

Ahead of the Curve

July 4, 2016

Market focus this week will on *INEGI's* monthly inflation report

- June's inflation report.** On Thursday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.18% m/m increase in June marginally above consensus forecast, according to Bloomberg. In the core index, we expect an increase of 0.27% m/m also according to estimates. Inflation during the period in question will be explained by pressures on merchandise and services prices. In the first case, we detected pressures both from food and other goods prices, probably a result of some pass-through from FX depreciations. In the services sub-index, our price monitoring suggests a greater contribution from housing costs as well as from other services. Meanwhile, agricultural prices could show pressures on the back of higher prices of products such as tomatoes
- We expect a 1.35% yoy expansion in April's GFI.** On Tuesday at 9:00am (EDT), *INEGI* will publish its gross fixed investment (GFI) report for the fourth month of the year. We anticipate GFI up by 1.3% yoy. However, April's expansion will be partially explained by a calendar effect, as GFI's accounting benefited from the *Holy Week* holiday that started in March (vs. April in 2015)

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Mexico weekly calendar

DATE	HOUR (EDT)	EVENT	PERIOD	UNIT	BANORTE-		
					IXE	CONSENSUS	PREVIOUS
Tue 5-Jul	9:00am	Gross fixed investment	April	% yoy	<u>1.3</u>	1.3	-3.0
		Machinery and equipment		% yoy	<u>0.7</u>	--	-5.0
		Domestic		% yoy	<u>8.3</u>	--	8.7
		Imported		% yoy	<u>-2.5</u>	--	-10.5
		Construction		% yoy	<u>1.7</u>	--	-1.6
Tue 5-Jul	10:00am	International reserves	3-Jul	US\$ bn	--	--	177.3
Tue 5-Jul	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 30y Mbono (Nov'42); 5y Bondes D					
Tue 5-Jul	4:30pm	Banamex bi-weekly survey of economic expectations					
Thu 7-Jul	9:00am	CPI inflation	June	% m/m	<u>0.18</u>	0.14	-0.45
				% yoy	<u>2.61</u>	2.56	2.60
		Core		% m/m	<u>0.27</u>	0.27	0.21
				% yoy	<u>2.99</u>	--	2.93
Fri 8-Jul	9:00am	Consumer confidence	June	index	<u>92.6</u>	92.2	90.9
Fri 8-Jul		Wage negotiations	June	%	<u>4.7</u>	--	3.9

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

We expect a 1.3% yoy expansion in April's GFI. On Tuesday at 9:00am (EDT), *INEGI* will publish its gross fixed investment (GFI) report for the fourth month of the year. We anticipate GFI up by 1.3% yoy. However, April's expansion will be partially explained by a calendar effect, as GFI's accounting benefited from the *Holy Week* holiday that started in March (vs. April in 2015).

We believe that within the report we will probably see a 2.5% yoy contraction in imported machinery and equipment, given that trade balance figures showed a similar decline for capital goods imports. Moreover, we expect an 8.3% growth in domestic machinery and equipment. Finally, we believe that construction spending increased 1.7% yoy derived from the higher construction spending observed in the latest industrial production figures.

April's GFI estimates

%yoy	Apr-16	Apr-15	Jan-Apr, '16	Jan-Apr, '15
Total	1.3	5.8	0.8	5.6
Machinery and equipment	0.7	6.6	0.5	7.7
Domestic	8.3	10.2	8.3	9.2
Imported	-2.5	5.2	-2.9	7.0
Construction	1.7	5.2	1.0	4.3
Annual contribution	Apr-16	Apr-15	Difference	
Total	1.3	5.8	-4.5	
Machinery and equipment	0.3	2.5	-2.3	
Domestic	1.0	1.1	-0.2	
Imported	-0.7	1.4	-2.1	
Construction	1.0	3.2	-2.2	

Source: Banorte-ixe

Weekly international reserves report. On Tuesday, at 10:00am (EDT), Banco de Mexico will release its weekly balance report. Last week, net international reserves increased by US\$44mn amounting to US \$177.3 billion on June 24. According to Banxico's report, this figure comes mainly as a result of: (1) Dollar sales by Banxico to the Federal Government for US\$108mn; and (2) US\$152mn 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. In this context, the Central Bank has accumulated US\$600mn international reserves this year (please refer to the table below).

