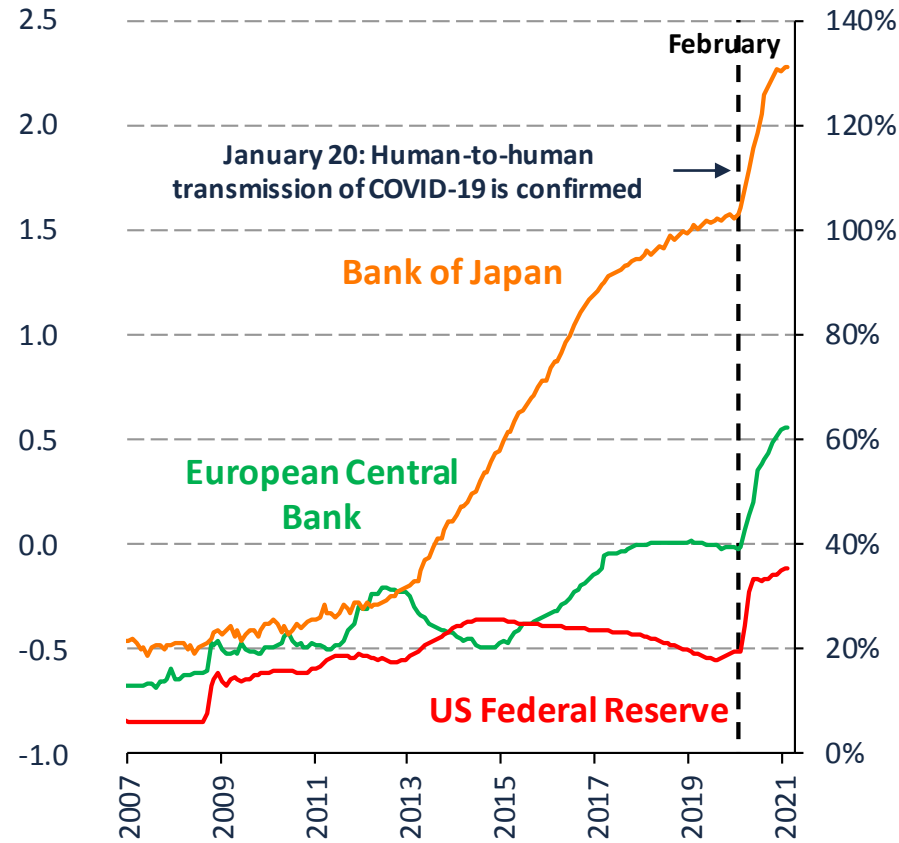
Advanced Economies

Reference Rates and Implied Trajectories in OIS Curves[1]
%

Implied target rate in OIS curve:
- - - Nov 25, 2020
— Mar 02, 2021

Forecasts
End 2021 | End 2022

US Federal Reserve[2]

Bank of Japan

European Central Bank

Balance Sheet of the Main Central Banks
% of GDP

January 20: Human-to-human transmission of COVID-19 is confirmed

February

Bank of Japan

European Central Bank

US Federal Reserve

Source: Bloomberg.

10-year Government Bonds Interest Rates
%

March

United States

Euro area
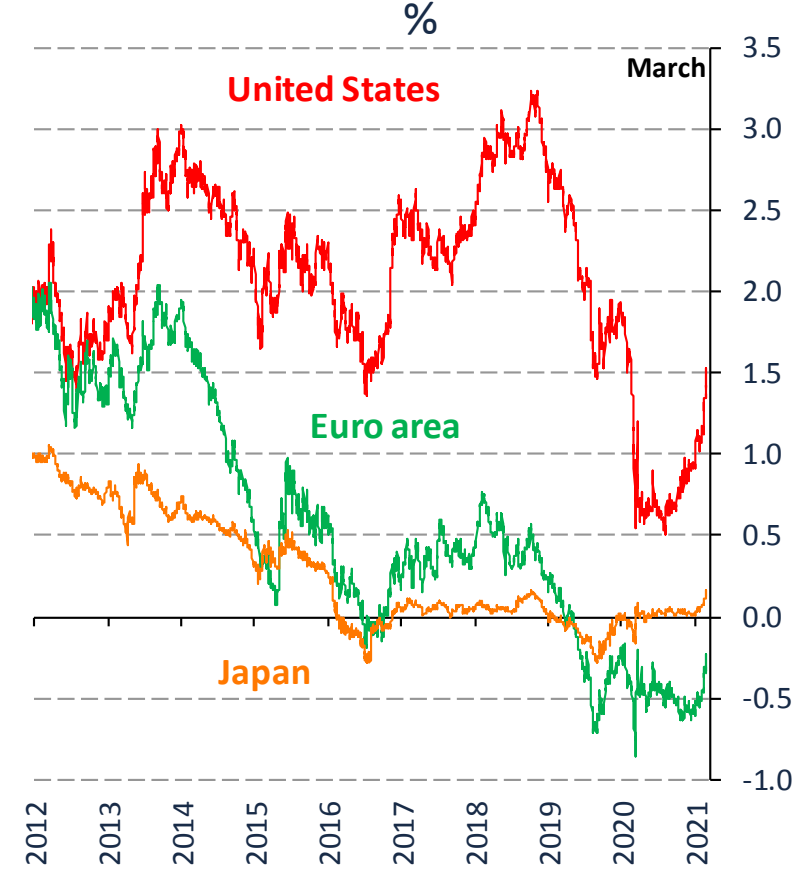
Japan

Source: Bloomberg.

1/ OIS: Fixed-for-floating swap where the fixed interest rate is the overnight effective reference rate. 2/ Data for the observed federal funds rate corresponds to the average between the lower and upper bounds of the target range (0.0% - 0.25%).
Source: Prepared by Banco de México with data from Bloomberg.

International commodity prices have increased due to the expectations of a global economic recovery.

**Commodity Prices**
Index 2014 = 100
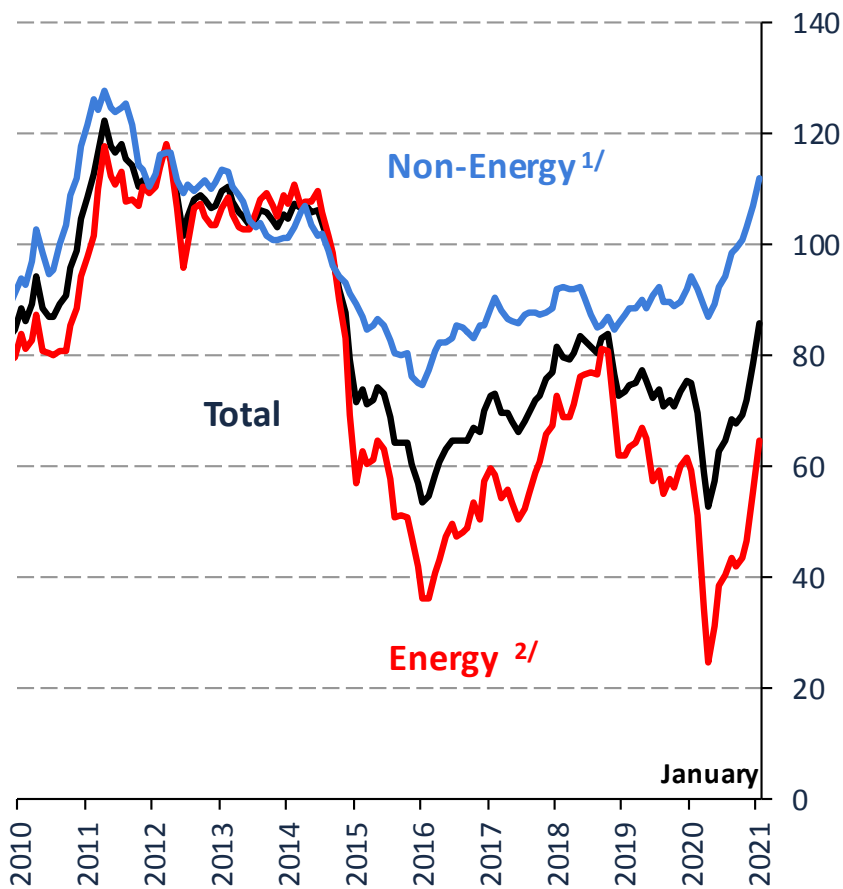
1/ Includes Precious Metal, Food and Beverages and Industrial Inputs Price Indices. 2/ Includes Crude oil (petroleum), Natural Gas, Coal Price and Propane Indices.
Source: International Monetary Fund.

Selected Metal Prices
Index Jan-01-2018=100
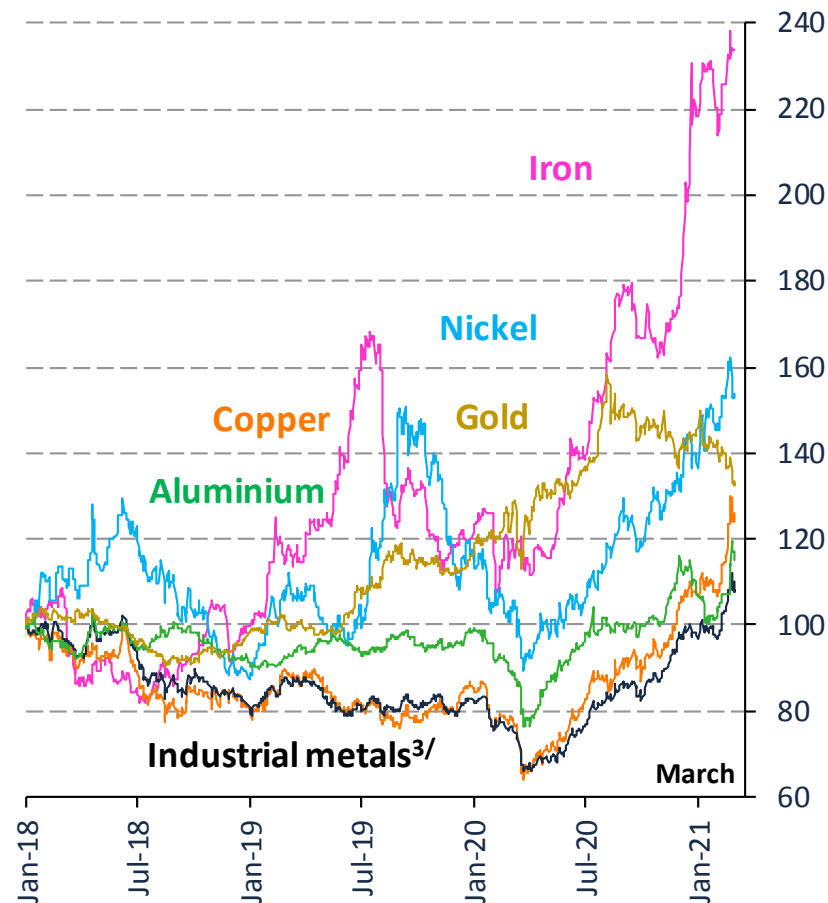
3/ This index follows the prices of aluminum, copper, nickel, zinc and lead.
Source: Bloomberg.

International Crude Oil Prices
US dollars per barrel
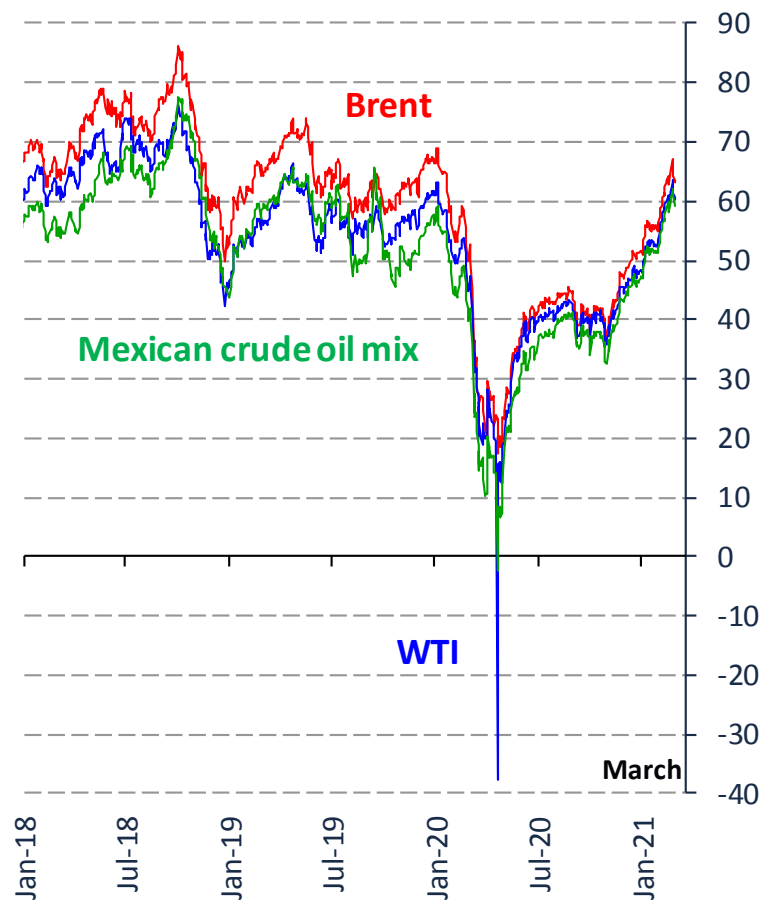
Source: Bloomberg.

At the end of 2020 and the beginning of 2021, international financial markets performed positively. Nevertheless, an episode of volatility was registered in recent weeks given the increase in long- term interest rates in the United States.

Global Risk Appetite Index
Index
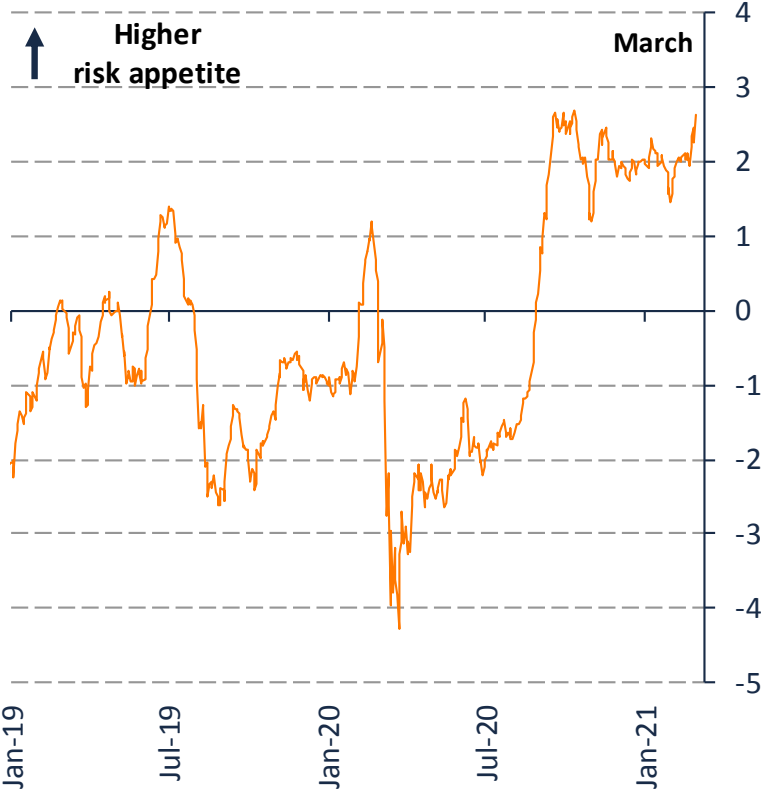
Note: The risk appetite index compares several financial assets, taking into account that in periods of high appetite for riskier assets these tend to register high returns, while safe assets, such as government bonds of the United States, the euro area and Japan, tend to present negative returns. On the other hand, during periods of low risk appetite, the opposite occurs. In this context, the index value refers to the coefficient of a regression of the daily yield of 64 assets based on their volatility. Source: Credit Suisse.

Stock Markets of Advanced and Emerging Economies
Index 01-Jan-2019=100
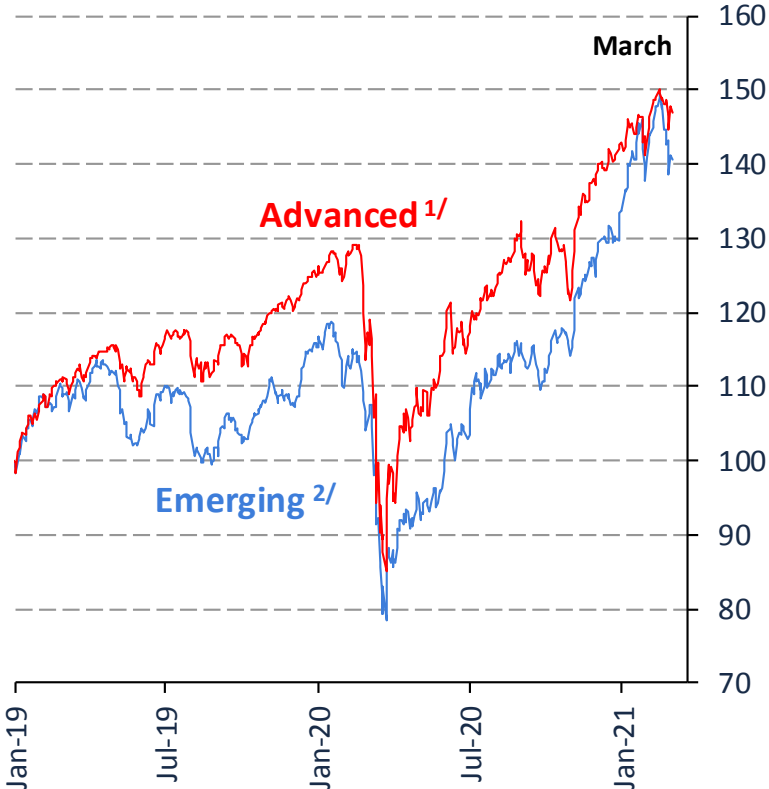
Note: The MSCI indices of both advanced (MSCI World Index) and emerging (MSCI Emerging Market Index) economies are presented.
1/ It includes Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Holland, New Zealand, Norway, Portugal, Singapore, Sweden, Switzerland, the United Kingdom and the United States. 2/ It includes Mexico, Brazil, Chile, China, Colombia, Peru, the Czech Republic, Egypt, Greece, Hungary, India, Indonesia, South Korea, Malaysia, the Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey and the United Arab Emirates. Source: Bloomberg.

## Global Financial Conditions Index
Index

Source: Goldman Sachs.

Although net capital flows to emerging economies have increased, this is mainly the result of the behavior of those directed into China (67.5% of net flows of the last 18 months). Financial markets in emerging economies exhibited a positive performance at the end of 2020 and the start of 2021. However, more recently they have shown volatility.

