

Ahead of the Curve

September 22, 2017

Market focus this week will be on Banxico's monetary policy announcement and July's IGAE

- Banxico's monetary policy announcement (September).** On Thursday, Banxico will announce its monetary policy decision at 3:00pm (EDT), where we do not expect an addition increase of the central bank's reference rate, which currently stands at 7%. We highlight that in the last *Quarterly Inflation Report (QIR)*, the central bank referred to the recovery of the Mexican economy, which prompted an upward revision to their GDP forecast for 2017 (current estimate: 2 - 2.5%; previous: 1.5 - 2.5%), as well as for 2018 (current estimate: 2 - 3%, previous: 1.7 - 2.7%). Similarly, the central bank also mentioned the convergence of inflation towards its 3% target in the third quarter of 2018. In this context, we consider that these two issues will be the most prominent within the monetary policy statement
- Economic activity indicator (July).** On Monday, *INEGI* will also release its monthly global economic indicator for July (GDP monthly proxy), where we expect a 1.5% yoy expansion, below June's 2.4% growth. As we had mentioned in our last report, IP's contraction in July was explained by the 8.6% yoy reduction in mining output, as a result of the significant fall in Mexico's oil production, as well as the lower investment in Mexico's drilling projects. Moreover, we believe that services will show a 3.2% yoy expansion

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

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

Francisco Flores
Economist, Mexico
francisco.flores.serrano@banorte.com

Document for distribution among the general public

Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS	
Mon 25-Sep	9:00am	Global economic indicator (sa)	July	% yoy	<u>1.5</u>	1.5	2.4	
		Primary activities		% m/m	<u>-0.4</u>	--	0.5	
		Industrial production		% yoy	<u>2.0</u>	--	2.0	
		Services		% yoy	<u>-1.6</u>	--	-0.3	
				% yoy	<u>3.2</u>	--	3.9	
Tue 26-Sep	9:00am	Unemployment rate	August	%	<u>3.47</u>	3.41	3.41	
		sa		%	<u>3.27</u>	3.29	3.24	
Tue 26-Sep	10:00am	International reserves	Sep-22	US\$ bn	--	--	175.9	
Tue 26-Sep	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 10y Mbono (Jun'27); 5y Bondes D						
Wed 27-Sep	9:00am	Trade balance	August	US\$ mn	<u>-1,959.8</u>	-1,527.5	-1,523	
		Total exports		% yoy	<u>4.3</u>	--	8.0	
		Oil exports		% yoy	<u>21.3</u>	--	19.3	
		Non-oil exports		% yoy	<u>3.4</u>	--	7.4	
		Total imports		% yoy	<u>4.3</u>	--	6.6	
Thu 28-Sep	2:00pm	Banxico's monetary policy decision		%	<u>7.00</u>	7.00	7.00	
Fri 29-Sep	10:00am	Comercial banking credit	August	% yoy	<u>5.4</u>	--	5.9	
		Consumption		% yoy	<u>2.9</u>	--	3.3	
		Housing		% yoy	<u>2.6</u>	--	2.9	
		Non-banking private firms		% yoy	<u>7.1</u>	--	7.5	
Fri 29-Sep	3:30pm	Budget balance	August	MXN bn	--	--	119.3	

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

We expect a 1.5% yoy expansion in July's IGAE. On Monday, *INEGI* will also release its monthly global economic indicator for July (GDP monthly proxy), where we expect a 1.5% yoy expansion, below June's 2.4% growth.

As we had mentioned in our last report, IP's contraction in July was explained by the 8.6% yoy contraction in mining output, as a result of the significant fall in Mexico's oil production, as well as the lower investment in Mexico's drilling projects. With July's figure, mining activity now adds 38 consecutive months in contraction. In addition, construction posted a significant 3.7% yoy contraction, which was explained by the 4.4% reduction in building projects, whereas public civil engineering construction projects declined 2.5% yoy, given the austerity program implemented by the Federal Government (refer to the table on the following page). By contrast, manufacturing output increased a scant 2.2% yoy.

Moreover, we believe that services will show a 3.2% yoy expansion, as a result of the positive trend in the formal labor market coupled with an above-trend growth in banking credit. However, we believe that the scant 0.4% yoy expansion in retail sales will limit services growth in July.

Unemployment rate in August will stand at 3.47%. On Tuesday, *INEGI* will publish its unemployment report for the eighth month of 2017, in which we estimate an unemployment rate of 3.47% nsa, above the 3.41% observed in July. In seasonally adjusted terms, we believe that the unemployment rate could stand at 3.27% which implies a 0.03%-pts increase from last month's figures.

Looking ahead, we believe that the unemployment rate will hover around this level as a result of: On the positive side: (1) the higher growth of domestic demand –particularly within the services–, will continue to foster the formal labor market; (2) the recovery of external demand will push forward job creation within the manufacturing industry; and on the downside: (3) the downward trend in public spending has translated in a higher number of unemployed workers, which has already affected private investment projects.

