Macro scenario - Mexico

November 18, 2024

More volatility ahead

- A stronger USD and a higher domestic risk premium add to the depreciation of the MXN. We updated our 2025 FX forecast to MXN 21.0/USD, from MXN 19.3/USD.
- We believe that Banxico's recent guidance opens the door for continued rate cuts and a sustained easing pace of 25-bp. Higher expected interest rates in the U.S. led to the upward revision of our YE25 call to 9.0% from 7.5%.
- We revised our 2025 growth forecast down to 1.0% from 1.3%, on higher rates and a continuous deterioration of the institutional investment outlook, plus uncertainty about the relationship with the U.S.

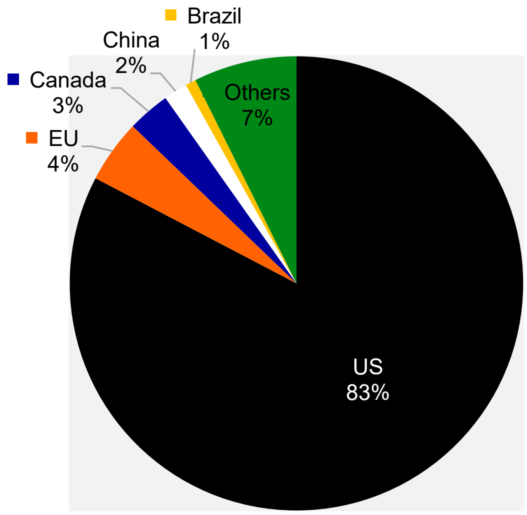
Trump administration is expected to have a limited impact on Mexico, but uncertainty and volatility are likely to increase

Mexico has significant exposure to the U.S. due to its geographical location and the integration of manufacturing supply chains, reflected in the high share of total exports to the U.S. (close to 80%). Despite the lingering uncertainties, we do not expect the incoming Trump administration to significantly jeopardize the relationship between the countries in the near term, given that it is highly beneficial for both.

Although rising tariffs on all exported goods is unlikely, we anticipate increased market volatility amid tariff threats and a stronger U.S. stance on bilateral trade. The country faced a similar situation of increased volatility and uncertainties during the first Trump administration, but Mexico ultimately benefitted from the higher growth in the U.S. and nearshoring opportunities. On a related note, the United States-Mexico-Canada Agreement (USMCA) is expected to be renegotiated in 2026. We believe that Mexico is in a less favorable position to negotiate, but is likely to cooperate to maintain the trade agreement.

We expect negotiations to focus on activity of Chinese firms operating and selling through Mexico, particularly auto parts. Immigration and increased border control will also take the spotlight.

Exports to the U.S. account for more than 80% of Mexico's exported goods



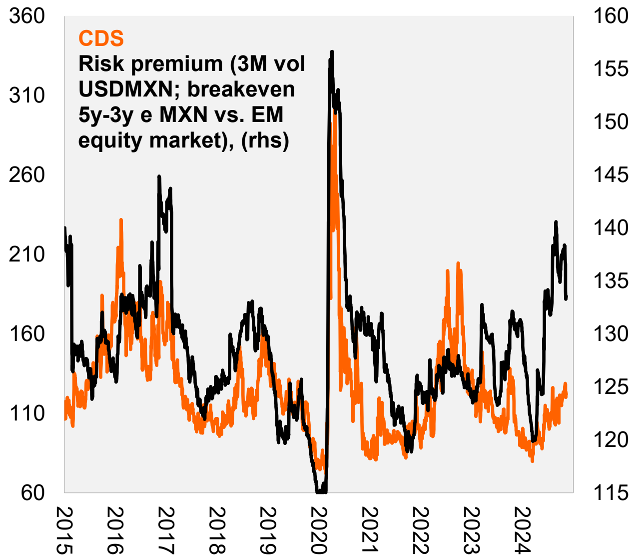
Source: INEGI, Itaú

MXN depreciation next year

We updated our FX forecast to MXN 20.0/USD for this year (from MXN 19.0/USD) and MXN 21.0/USD for next year (from MXN 19.3/USD). We now expect the USD to remain strong and end 2025 near the current levels. A higher domestic risk premium also adds to the depreciation in our MXN call.

