

Ahead of the Curve

August 14, 2015

Market focus this week will on GDP report

- GDP (2Q15).** Next Thursday, at 9:00am (EDT), *INEGI* will publish its GDP report for the second quarter of 2015, where we expect a 2.2% yoy expansion. In seasonally adjusted terms, we expect a 0.2% q/q expansion during 2Q15. Taking a look at the breakdown, we believe that the services sector will show a 2.9% yoy expansion, which would be marginally below the 3.1% yoy growth observed in the previous quarter. However, the current recession in the mining industry (-7.6% yoy) –derived from the significant contraction in Mexico’s oil production– has limited the recovery of industrial activity, which we believe grew 0.5% yoy in 2Q15
- IGAE (June).** Also on Thursday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for June (monthly proxy for the GDP). We expect a 3% yoy expansion of economic activity (0.4% m/m). As we had mentioned in our last IP report, the 1.4% expansion in industrial production during June was explained in part by the 4.2% yoy increase in manufacturing output. Moreover, given the fall in Mexico’s oil production, mining activity posted a 6.2% yoy reduction. Finally, for the agricultural sector we estimate a 6% yoy expansion

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Mexico weekly calendar

DATE	TIME (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Tue 18-Aug	10:00am	International reserves	14-Aug	US\$ bn	--	--	189.7
Tue 18-Aug	12:30pm	Government weekly auction: 1-, 3-, 6- and 12-month Cetes; 30y MBono (Nov'42); 30y Udibono (Nov'46); 5y Bondes D					
Thu 20-Aug	9:00am	GDP	2Q15	% yoy	2.2	2.2	2.6
		(sa)		% q/q	0.2	0.5	0.4
		Primary activities		% yoy	5.6	--	6.8
		Industrial production		% yoy	0.5	--	1.4
		Services		% yoy	2.9	--	2.9
Thu 20-Aug	9:00am	Global economic indicator	June	% yoy	3.0	2.9	1.5
		Primary activities		% yoy	6.0	--	6.6
		Industrial production		% yoy	1.4	--	-1.0
		Services		% yoy	3.7	--	2.6
Thu 20-Aug	4:30pm	Banamex bi-weekly survey of economic expectations					
Fri 21-Aug	9:00am	Retail sales	June	% yoy	4.8	4.6	4.1

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

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 \$1,041mn amounting to US \$189.7bn on August 7. According to Banxico's report, this figure comes mainly as a result of: (1) Dollar sales by the Federal Government to the Central Bank for US \$234mn; (2) US \$1,000mn decrease explained by the introduction of Banxico's USD daily auction without minimum price and US \$200mn with minimum price; along with a (3) US \$75mn reduction due to changes in the valuation of the Central Bank's assets and other operations. It is worth noting that Pemex is currently the only significant source of reserve accumulation. In this context, the central bank has an accumulated reduction of US \$3,521mn international reserves this year (please refer to the table below).

Banxico's foreign reserve accumulation details

US\$, million

	2014	07/Aug/2015	07/Aug/2015	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	193,239	189,718	-1,041	-3,521
(B) Gross international reserve	195,682	191,258	-2,079	-4,424
Pemex	--	--	-493	3,164
Federal govt	--	--	-125	-520
Market operations	--	--	-1252	-6,496
Other	--	--	-209	-572
(C) Short-term government's liabilities	2,443	1,539	-1038	-904

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 30-year fixed-rate Mbonos (Nov'42), 30-year inflation-linked Udibonos (Nov'46), as well as 5-year BondesD, in addition to the “more traditional” 1-, 3-, 6- and 12- 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 18, 2015)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	17-Sep-15	--	5,500	3.01
3m	19-Nov-15	--	9,500	3.33
6m	18-Feb-16	--	11,000	3.42
12m	18-Aug-16	--	11,000	3.62
Mbono				
30y	13-Nov-42	7.75	2,500	6.76
Udibono				
30y	08-Nov-46	4.00	500	3.61
Bondes D				
5y	30-Jul-20	--	4,000	0.24

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

GDP will show a 2.2% yoy expansion in 2Q15. Next Thursday, at 9:00am (EDT), *INEGI* will publish its GDP report for the second quarter of 2015, where we expect a 2.2% yoy expansion. In seasonally adjusted terms, we expect a 0.2% q/q expansion during 2Q15.

