

# Ahead of the Curve

July 22, 2016

Market focus this week will on *INEGI's* GDP preliminary report

- The Mexican economy probably grew 2.2% in 2Q16.** On Friday, *INEGI* will publish its preliminary estimation of GDP. Given the economic figures published for April and May, we believe that the preliminary estimation will show a 2.2% yoy growth for the Mexican economy during 2Q16, below the 2.6% observed in 1Q16. In this regard, the lower growth of the Mexican economy will be mainly explained by the scant expansion in the industrial sector (1% yoy) derived from the sharp deceleration in the manufacturing industry. Moreover, we believe that services will continue to show a favorable performance (+3% yoy) driven by the strong growth of remittances (10.7% yoy during April and May), the recovery of private bank credit (10.7% yoy in real terms over the same period), and the higher growth of the Mexican labor market (3.7% yoy).

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**Mexico weekly calendar**

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Mon 25-Jul	9:00am	Retail sales	May	% yoy	5.7	5.3	10.6
		sa		% m/m	-0.3	-0.6	-1.4
Tue 26-Jul	9:00am	Trade balance	June	US\$ mn	-688.0	-695.0	-527.4
		Total exports		% yoy	3.0	--	0.3
		Oil exports		% yoy	-26.5	--	-27.9
		Non-oil exports		% yoy	-1.4	--	2.5
		Total imports		% yoy	-3.3	--	-1.6
Tue 26-Jul	9:00am	Global economic indicator	May	% yoy	1.5	2.2	3.0
		Primary activities		% yoy	-0.8	--	2.2
		Industrial production		% yoy	0.4	--	1.9
		Services		% yoy	2.8	--	3.6
Tue 26-Jul	10:00am	International reserves	22-Jul	US\$ bn	--	--	177.7
Tue 26-Jul	12:30pm	Government weekly auction: 1-, 3-, 6-, and 12-month Cetes; 30y MBono (Nov'42); 30y Udibono (Nov'46); 5y Bondes D					
Wed 27-Jul	9:00am	Unemployment rate	June	%	4.05	4.05	4.03
		sa		%	4.07	4.0	4.00
Fri 29-Jul	9:00am	GDP	2Q16	% yoy	2.2	2.4	2.6
		(sa)		% q/q	-0.2	-0.2	0.8
		Primary activities		% yoy	3.7	--	3.1
		Industrial production		% yoy	1.0	--	0.4
		Services		% yoy	3.0	--	3.7
Fri 29-Jul	10:00am	Comercial banking credit	June	% yoy	10.4	--	10.9
		Consumption		% yoy	9.4	--	10.1
		Housing		% yoy	9.0	--	10.2
		Non-banking private firms		% yoy	11.9	--	11.9
Fri 29-Jul		Budget balance	June	MXN bn	--	--	72.8

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

**Retail sales will post a 5.7% yoy expansion in May.** On Monday at 9:00am (EDT), *INEGI* will publish its retail sales report for May, where we anticipate a 5.7% yoy expansion. Retail sales' growth will be explained by the favorable performance of durable goods sales. In particular, vehicles sales increased by 19.2% yoy according to *AMIA*'s report. Moreover, *ANTAD* total store sales edged-up 3.5% yoy in real terms during the period in question. However, retail sales growth will be bounded by the 3% yoy contraction in consumption goods imports –which have a strong correlation with retail sales.

Looking ahead, we believe that retail sales and private consumption will continue to show a favorable performance derived from: (1) An improvement in private banking credit; (2) the contained levels of inflation; (3) the stronger growth dynamics in the Mexican labor market; and (4) the higher growth in remittances inflows.

**We expect a 1.6% yoy expansion in May's IGAE.** On Tuesday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for May (GDP monthly proxy), where we expect a 1.6% yoy expansion. We believe that Mexico's economic growth in May will be explained by a 0.4% growth in industrial production, a 2.8% yoy increase in services output, and a 1.3% expansion in agricultural production.

As we had mentioned in our last IP report, the scant 0.4% yoy increase in industrial production during May was explained in part by the deceleration in manufacturing output (+0.8% yoy). Moreover, construction output increased 2.8%, as a result of the 5% growth in private building projects, whereas public civil engineering construction projects declined 8% yoy, given the fiscal cuts implemented by the Federal Government. On the other hand, mining activity declined 4.7% as a result of the significant contraction in Mexico's oil production.

We also believe that the 2.8% yoy estimated expansion in services will be explained by the recovery in private consumption. In particular consumers' spending is gaining momentum, whereas formal job creation has observed a significant recovery in the first five months of the year.

**Exports will continue to fall in June.** On Tuesday, at 10:00am (EDT), *INEGI* will make available its trade report for June, where we expect to see a US\$688 million deficit. On the exports side, we will probably see a 26.5% yoy contraction of oil exports given the significant fall in oil exports and prices during the period in question. Moreover, non-oil exports could have decreased 1.4% yoy, on the back of a 1.8% drop in manufacturing exports.

On the imports side, we estimate a 3.3% yoy contraction in total imports. Taking a look at the breakdown, we believe that imports consumption goods decreased 5.1% yoy, while imports of intermediate goods could have fallen 2.4% yoy. Finally, we estimate a 7.6% reduction in capital goods imports.

**Weekly international reserves report.** On Tuesday, at 10:00am (EDT), Banco de Mexico will release its weekly balance report. Last week, net international reserves decreased by US\$198mn amounting to US \$177.3 billion on July 15. According to Banxico's report, this figure comes mainly as a result of: (1) Dollar sales by Banxico to the Federal Government for US\$6mn; and (2) US\$192mn reduction due to changes in the valuation of the Central Bank's assets. In this context, the Central Bank has accumulated US\$580mn international reserves this year (please refer to the table below).

