

Preliminary GDP report – The Mexican economy falls 0.3% in 2Q16

July 29, 2016

- **INEGI released today its preliminary GDP report for 2Q16**
- **Gross Domestic Product (2Q16 P): 2.4% yoy; Banorte-Ixe: 2.4%; consensus: 2.4% (range of estimates: 2% to 2.7%); previous: 2.6%**
- **Gross Domestic Product (2Q16 P): -0.3% q/q; Banorte-Ixe: 0%; consensus: -0.1% (range of estimates: -0.3% to 0.4%); previous: 0.8%**
- **Domestic demand continues to be the main growth driver for the Mexican economy**
- **Looking ahead, we believe that the Mexican economy will show a higher growth in 3Q16, but still below 2% yoy given the recession in the mining industry coupled with the fall in public investment projects**
- **The revised figure will be published in August 22**

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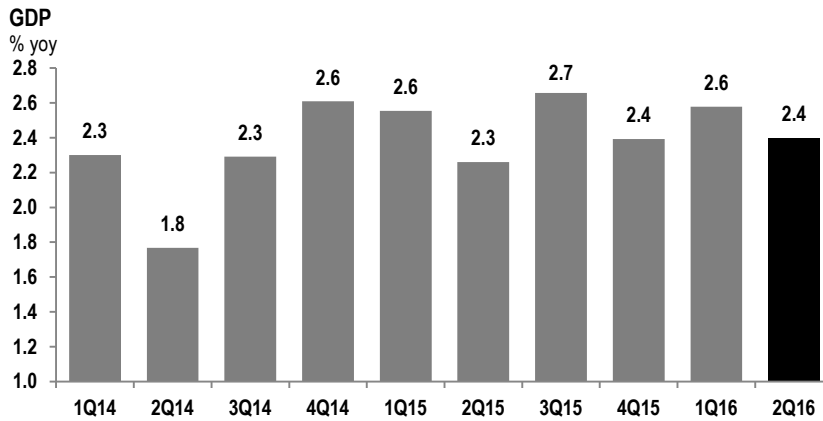
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The Mexican economy grew 2.4% in 2Q16, in line with our forecast. *INEGI* presented today its “*Preliminary Estimation of GDP*” report. With original figures, the Mexican economy expanded 2.4% yoy in 2Q16 (refer to the chart below), below the 2.6% observed in 1Q16. However, we highlight that the annual growth rate was positively affected by a seasonal effect, given that the *Holy Week* holidays added two working days in April. Controlling for this calendar effect, the Mexican economy grew a scant 1.4% yoy in 2Q16.

Taking a look at the breakdown, and analyzing the seasonal adjusted figures, primary activities increased 4.3% yoy, while the industrial sector fell 0.5% yoy, as a result of the deceleration in manufacturing output and the recession in the mining industry. Finally, services expanded 2.4% yoy, which suggests that domestic demand continues to be the main growth driver for the Mexican economy.

In seasonally adjusted terms, GDP fell 0.3% q/q. Taking a look at the breakdown, primary activities edged-down 0.1% q/q, while industrial production posted a 1.7% q/q contraction. Moreover, services posted a null growth. Given that *INEGI* has not published a comparable time series for the seasonally adjusted series, we can't compare this -0.3% q/q growth of 2Q16 with the 0.8% reported for the first quarter of 2016, considering that these figures are usually revised with the publication of new data.

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Source: INEGI; * Preliminary figure

Looking ahead, we believe that the Mexican economy will show a higher growth in 3Q16, but still below 2%. Domestic demand has stand out as Mexico’s main growth engine. In particular, Mexican households are spending more given the significant gains in real wages, and the more positive outlook that prevails for the Mexican economy. We believe that the recent upward trend in domestic demand will continue throughout the third quarter of 2016 given the following factors: (1) The recovery of the labor market; (2) the contained levels of inflation that will hold throughout the year; and (3) the better growth prospects in private consumption reflected in the recent spike observed in *INEGI* and *ANTAD* sales.

Moreover, despite the recent deceleration in manufacturing output, other indicators show that this sector will begin to marginally recover. In this regard, we believe that manufacturing production of final goods will strengthen in the third quarter of 2016 given: (1) Mexico’s manufacturing exports will recover given the still depreciated Mexican peso; and (2) the better growth prospects of US private consumption, which will translate into a stronger external demand for Mexico’s manufactured goods.

However, production and exports of intermediate goods will continue to show a marginal growth given the deceleration of the US manufacturing industry. Moreover, we believe that the overall growth in IP will be bounded in 3Q16 by the recession in the mining industry, coupled with the lower growth in construction given the fiscal cut announced in June 23 that incorporates a reduction in public investment projects.

Methodological note. For the estimation of this preliminary figure, *INEGI* uses the economic reports published for the first two months of each quarter, and adds the available information for the third month. The missing figures for the last month of the quarter are estimated using econometric models. In this regard, the preliminary estimation of GDP presented today will cover 80% with the direct information available, and will estimate the remaining 20%. Unlike other preliminary reports -as the U.S. GDP conducted by the *Bureau of Economic Analysis* (BEA)-, *INEGI*'s report only includes the three main sectors. BEA's preliminary report contains a complete breakdown of the quarterly GDP.

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