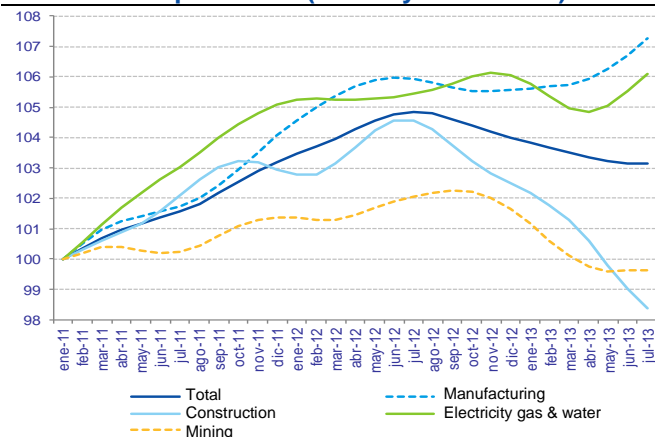


Mexico Weekly Flash

Next week...

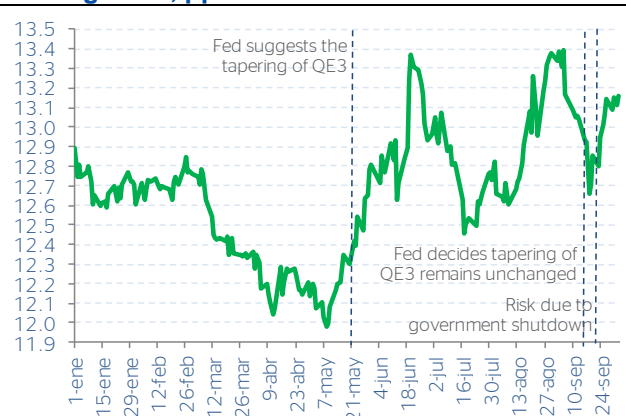
- Industrial output figures will guide economic growth forecasts for the third quarter of the year.**
 The performance of industrial output in August 2013 is set to be released on Friday, October 11. The figures are important for guidance on economic growth forecasts for Q3. It should be stated that Mexican industrial output in June fell to an annual rate (y/y) of -1.6% (corrected for seasonal variation, CSV). The decline in Mexican industrial output was due to the contraction in two of its four components, construction (-6.5% y/y, CSV) and mining (-2.2% y/y, CSV). Electricity, gas and water saw a minor rise of 0.8% y/y CSV and manufacturing increased 1.0% y/y CSV. Construction is highly likely to remain in decline although manufacturing will again see growth since US industrial output, especially manufacturing, saw major annual growth in August (2.7% y/y, 0.6% m/m, CSV). In this way, some recovery in the Mexican industrial indicator is forecast, going from -1.6% in July to -0.8% in August y/y CSV, i.e. monthly growth of 0.6%, CSV.
- Markets expect risks due to the political situation in the US**
 Financial markets this week continued in anticipation of a resolution to the temporarily operational closure of the US government and with just under two weeks to go until an increase in the Treasury debt ceiling requires approval. Financial variables saw moderate moves possibly due to lower uncertainty with regard to an expected increase in the debt ceiling being passed and because the negative effects from the government closure on growth point to the Fed continuing its non-conventional monetary policies. Nonetheless, risks remain latent. Our US analysis team estimates that the operational closure of the government will cut quarterly growth in 4Q13 at an annualized rate of between 0.17 and 0.34% but the main risks are centered around the need to increase the debt ceiling in the middle of the month. If this is not done, a spending cut equivalent to 4.2% of GDP would be required; linked to the default risks, the negative consequences on confidence and uncertainty surrounding global liquidity conditions would raise risk aversion. Until present, the impacts have been limited but an adverse scenario cannot be ruled out. In contrast, a solution in a context of an expansionary minded Fed would increase risk appetite.

Chart 1
Industrial Output: trend (January 2011 = 100)



Source: BBVA Research with INEGI data.

Chart 2
Exchange rate, ppp



Source: BBVA Research, Bloomberg.

AMIA automotive output in September and Gross fixed investment in July (October 7 and 8)

Close attention will need to be paid next week to reports on automotive output in September released by the Mexican Automotive Industry Association (AMIA). This indicator increased 4.3% CSV in August compared to the same month from last year and a slight increase is now expected. In addition, an important indicator for industrial output in Mexico is set for release - gross fixed investment in July, released by the INEGI. Gross fixed investment in June saw an annual decline of 1.8%.

