

Ahead of the Curve

July 31, 2015

Market focus this week will on July's inflation report

- July's monthly inflation report.** On Friday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.17% m/m increase in July in line with market consensus, according to *Bloomberg*. In the core index, we expect an increase of 0.16% m/m, also in line with consensus. Inflation will be explained by pressures on services prices along with higher prices of fruit and vegetables. In the first case, services prices were up, particularly in the first half of the month, given the start of the summer holiday season. Moreover, our price monitoring suggests pressures on the price of some important fruits and vegetables, such as tomatoes
- Consumer confidence.** On Thursday, at 9:00am (EDT), Banxico and *INEGI* will publish its July's monthly survey on consumer confidence, where we expect a 4.3% yoy expansion, with the index reaching 94.4 points (vs. 90.5 in July 2014). We highlight that this could be the nine positive annual growth rate since October 2013

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Document for distribution among the general public

Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Mon 3-Aug	10:00am	Family remittances	June	US\$ mn	<u>2,160</u>	2,128	2,198
Mon 3-Aug	10:00am	Banxico's survey of economic expectations	July				
Mon 3-Aug	1:00pm	PMI's survey (IMEF)	July				
		Manufacturing		index	<u>52.8</u>	52.8	53.1
		Non-manufacturing		index	<u>51.4</u>	--	51.3
Tue 4-Aug	9:00am	Gross fixed investment	May	% yoy	<u>3.0</u>	2.6	5.3
		Machinery and equipment		% yoy	<u>4.9</u>	--	7.2
		Domestic		% yoy	<u>10.6</u>	--	12.4
		Imported		% yoy	<u>2.4</u>	--	5.1
		Construction		% yoy	<u>1.9</u>	--	4.2
Tue 4-Aug	10:00am	International reserves	31-Jul	US\$ bn	--	--	190.7
Tue 4-Aug	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 20y Mbono (Nov'34); 5y Bondes D					
Wed 5-Aug	4:30pm	Banamex bi-weekly survey of economic expectations					
Thu 6-Aug	9:00am	Consumer confidence	July	index	<u>94.4</u>	94.8	94.7
Fri 7-Aug	9:00am	CPI inflation	July	% m/m	<u>0.17</u>	0.17	0.17
				% yoy	<u>2.76</u>	2.76	2.87
		Core		% m/m	<u>0.16</u>	0.17	0.21
				% yoy	<u>2.30</u>	--	2.33

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

Family remittances will post a 5.8% yoy expansion. On Monday, at 10:00am (EDT), Banxico will make its family remittances monthly data available. We expect Mexican workers living abroad -mainly in the US-, to have sent US\$2,160 mn to their families in Mexico during June. This would imply a 5.8% yoy expansion.

We believe that remittances in June will benefit from the better growth dynamics of the Mexican immigrant labor force in the U.S. Analyzing data from the Current Population Survey, the unemployment rate for illegal immigrants has fallen in the last three months which implies that we will probably continue to see an upward trend in these inflows.

Banxico's survey of economic expectations. Also on Monday, at 10:00am (EDT), Banco de México will publish its monthly survey of economic expectations. In our view, market participants' focus will be on three issues: (1) 2015 inflation expectations that currently are at 2.91% (Banorte-Ixe: 3%); (2) mid-term inflation expectations—quite important for the central bank's board—that are currently at 3.43% (Banorte-Ixe: 3%); and (3) the analysts' assessments of GDP growth for 2015 given the recent downward revisions made by several economists (currently at 2.6%; Banorte-Ixe: 3.2%).

July's PMI surveys. On Monday, *IMEF* (Mexican Institute of Financial Executives) will publish its PMI business confidence indicators. We expect manufacturing PMI at 52.8 in July, slightly below the 53.1 observed in June (seasonally adjusted terms), but above the 50 points threshold. We believe that manufacturing activity was supported by the recovery of consumer spending in Mexico and the significant depreciation of the MXN. However, we believe that the strong recovery in retail sales might have affected the “inventories” component.

Moreover, we believe that the non-manufacturing PMI will stand at 51.4 points. In this regard, we believe that the recent upward trend in domestic demand, given the recovery in both the labor market and the household's purchasing power, could have triggered a faster growth within the services in July.

We expect a 3% yoy expansion in May's GFI. Next Tuesday at 9:00am (EDT), *INEGI* will publish its May's gross fixed investment (GFI) report. We anticipate GFI up by 3% yoy. We believe that within the report we will probably see a 2.4% yoy expansion in imported machinery and equipment given that trade balance figures for May showed a similar growth rate. Moreover, we expect a 10.6% growth in domestic machinery and equipment. Finally, we believe that construction spending could increase 1.9% yoy.