Emerging Economies

Accumulated Capital Flows [1]
Billion dollars
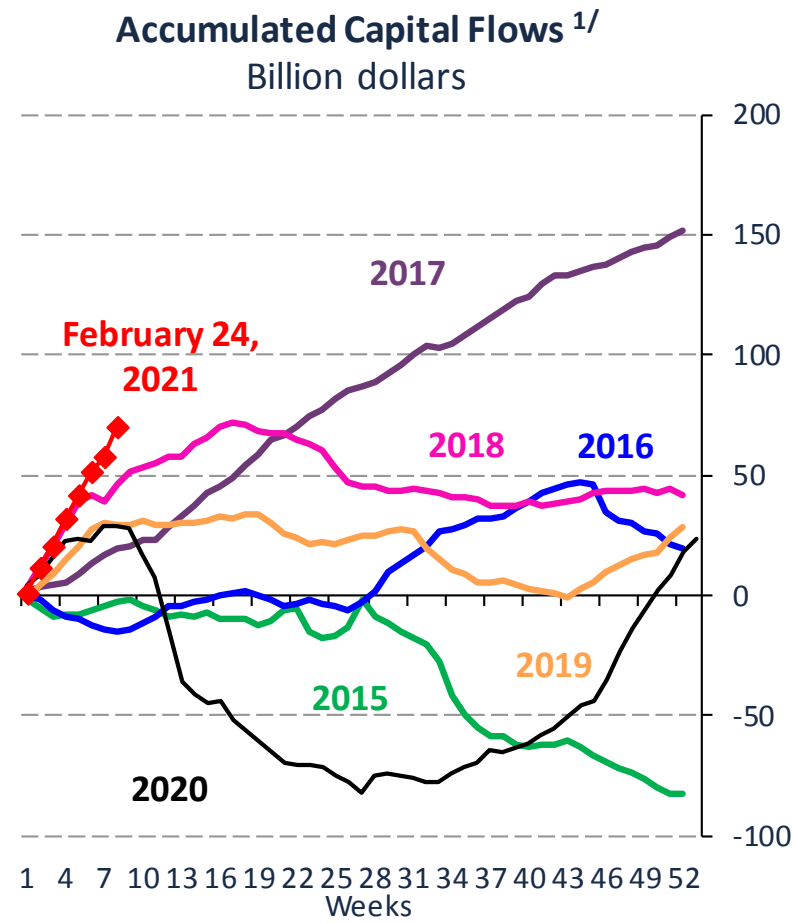
1/ The sample covers funds used for the buying-selling of stocks and bonds from emerging countries, recorded in advanced countries. Flows exclude portfolio performance and exchange rate fluctuations. Source: Emerging Portfolio Fund Research.

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

Source: Bloomberg.

10-year Government Bonds Nominal Interest Rates
%
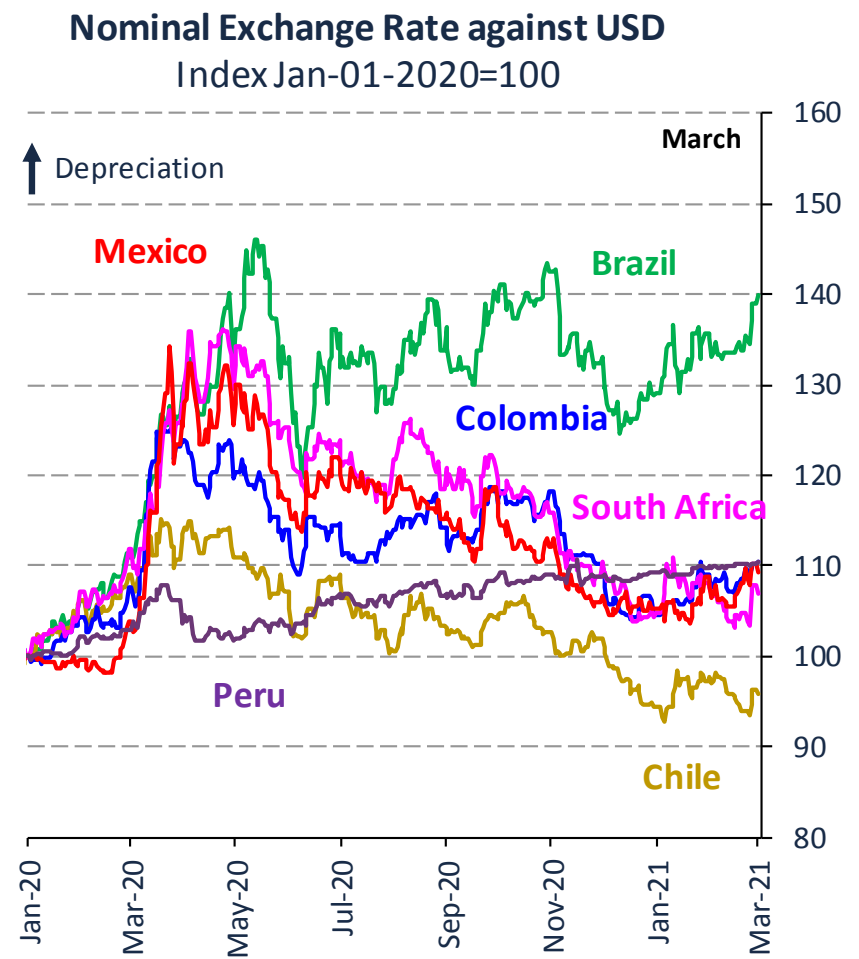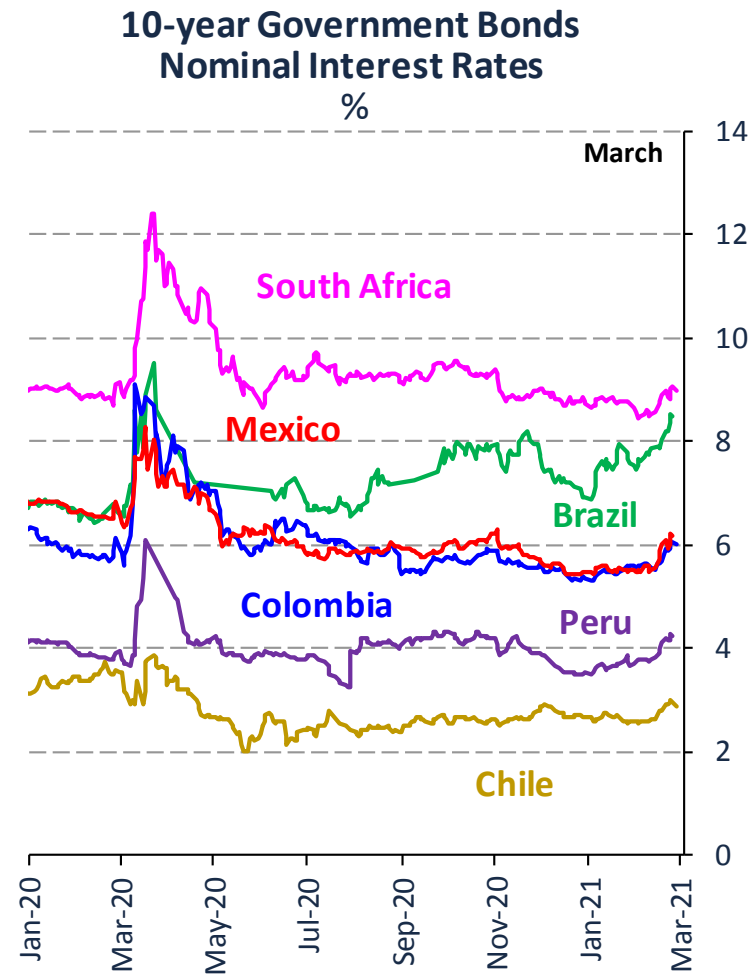
Source: Prepared by Banco de México with Bloomberg and Proveedor Integral de Precios (PiP) data.

Outline

1	**External conditions**
2	**Current situation of the Mexican economy**
3	**Inflation**
4	**Monetary policy**
5	**Forecasts and final remarks**

The recovery of economic activity observed during the third quarter continued into Q4-2020, although at a more moderate pace and with a slight weakening at the end of the year. The latter as a result of the resurgence of infections and of restrictions on production and social mobility implemented in certain states.

Gross Domestic Product

Quarterly % change and index Q4-2019=100, s. a.

Levels

Quarterly change

12.40

3.26

-16.82

Q4-2020
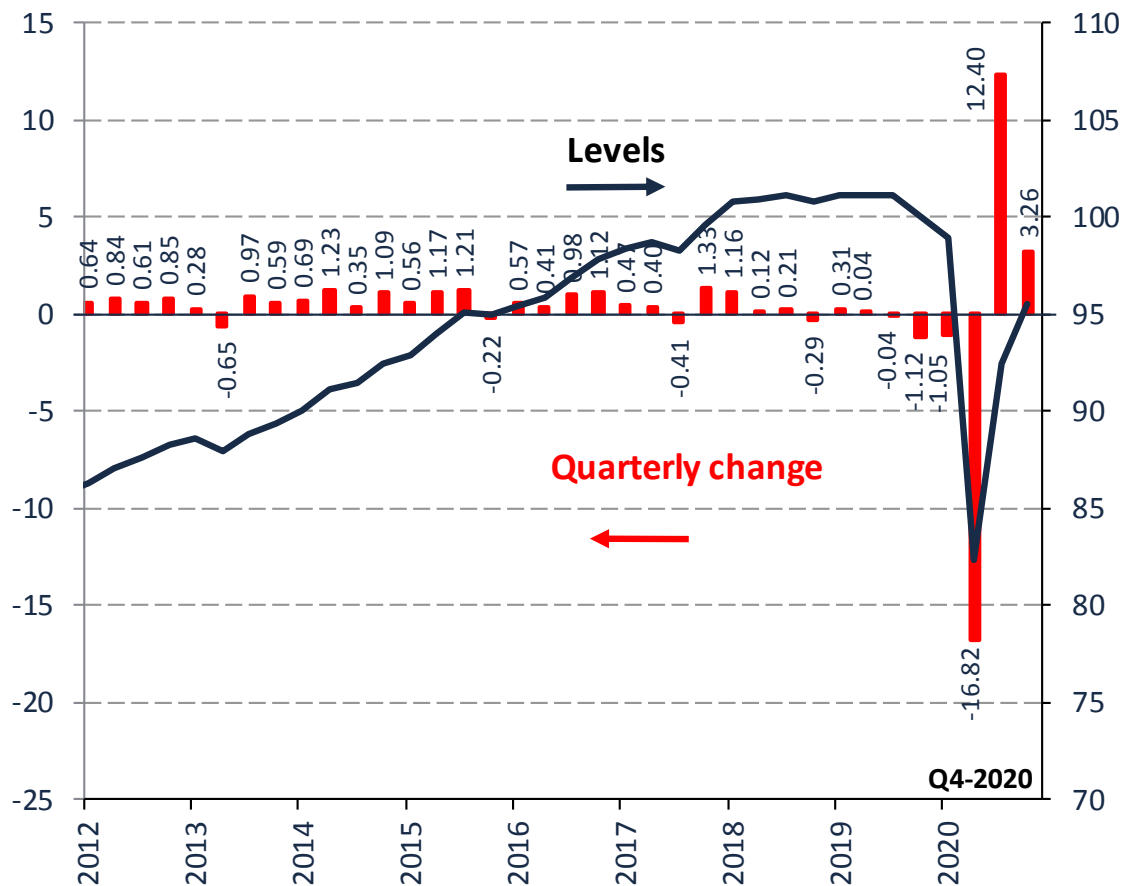
s. a./Seasonally adjusted figures.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Global Index of Economic Activity

Index Jan-2020=100, s. a.

Agricultural and livestock products (3.2%)

Total

Industrial (34.2%)

Services (62.7%)

December
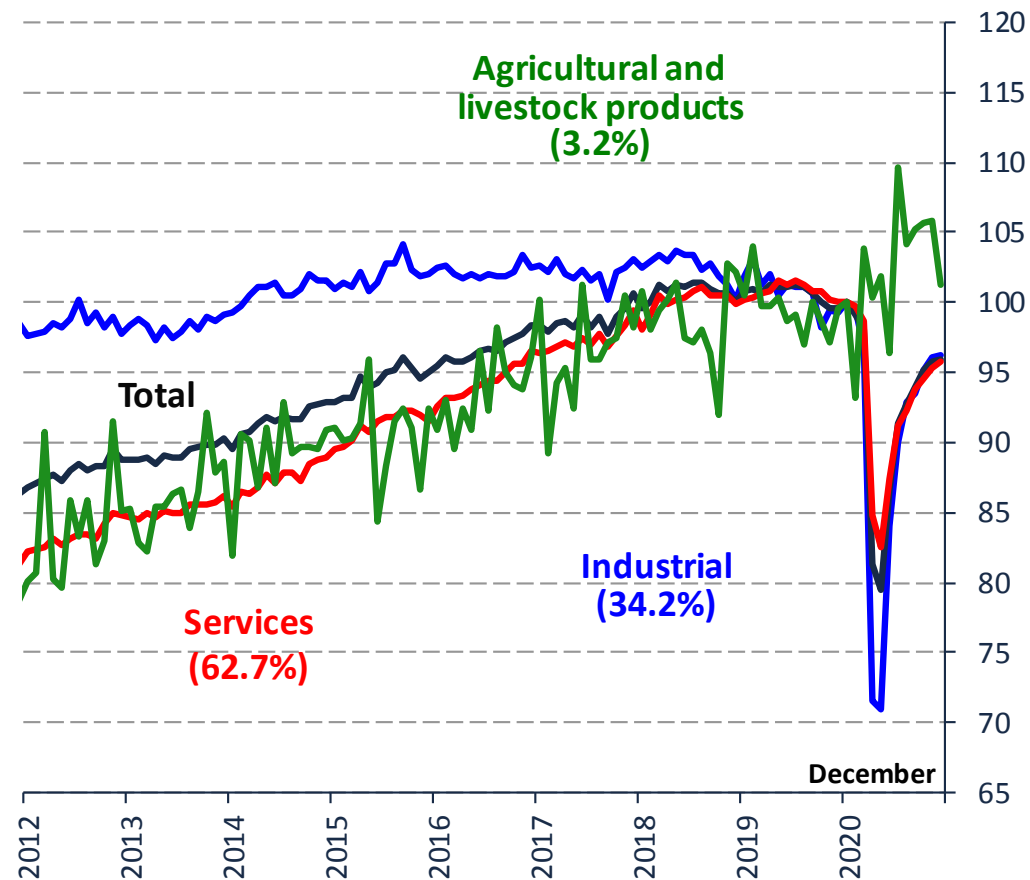
s. a./Seasonally adjusted figures.
Note: The sum of the components may not add up due to rounding.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Industrial activity increased in Q4-2020, although at a slower pace than in Q3-2020. Tertiary activities also continued to recover during Q4-2020, although at a moderate and heterogeneous pace across subsectors.

Industrial Activity
Index Jan-2020=100, s. a.

Mining (22.3%)

Total

Utilities (4.7%)

Manufacturing (49.7%)

Construction (23.3%)

December

s. a. / Seasonally adjusted figures.
Note: Figures in parentheses represent their share in 2013.
Source: Monthly Indicator of Industrial Activity, Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

IGAE Services
Index Jan-2020=100, s. a.
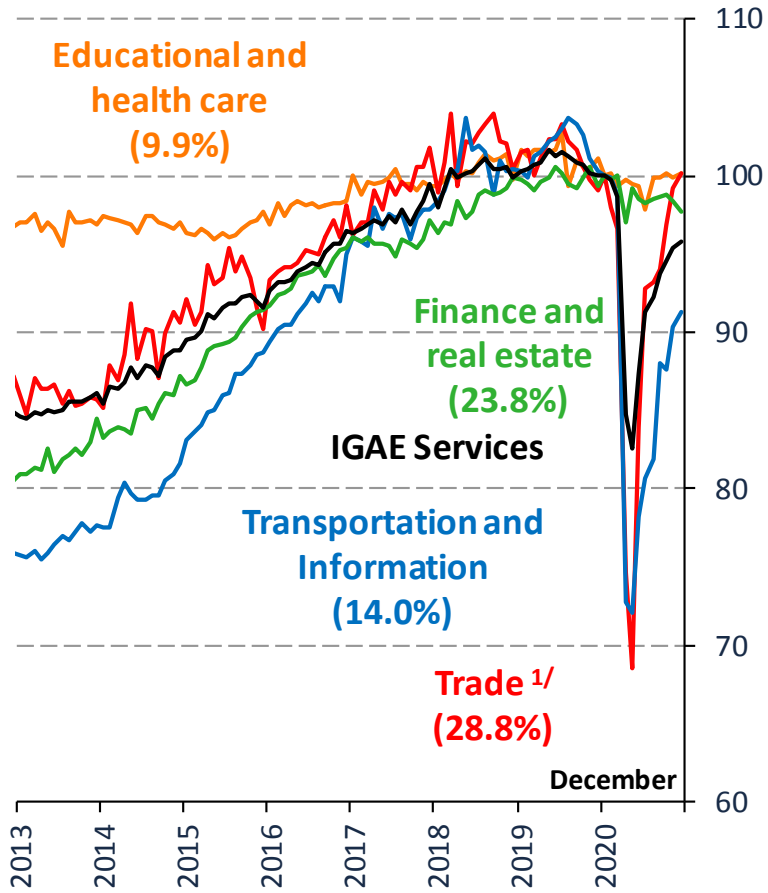
Educational and health care (9.9%)

Finance and real estate (23.8%)

IGAE Services

Transportation and Information (14.0%)

Trade [1/] (28.8%)

December

Public administration (7.1%)

IGAE Services

Professional, management of companies and Enterprises (8.9%)

Arts, entertainment, and recreation (3.8%)

Accommodation and food services (3.6%)