September inflation (October 9)

Forecast: 0.43% (3.45% y/y)

Consensus: 0.46%

Previous: 0.28% (3.46% y/y)

On Wednesday, INEGI will release the inflation figures for September which are set to continue to show no demand pressures. In monthly terms, we expect a 0.43% rise in inflation and 0.30% in core inflation. With this, in annual terms inflation will remain around 3.5%, while core inflation will see a slight increase to 2.5%. The figures will be useful to see the first temporary impact on inflation from the recent floods in many states in Mexico. Nevertheless, we believe most of these impacts will be seen in October. We continue to expect Banxico having to make an addition 25 basis point cut in the policy rate at the next meeting on October 25 in a benign context for inflation and continued economic weakness.

Industrial Output in August (October 11)

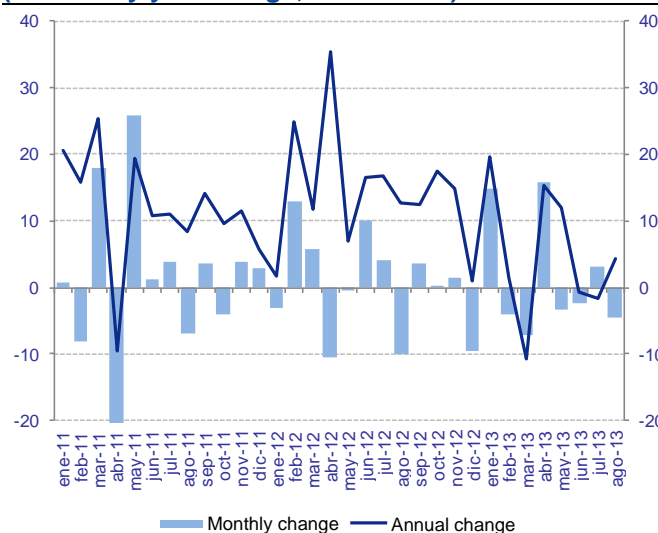
Forecast: -0.8% y/y, 0.58% m/m, CSV

Consensus: N/A

Previous: -1.6% y/y, -0.08% m/m, CSV

Chart 3

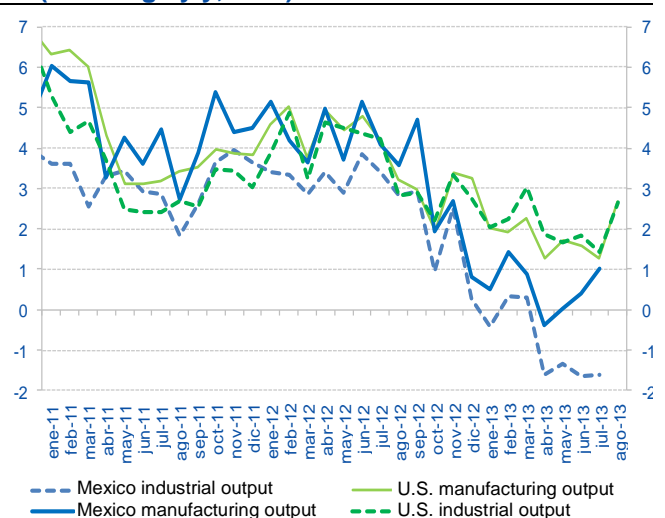
Automotive production in Mexico (m/m and y/y % change, CSV series)



Source: BBVA Research with AMIA data.

Chart 4

Industrial output and manufacturing: Mexico and US (% change y/y, CSV)

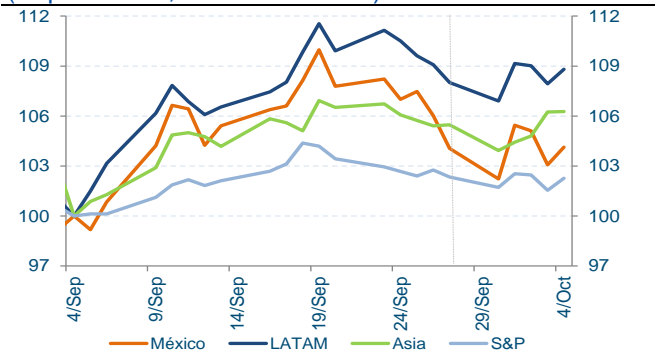


Source: BBVA Research with INEGI Bloomberg data.

Markets, activity and inflation

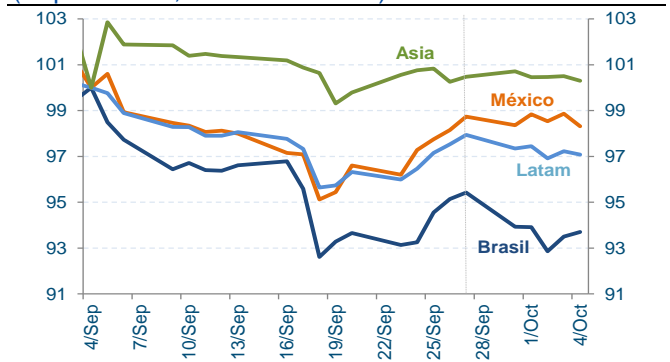
- Gains on stock markets and higher currencies at the end of the week after statements from the Republican majority leader in the US Congress regarding the country not being permitted to default on its loans. Linked to this, optimism regarding a rapid solution to the operational shutdown of the government led to the peso strengthening 0.4% over the week.