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\$205 million amounting to US\$173.4 billion. According to Banxico's report, this figure comes mainly as a result of: (1) US\$8 million dollar sales from Banxico to the Federal Government; and (2) a negative revalorization in central bank assets amounting to US\$197 million. In this context, the Central Bank's international reserves have diminished by US\$3.2 billion this year (please refer to the table in the next page).

Banxico's foreign reserve accumulation detail

US\$, million

	2016	Sep 15, 2017	Sep 15, 2017	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	176,542	173,370	-205	-3,171
(B) Gross international reserve	178,025	174,719	-382	-3,306
Pemex	--	--	-195	-709
Federal government	--	--	-4	-3,826
Market operations	--	--	0	-2,000
Other	--	--	-182	3,229
(C) Short-term government's liabilities	1,483	1,346	-177	-135

Source: Banco de México

Weekly government bond auction. On Tuesday, the Ministry of Finance (MoF) –via Banco de Mexico as its financial agent–, will offer 10-year fixed rate Mbonos (Jun '27), 5-year Bondes D, 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 26, 2017)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	26-Oct-17	--	7,000	6.98
3m	28-Dec-17	--	11,000	7.07
6m	28-Mar-18	--	11,500	7.14
Bondes D				
5y	08-Sep-22	--	3,750	0.19
M Bono				
10y	03-Jun-27	7.50	8,500	6.89

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

Exports will continue to recover. On Wednesday at 9:00am (EDT), Banxico and *INEGI* will make available its preliminary trade report for August, where we expect to see a US\$1.96 billion deficit. On the exports side, we will probably see an 21.3% yoy expansion of oil exports as a result of the higher prices for the Mexican crude oil basket (18.7% yoy). In addition, non-oil exports could have increased 3.4% yoy, on the back of an 3.4% hike in manufacturing exports.

On the imports side, we estimate a 4.3% yoy expansion in total imports, as a result of the increase in oil related imports. However, taking a look at the breakdown, we believe that non-oil consumption goods imports increased 4.9% yoy, while imports of intermediate goods could have increased 3.8% yoy. Finally, we estimate a 1.1% contraction in capital goods imports.

Banxico's monetary policy announcement – No additional hikes. On Thursday, Banxico will announce its monetary policy decision at 3:00pm (EDT), where we do not expect an additional increase of the central bank's reference rate, which currently stands at 7%. We highlight that in the last *Quarterly Inflation Report (QIR)*, the central bank referred to the recovery of the Mexican economy, which prompted an upward revision to their GDP forecast for 2017 (current estimate: 2 - 2.5%; previous: 1.5 - 2.5%), as well as for 2018 (current estimate: 2 - 3%, previous: 1.7 - 2.7%). Similarly, the central bank also mentioned the convergence of inflation towards its 3% target in the third quarter of 2018. In this context, we consider that these two issues will be the most prominent within the monetary policy statement.

Since Banxico's Board considers that the impact of the recent inflationary shocks is temporary, and the current level of the reference rate is consistent with the convergence of inflation to its 3% target, we maintain our forecast that the monetary authority will maintain the reference rate at 7% throughout the year. We also believe that Banxico will be able to initiate an easing cycle in 2018, given that inflation will be converging towards the 3% target, as the above-mentioned inflationary shocks fade. We consider that Banxico has room to reduce the reference rate between 150-200bps over the next two years, from which 100bps could take place in the second half of 2018.

Banking credit will show a 5.4% yoy increase in August. Banco de Mexico will make available its banking credit report on Friday at 10:00am (EDT). It is our take that banking credit continued flowing in August. In particular, we estimate a 5.4% yoy expansion in banking credit (in real terms), as a result of increases in the area of 2.9%, 2.6%, and 7.1% yoy in consumer, housing and business credit, respectively.

The MoF's monthly report. Additionally, on Friday, the Ministry of Finance (MoF) will release its monthly finance report available for the eighth month of the year. On the revenue side, we will be looking at non-oil tax collection, as it will provide additional information about domestic demand behavior, particularly given the volatile dynamics in income tax collection seen in the year. Moreover, given instability in Mexico's crude oil basket price during July, the behavior of oil revenues generated by the Federal Government will be particularly relevant.

In addition, markets will focus on the spending side of the report, in order to assess the execution of the fiscal cut announced by the *MoF* in Mexico's Fiscal Budget for 2017. Finally, it will be important to evaluate the evolution of public sector debt, which currently represents around 43.8% of Mexico's GDP.

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
Juan Carlos García Viejo	Economist, International	juan.garcia.viejo@banorte.com	(55) 1670 - 2252
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@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 Senior Strategist	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Santiago Leal Singer	Strategist 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	Technical Analysis	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Equity Research – Conglomerates / Financials/ Mining / Petrochemicals	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research – Airlines / Airports / Cement / Infrastructure / REITs	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@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	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@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.cebillos@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	rvelazquez@banorte.com	(55) 5004 - 5279
Victor Antonio Roldan Ferrer	Head of Corporate Banking	victor.rolan.ferrer@banorte.com	(55) 5004 - 1454