December

s. a. / Seasonally adjusted figures. Note: Figures in parentheses represent their share in 2013. 1/ Includes both wholesale and retail trade.
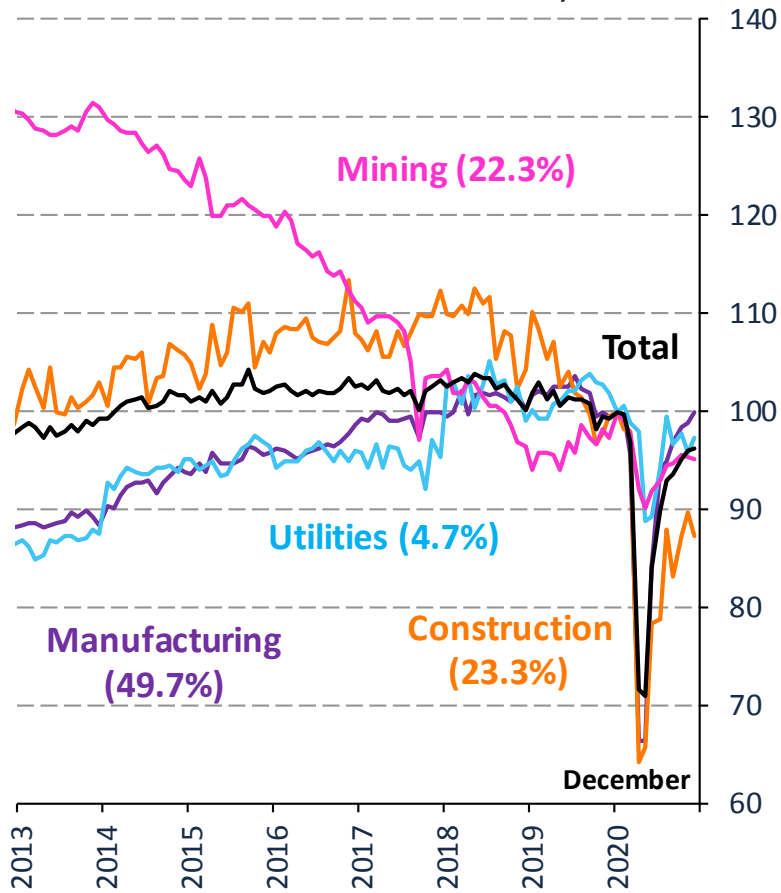Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.
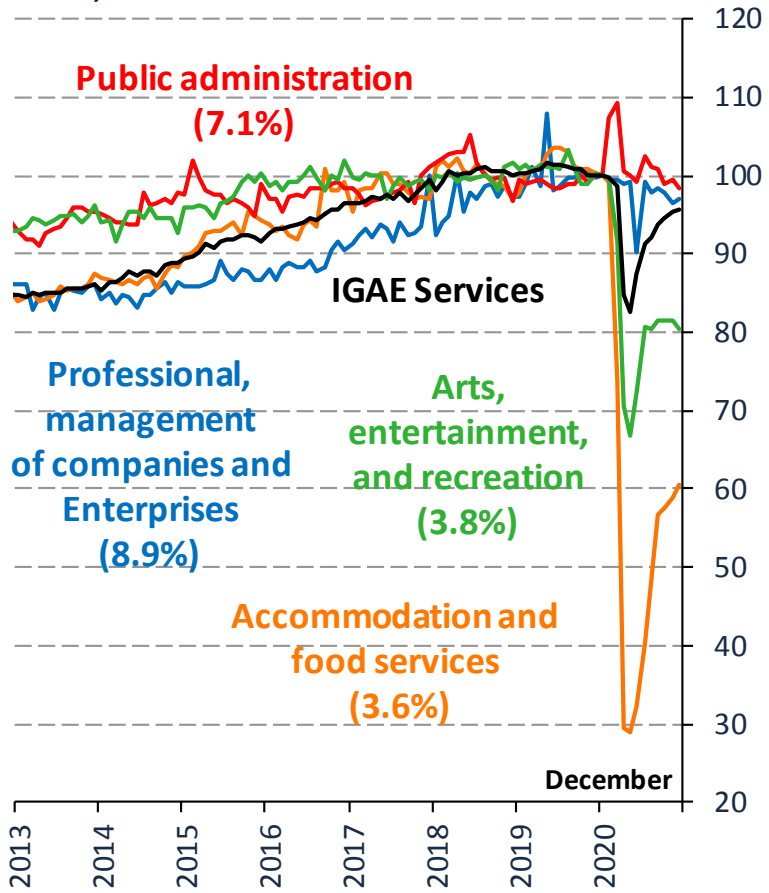
Due to the type of shocks that have been faced, economic sectors continue to perform heterogeneously, with primary activities and industrial production showing a more dynamic rebound, while the tertiary sector is recovering more slowly and with mixed results among its components.

## Global Index of Economic Activity and its Components
Average of Dec 2019 – Feb 2020 = 100, s. a. [1/]

Legend:
- Manufacturing
- Non-manufacturing industrial
- Services
- Primary

Color scale: 70 — 100 — 110

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	
Oil and coal derivatives	105.1	85.8	99.3	98.2	100.7	100.0	79.7	92.4	113.6	112.9	95.6	111.9	**Sectors that have recovered their pre-pandemic levels (20.7%)**
Computer, communication, measurement eq.	100.1	100.5	100.3	78.6	78.3	95.6	104.9	100.8	104.5	104.5	102.4	108.7	
Plastic and rubber	98.8	99.8	97.0	65.9	60.2	82.9	93.0	99.5	100.8	102.6	100.6	108.5	
Electrical appliances and electrical power eq.	101.7	98.3	101.0	89.2	79.0	82.5	99.1	102.5	106.6	107.1	108.6	106.5	
Wholesale trade	102.1	98.4	97.8	84.6	71.6	90.4	93.2	96.2	97.0	98.8	100.7	104.6	
Metal products	100.2	99.0	98.3	62.6	57.9	74.4	97.6	99.4	100.4	104.1	102.6	104.4	
Primary activities	102.5	95.5	106.4	102.8	104.3	98.7	112.4	106.7	107.8	108.3	108.4	103.7	
Mining of metallic and non-metallic minerals	99.8	101.2	94.0	68.8	69.2	87.5	96.7	98.7	100.1	102.6	101.9	103.0	
Non-metallic mineral based products	99.6	100.4	98.4	60.8	66.6	82.6	91.5	97.7	98.6	99.8	100.5	101.8	
Food	99.9	100.0	100.8	99.7	98.4	98.7	99.6	98.8	100.0	100.3	100.1	100.6	
Paper	100.4	99.5	101.3	94.9	82.5	87.5	94.5	98.4	99.7	100.5	100.8	100.5	
Machiney and equipment	98.1	103.7	93.6	63.1	59.4	84.2	86.5	92.0	92.8	97.8	98.3	99.8	**Sectors that remain less than 5% below their pre-pandemic levels (57.3%)**
Educational; health and social assistance	99.6	99.8	99.0	99.4	99.0	98.9	97.4	99.4	99.4	99.8	99.5	99.7	
Construction specialized jobs	100.9	99.2	96.9	76.0	69.5	82.0	84.3	90.1	97.3	97.4	96.2	99.5	
Utilities	100.1	100.2	97.8	95.7	94.4	96.3	96.5	97.5	98.1	98.5	99.1	98.9	
Textile inputs and textile finishing	98.3	100.9	98.1	27.6	29.1	56.4	71.8	82.9	89.2	89.8	91.1	98.7	
Basic metal	103.8	97.5	95.9	79.0	81.5	76.5	82.6	87.8	97.5	98.3	98.3	98.5	
Other manufacturing industries	99.8	99.9	99.0	73.3	77.3	82.1	90.2	96.5	97.6	97.4	99.3	98.4	
Transport equipment	101.4	102.8	82.9	14.1	20.7	75.1	94.0	91.3	96.2	96.1	96.5	98.3	
Wood	99.1	97.1	90.1	63.5	57.9	75.6	84.5	91.0	90.9	98.1	100.4	98.2	
Retail trade	100.0	99.5	97.2	67.5	67.2	80.0	94.1	92.2	93.1	96.9	99.7	98.2	
Textile products, except garments	103.5	99.0	99.5	41.4	54.8	73.2	91.2	93.6	95.4	96.4	95.8	98.1	
Chemical	99.7	99.5	101.1	94.4	88.6	91.5	94.8	97.5	97.7	98.8	98.4	98.0	
Financial and insurance; real state and rental	100.3	100.1	100.3	97.3	99.5	98.8	98.5	98.8	99.0	99.0	98.7	98.0	
Prof., management of comp. and enterprises	100.2	99.7	99.6	99.1	99.4	90.4	99.6	98.0	98.5	98.1	96.6	97.2	
Oil and gas extraction	100.2	100.1	100.8	100.0	95.9	94.4	94.2	95.9	96.2	96.6	96.4	96.6	
Beverage and tobacco	101.2	98.2	95.8	62.6	61.6	84.7	101.3	103.1	101.0	102.7	104.1	96.5	
Government	97.6	104.7	106.5	98.0	97.7	96.8	99.9	98.6	98.5	96.4	97.2	96.1	
Gen., trans. y dist. de energía eléctrica	98.7	99.8	98.0	97.2	86.2	86.4	92.5	98.7	95.2	96.4	93.7	95.6	
Printing industry and related industries	103.7	101.6	100.1	52.9	69.3	67.1	75.7	87.2	86.0	85.6	89.2	93.6	**Sectors that remain more than 5% below their pre-pandemic levels (22.0%)**
Furniture, mattresses and blinds	101.3	97.7	90.1	37.9	37.8	74.7	89.4	91.4	92.2	94.2	91.8	92.0	
Transportation, mail; information in the media	99.9	99.8	98.8	72.8	72.1	78.2	80.6	81.9	88.0	87.5	90.3	91.2	
Building	100.5	99.1	99.8	59.0	63.0	77.8	78.6	90.2	81.3	88.1	92.7	88.0	
Arts and entertainment; other services	99.9	99.7	91.6	70.7	66.8	72.2	80.5	80.4	81.4	81.4	81.5	80.5	
Mining related services	101.7	102.3	96.0	98.4	99.3	92.9	92.6	90.6	88.8	85.0	85.8	79.7	
Civil engineering works	100.3	98.4	96.4	80.5	79.1	80.0	79.6	81.7	81.2	81.5	80.1	79.3	
Leather and derivatives	100.1	98.4	91.5	14.9	14.7	49.0	66.6	71.8	74.2	79.9	79.3	78.5	
Garment	101.3	100.6	91.2	25.1	25.5	42.6	60.5	68.9	72.1	72.4	77.9	74.4	
Accommodation and food services	100.2	99.4	74.0	29.5	29.0	32.3	40.3	48.6	56.9	57.5	59.1	60.6	

s. a./ Seasonally adjusted figures. 1 / Obtained as the each month's index over its average during the period Dec-2019 to Feb-2020, multiplied by one hundred. The numbers in parentheses represent the share of each group in total IGAE in 2013. Prepared by Banco de México with data from INEGI.
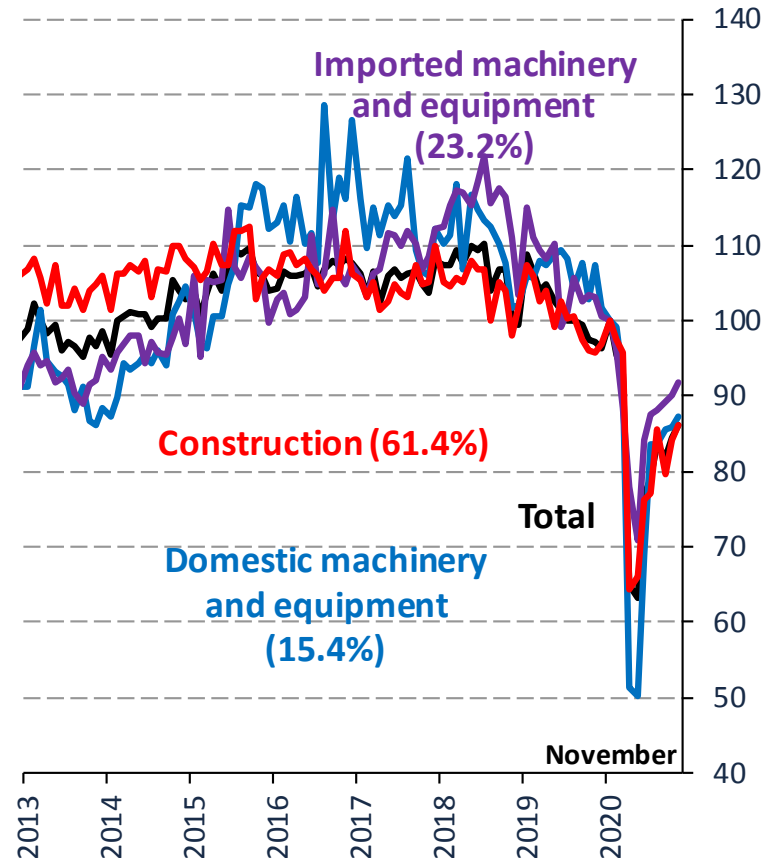
During the October-November 2020 period, private consumption continued to recover gradually, though at a more moderate pace than in the previous quarter. During the same period, gross fixed investment continued to recover at a slow pace, although it remains significantly below the levels reported in the first months of the year.

Total Private Consumption and Components
Index Jan-2020=100, s. a.
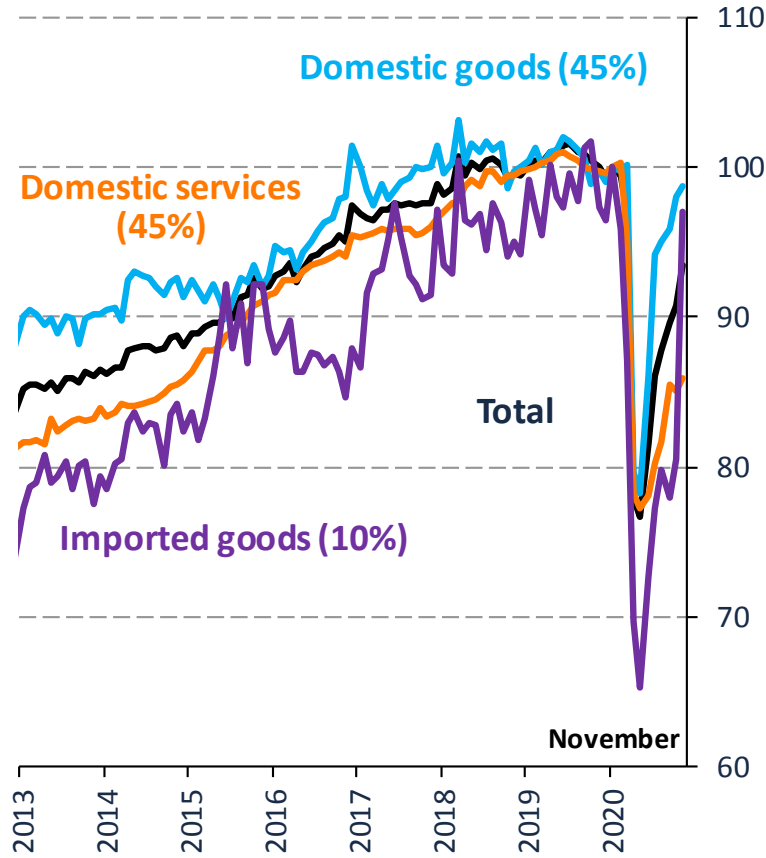
- Domestic goods (45%)
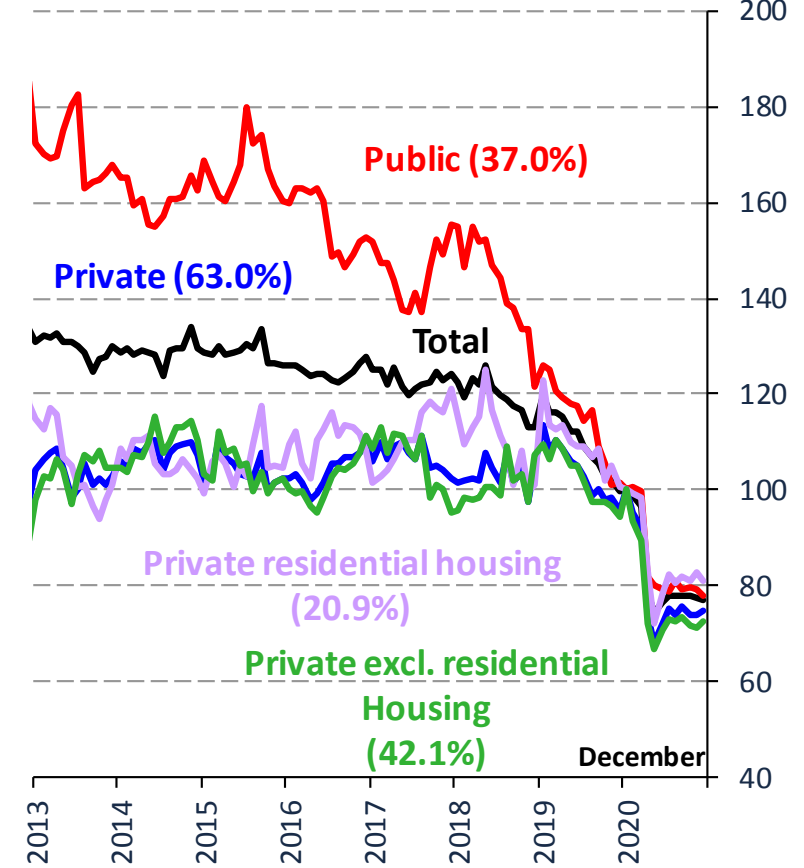- Domestic services (45%)
- Total
- Imported goods (10%)

November

s. a. / Seasonally adjusted figures.
Note: Figures in parentheses represent their share in 2013.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Investment and its Components
Index Jan-2020=100, s. a.

- Imported machinery and equipment (23.2%)
- Construction (61.4%)
- Total
- Domestic machinery and equipment (15.4%)

November

s. a. / Seasonally adjusted figures.
Note: Figures in parentheses represent their share in 2013.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI

Real Value of Construction Output by Sector
Index Jan-2020=100, s. a.[1]

- Public (37.0%)
- Private (63.0%)
- Total
- Private residential housing (20.9%)
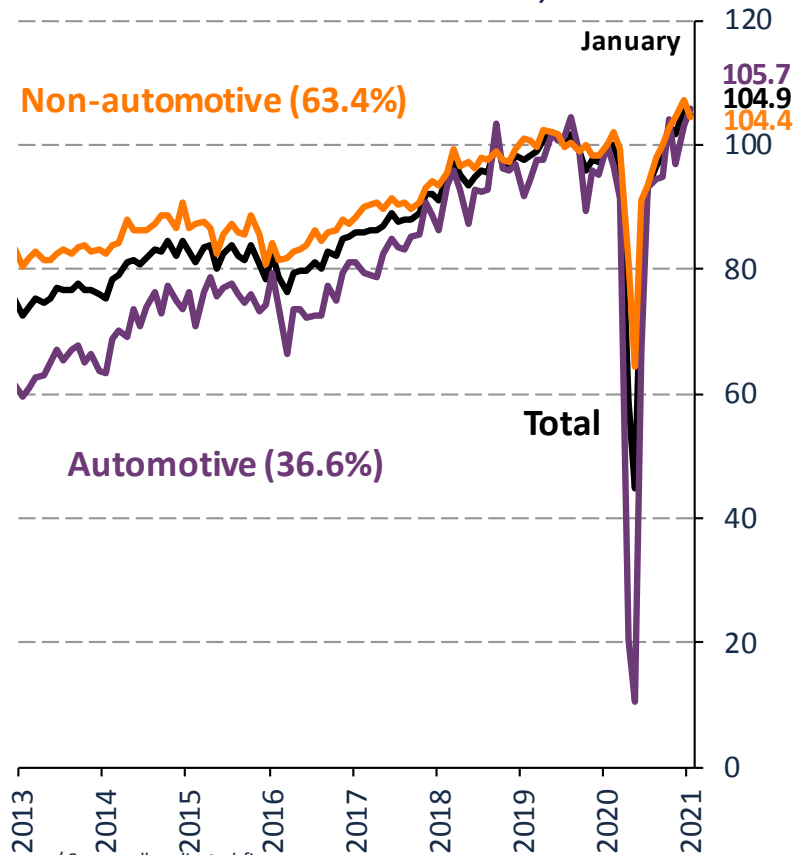- Private excl. residential Housing (42.1%)

December

s. a. / Seasonally adjusted figures.
Note: Figures in parentheses represent their share in 2020.
1/ Seasonally adjusted by Banco de México, except for the total series.
Source: Prepared by Banco de México with data from ENEC, INEGI.

