

# Ahead of the Curve

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## September's inflation contained on lower agricultural prices, with industrial production benefited by manufacturing strength

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- **Monthly inflation report (September).** We expect a 0.39% m/m increase in the headline and +0.26% in the core component. We believe inflation will be driven by higher energy and goods prices, albeit mitigated by the fall in the agricultural component. Twelve-month inflation would stand at 4.99%, higher than the 4.90% print in August, mostly explained by an adverse base effect, given the suspension of charges in some services in Mexico City after the September 19<sup>th</sup> earthquake last year
- **Industrial production (August).** We estimate 1.9% annual growth, stronger than the 1.3% observed in July. We anticipate a relatively high print of 3.2% in manufacturing, supported by the healthy performance of US industrial production and relatively high levels of forward-looking indicators in the IMEF index. We forecast a 5.4% contraction in mining, driven by weak oil and gas production, and a 3.5% increase in construction

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### Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Tue 9-Oct	9:00am	CPI inflation	September	% m/m	<u>0.39</u>	0.41	0.58
				% yoy	<u>4.99</u>	5.00	4.90
		Core	% m/m	<u>0.26</u>	0.26	0.25	
			% yoy	<u>3.61</u>	--	3.63	
Tue 9-Oct	10:00am	International reserves	6-Oct	US\$ bn	--	--	173.6
Tue 9-Oct	12:30pm	Government weekly auction: 1-, 3-, 6-, 12-month CETES; 10y Mbono (Jun'27); 30y Udibonos (Nov'46); 5y Bondes D					
Wed 10-Oct		Wage negotiations	September	%	<u>5.1</u>	--	5.50
Fri 12-Oct	9:00am	Industrial production	August	% yoy	<u>1.9</u>	--	1.3
				(sa)	% m/m	<u>0.9</u>	--
		Mining	% yoy	<u>-5.4</u>	--	-7.0	
		Utilities	% yoy	<u>4.6</u>	--	4.1	
		Construction	% yoy	<u>3.5</u>	--	4.5	
		Manufacturing		% yoy	<u>3.2</u>	--	2.4

Source: Banorte; Bloomberg

Proceeding in chronological order...

**Better-behaved inflation in September on lower agricultural prices, despite persistent increase in energy.** We are forecasting a 0.39% m/m increase in the headline figure and +0.26% in the core component. We believe inflation will be driven by higher energy and goods prices. Within the former, we expect a 18bps contribution due to the increase in gasoline prices during the month. In the case of goods, we expect a 6bps contribution from processed foods and 7bps from other goods. In spite of the latter, the impact will be mitigated by the fall in the agricultural component, where we expect a negative contribution of 2bps from fruits and vegetables.

With these results, 12-month inflation will stand at 4.99% in September, higher than the 4.90% seen in August. Moreover, we forecast core inflation at 3.61% yoy (previous: 3.63%). It is worth mentioning that the increase in the year-over-year comparison will be mostly explained by a base effect, given the suspension of charges in some services in Mexico City -in particular public transportation- after the September 19<sup>th</sup> earthquake. Last year, the latter helped year-over-year inflation to fall from 6.66% in August to 6.35% in September. Nevertheless, this effect will be eliminated as soon as the next print, placing inflation on its path towards our year-end forecast of 4.8%.

**Weekly international reserves report.** Last week, net international reserves decreased by US\$2 million amounting to US\$173.6 billion. According to Banxico's report, this figure comes mainly as a result of a positive valuation effect in central bank assets. In this context, the central bank's international reserves have increased by US\$764 million during 2018 (please refer to the following table).

**Banxico's foreign reserve accumulation detail**

US\$, million

	2017	Sep 28, 2018	Sep 28, 2018	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	172,802	173,566	-2	764
(B) Gross international reserve	175,450	177,040	341	1,590
Pemex	--	--	187	-549
Federal government	--	--	19	790
Market operations	--	--	0	0
Other	--	--	135	1,349
(C) Short-term government's liabilities	2,648	3,474	343	826

Source: Banco de México

**Weekly government bond auction.** The Ministry of Finance (MoF) –via Banco de Mexico as its financial agent–, will offer 10-year fixed-rate Mbonos (Jun'27), 30-year inflation-linked Udibonos (Nov'28), 5-year Bondes D, in addition to the “more traditional” 1-, 3-, 6-, and 12-month zero-coupon Cetes (please refer to the following table). As usual, results will be released at 12:30pm (ET).

**Auction specifics (Tuesday, October 9<sup>th</sup>, 2018)**

	Maturity	Coupon rate, %	To be auctioned <sup>1</sup>	Previous yield <sup>2</sup>
<b>Cetes</b>				
1m	08-Nov-18	--	7,000	7.67
3m	10-Jan-19	--	11,000	7.87
6m	11-Apr-19	--	11,000	8.00
6m	12-Sep-19	--	12,500	8.26
<b>Bondes D</b>				
5y	31-Aug-23	--	5,000	0.18
<b>M Bono</b>				
10y	03-Jun-27	7.50	9,000	7.83
<b>Udibonos</b>				
30y	08-Nov-46	4.00	450 UDIS	3.85

Source: Banorte 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

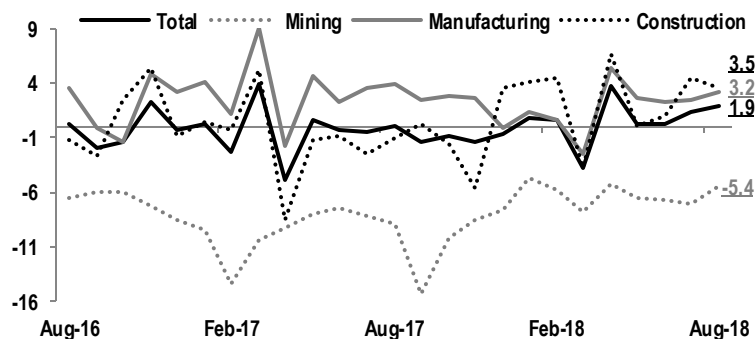
**Wage negotiations could have increased 5.1% during September.** This figure would stand below the 5.5% increase seen in August. We believe that this will continue to be driven by relatively high levels of inflation at the end of 2017 and the first half of 2018, as well as the lagged impact of the sharp increase in the minimum wage at the end of 2017.

**We expect a 1.9% yoy expansion in August industrial output.** This would be mainly explained by our estimate that manufacturing could present a relatively strong rebound, increasing 3.2% yoy. As usual, we expect mining to contract around 5.4%, as oil and gas production remains challenged. In this regard, oil Pemex reported a 5.9% decrease in oil production and 2.7% in natural gas during the period in question. Meanwhile, construction would moderate its expansion to 3.5% from a relatively strong 4.5% pace last month.

Using seasonally adjusted figures, we expect a 0.9% m/m expansion, which would be the highest advance so far this year. As already mentioned, this would be driven by positive manufacturing dynamics, supported by a healthy performance of US industrial production. Moreover, both the employment and new orders components in IMEF indexes have held relatively high levels, particularly the latter.

**Industrial production**

% yoy



Source: INEGI, Banorte

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