

Ahead of the Curve

March 6, 2015

Market focus this week will be February's inflation report

- February's inflation report.** On Monday, at 10:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.29% m/m increase in February above market consensus that is forecasting a 0.21% according to Banamex survey. In the core index, we expect an increase of 0.39% m/m above market consensus (0.37%)
- January's industrial production report.** Next Friday, at 10:00am (EDT), *INEGI* will release its monthly industrial production report. We anticipate a 2.1% yoy expansion in total output during the first month of 2015. Taking a look at the breakdown, we believe that construction output could have expanded 6.6% yoy. Moreover, we believe that manufacturing production could post a 3.9% yoy expansion, explained by faster growth in manufacturing exports and vehicle production. However, we believe that the increase in industrial output during January will be limited by the poor performance of mining activity. In this regard, we expect a 5.8% yoy contraction derived from lower oil production and the reduction in the extraction of other minerals

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

Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Mon 9-Mar	10:00am	CPI inflation	February	%m/m	<u>0.29</u>	0.21	-0.09
				%yoy	<u>3.10</u>	3.02	3.07
		Core	%m/m	<u>0.39</u>	0.37	-0.03	
			%yoy	<u>2.45</u>	--	2.34	
Tue 10-Mar	11:00pm	International reserves	6-Mar	US\$ bn	--	--	195.7
Tue 10-Mar	1:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 3y MBono (Dec'18); 3y Udibonos (Jun'19)					
Tue 10-Mar		Wage negotiations	February	%yoy	<u>4.3</u>	--	4.2
Fri 13-Mar	10:00am	Industrial production (sa)	January	%yoy	<u>2.1</u>	2.2	3.0
				%m/m	<u>0.4</u>	0.4	-0.3
		Mining	%yoy	<u>-5.8</u>	--	-6.2	
		Utilities	%yoy	<u>2.2</u>	--	2.3	
		Construction	%yoy	<u>6.6</u>	--	6.8	
		Manufactures	%yoy	<u>3.9</u>	--	5.7	

Source: Banorte-IXE; Bloomberg

Document for distribution among the general public

Proceeding in chronological order...

Logistics – U.S. is back to daylight saving time. On Sunday, the U.S. will begin its Daylight Savings Time (DST). However, Mexico’s Daylight Saving Time period will not begin until April 5 which implies that Mexico City will have a two-hour difference with EDT.

Inflation in February will be explained by pressures on the price of energy along with higher prices of agricultural goods, particularly in the second half of the month. On Monday, at 10:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.29% m/m increase in February above market consensus that is forecasting a 0.21% according to Banamex survey. In the core index, we expect an increase of 0.39% m/m above market consensus (0.37%).

Inflation during the period in question will be explained by pressures on energy prices on the back of higher gasoline prices in cities in the northern border. In addition, our price monitoring suggests higher prices of some important elements in the “*fruits & vegetables*” sub-index, such as tomatoes, whose prices increased particularly in the second half of the month, more than offsetting for the declines observed in the first fortnight of the month.

Nevertheless, we expect this figure to be 13.5bps higher than the observed in same period last year, derived from: (1) 7.4bps stemming from a higher contribution of energy prices (8.7bps vs. 1.3 in 2014); (2) 5bps stemming from a higher contribution of merchandise prices (5.5bps vs. 0.5 in 2014), while we expect (3) a lower contribution services inflation (5.6bps vs. 5.8 in 2014), as shown in the table below. With these results, annual inflation will remain at levels around 3.1% yoy in February, while core inflation is at 2.45% from 2.34% yoy.

Inflation by components in February

%monthly incidence

	Banorte-Ixe	2014	Difference
Headline	0.29	0.15	0.13
Core	0.11	0.06	0.05
Goods	0.06	0.00	0.05
Processed foods	0.00	0.00	0.00
Other goods	0.06	0.01	0.05
Services	0.06	0.06	0.00
Housing	0.03	0.02	0.00
Education	0.00	0.00	0.00
Other services	0.03	0.03	0.00
Non-core	0.18	0.09	0.09
Agricultural	0.08	0.07	0.01
Fresh fruits and vegetables	0.06	0.03	0.03
Meat and egg	0.02	0.03	-0.02
Energy and government regulated	0.10	0.02	0.08
Energy	0.09	0.01	0.07
Government regulated	0.01	0.01	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

Weekly international reserves report. On Tuesday, at 11:00am (EDT), Banco de Mexico will release its weekly balance report. Last week, net international reserves increased by US\$92mn amounting to US\$195.7bn on February 27. 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\$27mn; along with a (2) US\$119mn increase 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 Foreign Exchange Commission (FEC) decided to shut down the options scheme that Banxico also used to accumulate reserves. In this context, the central bank has accumulated US\$2,500mn this year (please refer to the table below).