The recent judicial reform – which includes the election of judges by popular vote – and progress in the initiative to strip autonomous entities (regulatory agencies) of their independence have contributed to the recent rise in domestic risk premium to peak levels.

Higher domestic risk premium



Source: Bloomberg, Itaú

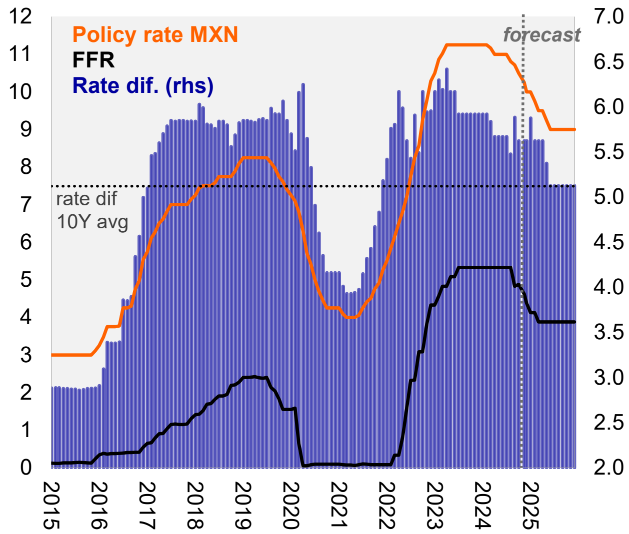
Fewer policy rate cuts in 2025

We believe that Banxico's recent guidance opens the door for continued rate cuts and a sustained easing pace of 25-bp (YE24 rate of 10%).

A well-behaved, albeit weaker, MXN, deteriorating growth outlook for next year, lower inflation, and the FOMC's easing cycle should open the door for Banxico to continue its rate cuts next year, but at a slower pace than we previously expected.

We revised our YE25 call to 9.0% from 7.5%, which implies a 25-bp cut at each of the meetings through June 2025. We now expect fewer cuts by the Fed next year, leaving Banxico with less room to continue to cut rates after March 2025 without affecting the domestic currency and inflation.

MXN/USD interest rate differential expected to return to historical average in 2025



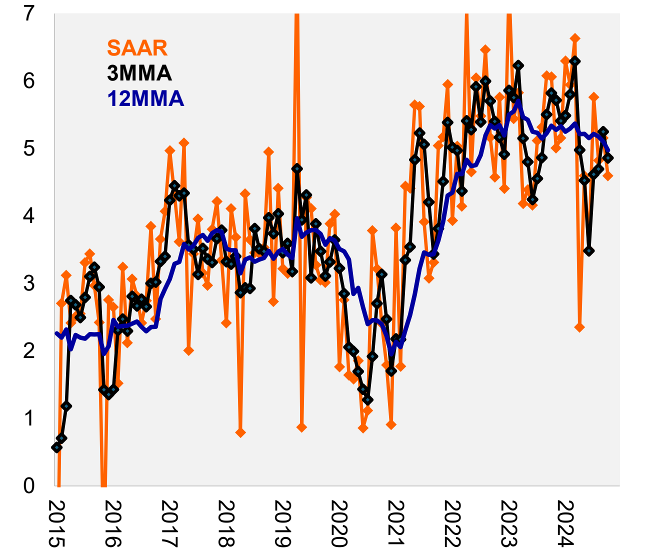
Source: Bloomberg, Itaú

Sticky service inflation

Headline CPI rose by 0.55% mom in October, while core CPI accelerated 0.28%. On an annual basis, headline inflation rose to 4.76% (from 4.58% in September), while core inflation fell to 3.80% (from 3.91% in September). On a positive note, tradables maintained the disinflation trend (down 2.8% yoy), which is expected to continue in the following month, especially due to the effect of temporary sales from "El Buen Fin" promotional campaigns. On the flipside, MXN depreciation during the second half of this year poses upside potential for goods inflation next year.