Taking a look at the breakdown, we believe that the services sector will show a 2.9% yoy expansion, which would be marginally below the 3.1% yoy growth observed in the previous quarter. We highlight that we have seen a significant recovery in several of the indicators associated with household spending. In particular, the creation of jobs in the formal sector during the period in question has been significantly higher, while trade has begun to show clear signs of acceleration. However, we believe that the lower growth in the Mexican manufacturing industry will have a negative impact on other services associated with this sector, such as transportation.

Regarding industrial activities, manufacturing output expanded 3% yoy as a result of the lower growth in the U.S. manufacturing sector, which led to a deceleration of Mexico's manufacturing output and exports. Moreover, construction output grew 2.8% yoy, as result of a significant downturn in non-residential construction and the recovery in household's spending, which reflected in the exceptional performance of construction in the residential sector. However, the current recession in the mining industry (-7.6% yoy) –derived from the significant contraction in Mexico's oil production– has limited the recovery of industrial activity, which we believe grew 0.5% yoy in 2Q15.

We expect a 3% yoy expansion in June's IGAE. Also on Thursday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for June (monthly proxy for the GDP). We expect a 3% yoy expansion of economic activity (0.4% m/m).

As we had mentioned in our last IP report, the 1.4% growth in industrial production during June was explained in part by the 4.2% yoy expansion in manufacturing output. However, construction increased a 2.1% yoy as a result of lower investment projects within the private and public sector. In this regard, we believe that despite the deceleration observed in construction investment during June, construction output will show better growth prospects given the higher expectations that prevail today in most of Mexico's private firms regarding economic growth. The recovery of households' purchasing power - given the lower inflation levels and the recovery of the Mexican labor market- has led to a significant expansion in residential construction which will continue throughout the second half of the year. Finally, given the fall in Mexico's oil production, mining activity posted a 6.2% yoy reduction.

As we already explained in the GDP section, we believe that growth in June was driven by the performance of the service sector, which we forecast at 3.7% yoy. We highlight that trade has begun to show clear signs of acceleration. However, we believe that the lower growth in the Mexican manufacturing industry will have a negative impact on other services associated with this sector, such as transportation. Finally, for the agricultural sector, we estimate a 6% yoy expansion.

Banamex Survey: Market participants will focus on analysts' monetary policy assessments. On Thursday at 3:30pm (EDT) *Banamex* will release its bi-weekly survey of economic expectations. In the last survey published by *Banamex* 21 out of 24 analysts surveyed expected a rate hike in 2015. Furthermore, analysts will also focus on August's first half inflation forecast (to be published on Monday August 24), as well as on CPI estimations for 2015. Moreover, we expect moderate downward revisions to the economic growth estimates for 2015.

Retail sales will post a 4.8% yoy expansion in June. On Friday (August 21) at 9:00am (EDT), *INEGI* will publish its retail sales report for June 2015. We anticipate a 4.8% yoy expansion explained by the 27.1% yoy growth in vehicle sales (*AMIA*), which will have a positive impact on the overall growth rate. Moreover, consumption goods imports -which have a strong correlation with retail sales- posted a 10.1% yoy expansion, while *ANTAD* total store sales increased 5.8% yoy in real terms during the period in question.

Looking ahead, we believe that retail sales performance will show a visible recovery in the second half of the year. In particular, private consumption in Mexico will show better growth prospects derived from: (1) An improvement in consumer's expectations regarding economic growth; (2) the recent downward trend in inflation; and (3) the stronger growth dynamics in the Mexican labor market.

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