

Ahead of the Curve

June 19, 2015

Market focus this week will on IGAE's report

- April's IGAE.** On Wednesday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for April (GDP monthly proxy), where we expect a 2.6% yoy expansion. We believe that IGAE's growth during the third month of 2015 was driven by the performance of the service sector, which we forecast at 3.6% yoy. Similarly, we highlight that industrial production increased 1.1% yoy
- Bi-weekly inflation report.** On Wednesday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.16% 2w/2w increase in the first half of June above market consensus that is forecasting a 0.10% according to Bloomberg. In the core index, we expect an increase of 0.08% 2w/2w below market consensus (0.10%). Inflation during the period in question would be explained by pressures on agricultural and services prices. With these results, annual inflation will remain at 2.9% yoy in the first half of June, while core inflation would be at 2.3% yoy

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 |
|------------|------------|--|--------|---------|--------------|-----------|----------|
| Mon 22-Jun | 9:00am | Retail sales | April | % yoy | <u>5.3</u> | 5.2 | 5.5 |
| Mon 22-Jun | 4:30pm | Banamex bi-weekly survey of economic expectations | | | | | |
| Tue 23-Jun | 10:00am | International reserves | 19-Jun | US\$ bn | -- | -- | 193.2 |
| Tue 23-Jun | 12:30pm | Government weekly auction: 1-, 3-, 6-, and 12-month Cetes; 20y Mbono (Nov'34); 30y Udibono (Nov'46); 5y Bondes D | | | | | |
| Wed 24-Jun | 9:00am | Global economic indicator | April | % yoy | <u>2.6</u> | 2.3 | 2.7 |
| | | (sa) | | % m/m | <u>1.0</u> | -- | -0.6 |
| | | Primary activities | | % yoy | <u>2.0</u> | -- | -0.8 |
| | | Industrial production | | % yoy | <u>1.1</u> | -- | 1.7 |
| | | Services | | % yoy | <u>3.6</u> | -- | 3.3 |
| Wed 24-Jun | 9:00am | CPI inflation | 1Q Jun | % 2w/2w | <u>0.16</u> | 0.10 | 0.04 |
| | | | | % yoy | <u>2.90</u> | -- | 2.88 |
| | | Core | | % 2w/2w | <u>0.08</u> | 0.10 | 0.08 |
| | | | | % yoy | <u>2.26</u> | -- | 2.33 |
| Fri 26-Jun | 9:00am | Unemployment rate | May | % | <u>4.17</u> | 4.27 | 4.31 |
| | | sa | | % | <u>4.27</u> | -- | 4.32 |
| Fri 26-Jun | 9:00am | Trade balance | May | US\$ mn | <u>739.1</u> | -80 | -85.3 |
| | | Total exports | | % yoy | <u>0.1</u> | -- | -3.2 |
| | | Oil exports | | % yoy | <u>-32.9</u> | -- | -50.4 |
| | | Non-oil exports | | % yoy | <u>4.2</u> | -- | 2.7 |
| | | Total imports | | % yoy | <u>-1.7</u> | -- | -1.6 |

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

Retail sales will post a 5.3% yoy expansion in April. On Monday (June 22) at 9:00am (EDT), *INEGI* will publish its retail sales report for April 2015. We anticipate a 5.3% yoy expansion explained by the 23.3% 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.

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.

Banamex Survey: Market participants will focus on analysts' monetary policy assessments. On Monday at 4:30pm (EDT) *Banamex* will release its bi-weekly survey of economic expectations. In the last survey published by *Banamex* 24 out of 24 analysts surveyed expected a rate hike in 2015. Furthermore, analysts will also focus on June's first half inflation forecast (to be published on Wednesday, June 24), as well as on CPI estimations for 2015. Moreover, we expect moderate downward revisions to the economic growth estimates for 2015.

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 \$67mn amounting to US \$193.2bn on June 12. 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 \$43mn; (2) US \$260mn decrease explained by the introduction of Banxico's USD daily auction; along with a (3) US \$236mn 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 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 \$1mn international reserves this year (please refer to the table below).

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

| | 2014 | 12/Jun/2015 | 12/Jun/2015 | Year-to-date |
|---|---------|-------------|-------------|--------------|
| | Balance | | Flows | |
| International reserves (B)-(C) | 193,239 | 193,238 | -67 | -1 |
| (B) Gross international reserve | 195,682 | 195,385 | 36 | -297 |
| Pemex | -- | -- | -450 | 2,992 |
| Federal govt | -- | -- | 511 | 876 |
| Market operations | -- | -- | -260 | -3,424 |
| Other | -- | -- | 234 | -741 |
| (C) Short-term government's liabilities | 2,443 | 2,147 | 102 | -296 |

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 20-year fixed-rate Mbonos (Nov’34), 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, June 23, 2015)

| | Maturity | Coupon rate, % | To be auctioned ¹ | Previous yield ² |
|-----------------|-----------|----------------|------------------------------|-----------------------------|
| Cetes | | | | |
| 1m | 23-Jul-15 | -- | 5,500 | 2.94 |
| 3m | 24-Sep-15 | -- | 9,500 | 3.14 |
| 6m | 24-Dec-15 | -- | 11,000 | 3.26 |
| 12m | 23-Jun-16 | -- | 11,000 | 3.50 |
| Mbono | | | | |
| 20y | 23-Nov-34 | 7.75 | 3,000 | 6.61 |
| Udibono | | | | |
| 30y | 08-Nov-46 | 4.00 | 500 | 3.52 |
| Bondes D | | | | |
| 5y | 28-May-20 | -- | 3,000 | 0.24 |

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

We expect a 2.6% yoy expansion in April’s IGAE. On Wednesday, at 9:00am (EDT), *INEGI* will release its monthly global economic indicator for April (GDP monthly proxy), where we expect a 2.6% yoy expansion. We believe that IGAE’s growth during the third month of 2015 was driven by the performance of the service sector, which we forecast at 3.6% yoy. Similarly, we highlight that industrial production increased 1.1% yoy.