Exports of goods continued to show dynamism in Q4-2020, reaching levels higher than those observed prior to the pandemic, although a certain slowdown was observed at the beginning of 2021.

Total Manufacturing Exports

Automotive and Non-automotive
Index Jan-2020=100, s. a.

Non-automotive (63.4%)
105.7
104.9
104.4
January
Total
Automotive (36.6%)

By Destination
Index Jan-2020=100, s. a.

January
United States (82.5%)
106.2
104.9
98.5
Total
Rest of the world (17.5%)

Capital Goods and Non-Oil Imports [1]
Index Jan-2020=100, s. a.

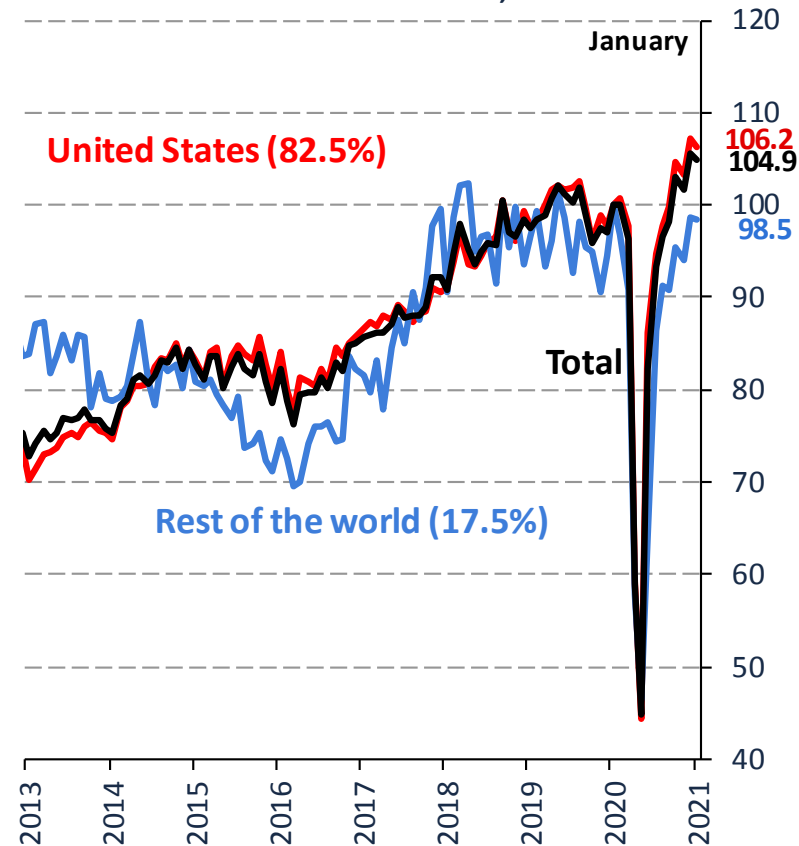Imports of Capital Goods
January
103.78
95.49
Non-Oil Imports

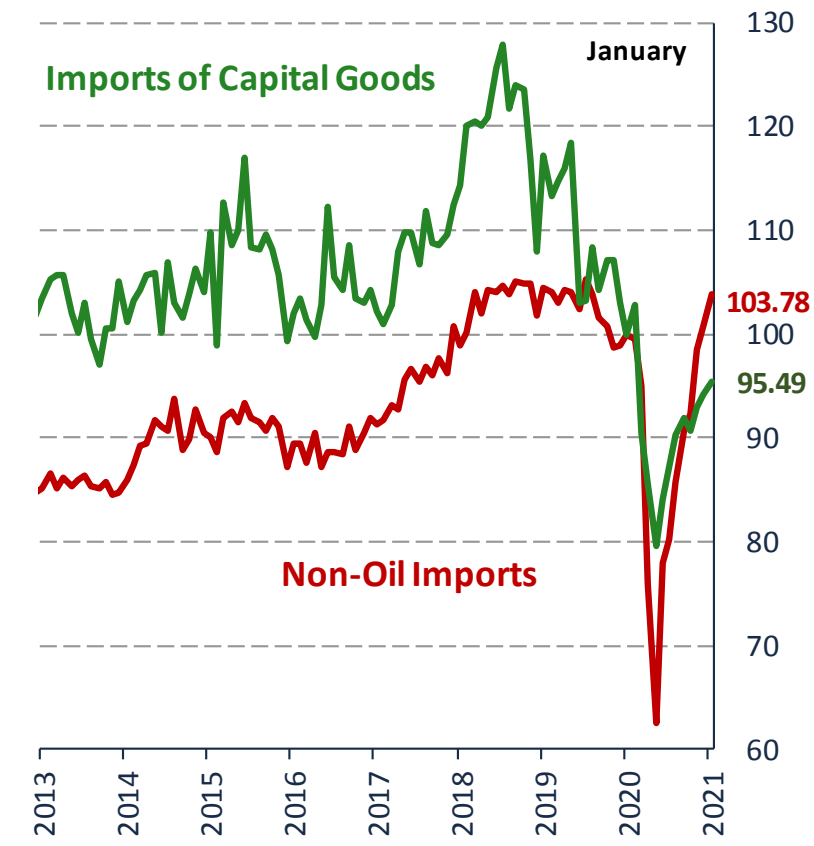s. a. / Seasonally adjusted figures.
Note: Figures in parentheses represent their share in total in Jan-2020.
Source: Prepared by Banco de México with data from PMI Comercio Internacional, S.A. de C.V., SAT, SE, Banco de México, INEGI. Commercial Balance of Goods of Mexico. SNIEG. Information of National Interest.
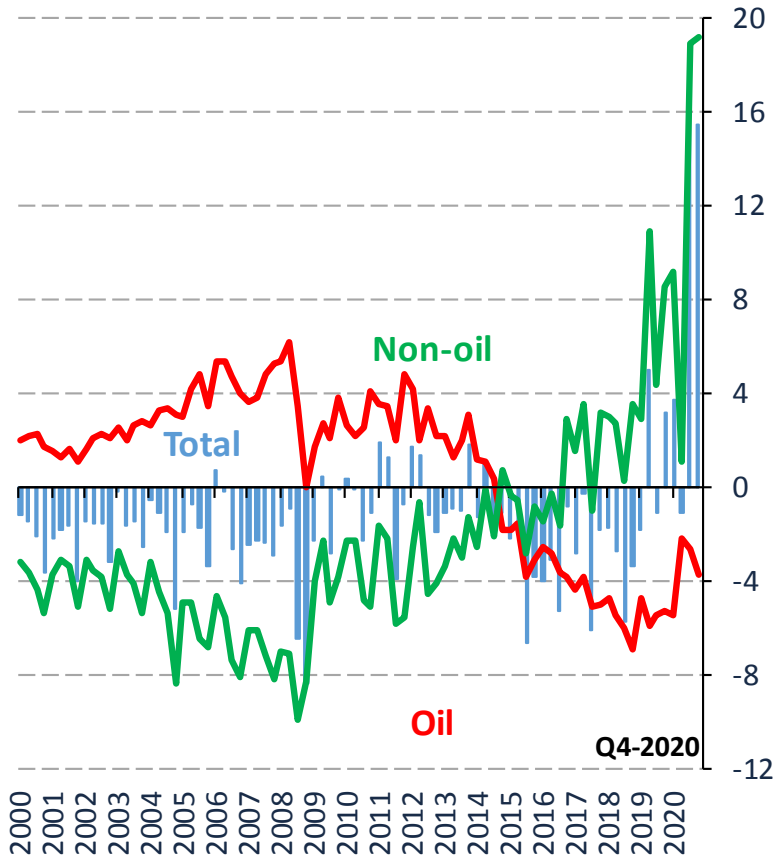
s. a. / Seasonally adjusted figures.
1/ Figures in current US dollars.
Source: Prepared by Banco de México with data from PMI Comercio Internacional, S.A. de C.V., SAT, SE, Banco de México and INEGI. Commercial Balance of Goods of Mexico. SNIEG. Information of National Interest.
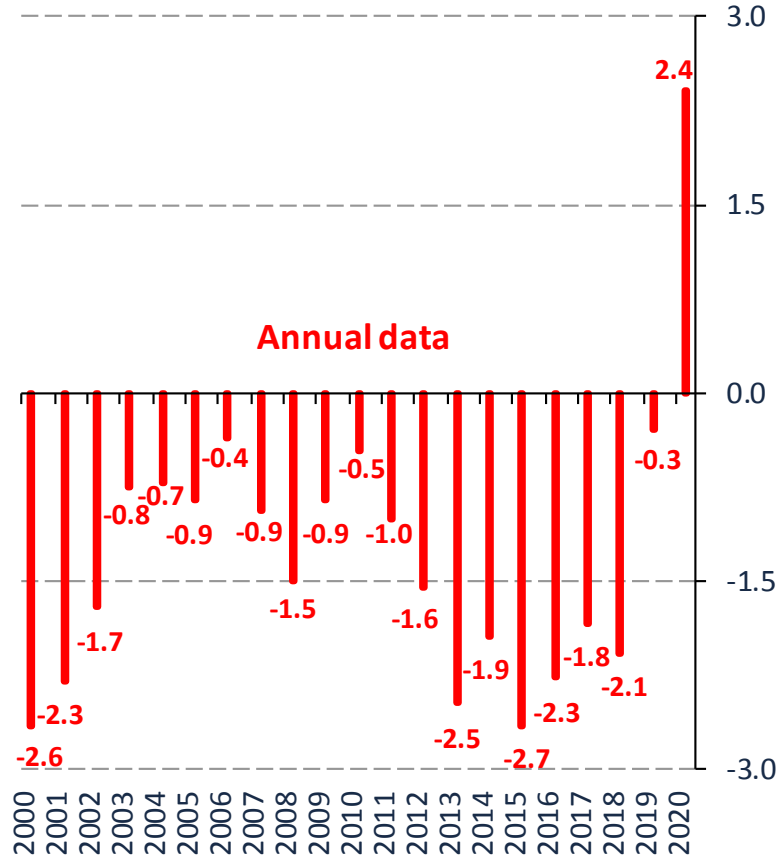
During the second half of 2020, exports recovered at a relatively faster rate than imports. For 2020 as a whole, a current account surplus of 2.4% of GDP was observed, the highest surplus figure recorded since 1983.
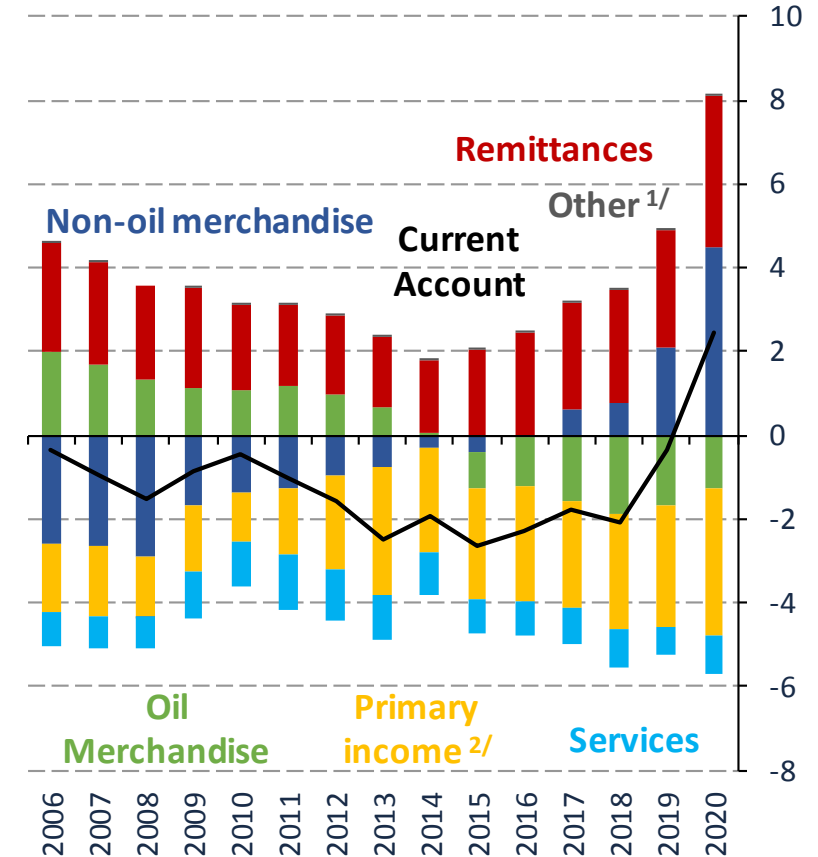

Trade Balance
USD billion

Current Account
% of GDP

Current Account Components, Balances
% of GDP

Source: SAT, SE, Banco de México, INEGI. Mexico's Merchandise Trade Balance. SNIEG. Information of national interest.

Source: Banco de México and INEGI.

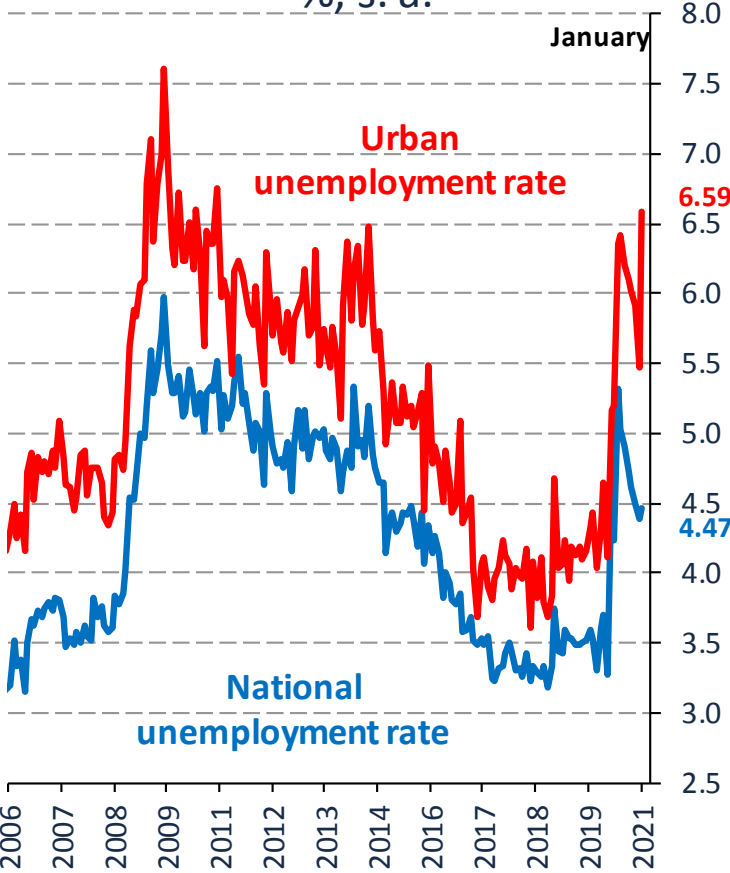1/ Corresponds to the aggregation of the balance of other components of secondary income (other than remittances) and the balance of goods acquired in ports by means of transport. 2 / The primary income account includes credits and debits for profits and dividends, other interests and an item line of (for example, income from cross-border workers and other types of income) Source: Banco de México and INEGI.

Part of the recovery of the labor market reverted between November 2020 and January 2021. Although the national unemployment rate continued to decrease, there is still high level of urban unemployment.
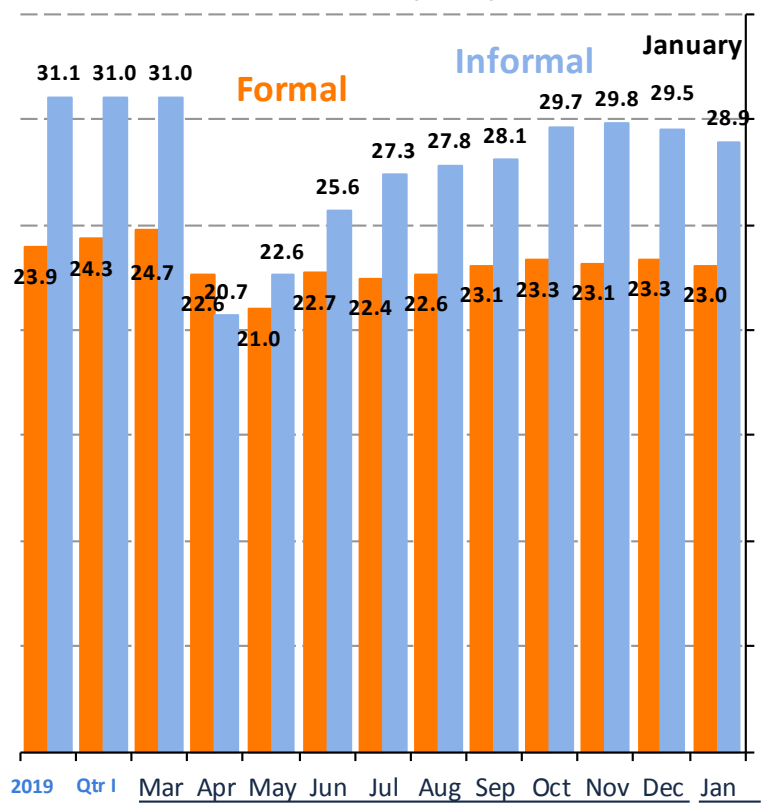
National and Urban Unemployment Rates
%, s. a.

Urban unemployment rate

January

6.59

National unemployment rate

4.47

s. a. / Seasonally adjusted figures
Source: Prepared by Banco de México with data from INEGI (SCNM, ENOE, ETOE and ENOE[N]).

Employed Population by Condition of Occupation [1/]
Million people

Formal   Informal   January

31.1 31.0 31.0   29.7 29.8 29.5 28.9
                    25.6 27.3 27.8 28.1
                22.6
23.9 24.3 24.7 22.6 21.0 22.7 22.4 22.6 23.1 23.3 23.1 23.3 23.0
             20.7

2019 Qtr I   Mar Apr May Jun Jul Aug Sep Oct Nov Dec Jan
                              2020   2021

1/ The April-June 2020 figures are those released in the Telephone Survey of Occupation and Unemployment (ETOE, for its acronym in Spanish) and the figures from July onwards correspond to the New Edition of the National Survey of Occupation and Unemployment (ENOE[N], for its acronym in Spanish). Source: Prepared by Banco de México with data from INEGI (ENOE, ETOE and ENOE[N])

IMSS-insured Jobs, Total IGAE and Employed Population
Indices Jan-2020 and Q4-2019=100, s. a.