Chart 6
Stock markets: MSCI indices
(September 4, 2013 index=100)



Source: BBVA Research with data from Bloomberg

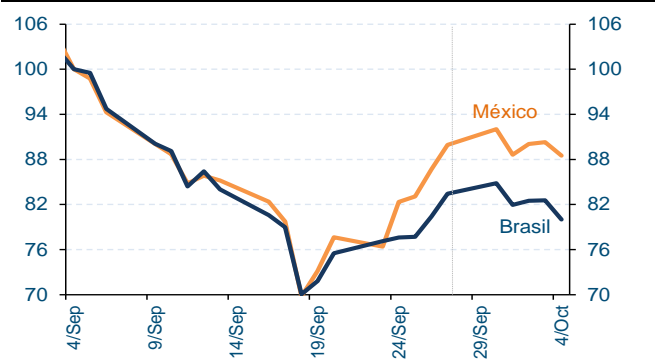
Chart 7
Foreign exchange: dollar exchange rates
(September 4, 2013 index=100)



Source: BBVA Research with Bloomberg data NB: LATAM includes Argentina, Brazil, Chile, Colombia and Peru. Asia includes the Philippines, South Korea, Taiwan, Singapore, Indonesia and Thailand.

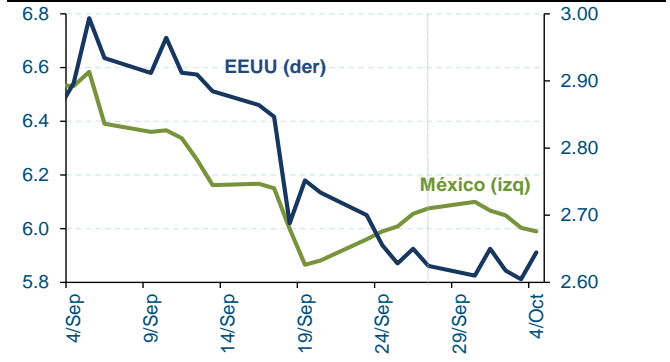
- Slight upswing in long-term US rates toward the end of the week after hitting two-month lows, with a new 10-year issuance this coming Monday. Rates for bonds with up to three month maturities increased faced with the risk of failing to reach agreement on the debt ceiling. Long-term rates in México fell slightly over the week.

Chart 8
Risk: 5-year CDS (September 4, 2013 index=100)



Source: BBVA Research with data from Bloomberg

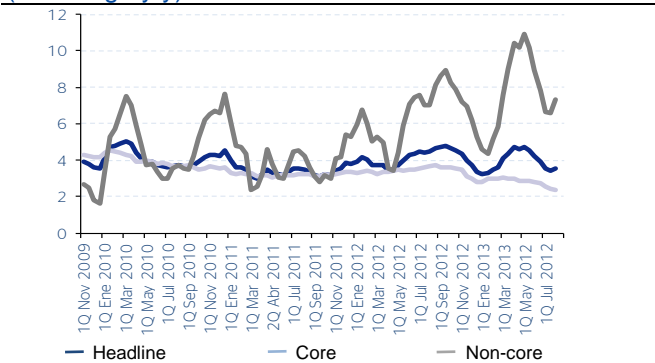
Chart 9
10-year interest rates, last month



Source: BBVA Research with data from Bloomberg

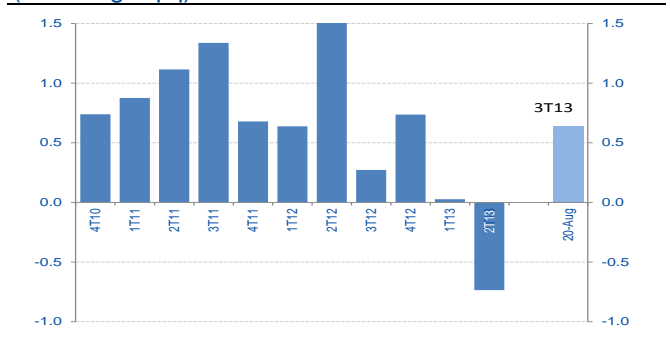
- The slack economic output points to core inflation remaining near current levels in coming months. Economic growth is expected to see a bounce this quarter, although recent data show persistent weakness.

Chart 10
Inflation Breakdown
(% change y/y)



Source: INEGI and BBVA Research

Chart 11
Observed and estimated GDP 3Q13
(% change q/q)



Source: BBVA Research

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