

Ahead of the Curve

July 17, 2015

Market focus this week will on IGAE's report

- May's IGAE.** On Friday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for May (GDP monthly proxy), where we expect a scant 1.2% yoy expansion. We believe that IGAE's growth during the fifth month of 2015 was driven by the performance of the service sector, which we forecast at 2.4% yoy. Similarly, we highlight that industrial production fell 0.9% yoy, given the scant 0.8% yoy growth in manufacturing output and the current recession in the mining industry derived from the significant contraction in Mexico's oil production
- Bi-weekly inflation report.** On Thursday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.2% 2w/2w increase in the first half of July, in line with consensus, according to *Bloomberg*. In the core index, we expect an increase of 0.17% 2w/2w above market consensus (0.13%). Inflation during the period in question will be explained by pressures on the prices of services along with higher agricultural prices

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

Document for distribution among the general public

Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Tue 21-Jul	10:00am	International reserves	17-Jul	US\$ bn	--	--	191.8
Tue 21-Jul	12:30pm	Government weekly auction: 1-, 3-, 6-, and 12-month Cetes; 10y Mbono (Dec'24); 30y Udibono (Nov'46); 5y Bondes D					
Tue 21-Jul	4:30pm	Banamex bi-weekly survey of economic expectations					
Wed 22-Jul	9:00am	Retail sales	May	% yoy	<u>5.5</u>	4.9	4.6
Thu 23-Jul	9:00am	CPI inflation	1Q Jul	% 2w/2w	<u>0.20</u>	0.20	0.03
				% yoy	<u>2.87</u>	2.87	2.87
		Core		% 2w/2w	<u>0.17</u>	0.13	0.08
				% yoy	<u>2.38</u>	--	2.35
Fri 24-Jul	9:00am	Unemployment rate	June	%	<u>4.27</u>	4.37	<u>4.5</u>
		sa		%	<u>4.32</u>	--	<u>4.4</u>
Fri 24-Jul	9:00am	Global economic indicator	May	% yoy	<u>1.2</u>	1.0	2.1
		(sa)		% m/m	<u>-0.7</u>	--	0.7
		Primary activities		% yoy	<u>3.2</u>	--	4.7
		Industrial production		% yoy	<u>-0.9</u>	--	1.1
		Services		% yoy	<u>2.4</u>	--	2.5

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 \$388mn amounting to US \$191.8bn on July 10. 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 \$12mn; (2) US \$260mn decrease explained by the introduction of Banxico's USD daily auction; along with a (3) US \$116mn 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 \$1,419mn international reserves this year (please refer to the table below).

Banxico's foreign reserve accumulation details

US\$, million

	2014	10/Jul/2015	10/Jul/2015	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	193,239	191,819	-388	-1,419
(B) Gross international reserve	195,682	192,957	-698	-2,725
Pemex	--	--	-440	2,746
Federal govt	--	--	169	103
Market operations	--	--	-312	-4,464
Other	--	--	-114	-1,110
(C) Short-term government's liabilities	2,443	1,137	-310	-1,306

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 10-year fixed-rate Mbonos (Dec'24), 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, July 21, 2015)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	20-Aug-15	--	5,500	2.96
3m	22-Oct-15	--	9,500	3.12
6m	21-Jan-16	--	11,000	3.26
12m	23-Jun-16	--	11,000	3.54
Mbono				
10y	05-Dec-34	10.00	8,000	6.25
Udibono				
30y	08-Nov-46	4.00	500	3.51
Bondes D				
5y	28-May-20	--	4,000	0.22

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 Tuesday at 4:30pm (EDT) *Banamex* will release its bi-weekly survey of economic expectations. In the last survey published by *Banamex* 22 out of 25 analysts surveyed expected a rate hike in 2015. Furthermore, analysts will also focus on July's first half inflation forecast (to be published on Thursday, July 23), 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 5.5% yoy expansion in May. On Wednesday (July 22) at 9:00am (EDT), *INEGI* will publish its retail sales report for May 2015. We anticipate a 5.5% yoy expansion explained by the 15.6% yoy growth in vehicle sales (*AMIA*), which will have a positive impact on the overall growth rate. Moreover, *ANTAD* total store sales increased 7.9% yoy in real terms during the period in question, which will also be reflected in a more positive figure for May's retail headline index.

Looking ahead, we believe that retail sales performance will show a visible recovery in the second quarter of the year. In particular, private consumption in Mexico will show better growth prospects derived from: (1) A significant 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.

Inflation in the first half of July will be explained by pressures on the prices of services along with higher agricultural prices. On Thursday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.2% 2w/2w increase in the first half of July, in line with consensus, according to *Bloomberg*. In the core index, we expect an increase of 0.17% 2w/2w above market consensus (0.13%).