Q4-2020
December
January
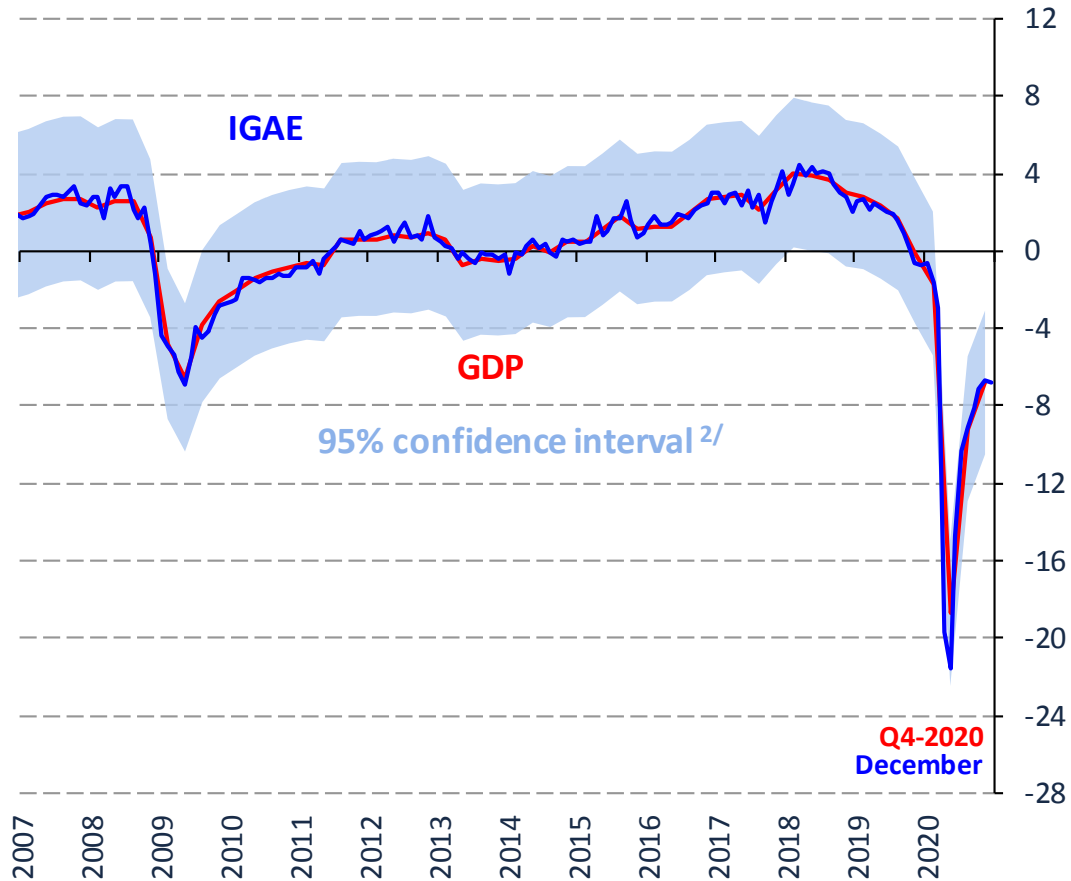
Total IGAE

Employed population

IMSS-insured jobs [2/]
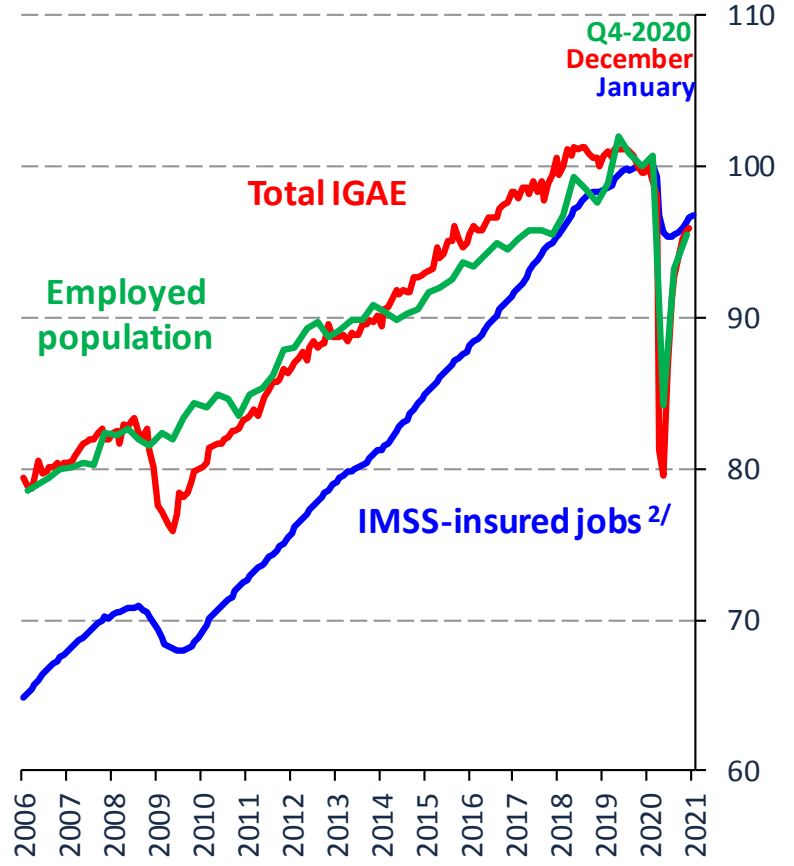
s. a. / Seasonally adjusted figures. 2/Refers to permanent and temporary urban workers. Seasonal adjustment by Banco de México. Source: Prepared by Banco de México with data from IMSS and INEGI (ENOE, ETOE and ENOE[N]).
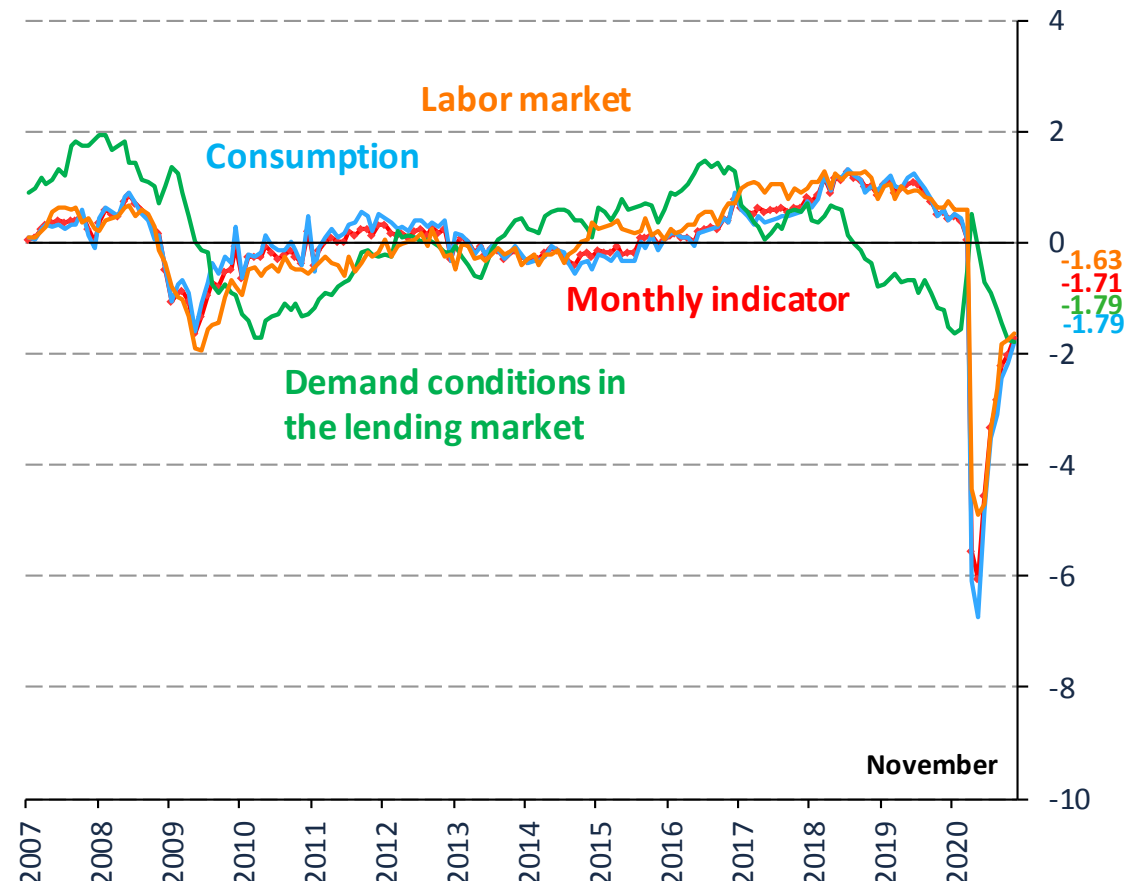
Regarding the economy's cyclical position, slack conditions continued to narrow in Q4-2020, although they remained significantly ample.

Output Gap Estimate [1]
% of potential output, s. a.

IGAE

GDP

95% confidence interval [2]

Q4-2020
December

12
8
4
0
-4
-8
-12
-16
-20
-24
-28

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020

s. a. / Seasonally adjusted data.
1/ Output gap estimated with a tail-corrected Hodrick-Prescott filter; see "Inflation Report April – June 2009", Banco de México, p. 74.
2/ Output gap confidence interval calculated with a method of unobserved components.
Source: Prepared by Banco de México with data from INEGI and Banco de México.

Monthly Slack Indicators: First Principal Component by Group of Indicators [3]
%

Labor market

Consumption

Monthly indicator

Demand conditions in the lending market

November

-1.63
-1.71
-1.79
-1.79

4
2
0
-2
-4
-6
-8
-10

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020

3/ Main Indicators constructed using CCM methodology; see Banco de México (2018), "Quarterly Report, October December 2017", p.47. Monthly slack indicators are constructed with the main component of a set of series which includes 11 indicators. Slack indicators of consumption, labor market and demand conditions in the lending market are based on the first main component of sets of series which includes 6, 3 and 6 indicators, respectively.
Source: Prepared by Banco de México with data from INEGI and Banco de México.
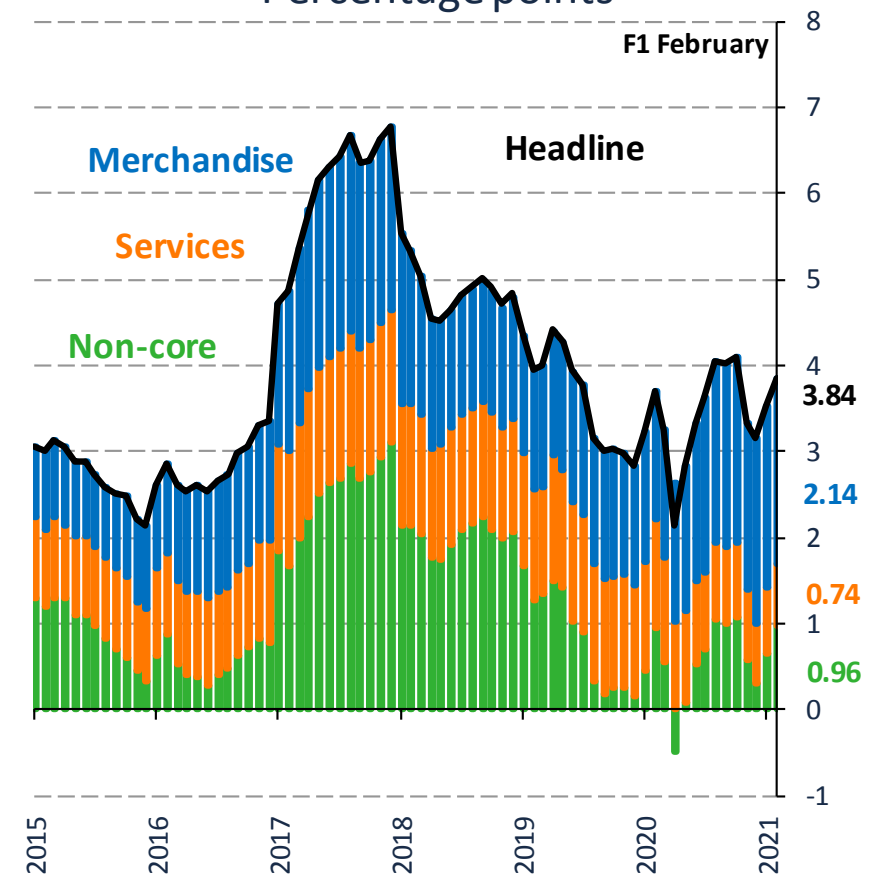
Outline

Inflation continues to be affected by the shocks derived from the pandemic. Annual headline inflation decreased from an average of 3.90% in Q3-2020 to 3.52% in Q4-2020 due to lower core and non-core inflation levels. During F1-February 2021, annual headline inflation was 3.84%.

Consumer Price Index

Annual % change [1]
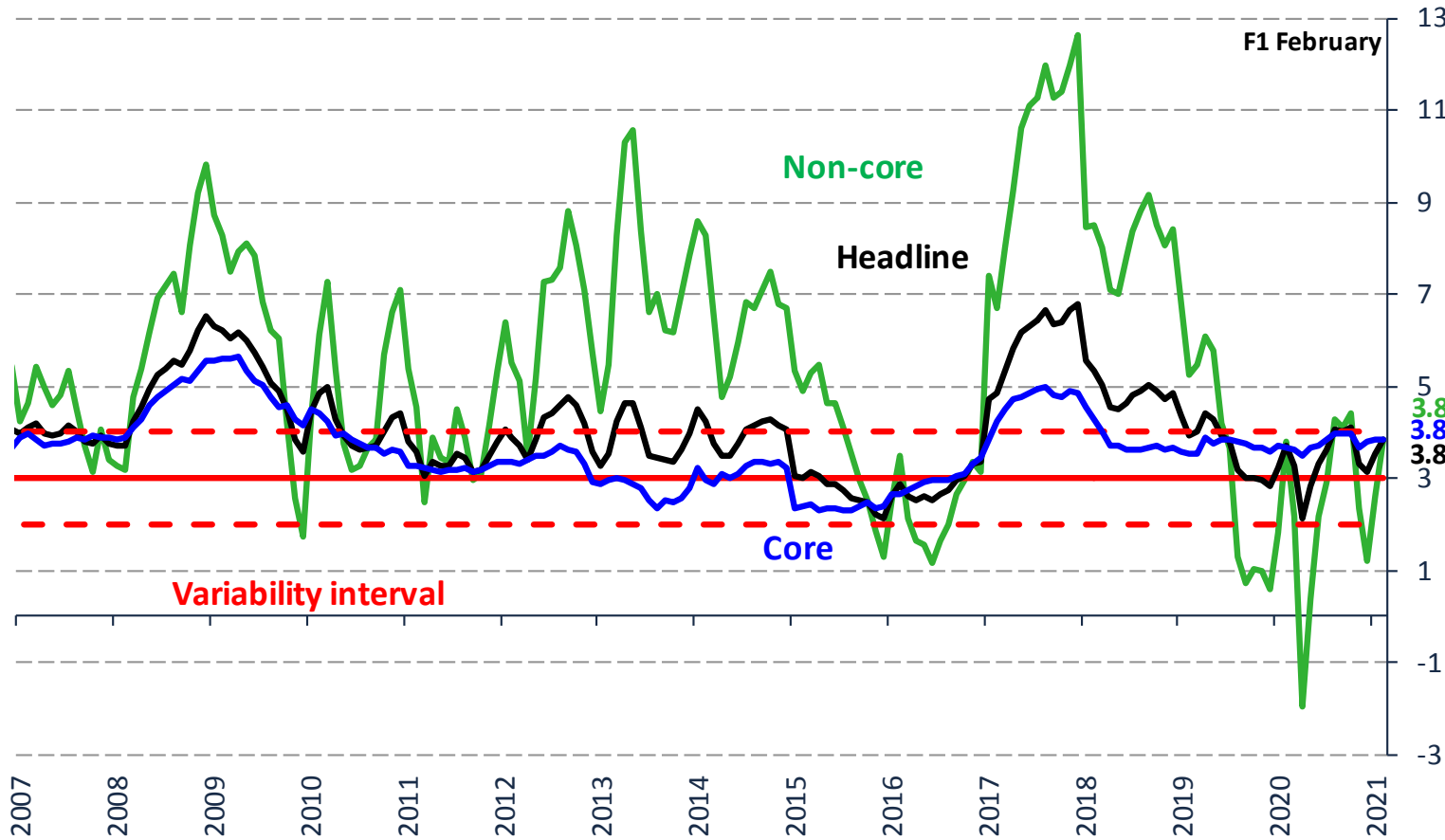
Annual Incidences [2]
Percentage points

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.

2/ The sum of inflation's components may not add up due to rounding.
Source: Prepared by Banco de México with data from INEGI.

Core inflation fell between Q3-2020 and Q4-2020, reaching 3.84% in F1-February 2021, as a result of a decline in the services component, a certain reduction in food merchandise inflation and some upward pressures in non-food merchandise inflation. The latter exhibited volatility associated with the "El Buen Fin" sales campaign.