Banxico's foreign reserve accumulation details
US\$, million

	Foreign Reserve		Breakdown			
	Level	Chg	Pemex	Federal govt ¹	Market operations ²	Other
2006	67,680					
2007	77,991	10,311	12,899	-4,218	-4,240	5,870
2008	85,441	7,450	22,754	-5,413	-18,674	8,783
2009	90,838	5,397	11,529	6,573	-16,246	3,541
2010	113,597	22,759	16,037	2,338	4,466	-83
2011	142,475	28,878	18,692	2,439	4,614	3,134
2012	163,516	21,116	17,867	2,805	-646	1,089
2013	176,522	13,063	18,100	-1,251	0	-3,788
2014	193,239	16,717	14,500	2,570	-200	-154
27-Feb-15	195,739	2,500	3,000	-27	0	-473

Source: Banorte-Ixe, Banco de México; *Year-to-date

1. Includes short-term government's liabilities

2. Includes Banxico's US dollar sales to Mexican financial institutions as well as the Foreign Exchange Commission's USD Put/MXN Call options
*Year-to-date

Weekly government bond auction. Also on Tuesday, the Ministry of Finance (MoF) –via Banco de Mexico as its financial agent-, will offer 3-year fixed-rate Mbonos (Dec'18) as well as 3-year inflation-linked Udibonos (Jun'19), 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 1:30pm (EDT).

Auction specifics (Tuesday, March 10, 2015)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	03-Apr-15	--	5,500	3.01
3m	11-Jun-15	--	9,500	3.01
6m	03-Sep-15	--	11,000	3.20
Mbono				
3y	13-Dec-18	8.50	9,500	4.93
Udibono				
3y	13-Jun-19	4.00	850	2.00

Source: Banco de México

February's wage negotiations. On Tuesday, 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 4.3% in February. This would be slightly above the average observed in 2014 (4.2%). In this regard, we believe that February's figure was mainly driven by the increase in wage negotiations in the education sector, specifically wage increases in different labor unions of public universities, coupled with increases in the government sector and restaurant industry.

We expect a 2.1% yoy expansion in January's industrial output. Next Friday, at 10:00am (EDT), *INEGI* will release its monthly industrial production report. We anticipate a 2.1% yoy expansion in total output during the first month of the year. Taking a look at the breakdown, we believe that construction output could have expanded 6.6% yoy. We believe that construction has consolidated its recovery given the better growth dynamics in households' durable goods expenditure. Moreover, formal employment generated within this sector has shown a significant recovery in the past 10 months, which supports our view of a more positive perspective regarding the recovery of this sector. This would imply that construction could reach its eight positive growth rate after adding 17 consecutive months in contraction.

Additionally, we believe that manufacturing production could post a 3.9% yoy expansion, explained by faster growth in manufacturing exports (5.6% yoy) and vehicle production (6.8% yoy). We believe that in the short run 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.

However, we believe that the increase in industrial output during January will be limited by the poor performance of mining activity. In this regard, we expect a 5.8% yoy contraction derived from lower oil production and the reduction in the extraction of other minerals.

Industrial production estimates: January 2015

% yoy	Jan-15	Jan-14	Jan-Dec, '14	Jan-Dec, '13
Total		1.1	1.9	-0.5
Mining	-5.8	-0.7	-2.3	-0.1
Utilities	2.2	0.9	1.8	0.5
Construction	6.6	-2.0	1.9	-4.8
Manufacturing	3.9	3.3	3.7	1.1
% m/m sa	Jan-15	Dec-14	Difference	
Total	0.4	-0.3	0.7	
Mining	-0.6	-0.8	0.2	
Utilities	0.4	1.7	-1.3	
Construction	-0.2	1.1	-1.3	
Manufacturing	1.2	-1.6	2.9	

Source: Banorte-ixe

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
Julieta Álvarez Espinosa	Assistant	julieta.alvarez@banorte.com	(55) 5268 - 1613
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
Julia Elena Baca Negrete	Economist, U.S.	julia.baca.negrete@banorte.com	(55) 1670 - 2221
Livia Honsel	Economist, Europe	livia.honsel@banorte.com	(55) 1670 - 1883
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) 5004 - 1275
Victor Hugo Cortes Castro	Equity Research Analyst	victorh.cortes@banorte.com	(55) 5004 - 1231
Marissa Garza Ostos	Senior Equity Research Analyst – Conglomerates/Financials/ Mining/ Chemistry	marissa.garza@banorte.com	(55) 5004 - 1179
Marisol Huerta Mondragón	Equity Research Analyst – Food/Beverages	marisol.huerta.mondragon@banorte.com	(55) 5004 - 1227
José Itzamna Espitia Hernández	Equity Research Analyst – Airports / Cement / Infrastructure / Fibras	jose.espitia@banorte.com	(55) 5004 - 1266
Valentín III Mendoza Balderas	Equity Research Analyst	valentin.mendoza@banorte.com	(55) 5268 - 9000 x 1267
María de la Paz Orozco García	Analyst	maripaz.orozco@banorte.com	(55) 5004 - 5262

Corporate Debt

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5004 - 1405
Hugo Armando Gómez Solís	Analyst, Corporate Debt	hugo.gomez@banorte.com	(55) 5004 - 1340
Idalia Yanira Céspedes Jaén	Analyst, Corporate Debt	idalia.cespedes@banorte.com	(55) 5004 - 1437

Wholesale Banking

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Eric Faesi Puente	Managing Director – Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Jorge de la Vega Grajales	Managing Director – Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Managing Director – Private Banking	lpietrini@ixe.com.mx	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Managing Director – Asset Management	pimentelr@ixe.com.mx	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Managing Director – International Banking	rvelazquez@ixe.com.mx	(55) 5268 - 9879
Victor Antonio Roldan Ferrer	Managing Director – Transactional Banking	voldan@ixe.com.mx	(55) 5004 - 1454