Inflation during the period in question will be explained by pressures on the prices of services along with higher agricultural prices. Our price monitoring suggests higher prices of some important items in the "fruit and vegetables" sub-index, such as tomatoes. Meanwhile, in the services sub-index we expect pressures on tourism services given the summer holiday season.

Nevertheless, we expect this figure to be 0.4bps higher than the observed in the same period last year, derived from: (1) 5.4bps stemming from a higher contribution of merchandise prices (4.7bps vs. -0.7 in 2014); (2) 2.8bps stemming from a higher contribution of agricultural prices (7bps vs. 4.2 in 2014). By contrast, we expect (3) a lower contribution energy prices (0bps vs. 4.8 in 2014), along with (4) -2.9bps stemming from a lower contribution of services prices (8.3bps vs. 11.2 in 2014), as shown in the table below

With these results, annual inflation will edged down to 2.8% yoy in the first half of July from previous 2.9%, while core inflation remains at 2.3% yoy.

1H-July inflation by components

% bi-weekly incidence

	Banorte-Ixe	2014	Difference
Total	0.202	0.198	0.00
Core	0.130	0.106	0.02
Goods	0.047	-0.007	0.05
Processed foods	0.042	0.021	0.02
Other goods	0.005	-0.028	0.03
Services	0.083	0.112	-0.03
Housing	0.014	0.012	0.00
Education	0.002	0.002	0.00
Other services	0.067	0.100	-0.03
Non-core	0.072	0.093	-0.02
Agricultural	0.070	0.042	0.03
Fresh fruits and vegetables	0.080	0.062	0.02
Meat and egg	-0.010	-0.019	0.01
Energy and government regulated	0.002	0.051	-0.05
Energy	0.000	0.048	-0.05
Government regulated	0.002	0.004	0.00

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

Unemployment rate in June will stand at 4.27%. Next Friday, *INEGI* will publish its employment report for the sixth month of 2015, in which we estimate an unemployment rate of 4.27% nsa, below the 4.45% observed in May. In seasonally-adjusted terms, we believe that the unemployment rate could stand at 4.32%, which implies a monthly fall of 0.1%-pts.

It is likely that the job creation in June was positively affected by better growth dynamics of the economy. In this regard, we believe that the Mexican labor market will continue to recover given the recent upward trend in the Mexican economy, which will eventually reduce the level of unemployed workers.

Looking ahead, we are still positive on the outlook regarding the recovery Mexico's economic activity, which will have a positive impact on firms' expectations about domestic demand, resulting in a more dynamic labor market.

We expect a 1.2% yoy expansion in May's IGAE. On Friday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for May (GDP monthly proxy), where we expect a scant 1.2% yoy expansion. We believe that IGAE's growth during the fifth month of 2015 was driven by the performance of the service sector, which we forecast at 2.4% yoy. Similarly, we highlight that industrial production fell 0.9% yoy.

As we had mentioned in our last IP report, the 0.9% yoy contraction in industrial production during May was explained in part by the scant 0.8% yoy growth in manufacturing output. In this regard, even though May's figure disappointed market participants, we believe that the recovery of this industry is on the way, and will strengthen in the second half of the year given: (1) The significant recovery in external demand, particularly from the U.S.; (2) Mexico's manufacturing exports will show solid growth given the recent and significant depreciation of the Mexican currency; and (3) the recent Mexican car industry figures remain strong.

In this regard, we believe that the recovery of both manufacturing and construction industries will continue in 2H15. Moreover, IP's headline figure was also affected by the current recession in the mining industry –derived from the significant contraction in Mexico's oil production–.

We also believe that the 2.4% yoy estimated expansion in services will be explained by the recovery in private consumption. In this regard, *INEGI's* May's retail sales report will show that consumers' spending is gaining momentum, whereas formal job creation has observed a significant recovery in the last 5 months. However, it is likely that the 0.8% yoy growth in manufacturing output during May will affect certain subsectors within the services, such as the transport and trade.

Disclaimer

The information contained in this document is illustrative and informative so it should not be considered as an advice and/or recommendation of any kind. BANORTE is not part of any party or political trend.

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 Godínez	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
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	hugo.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	Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Jorge de la Vega Grajales	Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Private Banking	lpietrini@ixe.com.mx	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Asset Management	pimentelr@ixe.com.mx	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	International Banking	rvelazquez@ixe.com.mx	(55) 5268 - 9879
Victor Antonio Roldan Ferrer	Transactional Banking	vrolan@ixe.com.mx	(55) 5004 - 1454