Core Price Subindex
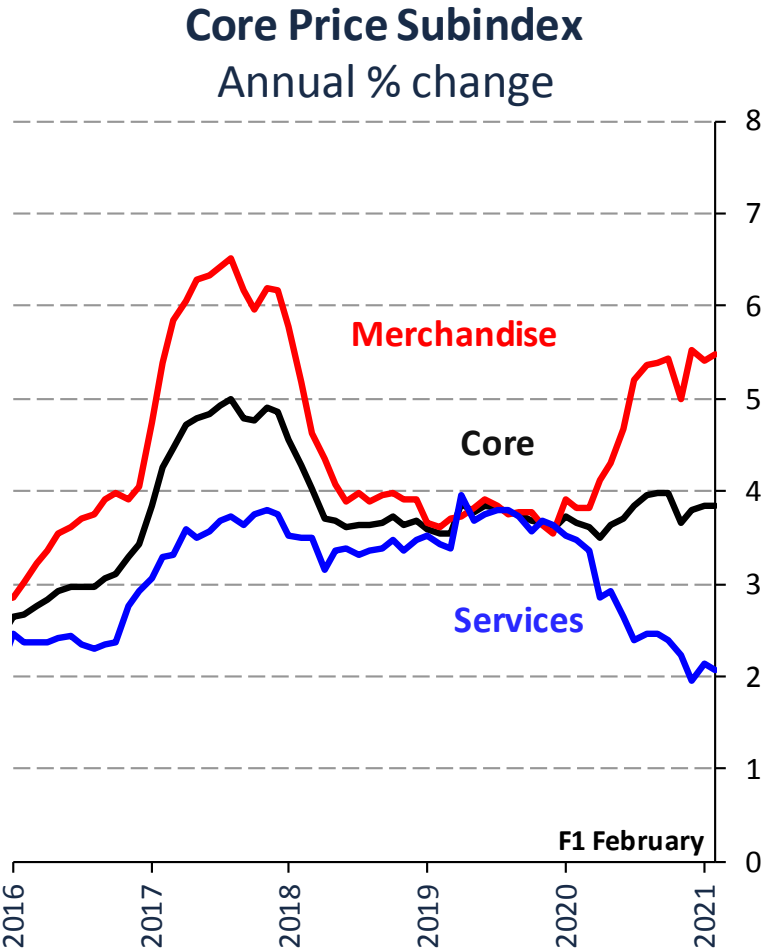
Core Price Subindex
Annual % change

Merchandise
Annual % change

Services
Annual % change

Source: Banco de México and INEGI.
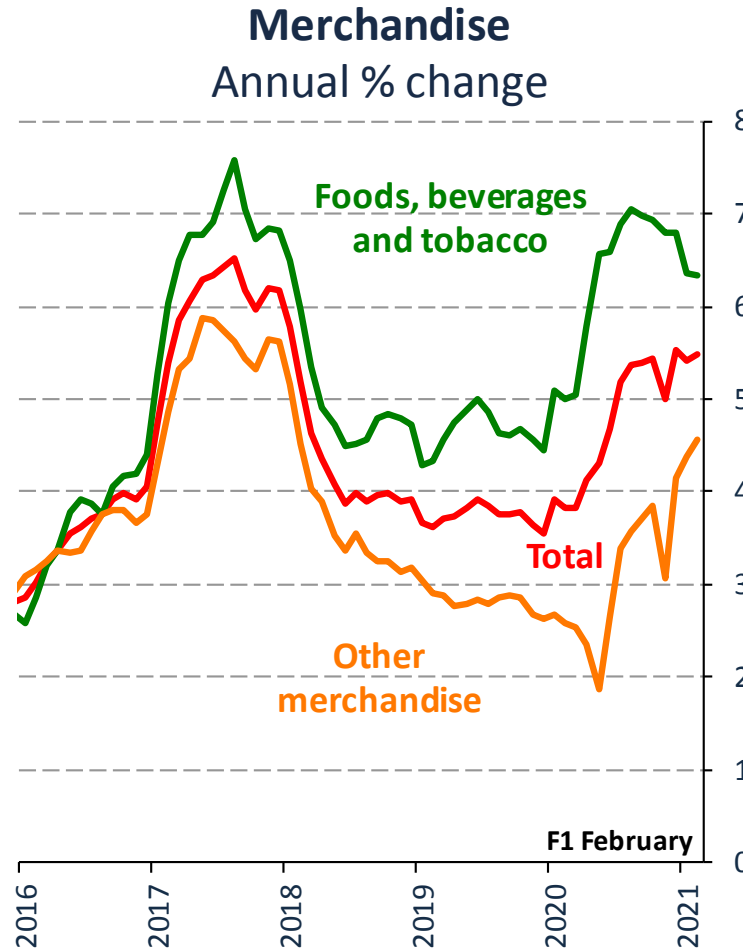
Source: Banco de México and INEGI.

Source: Banco de México and INEGI.

Non-core inflation decreased between Q3-2020 and Q4-2020 due to lower annual changes in energy prices, as well as to a decline in fruit and vegetable inflation. In F1-February 2021, it reached 3.85% associated with the increase in energy inflation.

Non-core Price Subindex

Annual Incidences [1/]
Percentage points

Agricultural and livestock products

Non-core

F1 February

Electricity

Government authorized prices

Gasoline

Domestic gas [2/]

3.85
2.24
0.28
0.43
0.91
-0.01

15
12
9
6
3
0
-3
-6
-9

2016 2017 2018 2019 2020 2021
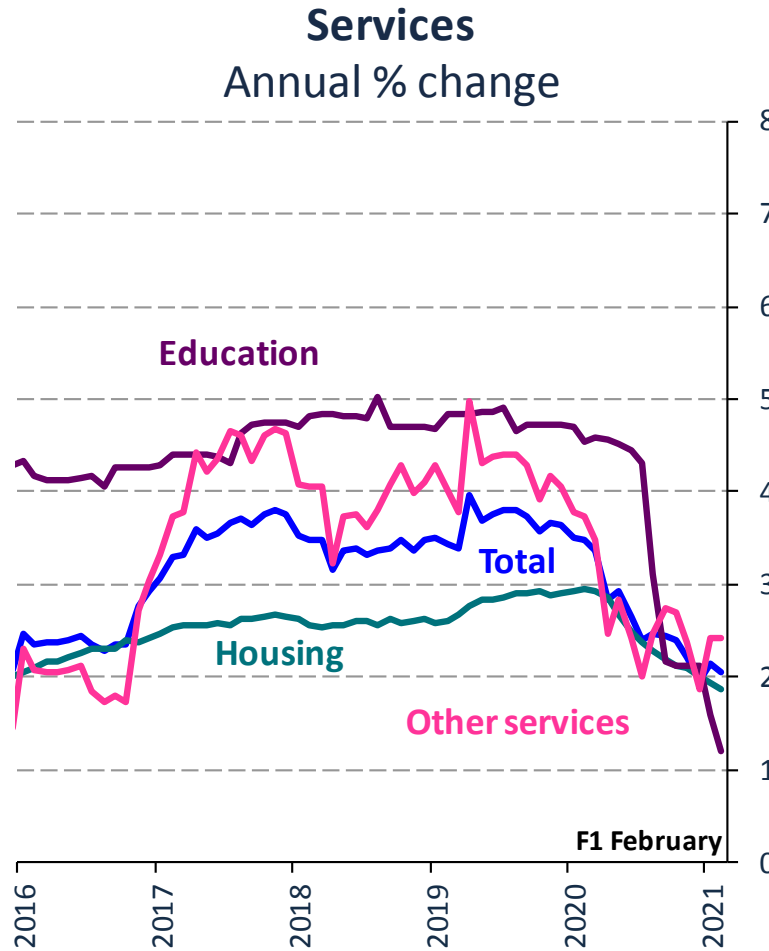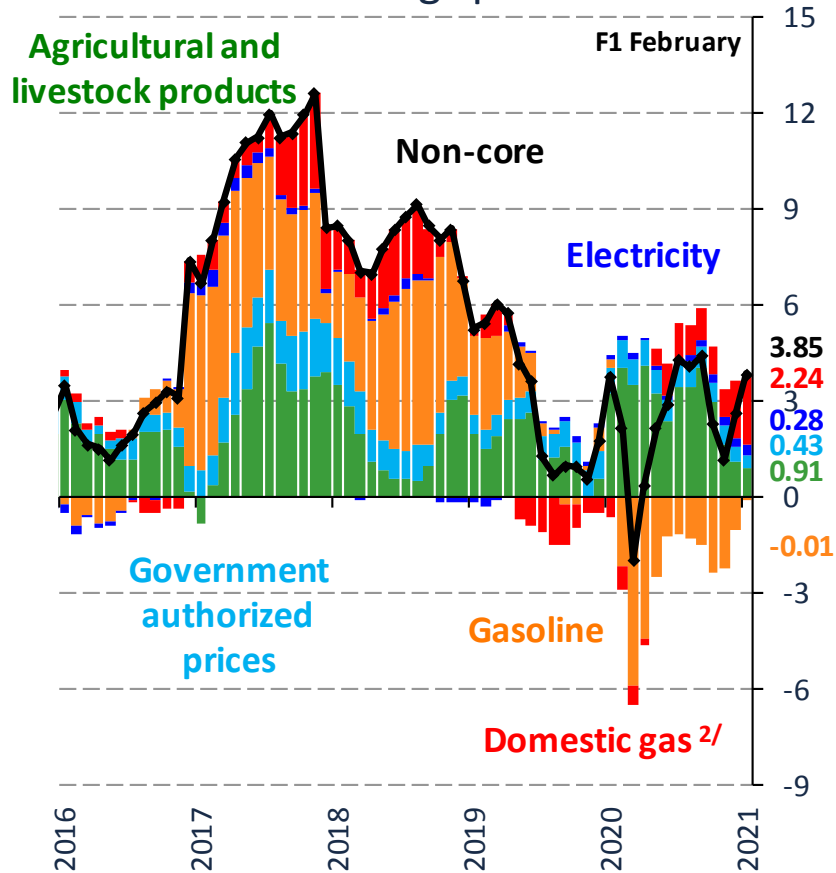
1/In certain cases, the sum of inflation's components may not add up due to rounding. 2/ Includes LP gas and natural gas.
Source: Calculated by Banco de México with data from INEGI.

Agricultural and Livestock Products
Annual % change

F1 February

Total

Livestock products

Fruits and vegetables

30
25
20
15
10
5
0
-5
-10
-15

2016 2017 2018 2019 2020 2021
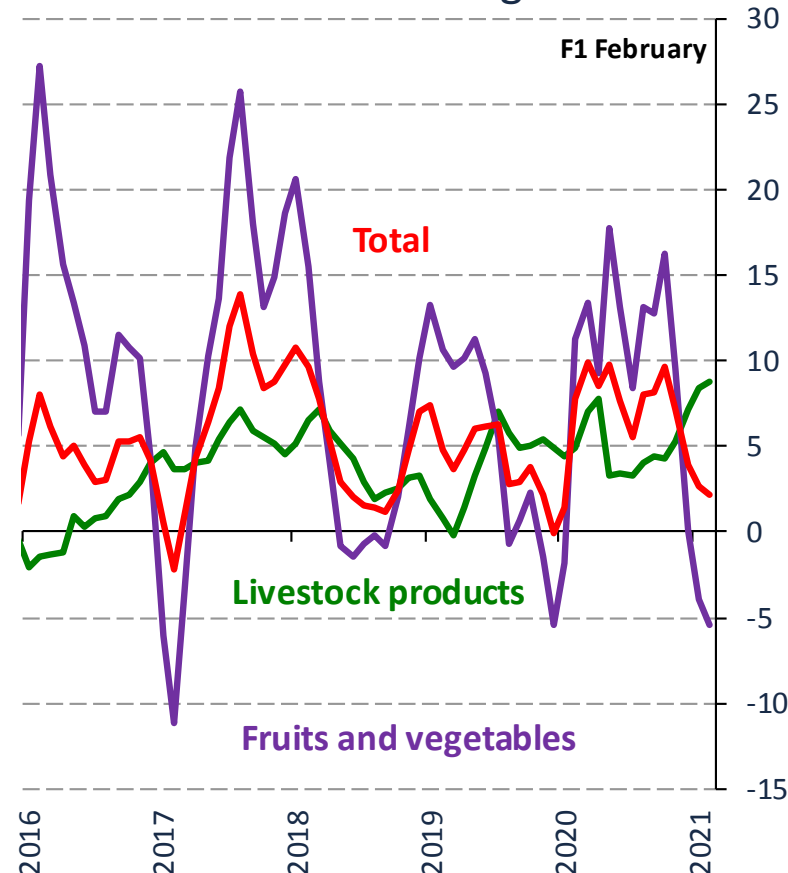
Source: Banco de México and INEGI.

Selected Energy Price Indexes
Annual % change

F1 February

Energy products

LP gas

Natural gas

Gasoline

50
40
30
20
10
0
-10
-20
-30

2016 2017 2018 2019 2020 2021
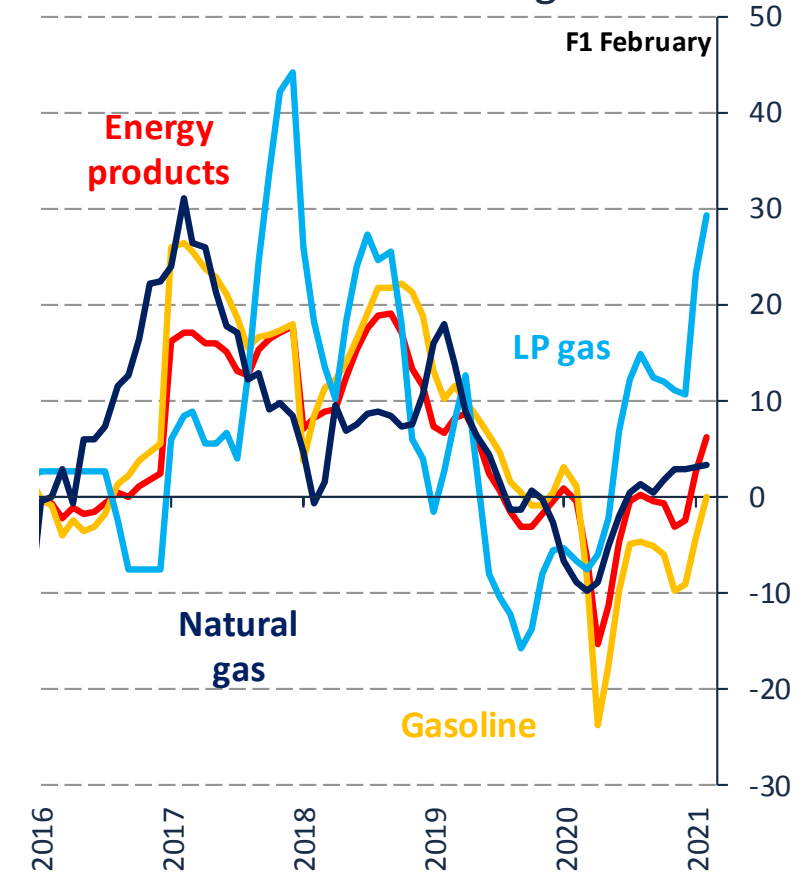
Source: Banco de México and INEGI.

Outline

1	External conditions
2	Current situation of the Mexican economy
3	Inflation
4	**Monetary policy**
5	Forecasts and final remarks

During Q4-2020, Banco de México's Governing Board left the target for the overnight interbank interest rate unchanged at 4.25%, while in its February 2021 decision it lowered the target by 25 basis points to 4.00%.

Target for the Overnight Interbank Interest Rate and Headline Inflation [1]
%, annual % change

March
F1 February

Target for the overnight interbank interest rate (policy rate)

Headline inflation

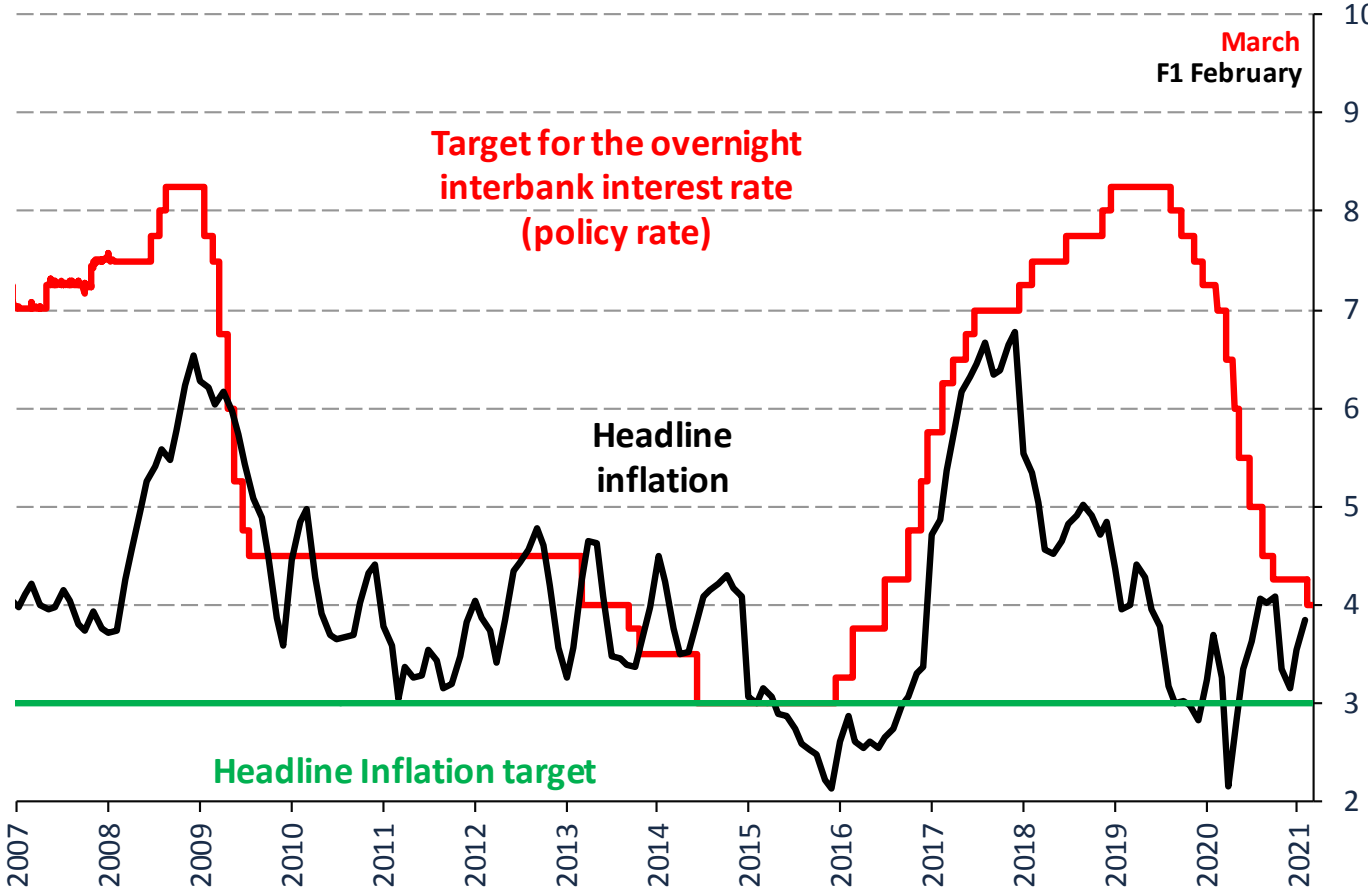Headline Inflation target

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]
%

March

Short-term neutral real rate range in the long term

Short-term ex-ante real rate
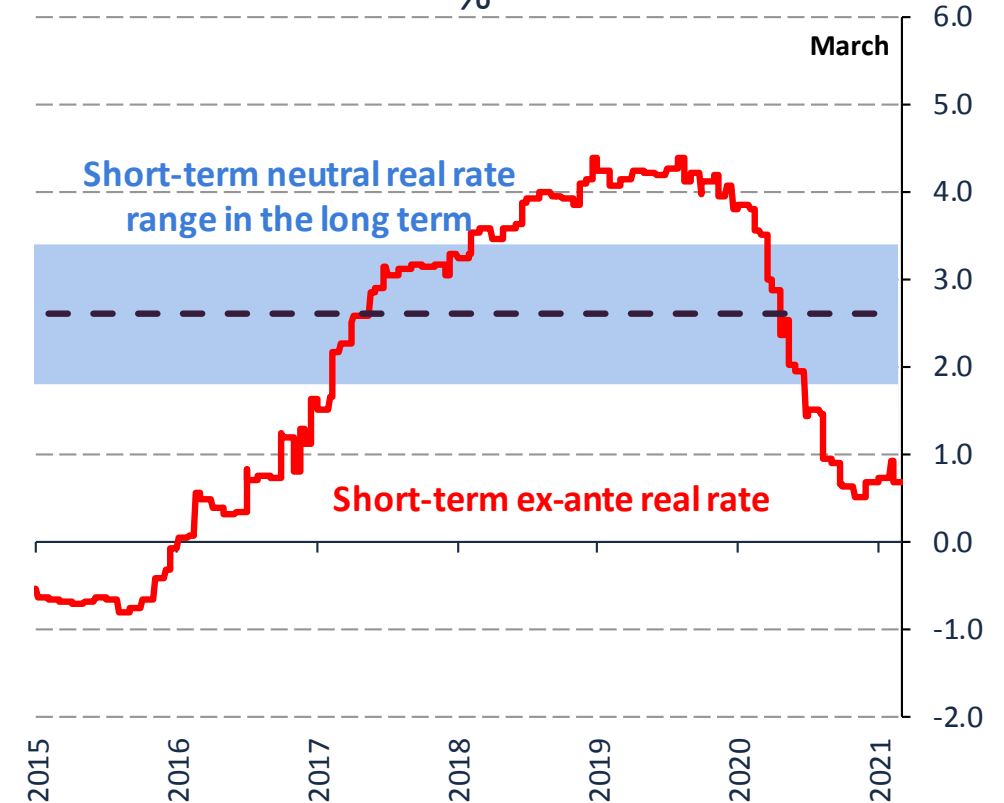
2/ The short-term ex-ante real rate is constructed using the Target for the Overnight Interbank Interest Rate and 12-month inflation expectations from Banco de México's Survey. The dotted line corresponds to the midpoint of the range for the short-term neutral real rate in the long term, which is now between 1.8 and 3.4%. Source: Banco de México.