Banxico's foreign reserve accumulation details

US\$, million

	2015	24/Jun/2016	24/Jun/2016	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	176,735	177,335	44	600
(B) Gross international reserve	177,597	181,476	948	3,880
Pemex	--	--	2,022	4,903
Federal govt	--	--	-1,326	1,683
Market operations	--	--	0	-5,562
Other	--	--	251	2,855
(C) Short-term government's liabilities	861	4,141	904	3,280

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 30-year fixed-rate Mbonos (Nov’42) as well as 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, July 5, 2016)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	4-Aug-16	--	5,500	3.86
3m	6-Oct-16	--	9,500	4.19
6m	5-Jan-17	--	11,000	4.33
Mbono				
20y	23-Nov-34	7.75	2,500	6.80
Bondes D				
5y	20-May-21	--	3,000	0.21

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 monetary policy forecasts. On Tuesday at 4:30pm (EDT) *Banamex* will release its bi-weekly survey of economic expectations, where market participants will focus on analysts’ monetary policy assessments given Banxico’s latest monetary policy announcement, in which the central bank decided to by 50bps the reference rate.

Furthermore, analysts will also focus on the inflation report for June (to be published on Thursday, July 9), as well as on CPI estimations for 2016 and 2017. Moreover, *Banamex* will also publish consensus’ growth and FX forecasts for 2016-17. In the first case, we do not expect strong revisions to the median GDP forecast. In the second case, we expect moderate upward revisions to the FX estimates for 2016.

Inflation in June will be explained by pressures on core prices. On Thursday, at 9:00am, *INEGI* will release its monthly inflation report. We are forecasting a 0.18% m/m increase in June, marginally above consensus forecast, according to *Bloomberg*. In the core index, we expect an increase of 0.27% m/m also according to estimates.

Inflation during the period in question will be explained by pressures on merchandise and services prices. In the first case, we detected pressures both from food and other goods prices, probably a result of some pass-through from FX depreciations. In the services sub-index, our price monitoring suggests a greater contribution from housing costs as well as from other services. Meanwhile, agricultural prices could show pressures on the back of higher prices of products such as tomatoes.

Nevertheless, we expect this figure to be 1.2bps higher than the observed in same period last year, derived from: (1) 4.2bps stemming from a higher contribution of energy (7bps vs. 2.8 in 2015); and (2) 4.2bps stemming from a higher contribution of goods prices (11.4bps vs. 7.3 in 2015). By contrast, we expect -6.9bps from a lower contribution agriculture prices (-9.2bps vs. -2.3 in 2015), as shown in the table below.

With these results, annual inflation should remain around 2.61% yoy in June, while core inflation will edged up to 2.99% from 2.93% yoy.

Inflation by components in June
%monthly incidence

	Banorte-Ixe	2015	Difference
Total	0.18	0.17	0.01
Core	0.20	0.16	0.04
Goods	0.11	0.07	0.04
Processed foods	0.06	0.04	0.02
Other goods	0.06	0.03	0.02
Services	0.09	0.08	0.00
Housing	0.04	0.03	0.01
Education	0.00	0.00	0.00
Other services	0.05	0.05	0.00
Non-core	-0.02	0.01	-0.03
Agriculture	-0.09	-0.02	-0.07
Fruits & vegetables	-0.05	0.00	-0.05
Meat & eggs	-0.04	-0.02	-0.02
Energy & government tariffs	0.07	0.03	0.04
Energy	0.07	0.03	0.04
Government tariffs	0.00	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.

Consumer confidence will marginally recover in June. On Friday at 9:00am (EDT), Banxico and *INEGI* will publish its June's monthly survey on consumer confidence, where we expect a 2.2% yoy contraction, with the index reaching 92.6 points. However, in seasonally adjusted terms, we expect confidence levels to increase 0.5% m/m.

We believe that consumer confidence (measured in seasonally adjusted terms) will show a moderate growth given the relative low inflation levels, which will be reflected in a higher growth of consumer's expectations regarding the country's present and future economic outlook, and will also translate in an expansion of the purchasing power component.

Looking ahead, we believe that the low inflation levels, the higher growth of the labor market, and the upward trend in credit to the private sector will translate in a more visible recovery of consumer confidence.

June's wage negotiations. Finally, on Friday, the Ministry of Labor (*STPS*) will make its contractual wage negotiations monthly data available. We anticipate workers to have negotiated an average wage increase of 4.7% in June. This would be above the 4.3% observed in year-to-date. In this context, we believe that June's figure was mainly driven by the increase in wage negotiations within the syndicates of most of the local governments of Mexico's federal entities.

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