Ahead of the Curve

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www.banorte.com
www.ixe.com.mx
@analisis_fundam

Gabriel Casillas
Chief Economist and Head of Research
gabriel.casillas@banorte.com

Delia Paredes
Executive Director of Economic Analysis
delia.paredes@banorte.com

Alejandro Cervantes
Senior Economist, Mexico
alejandro.cervantes@banorte.com

Market focus this week will on the *2016 Economic Package*

- **Mexico's *Economic Package* will be presented on September 8th.** According to the Fiscal Responsibility and Budget Law, the government will submit to Congress, the so-called *Economic Package*, which includes the *Revenue Law*, the *Spending Budget* and the *General Economic Policy Guidelines*. The Lower-House has until October 20 to approve the *Revenue Law* while the Senate has until October 31. In terms of the spending budget, it is reviewed only by the Lower-House, which has until November 15 to approve it. In this regard, President Peña Nieto announced that the *2016 Economic Package* will be presented on Tuesday

- **August's monthly inflation report.** On Wednesday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.19% m/m increase in August, below market consensus that is forecasting a 0.24% according to *Bloomberg*. In the core index, we expect an increase of 0.17% m/m below market consensus (0.2%). Inflation during the period in question will be explained by pressures on goods prices along with higher government tariffs prices, particularly in the first half of the month. With these results, annual inflation is at 2.57% yoy in August from 2.74%, while core inflation would be at 2.27% from 2.31% yoy

Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Mon 7-Sep	**4:30pm**	**Banamex bi-weekly survey of economic expectations**					
Tue 8-Sep	**10:00am**	**International reserves**	4-Sep	US$ bn	--	--	185.8
Tue 8-Sep	**12:30pm**	**Government weekly auction: 1-, 3-, 6-month CETES; 5y Mbono (Jun'21); 10y Udibono (Dec'25)**					
Tue 8-Sep		**Mexico's *2016 Economic Package***					
Wed 9-Sep	**9:00am**	**CPI inflation**	August	% m/m	0.19	0.24	0.15
				% yoy	2.57	2.62	2.74
		Core		% m/m	0.17	0.20	0.17
				% yoy	2.27	--	2.31
Thu 10-Sep		**Wage negotiations**	August	%	4.5	--	4.8
Fri 11-Sep	**9:00am**	**Industrial production**	July	% yoy	0.0	0.6	1.4
		(sa)		% m/m	-0.4	--	0.2
		Mining		% yoy	-6.1	--	-6.2
		Utilities		% yoy	2.6	--	2.1
		Construction		% yoy	1.7	--	2.1
		Manufactures		% yoy	1.6	2.5	4.2

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

***Banamex* Survey: Market participants will focus on analysts' monetary policy assessments.** On Monday at 4:30pm (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 inflation forecast (to be published on Wednesday September 9), as well as on CPI estimations for 2015. Moreover, we expect moderate downward revisions to the economic growth estimates for 2015.

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$1,548mn amounting to US $185.8bn on August 28. 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$35mn; (2) US$1,000mn decrease explained by the introduction of Banxico's USD daily auction without minimum price and US$303mn with minimum price; along with a (3) US$210mn 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$7,453mn international reserves this year.

Banxico's foreign reserve accumulation details
US$, million

	2014	28/Aug/2015	28/Aug/2015	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	193,239	185,785	-1,548	-7,453
(B) Gross international reserve	195,682	187,134	-1,461	-8,548
Pemex	--	--	202	2,953
Federal govt	--	--	32	-806
Market operations	--	--	-1,503	-10,205
Other	--	--	-191	-489
(C) Short-term government's liabilities	2,443	1,349	87	-1,094

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 5-year fixed-rate Mbonos (Jun'21) as well as 10-year inflation-linked Udibonos (Dec'25), 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, September 8, 2015)

	Maturity	Coupon rate, %	To be auctioned[1]	Previous yield[2]
Cetes				
1m	08-Oct-15	- -	5,500	3.09
3m	10-Dec-15	- -	9,500	3.39
6m	03-Mar-16	- -	11,000	3.51
Mbono				
5y	10-Jun-21	6.50	8,500	5.59
Udibono				
10y	04-Dec-25	4.50	750	3.00

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

Mexico's *Economic Package* will be presented on September 8th. According to the Fiscal Responsibility and Budget Law, the government will submit to Congress, the so-called *Economic Package*, which includes the *Revenue Law*, the *Spending Budget* and the *General Economic Policy Guidelines*. The Lower-House has until October 20 to approve the *Revenue Law* while the Senate has until October 31. In terms of the spending budget, it is reviewed only by the Lower-House, which has until November 15 to approve it. In this regard, President Peña Nieto announced that the *2016 Economic Package* will be presented on Tuesday.

Inflation in August will be explained by pressures on the price of goods along with higher prices of government tariffs. On Wednesday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.19% m/m increase in August, below market consensus that is forecasting a 0.24% according to *Bloomberg*. In the core index, we expect an increase of 0.17% m/m below market consensus (0.2%). Inflation during the period in question will be explained by pressures on goods prices along with higher government tariffs prices, particularly in the first half of the month.

