Ahead of the Curve

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Market focus this week will on INEGI's bi-weekly inflation report

- **Bi-weekly inflation report.** On Thursday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.46% 2w/2w increase in the first half of October below with consensus 0.48% according to *Bloomberg*. In the core index, we expect an increase of 0.14% 2w/2w below market consensus (0.18%). Inflation during the period in question will be explained by pressures on energy prices, as summer discounts to electricity tariffs come to an end. In addition, we expect to see some pressure on merchandise prices as we are starting to perceive an incipient pass through from FX depreciation to prices. With these results, annual inflation remains at 2.5%yoy in the first half of October, while core inflation will edge up to 2.5% from 2.4% yoy

- **Retail sales (August).** On Wednesday (October 21) at 9:00am (EDT), *INEGI* will publish its retail sales report for August 2015. We anticipate a 4.9% yoy expansion explained by the 6.8% yoy growth in vehicle sales (*AMIA*), which will have a positive impact on the overall growth rate. Moreover, *ANTAD* total store sales increased 8.7% yoy in real terms during the period in question. However, consumption goods imports -which have a strong correlation with retail sales- posted a scant 1.6% yoy expansion, which could limit August's growth rate

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Mexico weekly calendar

DATE	TIME (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Tue 20-Oct	10:00am	International reserves	16-Oct	US$ bn	--	--	179.3
Tue 20-Oct	12:30pm	Government weekly auction: 1-, 3-, and 6-month Cetes; 3y MBono (Dec'18); 3y Udibono (Jun'19)					
Tue 20-Oct	4:30pm	Banamex bi-weekly survey of economic expectations					
Wed 21-Oct	9:00am	Retail sales	August	% yoy	4.9	4.8	5.8
Thu 22-Oct	9:00am	CPI inflation	1Q Oct	% 2w/2w	0.46	0.48	0.00
				% yoy	2.47	2.51	2.51
		Core		% 2w/2w	0.14	0.18	0.10
				% yoy	2.45	--	2.38
Fri 23-Oct	9:00am	Unemployment rate	September	%	4.57	4.68	4.68
		sa		%	4.27	--	4.32

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

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$1,000mn amounting to US $179.3bn on October 9. 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$92mn; (2) US$1,000mn decrease explained by the introduction of Banxico's USD daily auction without minimum price; along with a (3) US$92mn 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 an accumulated reduction of US$13,931mn international reserves this year (please refer to the table below).

Banxico's foreign reserve accumulation details
US$, million

	2014	9/Oct/2015	9/Oct/2015	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	193,239	179,308	-1,000	-13,931
(B) Gross international reserve	195,682	181,680	-752	-14,001
Pemex	--	--	244	3,857
Federal govt	--	--	35	-991
Market operations	--	--	-970	-16,775
Other	--	--	-61	-92
(C) Short-term government's liabilities	2,443	2,373	248	-70

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 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 12:30pm (EDT).

Auction specifics (Tuesday, October 20, 2015)

	Maturity	Coupon rate, %	To be auctioned[1]	Previous yield[2]
Cetes				
1m	19-Nov-15	- -	5,500	3.00
3m	21-Jan-16	- -	9,500	3.13
6m	14-Apr-16	- -	11,000	3.24
Mbono				
3y	13-Dec-18	8.50	9,000	4.80
Udibono				
3y	13-Jun-19	4.00	850	1.74

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 analysts' monetary policy assessments.** 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 just after Banxico's minutes. In the last survey published by *Banamex* 18 out of 26 analysts surveyed expected a rate hike in 2015. Furthermore, analysts will also focus on October's first half inflation forecast (to be published on Thursday October 22), as well as on CPI estimations for 2015. Moreover, we expect moderate downward revisions to the economic growth estimates for 2015.

Retail sales will post a 4.9% yoy expansion in August. On Wednesday (October 21) at 9:00am (EDT), *INEGI* will publish its retail sales report for August 2015. We anticipate a 4.9% yoy expansion explained by the 6.8% yoy growth in vehicle sales (*AMIA*), which will have a positive impact on the overall growth rate. Moreover, *ANTAD* total store sales increased 8.7% yoy in real terms during the period in question. However, consumption goods imports - which have a strong correlation with retail sales- posted a scant 1.6% yoy expansion, which could limit August's growth rate.

Looking ahead, we believe that retail sales performance will show a visible recovery in the second half of the year. In particular, private consumption in Mexico will show better growth prospects derived from: (1) An 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.

Inflation in the first half of October will be explained by pressures on the price of energy, as summer discounts on electricity tariffs come to an end. On Thursday, at 9:00am, *INEGI* will release its bi-weekly inflation report. We are forecasting a 0.46% 2w/2w increase in the first half of October below with consensus 0.48% according to *Bloomberg*. In the core index, we expect an increase of 0.14% 2w/2w below market consensus (0.18%).

Inflation during the period in question will be explained by pressures on energy prices, as summer discounts to electricity tariffs come to an end. In addition, we expect to see some pressure on merchandise prices as we are starting to perceive an incipient pass through from FX depreciation to prices.

Nevertheless, we expect this figure to be 3.5bps lower than the observed in same period last year, derived from: (1) 5.9bps stemming from a higher contribution of agricultural prices (4.8bps vs. -1.2 in 2014); (2) 4.9bps stemming from a higher contribution of merchandise prices (7.5bps vs. 2.6 in 2014). By contrast, we expect (3) a lower contribution energy prices (30.6bps vs. 44.9 in 2014); and (4) -2.8bps stemming from a lower contribution of services (3.2bps vs. 6.1 in 2014), as shown in the table below

With these results, annual inflation remains at 2.5%yoy in the first half of October, while core inflation will edge up to 2.5% from 2.4% yoy.

1H-October inflation by components
% bi-weekly incidence

	Banorte-Ixe	2014	Difference
Total	0.46	0.50	-0.04
Core	0.11	0.09	0.02
Goods	0.08	0.03	0.05
Processed foods	0.04	0.03	0.00
Other goods	0.04	-0.01	0.05
Services	0.03	0.06	-0.03
Housing	0.01	0.01	0.00
Education	0.00	0.00	0.00
Other services	0.02	0.05	-0.03
Non-core	0.35	0.42	-0.07
Agricultural	0.05	-0.01	0.06
Fresh fruits and vegetables	0.04	0.00	0.04
Meat and egg	0.01	-0.01	0.01
Energy and government regulated	0.31	0.44	-0.13
Energy	0.31	0.45	-0.14
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 September will stand at 4.57%. Next Friday, *INEGI* will publish its employment report for the ninth month of 2015, in which we estimate an unemployment rate of 4.57% nsa, below the 4.68% observed in August. In seasonally-adjusted terms, we believe that the unemployment rate could stand at 4.27%, which implies a monthly fall of 0.05%-pts.

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

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