Between September 2020 and February 2021, inflation expectations for the end of 2021 were revised upwards and those for the medium and long terms remained stable.
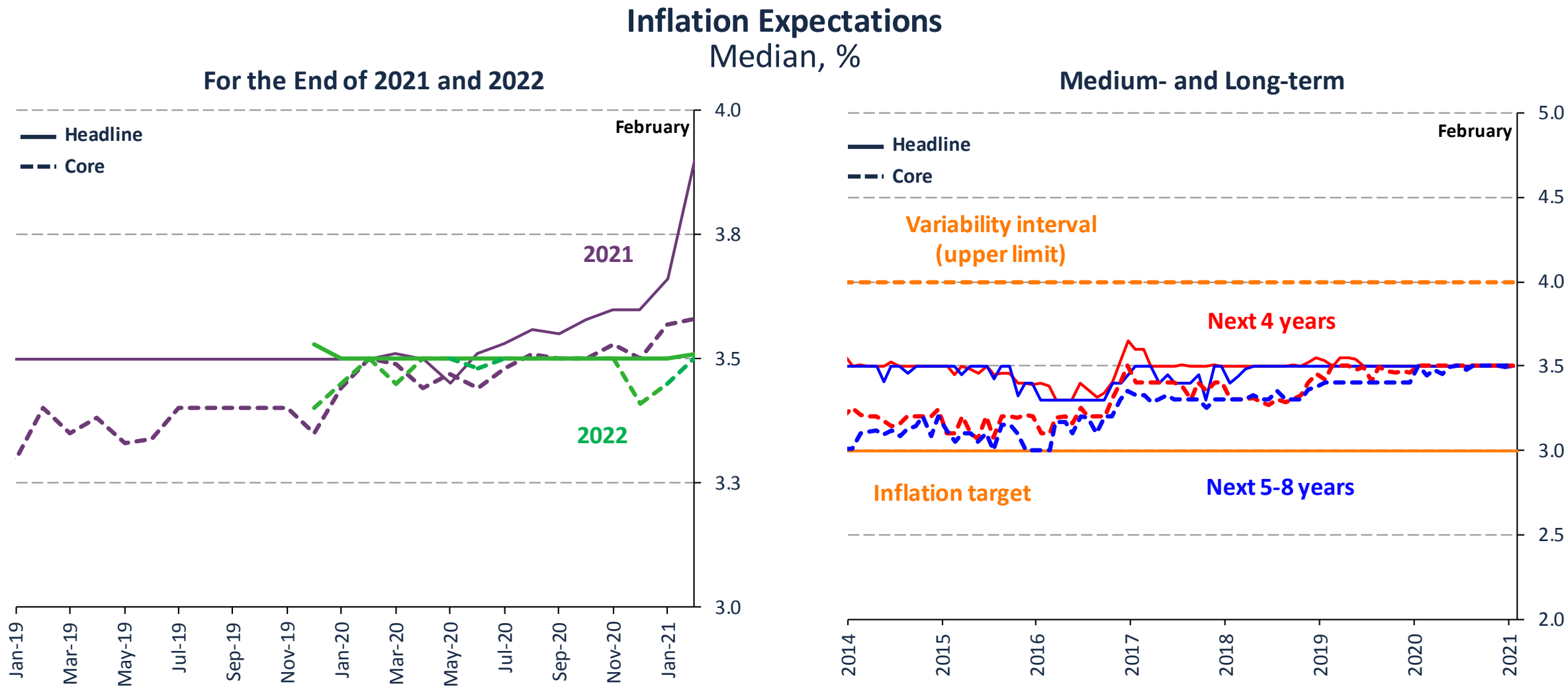
Inflation Expectations
Median, %

For the End of 2021 and 2022

Legend:
— Headline
-- Core

Labels: February, 2021, 2022

Y-axis: 3.0, 3.3, 3.5, 3.8, 4.0

X-axis: Jan-19, Mar-19, May-19, Jul-19, Sep-19, Nov-19, Jan-20, Mar-20, May-20, Jul-20, Sep-20, Nov-20, Jan-21

Source: Banco de México's Survey of Private Sector Forecasters.

Medium- and Long-term

Legend:
— Headline
-- Core

Labels: February, Variability interval (upper limit), Next 4 years, Next 5-8 years, Inflation target

Y-axis: 2.0, 2.5, 3.0, 3.5, 4.0, 4.5, 5.0

X-axis: 2014, 2015, 2016, 2017, 2018, 2019, 2020, 2021

Source: Banco de México's Survey of Private Sector Forecasters.

During most of Q4-2020, Mexican financial markets performed favorably, although recently volatility increased and the exchange rate depreciated.

Market Indicators that Measure Domestic Sovereign Credit Risk[1]
Basis points

South Africa (BB-)
Brazil (BB-)
Mexico (BBB)
Colombia (BBB-)
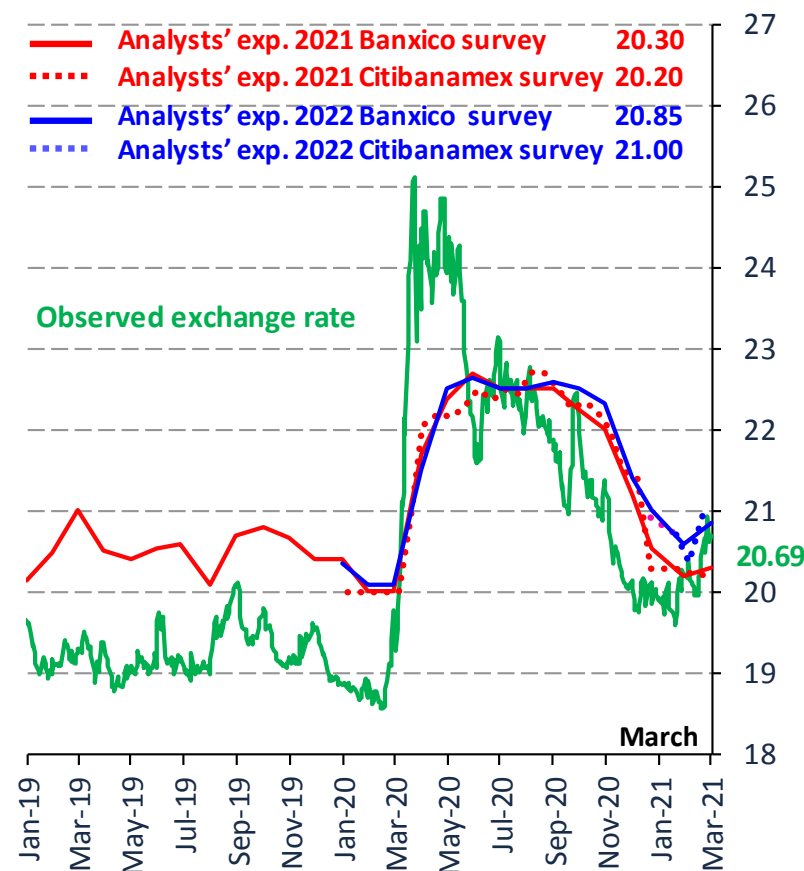Peru (BBB+)
Chile (A+)
Thailand (BBB+)

March
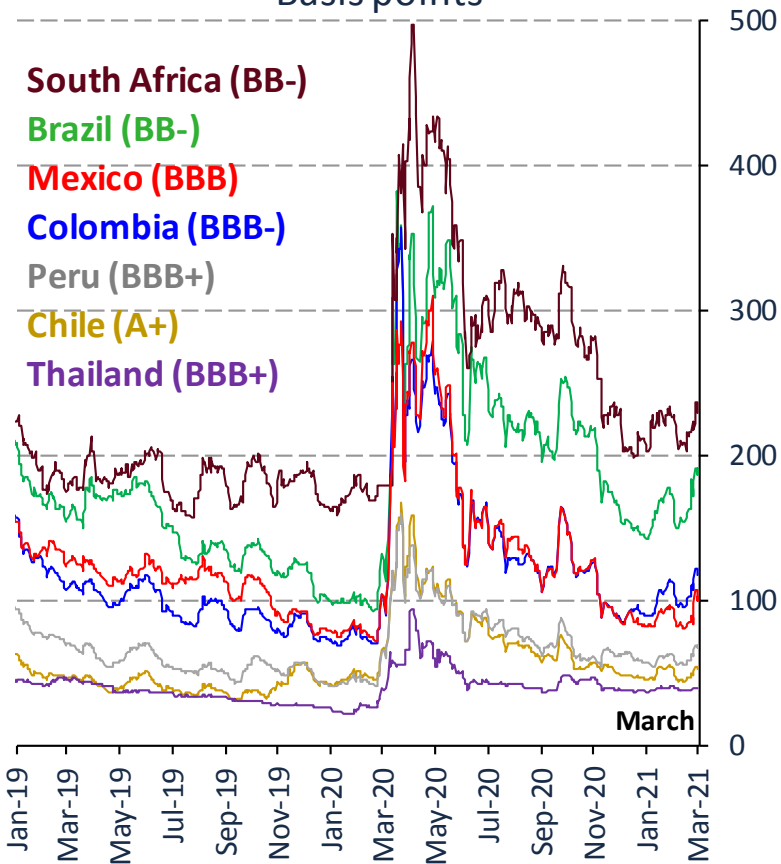
1/ Refers to 5-year Credit Default Swaps (CDS).
Note: The mean of the sovereign rate for each country is shown in parenthesis and corresponds to the mean of the rates by Fitch Ratings, Moody's and Standard & Poor's, normalized to the scale of the latter.
Source: Bloomberg.

Volatility in Mexican Financial Markets
%

Fixed-income markets[4]
Stock markets[2]
FX markets[3]

March
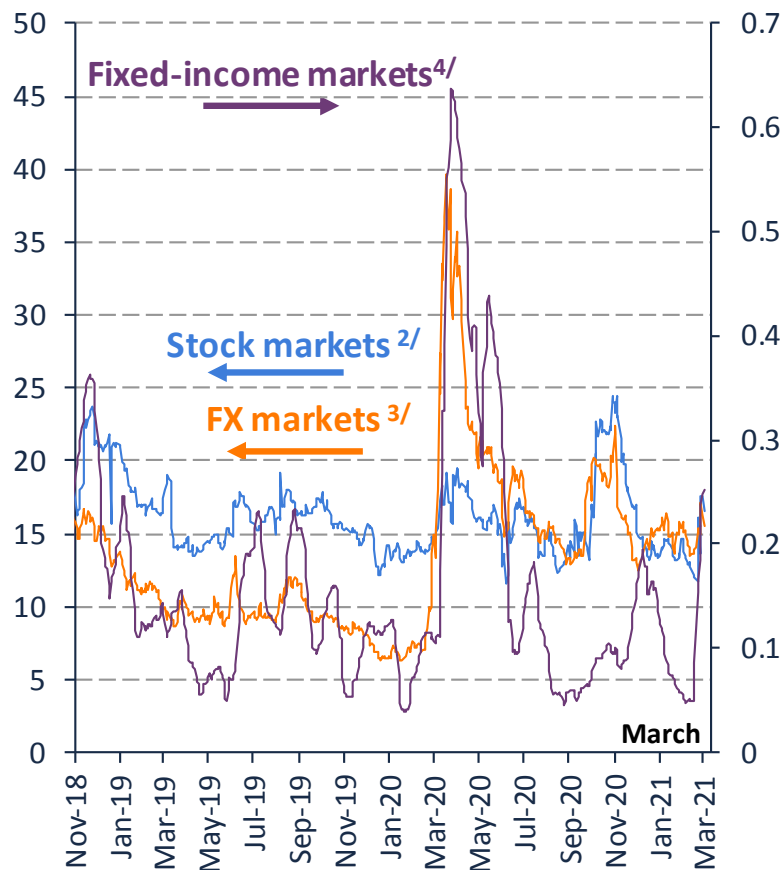
2/ Refers to the volatility index of S&P of the Mexican Stock Exchange.
3/ Refers to volatility implied in 1-month Mexican peso options.
4/ Refers to a standard deviation of a 30-day moving window of 10-year interest rates in Mexico.
Source: Bloomberg and Proveedor Integral de Precios (PiP).

Nominal Exchange Rate [5]
Pesos per US dollar

Analysts' exp. 2021 Banxico survey	20.30
Analysts' exp. 2021 Citibanamex survey	20.20
Analysts' exp. 2022 Banxico survey	20.85
Analysts' exp. 2022 Citibanamex survey	21.00

Observed exchange rate

20.69

March

5/ Observed exchange rate refers to the daily FIX exchange rate. Numbers In blue and red correspond to the medians of Banco de México's survey for February and the Citibanamex survey for February 22, 2021.
Source: Banco de México and Citibanamex.

During Q4-2020 and until F1-February, interest rates in general registered decreases. However, recently, longer-term rates exhibited increases, in line with US long-term rates.

Government Bond Interest Rates In Mexico
%

30 years
10 years
3 years
1 day
March
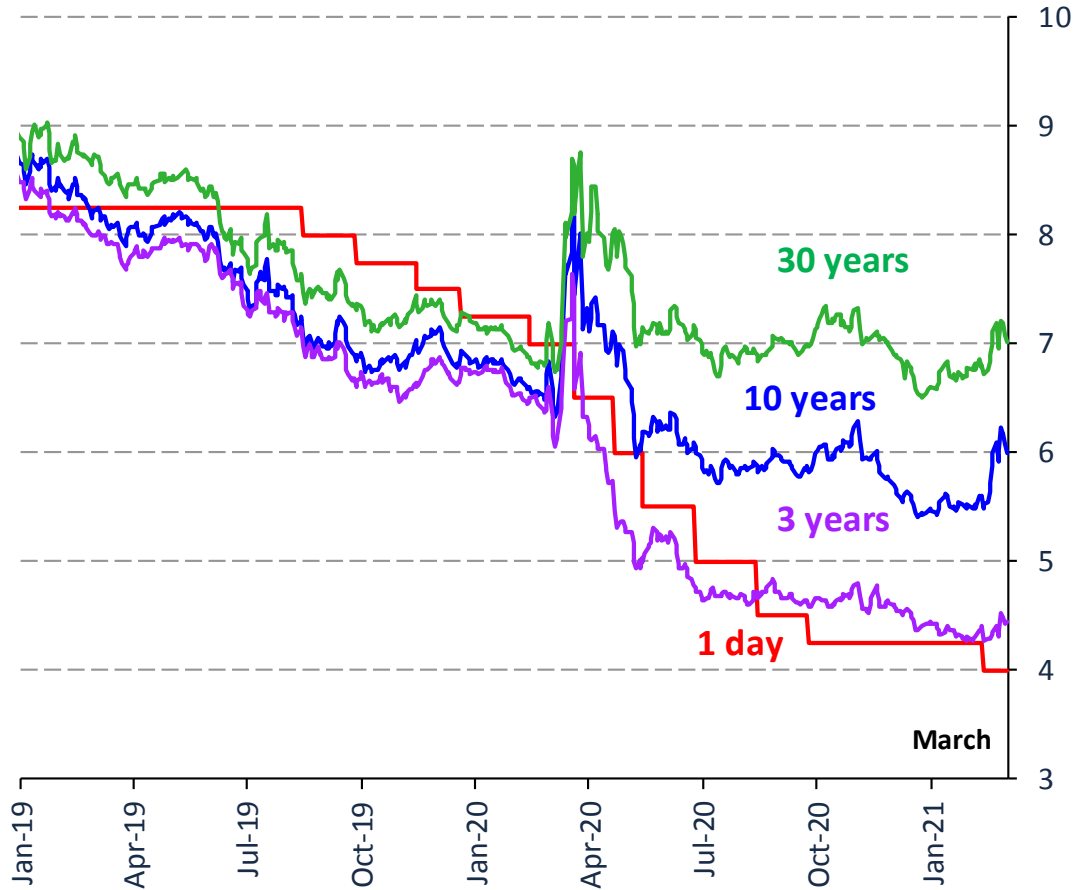
Source: Proveedor Integral de Precios (PiP).

Yield Curve of Mexico
%

Mar-31-20
Sep-30-20
Dec-31-20
Mar-02-21

Note: The gray lines refer to the daily yield curves since March 30, 2020.
Source: Proveedor Integral de Precios (PiP).