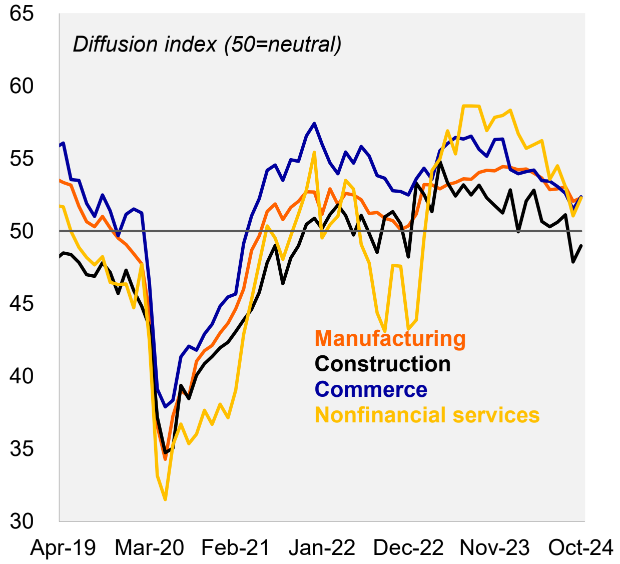
Service inflation remains sticky and above Banxico's target range of 3+/-1% (5.0% yoy), mainly reflecting the still-tight labor market. The unemployment rate is running close to 3%, still near the historical lows.

Core services remain close to 5%



Source: INEGI, Itaú

Some improvement on business confidence at the margin



Source: INEGI, Itaú

Weaker activity outlook for 2025

Preliminary data from leading indicators showed some recent improvement. We forecast 2024 GDP growth of 1.4%, consistent with a gain of 1.0% qoq in 3Q24 and 0.2% qoq in 4Q24.

We now expect 2025 GDP growth of 1.0%, from 1.3% previously. We expect growth to lose momentum next year, to an average pace close to 0.1% qoq. The investment outlook is set to continue to deteriorate. Higher than previously expected rates will also affect the economy next year.

With deteriorating activity, higher rates, and a weaker currency, with conflicting effects on prices, we maintained our CPI forecast unchanged at 4.3% for this year and 3.9% for next year.