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 \$591mn amounting to US \$190.7bn on July 24. According to Banxico's report, this figure comes mainly as a result of: (1) Dollar sales by the Central Bank to the Federal Government for US \$199mn; (2) US \$260mn decrease explained by the introduction of Banxico's USD daily auction; along with a (3) US \$132mn decrease due to changes in the valuation of the Central Bank's assets. It is worth noting that Pemex is currently the only significant source of reserve accumulation, given that on November 2011, the FEC (Federal Exchange Commission) decided to shut down the options scheme that Banxico also used to accumulate reserves. In this context, the central bank has an accumulated reduction of US \$2,527mn international reserves this year (please refer to the table below).

Banxico's foreign reserve accumulation details
US\$, million

	2014	24/Jul/2015	24/Jul/2015	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	193,239	190,711	-591	-2,527
(B) Gross international reserve	195,682	191,781	-1,005	-3,901
Pemex	--	--	-234	2,875
Federal govt	--	--	-367	-364
Market operations	--	--	-260	-4,984
Other	--	--	-144	-1,427
(C) Short-term government's liabilities	2,443	1,070	-414	-1,373

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 20-year fixed-rate Mbonos (Nov'34) as well as 5-year Bondes D, 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, August 4, 2015)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	03-Sep-15	--	5,500	3.01
3m	05-Nov-15	--	9,500	3.17
6m	04-Feb-16	--	11,000	3.29
Mbono				
20y	23-Nov-34	7.75	3,000	6.73
Bondes D				
5y	30-Jul-20	--	4,000	0.23

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. 2. Yield-to-maturity reported for Cetes, Mbonos and Udibonos

Banamex Survey: Market participants will focus on analysts' monetary policy assessments. On Wednesday at 4:30pm (EDT) *Banamex* will release its bi-weekly survey of economic expectations. In the last survey published by *Banamex* 23 out of 25 analysts surveyed expected a rate hike in 2015. Furthermore, analysts will also focus on July's inflation forecast (to be published on Friday, August 7), as well as on CPI estimations for 2015. Moreover, we expect moderate downward revisions to the economic growth estimates.

Consumer confidence will show a contraction in July. On Thursday, at 9:00am (EDT), Banxico and *INEGI* will publish its July's monthly survey on consumer confidence, where we expect a 4.3% yoy expansion, with the index reaching 94.4 points (vs. 90.5 in July 2014). We highlight that this could be the nine positive annual growth rate since October 2013.

However, in seasonally adjusted terms, we expect confidence levels to decrease 1.5% m/m. We believe that consumer confidence (measured in seasonally adjusted terms) could show a contraction given the following factors: (1) The escape of Joaquin "El Chapo" Guzman, which possibly generated a significant reduction in consumer expectations regarding the country's current performance; (2) the sharp depreciation of the Mexican currency, which could undermine consumer expectations regarding Mexico's future economic outlook; and (3) the results of the first tender of Round 1 of the Energy reform, given the negative and disappointing comments made by the majority of economic analysts and reporters.

Inflation in July will be explained by pressures on services prices along with higher prices of fruit and vegetables. On Friday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.17% m/m increase in July in line with market consensus, according to *Bloomberg*. In the core index, we expect an increase of 0.16% m/m, also in line with consensus.

Inflation in July will be explained by pressures on services prices along with higher prices of fruit and vegetables. In the first case, services prices were up, particularly in the first half of the month, given the start of the summer holiday season. Moreover, our price monitoring suggests pressures on the price of some important fruits and vegetables, such as tomatoes.

Nevertheless, we expect this figure to be 10.9bps lower than the observed in same period last year, derived from: (1) A lower contribution of services prices (14.4bps vs. 15.5 in 2014); (2) -5.1bps stemming from a lower contribution energy prices (0.9bps vs. 6 in 2014); and (3) -3.1bps stemming from a lower contribution of agriculture (3.7bps vs. 6.9 in 2014), as shown in the table below.

With these results, annual inflation is at 2.8% yoy in July from previous 2.9% while core inflation will remain at 2.3% yoy.

Inflation by components in July
% monthly incidence

	Banorte-Ixe	2014	Difference
Headline	0.17	0.28	0.17
Core	0.12	0.14	0.12
Goods	-0.03	-0.01	-0.03
Processed foods	0.01	0.03	0.01
Other goods	-0.04	-0.04	-0.04
Services	0.14	0.16	0.14
Housing	0.03	0.02	0.03
Education	0.01	0.00	0.01
Other services	0.11	0.13	0.11
Non-core	0.05	0.13	0.05
Agricultural	0.04	0.07	0.04
Fresh fruits and vegetables	0.07	0.09	0.07
Meat and egg	-0.03	-0.02	-0.03
Energy and government regulated	0.01	0.07	0.01
Energy	0.01	0.06	0.01
Government regulated	0.00	0.01	-0.01

Source: Banorte-Ixe with data from INEGI and Banco de México

Note: Contributions might not add due to the number of decimals allowed in the table. Previous to year 2011, contributions might not add because of the change in CPI-calculation methodology

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