**Banxico's foreign reserve accumulation details**

US\$, million

	2015	15/Jul/2016	15/Jul/2016	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	176,735	177,315	-198	580
(B) Gross international reserve	177,597	179,843	333	2,246
Pemex	--	--	614	3,611
Federal government	--	--	-90	1,825
Market operations	--	--	0	-5,562
Other	--	--	-191	2,372
(C) Short-term government's liabilities	861	2,528	531	1,667

Source: Banco de México

**Weekly government bond auction.** Also on Tuesday, the Ministry of Finance (MoF) –via Banco de Mexico as its financial agent-, will offer 3-year fixed-rate Mbonos (Dec'19), and 3-year inflation-linked Udibonos (Jun'19), in addition to the “more traditional” 1-, 3-, and 6- month zero-coupon Cetes (please refer to the table below). As usual, the results will be released at 12:30pm (EDT).

**Auction specifics (Tuesday, July 26, 2016)**

	Maturity	Coupon rate, %	To be auctioned <sup>1</sup>	Previous yield <sup>2</sup>
<b>Cetes</b>				
1m	25-Aug-16	--	5,500	4.21
3m	27-Oct-16	--	9,500	4.38
6m	19-Jan-17	--	11,000	4.58
<b>Mbono</b>				
3y	11-Dec-19	5.00	7,500	5.26
<b>Udibono</b>				
3y	13-Jun-19	4.00	750	2.02

Source: Banorte-ixe with data from Banco de México

1. Except for Udibonos, which are expressed in UDI million, everything else is expressed in MXN million.

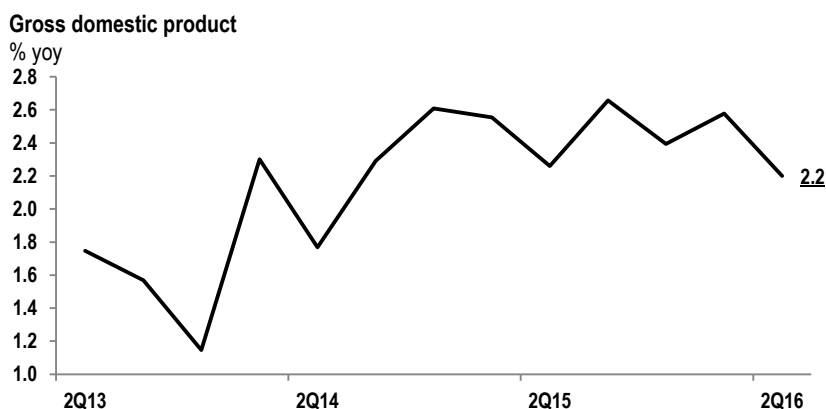
**Unemployment rate in June will stand at 4.05%.** On Wednesday, *INEGI* will publish its employment report for the sixth month of 2016, in which we estimate an unemployment rate of 4.05% nsa, marginally above the 4.03% observed in May. In seasonally-adjusted terms, we believe that the unemployment rate could stand at 4.07%, which implies a 0.07%-pts increase.

It is likely that June's labor market report will reflect the lower growth dynamics of the Mexican economy. In particular, the downward trend in public spending has already affected private investment projects, and these collateral effects will also have a negative impact in the Mexican labor market. Looking ahead, we believe that the labor market will continue to grow, but at a slower pace given the fiscal cuts that the Federal Government will continue to implement throughout the second half of the year.

**Mexico's preliminary GDP will stand at 2.2% yoy in 2Q16.** On Friday, *INEGI* will publish its preliminary estimation of GDP. For this preliminary figure, *INEGI* uses the economic reports published for the first two months of each quarter, and adds the available information for the third month. The missing figures for the last month of the quarter are estimated using econometric models. In this regard, the preliminary estimation of GDP will cover 80% with the direct information available, and will estimate the remaining 20%.

Given the economic figures published for April and May, we believe that the preliminary estimation will show a 2.2% yoy growth for the Mexican economy during 2Q16, below the 2.6% observed in 1Q16. In this regard, the lower growth of the Mexican economy will be mainly explained by the scant expansion in the industrial sector (1% yoy) derived from the sharp deceleration in the manufacturing industry, coupled with the recession in the mining sector, and the marginal recovery in construction output given the upward trend in private investment projects and the contraction in public investment projects.

Moreover, we believe that services will continue to show a favorable performance (+3% yoy) driven by the strong growth of remittances (10.7% yoy during April and May), the recovery of private bank credit (10.7% yoy in real terms over the same period), and the higher growth of the Mexican labor market (3.7% yoy).



Source: Banorte-ixe

**Banking credit will show a 10.4% yoy increase in June.** Banco de Mexico will make available its banking credit report on Friday at 10:00am (EDT). It is our take that banking credit continued flowing in June. In particular, we estimate a 10.4% yoy expansion in banking credit (in real terms), as a result of increases in the area of 9.4%, 9%, and 11.9% yoy in consumer, housing and business credit, respectively.

**The MoF's quarterly report.** On Thursday, the Ministry of Finance (MoF) will make its monthly finance report available for May. On the revenue side, we will be looking at non-oil tax collection as it provides additional information about domestic demand dynamics. Moreover, markets will focus on the spending side of the report, in order to assess the execution of the fiscal cuts announced by the *MoF*. Finally, it will be important to evaluate the evolution of public sector debt, which currently represents about 48% of Mexico's GDP.

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