Andrés Pérez M.
Julia Passabom

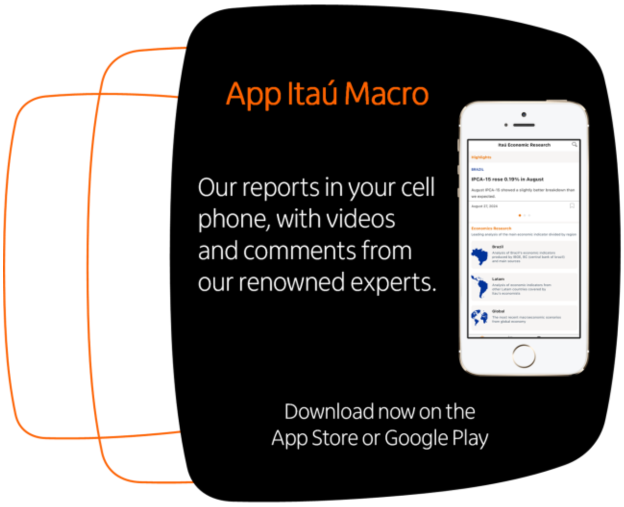
Mexico | Forecast

	2019	2020	2021	2022	2023	2024F		2025F	
						Current	Previous	Current	Previous
Economic Activity									
Real GDP growth - %	-0.4	-8.4	6.0	3.7	3.2	**1.4**	1.4	**1.0**	1.3
Nominal GDP - USD bn	1,298	1,129	1,318	1,463	1,796	**1,931**	1,931	**1,877**	1,908
Population (millions)	125.6	127.7	129.0	130.1	131.2	**132.3**	132.3	**133.4**	133.4
Per Capita GDP - USD	10,335	8,844	10,218	11,241	13,688	**14,593**	14,593	**14,075**	14,305
Unemployment Rate - year avg	3.5	4.4	4.1	3.3	2.8	**2.7**	2.7	**3.0**	2.7
Inflation									
CPI - %	2.8	3.2	7.4	7.8	4.7	**4.3**	4.3	**3.9**	3.9
Interest Rate									
Monetary Policy Rate - eop - %	7.25	4.25	5.50	10.50	11.25	**10.00**	10.00	**9.00**	7.50
Balance of Payments									
MXN / USD - eop	18.9	19.9	20.5	19.5	17.0	**20.0**	19.0	**21.0**	19.3
Trade Balance - USD bn	5.4	34.2	-10.8	-26.9	-5.5	**-10.0**	-10.0	**-15.0**	-15.0
Current Account - % GDP	-0.3	2.4	-0.3	-1.2	-0.3	**-0.4**	-0.4	**-0.6**	-0.6
Foreign Direct Investment - % GDP	2.3	2.8	2.7	2.7	1.7	**3.0**	3.0	**3.5**	3.5
International Reserves - USD bn	180.9	195.7	202.4	199.1	212.8	**225.0**	220.0	**225.0**	225.0
Public Finances									
Nominal Balance - % GDP	-1.6	-2.8	-2.8	-3.2	-3.3	**-5.9**	-5.0	**-3.9**	-2.5
Primary Balance - % GDP	1.1	0.1	-0.3	-0.4	-0.1	**-1.4**	-1.4	**0.6**	0.9
Net Public Debt - % GDP	43.9	49.9	48.9	47.6	46.8	**51.4**	50.2	**51.8**	50.6

Source: IMF, Bloomberg, INEGI, Banxico, Haver and Itaú

Macro Research – Itaú
Mario Mesquita – Chief Economist

To access our reports and forecast visit our website:
https://www.itau.com.br/itaubba-pt/macroeconomic-analysis



Relevant Information

1. This report has been prepared and released by the Macro Research Department of Itaú Unibanco S.A. (“Itaú Unibanco”). This report is not a product of the Equity Research Department of Itaú Unibanco or Itaú Corretora de Valores S.A. and shall not be construed as a research report (“relatório de análise”) for the purposes of Article 1 of the CVM Instruction NR. 20, dated 2021.

2. The exclusive purpose of this report is to provide macroeconomics information and it does not constitute and shall not be construed as an offer to buy or sell or a solicitation of an offer to buy or sell any financial product, or to participate in any particular trading strategy in any jurisdiction. The information herein is believed to be reliable as of the date on which this report was released and it has been obtained from public sources believed to be reliable. However, Itaú Unibanco does not make any explicit or implied representation or warranty as to the completeness, reliability or accuracy of such information, nor does this report intend to be a complete statement or summary of the markets or developments referred to herein. Itaú Unibanco has no obligation whatsoever to update, modify or amend this report and inform the reader accordingly.

3. The opinions contained herein reflect exclusively the personal views of the analyst responsible for this report and were prepared independently and autonomously, including in relation to Itaú Unibanco, Itaú Corretora de Valores S.A. and any other companies within their economic group.

4. This report may not be reproduced or redistributed to any other person, in whole or in part, for any purpose, without the prior written consent of Itaú Unibanco. Additional information on the financial products mentioned in this report may be available upon request. Itaú Unibanco and/or any other company within its economic group is not and shall not be liable for any investment decisions (or otherwise) based on the information provided herein.

Additional Note: This material does not take into consideration the objectives, financial situation or specific needs of any particular client. Clients must obtain financial, tax, legal, accounting, economic, credit and market advice on an individual basis, based on their personal characteristics and objectives, prior to making any decision based on the information contained herein. By accessing the material, you represent and confirm that you understand the risks related to the financial instruments described in this material and the laws in your jurisdiction relating to the provision and sale of financial service products. You acknowledge that this material contains proprietary information and you agree to keep this information confidential for your exclusive use.

For inquiries, suggestions, complaints, criticisms and compliments, talk to Itaú’s CSCC: 0800 728 0728. Or contact us through our portal https://www.itau.com.br/atenda-itau/para-voce/. If you are not satisfied with the proposed solution, please contact the Itaú Corporate Ombudsman: 0800 570 0011 (on weekdays from 9 AM to 6 PM) or our PO Box 67.600, São Paulo-SP, Zip Code 03162-971. Hearing impaired, every day, 24h, 0800 722 1722.