

# Ahead of the Curve

Annual inflation to climb in April while industrial production in March will be boosted by a calendar effect

- Monthly inflation report (April).** We estimate headline inflation at 0.10% m/m, while the core component would rise 0.52%. This figures would be driven by a seasonal effect associated with the Easter holiday that induce higher prices in tourism services and airfares (contribution: +9bps) but more than compensated by summer discounts on electricity tariffs (-26bps). In addition, we still expect pressures in core goods, contributing with 16bps. With these results, annual inflation would pick up from 4.00% in the previous month to 4.46%, with the core component from 3.55% to 3.94%, Looking ahead, we expect inflation to come down back to Banxico's target range between July and August, to later on speed up its convergence to our 3.5% forecast as the base-effect starts to have a positive impact
- Industrial production (March).** We expect an increase to -0.1% yoy from -0.8% in the previous month. However, this would be mostly explained by a favorable base effect due to the Easter holiday that added working days in the annual comparison. Using seasonally adjusted figures, we expect a 0.4% m/m contraction. By sector, we expect manufacturing at 2.3% yoy nsa, with mining and construction on the downside at -5.6% and -2.4%, respectively. Going forward, we believe industry will be limited, with data from the US for April suggesting weakness and likely with a negative impact from delays in freight crossings at the Northern Border, among other factors

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## Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 6-May	9:00am	Consumer confidence	April	index	<u>112.4</u>	--	112.7
Tue 7-May	9:00am	Gross fixed investment	February	% yoy	<u>-3.2</u>	--	1.6
		Machinery and equipment		% yoy	<u>-5.9</u>	--	-0.2
		Domestic		% yoy	<u>-3.5</u>	--	-4.6
		Imported		% yoy	<u>-7.4</u>	--	2.3
		Construction		% yoy	<u>-1.5</u>	--	2.9
Tue 7-May	10:00am	International reserves	May-3	US\$ bn	--	--	176.7
Tue 7-May	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 10y Mbono (May'29); 5y Bondes D					
Tue 7-May	4:30pm	Citibanamex bi-weekly survey of economic expectations					
Thu 9-May	9:00am	CPI inflation	April	% m/m	<u>0.10</u>	0.04	0.38
				% yoy	<u>4.46</u>	4.40	4.00
		Core		% m/m	<u>0.52</u>	0.48	0.34
				% yoy	<u>3.94</u>	--	3.60
Fri 10-May		Wage negotiations	April	%	<u>5.2</u>	--	6.5
Fri 10-May	10:00am	Industrial production	March	% yoy	<u>-0.1</u>	--	-0.8
		(sa)		% m/m	<u>-0.4</u>	--	0.3
		Mining		% yoy	<u>-5.6</u>	--	-6.4
		Utilities		% yoy	<u>2.8</u>	--	-1.1
		Construction		% yoy	<u>-2.4</u>	--	-1.1
		Manufacturing		% yoy	<u>2.3</u>	--	1.1

Source: Banorte; Bloomberg

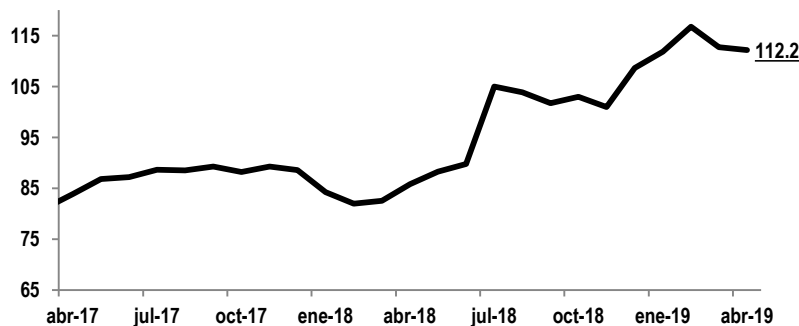
Proceeding in chronological order...

**Consumer confidence could decline modestly in April.** We expect consumer confidence to fall for a second consecutive month to 112.2pts from 112.7 in March. In spite of this, the annual comparison would remain high at 30.7% yoy, considering its accumulated advance after the 2018 election and favorable sentiment about the new administration, in particular the president’s popularity. Nevertheless, using seasonally-adjusted figures we anticipate a 1.8% m/m decline. Increased focus in his security policies, as suggested by questions in the daily press conference, could weigh some on sentiment among consumers.

To the latter, we should add the rebound in inflation during the 1<sup>st</sup> half, with the annual rate from 4.00% yoy in March to 4.38%, mainly driven by the seasonal increase due to the Easter holiday. Apart from this, processed foods and other goods were also pressured, which could impact the purchasing power component. This could be partially mitigated by the relative strength of the Mexican peso, considering the 2.5% monthly gain even reaching up to 18.75 per dollar, not observed since October.