On February 25, 2021, Banco de México announced the modification to the term of the facilities approved by the Governing Board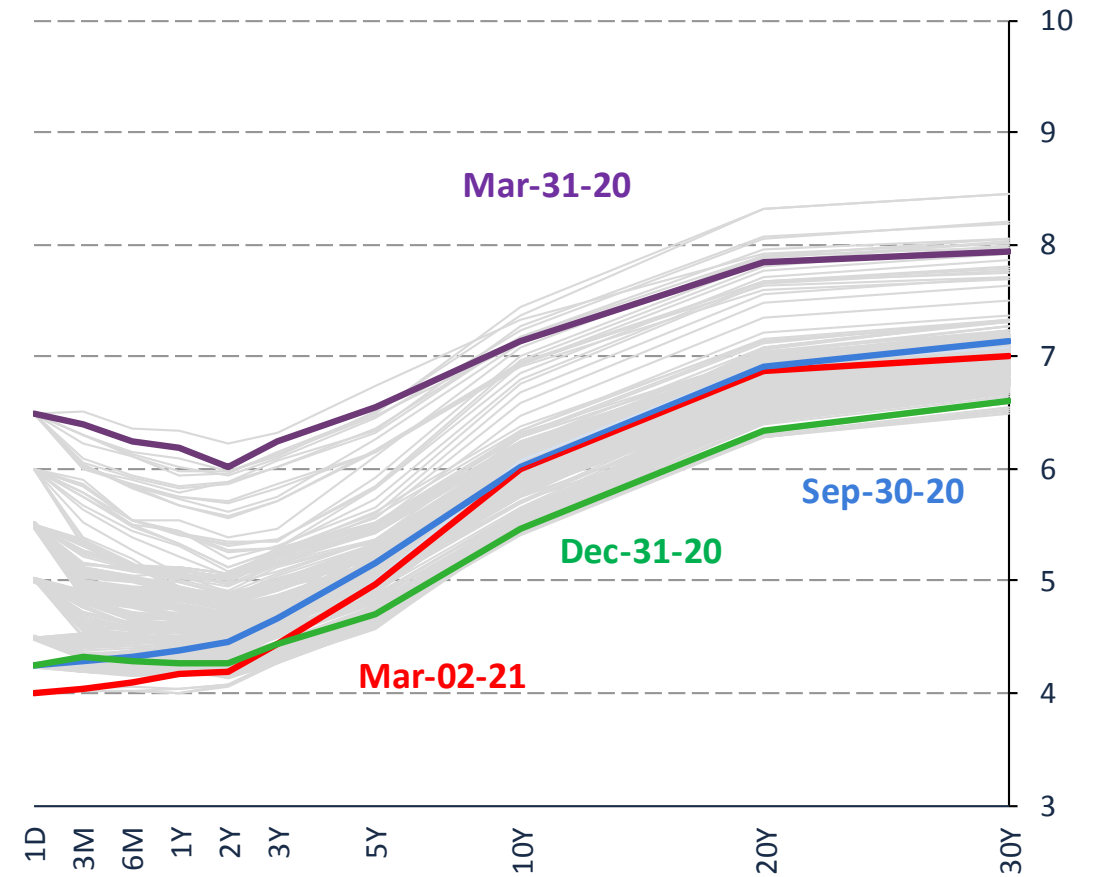 on April 21, 2020. These contributed to generate more favorable financial conditions in Mexico, which, at the margin, may have reduced the probability of a more adverse growth scenario.

A first group of measures aims at **ensuring the stability of the national currency's purchasing power,** promoting the **sound development of the financial system,** and fostering the **well-functioning of the payment systems.**

A second group of measures aims at **providing liquidity and strengthening credit channels** for the sound development of the financial system and complements the set of tools that Banco de México has permanently in place.

Distribution of the Difference of IGAE Annualized Growth Rate for Six Months Ahead Under Different FCIs [1]

In percentage points

Estimated distribution in December minus counterfactual distribution

1.1
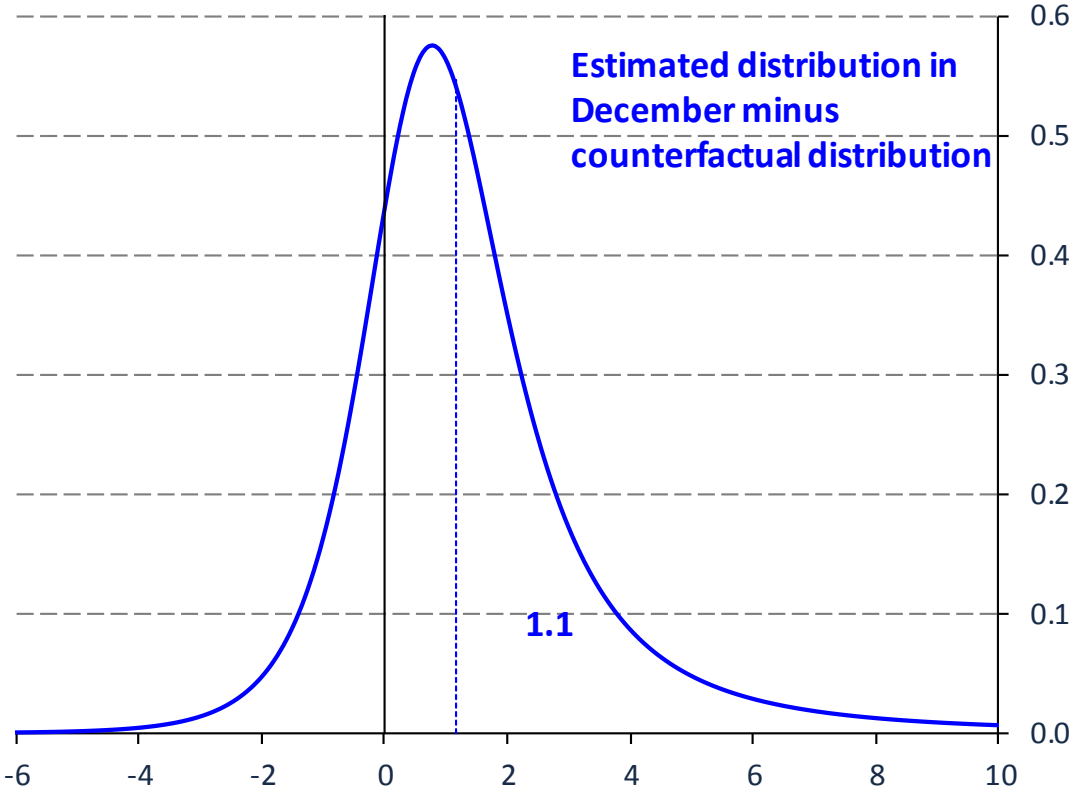
1/ Refers to Financial Conditions Indexes.
Note: Dotted line shows the median of the distribution. The distribution of the difference between the growth distributions is obtained based on a random sampling of the observed and counterfactual distributions assuming a correlation of 0.9 between them considering that the growth results between both distributions should only differ due to differences in financial conditions and not due to independent effects.
Source: Prepared by Banco de México with data from Haver Analytics and Bloomberg.

Outline

Economic Activity Outlook

Scenarios for the Trajectory of GDP[1]
Percentage growth rates

Report		2021	2022
Current	Central Scenario	4.8	3.3
	Lower Limit Trajectory	2.8	3.0
	Upper Limit Trajectory	6.7	3.4
Previous	Central Scenario	3.3	2.6
	Lower Limit Trajectory	0.6	3.8
	Upper Limit Trajectory	5.3	2.7

1/ For more details about the central baseline scenarios and trajectories, see the October – December 2020 Quarterly Report, Banco de México, pages 101-102.

Current Account
% of GDP

Report	2021	2022
Current	-0.5 to 0.3	-0.9 to -0.2
Previous	-0.8 to 0.2	-1.0 to -0.4

Increase in Number of IMSS-insured Jobs
Thousands

Report	2021	2022
Current	250 to 570	390 to 590
Previous	150 to 500	300 to 500

Trajectory of Mexico's GDP
Q4-2019 = 100, s. a.

Legend:
- Central Scenario previous Report
- Interval previous Report
- Central Scenario
- Interval
- Observed
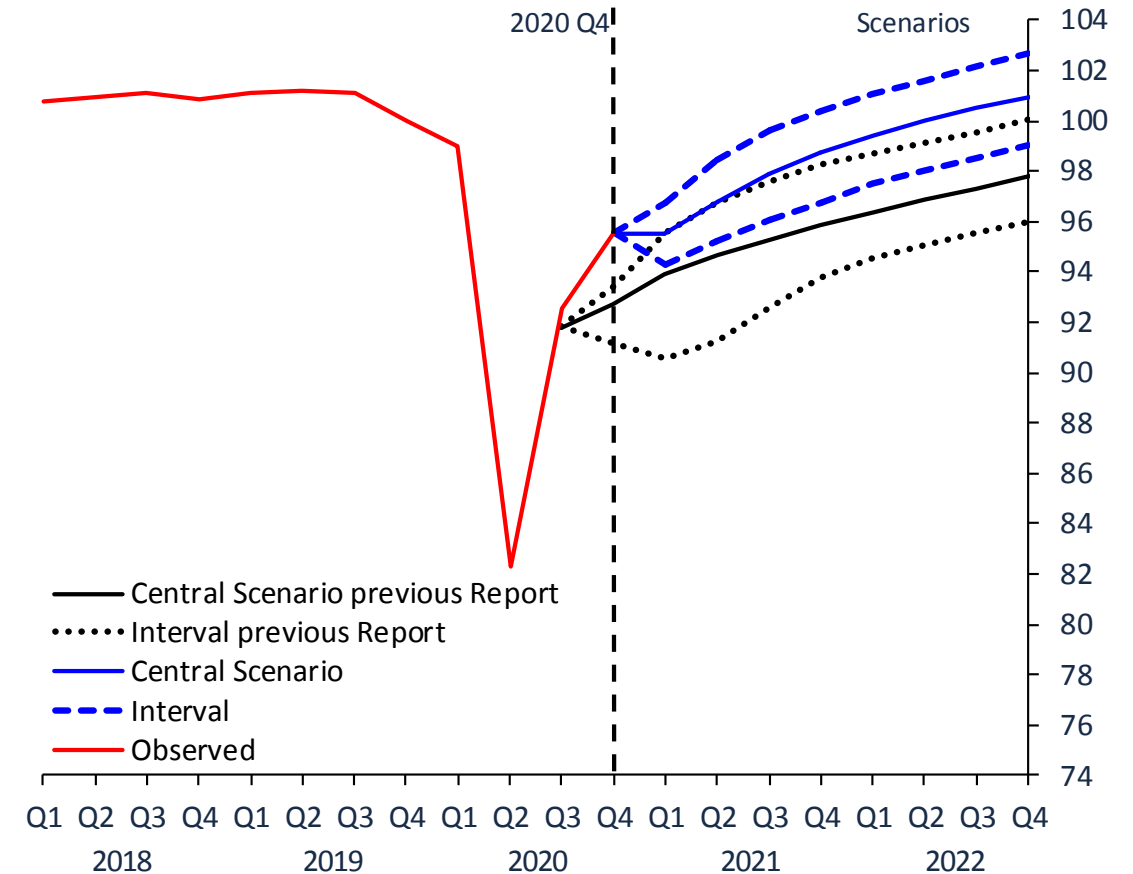
s. a. / Seasonally adjusted series.
Note: The forecasts for the scenarios of the present Report begin in Q1-2021, whereas the scenarios of the previous Report started in Q4-2020.
Source: INEGI and Banco de México.

Risks to Growth

The risks to the central baseline scenario are biased to the downside.

To the downside

⬇ **Greater social distancing measures or delays in the vaccination process.**

⬇ **Additional episodes of financial volatility in international financial markets.**

⬇ **Greater or more permanent pandemic repercussions.**

⬇ **Sovereign and Pemex's credit ratings downgrades.**

⬇ **An environment of domestic uncertainty that affects investment.**

⬇ **That no adequate agreement is reached on the outsourcing regulation.**

To the upside

⬆ **That the pandemic fades, as a result of vaccines and treatments.**

⬆ **That the provided stimulus offsets the effects of the pandemic and supports the global economic recovery.**

⬆ **That external demand boosts exports more than anticipated.**

⬆ **That the recent entry into force of USMCA fosters greater-than-expected investment.**

⬆ **That the ongoing electoral process leads to higher aggregate spending levels.**
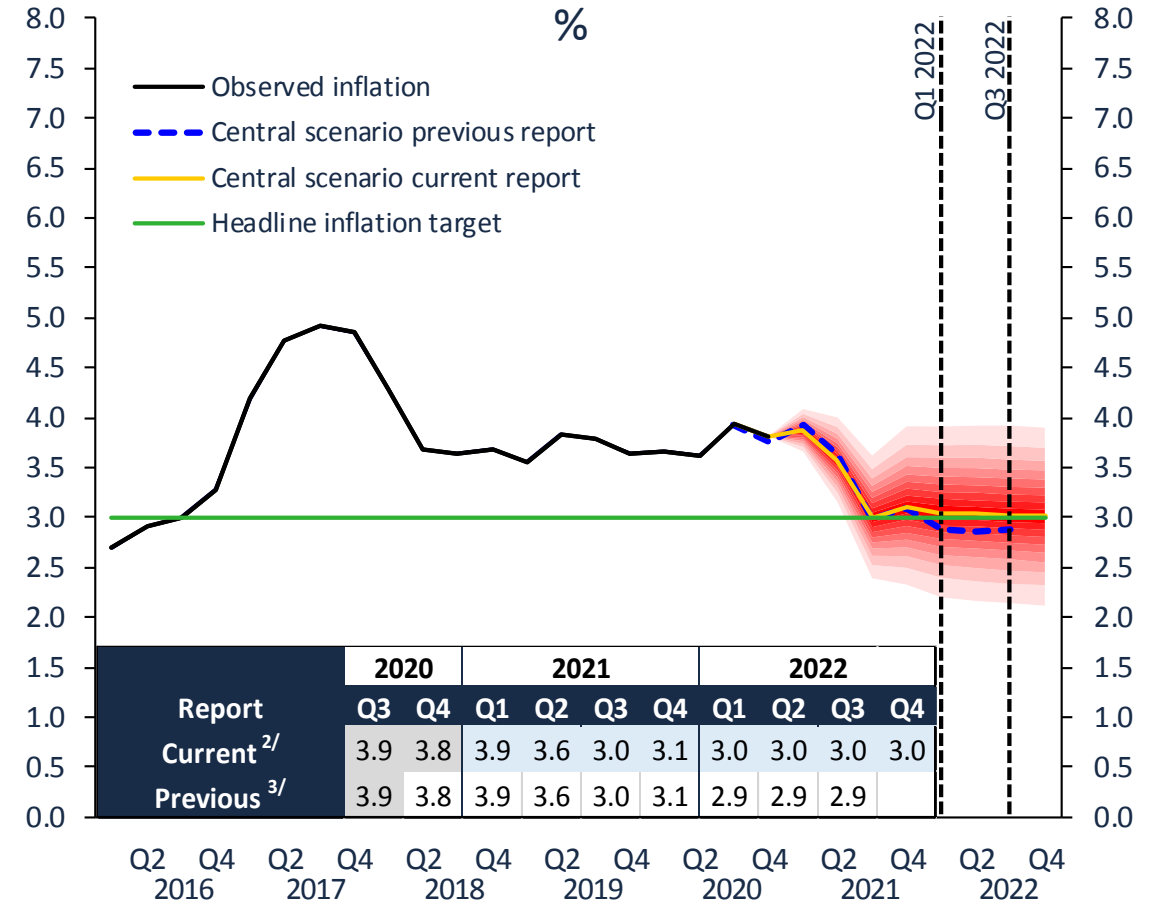
Annual <u>headline inflation</u> is expected to increase in Q2-2021 due to the arithmetic effects of the decline in energy prices in the previous year, and then decrease, albeit with some rebound in Q4-2021. Headline inflation will be around 3% in the 12-24 month forecast horizon. <u>Core inflation</u> remains practically at the same levels of the previous forecast at around 3% from 3Q-2021.

Fan Charts [1/]

Annual Headline Inflation

%

Q1 2022 | Q3 2022

- Observed inflation
- Headline inflation target
- Central scenario previous report
- Central scenario current report
- Variability interval

Report	2020		2021				2022			
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Current [2/]	3.9	3.5	3.8	4.5	3.2	3.6	3.1	3.0	3.2	3.0
Previous [3/]	3.9	3.6	3.6	4.3	3.1	3.3	3.2	3.1	3.1	

Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4
2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022

Annual Core Inflation

%

Q1 2022 | Q3 2022

- Observed inflation
- Central scenario previous report
- Central scenario current report
- Headline inflation target

Report	2020		2021				2022			
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Current [2/]	3.9	3.8	3.9	3.6	3.0	3.1	3.0	3.0	3.0	3.0
Previous [3/]	3.9	3.8	3.9	3.6	3.0	3.1	2.9	2.9	2.9	

Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4 | Q2 Q4
2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022

1 / Quarterly average of annual inflation. The next four and six quarters are indicated with dotted vertical lines from the first quarter of 2021, that is, the first and third quarters of 2022 respectively; periods in which the monetary policy transmission channels fully operate. 2/ Forecast since February 2021. 3/ Forecast since November 2020. Source: Banco de México and INEGI.
Fuente: Banco de México and INEGI.

Risks to Inflation Outlook within the Forecast Horizon
The balance of risks for the inflation forecast remains uncertain.

To the downside

⬇ **Greater effects of a negative output gap or of additional social distancing measures.**

⬇ **Lower inflationary pressures worldwide.**

⬇ **That the exchange rate appreciates.**

⬇ **That energy prices are lower than anticipated.**

⬇ **That, as a result of the slack in the economy, wage revisions do not exert pressure on prices.**

To the upside

⬆ **Pressures on some components of core inflation due to the recomposition of spending patterns.**

⬆ **Episodes of exchange rate depreciation.**

⬆ **Diverse cost-related pressures for firms.**

⬆ **Increase in the relative demand for certain goods and services.**

⬆ **That energy prices reach higher-than-anticipated levels.**

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 Banco de México's target**, during the time frame in which monetary policy operates.

- It is necessary **to strengthen the macroeconomic fundamentals** and adopt the **necessary actions** in the monetary and fiscal fronts, to promote a **better adjustment of the national financial markets** and the **economy as a whole**.

- **Conditions** to attract **more investment, improve the perception on the country's business climate**, and **safeguard and strengthen the institutional environment** need to be fostered. It is also necessary to **address pending institutional and structural problems**, maintain **flexibility in resource allocation**, and **ensure the necessary microeconomic** functioning to promote the reactivation of productive activity and employment.

Annex – Boxes

1   Foreign Currency Flows to Mexico and Support Measures for Mexican Migrants and their Families

2   Impact of the COVID-19 Pandemic on Sectoral Economic Activity in Mexico and the U.S.

3   The Labor Participation Rate in light of the COVID-19 Shock

4   The Reform to Mexico's Pension System: Potential Effects on Retirement, the Dynamics of Mandatory Savings, and Public Finances

5   Intensive and Extensive Margins in the Effects of the 2020 "Buen Fin" Sales Campaign on Non-Food Merchandise Inflation

6   Evolution of Exchange Rate Volatility

7   The Effects of Financial Conditions on Mexico's Economic Outlook