As we had mentioned in our last IP report, the 1.1% expansion in industrial production during April was explained in part by the 3.7% yoy growth in manufacturing output. In this regard, we believe that the recovery of this industry is on the way, and will strengthen in the first half of the year given: (1) A significant recovery in external demand, particularly from the U.S.; (2) Mexico’s manufacturing exports have shown solid growth rates; (3) the recent and significant depreciation of the Mexican currency will translate into stronger growth dynamics for the manufacturing exports; and (4) 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 2Q15.

Moreover, construction output grew 4.8% yoy. We believe that the significant expansion in construction in the last semester reflects the better growth expectations that prevail today in most of Mexico’s private firms. In addition, the recovery of households’ purchasing power –given the lower inflation levels and the recovery of the Mexican labor market– has led to a significant increase in residential projects. However, IP’s headline figure was confined by the current recession in the mining industry –derived from the significant contraction in Mexico’s oil production–.

We also believe that the 3.6% yoy estimated expansion in services will be explained by the recovery in private consumption. In this regard, *INEGI's* April'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. Moreover, it is likely that the 3.7% yoy growth in manufacturing output during April will boost certain subsectors within the services, such as the transport and trade.

Inflation in the first half of June will be explained by pressures on agricultural and services prices. On Wednesday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.16% 2w/2w increase in the first half of June above market consensus that is forecasting a 0.10% according to *Bloomberg*. In the core index, we expect an increase of 0.08% 2w/2w below market consensus (0.10%).

Inflation during the period in question will be explained by pressures on agricultural and services prices. According to our price monitoring, changes in the prices of *fruit and vegetables* continue to be mixed, but with higher prices in some important products such as tomatoes, bananas and apples, among others. In terms of services inflation, we are estimating a contribution of 2.1bps in housing costs.

Nevertheless, we expect this figure to be 7.4bps higher than the observed in same period last year derived from: (1) 13.2bps stemming from a higher contribution of agricultural prices (9bps vs. -4.2 in 2014); (2) a lower contribution of energy prices (0.7bps vs. 3.7 in 2014); along with (3) -2.3bps stemming from a lower contribution of services prices (3.3bps vs. 5.5 in 2014), as shown in the table below.

With these results, annual inflation will remain at 2.9% yoy in the first half of June, while core inflation would be at 2.3% yoy.

1H-June inflation by components

% bi-weekly incidence

| | Banorte-Ixe | 2014 | Difference |
|---------------------------------|-------------|-------|------------|
| Total | 0.16 | 0.08 | 0.07 |
| Core | 0.06 | 0.09 | -0.03 |
| Goods | 0.03 | 0.03 | -0.01 |
| Processed foods | 0.02 | 0.03 | -0.01 |
| Other goods | 0.01 | 0.01 | 0.00 |
| Services | 0.03 | 0.06 | -0.02 |
| Housing | 0.02 | 0.02 | 0.00 |
| Education | 0.00 | 0.01 | -0.01 |
| Other services | 0.01 | 0.03 | -0.02 |
| Non-core | 0.10 | -0.01 | 0.10 |
| Agricultural | 0.09 | -0.04 | 0.13 |
| Fresh fruits and vegetables | 0.07 | -0.04 | 0.11 |
| Meat and egg | 0.02 | 0.00 | 0.02 |
| Energy and government regulated | 0.01 | 0.04 | -0.03 |
| Energy | 0.01 | 0.04 | -0.03 |
| Government regulated | 0.00 | 0.00 | 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 May will stand at 4.18%. Next Friday, *INEGI* will publish its employment report for the fifth month of 2015, in which we estimate an unemployment rate of 4.18% nsa, below the 4.31% observed in April. In seasonally-adjusted terms, we believe that the unemployment rate could stand at 4.27%, which implies a monthly fall of 0.1%-pts.

It is likely that the job creation in May 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 of the economic activity, which will have a significant positive impact on firms' expectations about domestic demand, resulting in a more dynamic labor market.

Non-oil exports continue to expand vigorously. Finally, on Friday (June 26), at 9:00am (EDT), *INEGI* will make its May's trade report available, where we expect to see a US\$ 739 million surplus. On the exports side, we will probably see a 32.9% yoy contraction of oil exports given the significant fall in oil prices. Moreover, non-oil exports could have expanded 4.2% yoy.

On the imports side, we estimate a 1.7% yoy reduction in total imports. Taking a look at the breakdown, we estimate that imports of consumption goods (excluding oil) decreased 4.5% yoy, while imports of intermediate goods (excluding oil) could have fallen 1.8% yoy. Finally, we estimate a 3.1% expansion in capital goods imports.

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 |