Going forward, we believe consumer confidence will decline gradually as political optimism fades away, eventually returning towards its long-term average. Nevertheless, the path could be very volatile (as a result of the specific political events in the period) and relatively slow, as consumer fundamentals remain strong.

**Consumer confidence**  
Index, nsa



Source: INEGI

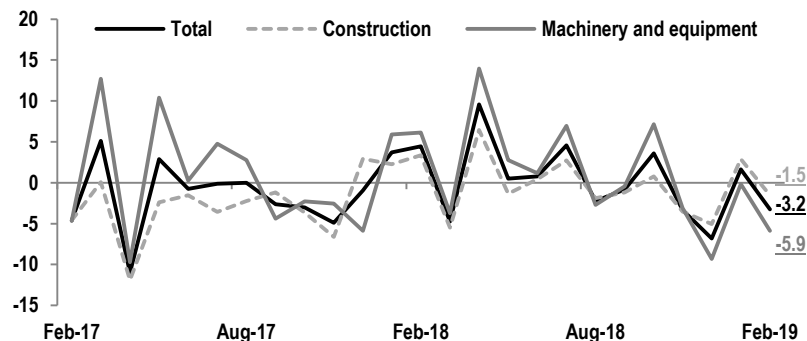
**GFI to negative territory in February.** We anticipate gross fixed investment at -3.2% yoy, paring back after the 1.6% increase in January. Based on available data, we anticipate weakness in all components.

In particular, we expect construction down 1.5%, returning to negative after a positive blip in the previous month. This dynamic is backed by figures already published in the industrial production report, which showed a 1.1% decline. Within, edification grew only 0.5% and civil engineering projects fell 3.6%, in line with the slowdown in public spending seen in the first quarter. In this context, investments in physical assets by the Federal Public Sector fell 26.2% yoy in real terms in February, reversing the 14.4% increase of the previous month.

Considering the latter, we believe construction will be limited by austerity measures along the typical slowdown in the first year of a new federal administration, while private investment could also be constrained by global and domestic uncertainty. In this respect, the sub-index about the “adequate moment to invest” in business confidence has remained depressed following the strong decline that started in 4Q18.

We forecast a 5.9% yoy contraction in machinery and equipment, which would result in four consecutive months in negative territory. The downfall would be concentrated in the imported component at -7.4%. In this context, capital imports within the trade balance posted a 5.5% decline (weakest in almost two years), which would drive GFI. Finally, the domestic component would extend its decline for an eight straight month, albeit with a moderation to -3.5% yoy vs. -4.6% in January.

**GFI**  
% yoy



Source: INEGI, Banorte

**Weekly international reserves report.** Last week, net international reserves increased US\$205 million, closing at US\$176.7 billion. According to Banxico’s report, this figure comes mainly from a positive valuation effect in central bank assets. In this context, the central bank’s international reserves have increased US\$1.9 billion during 2019 (please refer to the following table).

**Banxico's foreign reserve accumulation detail**  
US\$, million

	2018	Apr 26, 2019	Apr 26, 2019	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	174,793	176,661	205	1,868
(B) Gross international reserve	176,384	184,230	-62	7,846
Pemex	--	--	-178	158
Federal government	--	--	-100	6,156
Market operations	--	--	0	0
Other	--	--	216	1,533
(C) Short-term government's liabilities	1,592	7,570	-268	5,978

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 (May’29), 5-year Bondes D, in addition to the 1-, 3-, and 6-month zero-coupon Cetes (see following table). As usual, results will be released at 12:30pm (ET).

**Auction specifics (Tuesday, May 7<sup>th</sup>, 2019)**

	Maturity	Coupon rate, %	To be auctioned <sup>1</sup>	Previous yield <sup>2</sup>
<b>Cetes</b>				
1m	06-Jun-19	--	5,000	8.20
3m	08-Aug-19	--	10,000	8.15
6m	07-Nov-19	--	11,500	8.25
<b>Bondes D</b>				
5y	25-Abr-24	--	6,000	0.14
<b>Mbonos</b>				
10y	31-May-29	8.50	10,200	8.01

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

**Citibanamex Survey.** Market focus will center on analysts’ inflation forecasts for April (to be published on Thursday, May 9<sup>th</sup>) along with the 2019 year-end estimate. It will be important to see monetary policy assessments for the rest of the year, looking ahead to the monetary policy meeting that will take place on May 16. We will also be paying attention to forecasts for GDP growth and USD/MXN exchange rate.