Nevertheless, we expect this figure to be 16.7bps lower than the observed in same period last year, derived from: (1) 1.8bps stemming from a higher contribution of government tariffs (2.6bps vs. 0.9 in 2014); (2) 1.7bps stemming from a higher contribution of services prices (2.4bps vs. 0.7 in 2014). By contrast, we expect (3) a lower contribution agriculture prices (2bps vs. 17.2 in 2014) and (4) -4.7bps stemming from a lower contribution of goods (10.8bps vs. 15.5 in 2014), as shown in the table below.

With these results, annual inflation is at 2.57% yoy in August from 2.74%, while core inflation would be at 2.27% from 2.31% yoy.

Inflation by components in August
% monthly incidence

	Banorte-Ixe	2014	Difference
Headline	0.192	0.359	-0.17
Core	0.132	0.161	-0.03
Goods	0.108	0.155	-0.05
Processed foods	0.034	0.058	-0.02
Other goods	0.074	0.098	-0.02
Services	0.024	0.007	0.02
Housing	0.027	0.028	0.00
Education	0.057	0.048	0.01
Other services	-0.060	-0.070	0.01
Non-core	0.060	0.202	-0.14
Agricultural	0.020	0.172	-0.15
Fresh fruits and vegetables	0.022	0.064	-0.04
Meat and egg	-0.002	0.109	-0.11
Energy and government regulated	0.041	0.024	0.02
Energy	0.014	0.015	0.00
Government regulated	0.026	0.009	0.02

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

August's wage negotiations. On Thursday, the Ministry of Labor (STPS) will make its contractual wage negotiations monthly data available. We anticipate workers to have negotiated an annual average wage increase of 4.5% in August. This would be slightly above the 4.3% average observed year-to-date. In this regard, we believe that August's figure was mainly driven by the increase in wage negotiations in the automotive sector, specifically wage increases in the *Volkswagen's Union*; coupled with increases in the mining sector (*ArcelorMittal*); as well as revisions by labor unions of the government sector.

We expect a null annual growth in July's industrial output. Finally, on Friday, at 9:00am (EDT), *INEGI* will release its monthly industrial production report. We anticipate a null annual expansion in total output during the seventh month of the year. Taking a look at the breakdown, we believe that construction output could have expanded 1.7% yoy. In this regard, construction has consolidated its recovery. However, the latest IP reports show that construction output has decelerated significantly, probably as a result of the recent volatility in financial markets, which has driven Mexican firms to postpone their investment projects.

Moreover, we believe that manufacturing production could post a scant 1.6% yoy expansion, explained by a 2% yoy increase in manufacturing exports, a 2% yoy decline in July's vehicle production, and a 1.9% yoy expansion in U.S. manufacturing output, which has a strong correlation with Mexico's manufacturing sector. In this regard, we believe that the Mexican manufacturing sector will show better growth prospects, derived from: (1) A stronger external demand, particularly coming from the U.S.; (2) the recent depreciation of the Mexican currency; and (3) the recovery of private consumption in Mexico, which will eventually translate into a higher domestic demand for manufacturing products.

Finally, we believe that the null growth in industrial output during July will be mainly explained by the poor performance of mining activity. In this regard, we expect a 6.1% yoy contraction derived from lower oil production and the reduction in the extraction of other minerals.

GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Economic Analysis			
Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Alejandro Cervantes Llamas	Senior Economist, Mexico	alejandro.cervantes@banorte.com	(55) 1670 - 2972
Katia Celina Goya Ostos	Senior Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Miguel Alejandro Calvo Domínguez	Economist, Regional & Sectorial	miguel.calvo@banorte.com	(55) 1670 - 2220
Juan Carlos García Viejo	Economist, International	juan.garcia.viejo@banorte.com	(55) 1670 - 2252
Rey Saúl Torres Olivares	Analyst	saul.torres@banorte.com	(55) 1670 - 2957
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Fixed income and FX Strategy			
Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Juan Carlos Alderete Macal, CFA	FX Strategist	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Santiago Leal Singer	Analyst Fixed income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Equity Strategy			
Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Victor Hugo Cortes Castro	Equity Research Analyst	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Senior Equity Research Analyst – Conglomerates/Financials/ Mining/ Chemistry	marissa.garza@banorte.com	(55) 1670 - 1719
Marisol Huerta Mondragón	Equity Research Analyst – Food/Beverages	marisol.huerta.mondragon@banorte.com	(55) 1670 - 1746
José Itzamna Espitia Hernández	Equity Research Analyst – Airports / Cement / Infrastructure / Fibras	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research Analyst – Auto parts	valentin.mendoza@banorte.com	(55) 1670 - 2250
María de la Paz Orozco García	Analyst	maripaz.orozco@banorte.com	(55) 1670 - 2251
Corporate Debt			
Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Idalia Yanira Céspedes Jaén	Analyst, Corporate Debt	idalia.cespedes@banorte.com	(55) 1670 - 2248
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Asset Management	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rircado.velazquez@banorte.com	(55) 5268 - 9879
Víctor Antonio Roldan Ferrer	Head of Corporate Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454