**Inflation in April to be pushed higher by seasonal pressures at the core component, partially compensated by energy.** We estimate headline inflation at 0.10% m/m, while the core component would rise 0.52%, considerably higher than the previous print at 0.34%. Within the latter, dynamics will mostly be influenced by a seasonal effect due to the Easter holiday, as tourism services and airfares increased in the previous fortnight ahead of the actual holiday. In this context, these two components added 11bps in the 1<sup>st</sup> half. However, in the 2<sup>nd</sup> half we expect a slight retracement, leaving the overall contribution during the month at 9bps. Moreover, we expect additional pressures in core goods, contributing 16bps to the overall index.

Going to the non-core component, we expect a negative contribution of 29bps. As explained previously, discounts on electricity tariffs started in the 1<sup>st</sup> half, resulting in a 26bps reduction. This effect will continue to help inflation, while expecting low-grade gasoline to keep falling as subsidies have continued to go up, reaching 41.4% in the last week of April, at its highest since October 2018:

With these results, annual inflation would pick up from 4.00% month to 4.46%, highest so far in 2019. Core inflation would rise to 3.94% from 3.55%, not seen in a little more than a year. Since the start of 2019 we expected an increase in annual inflation during this period; however, given that the decline in 1Q19 was so strong, it seems that some “payback” could be taking place, putting additional pressures. Going ahead, we expect inflation to come down back into Banxico’s target range between July or August, to speed up later on its convergence to our 3.5% forecast as the base-effect starts to have a positive impact.

**We forecast wage negotiations up 5.2% in April.** This would represent a lower advance relative to the 6.5% of the previous month. This would continue to be driven by the 16.2% increase in the minimum wage, which came into effect on January 1<sup>st</sup>. According to our monitoring, the electrician's union agreed with CFE a 3.4% wage hike, which could benefit around 40% of total workers with negotiations in this period. Nevertheless, for the rest we anticipate higher adjustments, considering that the private-sector had averaged 6% in 1Q19. Going forward, and as mentioned in other releases, wage negotiations will likely remain skewed to the upside due to the minimum wage revision, as well as a lagged impact from high inflation in the previous two years. However, we do not rule out a moderation in the 2<sup>nd</sup> half of the year as inflation inches closer towards target and activity slows down, resulting in a wider output gap.

**Industrial production in March influenced by a favorable calendar effect.** We estimate a 0.1% yoy contraction, above the -0.8% in February. Nevertheless, this would be mostly explained by the favorable base effect due to the Easter holiday which added working days in the annual comparison. Considering the latter using seasonally adjusted figures, we expect a 0.4% m/m contraction, matching December's fall.

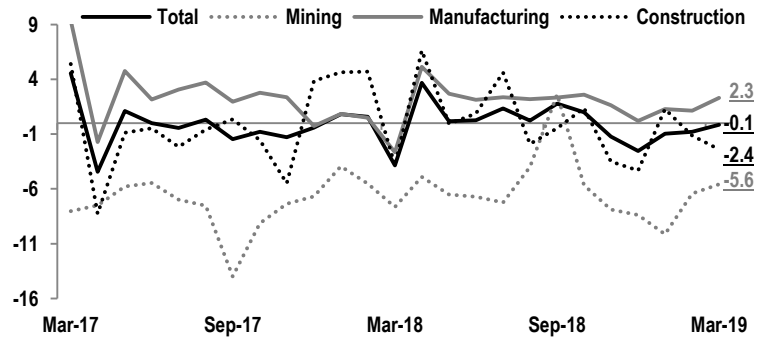
Taking a look at the breakdown, we expect 2.3% yoy nsa growth in manufacturing. Some figures point to better results considering the already-mentioned calendar effect, such as auto production which according to *AMIA* increased 4.8% yoy from -5.0% in the previous month. In addition, industrial production in the US grew 1.4%, in line with February's expansion. Nevertheless, some indicators such as non-oil intermediate imports point to added weakness, as they moderated to only +0.7%.

We expect mining to stay in contraction at -5.6% yoy. Pemex oil production fell 8.4% and natural gas output rose 4.5%, both improving at the margin from February's figures. We forecast a construction at -2.4%, believing that the overall trend continues to be skewed to the downside despite a positive blip in January. As in recent months, weakness would be concentrated in civil engineering as expenditures in public infrastructure by the federal government fell 58.6% yoy in real terms. In addition, services within the sector could also debilitate, considering that formal employment in the sector fell 0.04% yoy.

All in all, and excluding the base effect, we expect industrial production to have decelerated significantly, as already suggested by 1Q19 GDP preliminary results. Going forward, we believe industry will remain limited by the contraction in mining and slowdown in manufacturing. In this regard, data from the US (Manufacturing ISM and employment in the sector according to the non-farm payrolls report), along with delays in freight crossings in the Northern Border could weigh. However, this could be partially compensated by other signs of improvement, such as the performance of IMEF's manufacturing PMI in April.

### Industrial production

% yoy



Source: INEGI, Banorte

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