Mexico Weekly Flash

Next week…

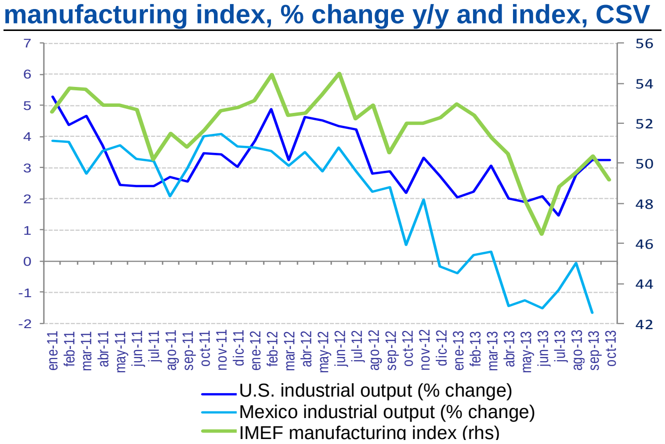
- **Industrial output for October will provide information on the strength of the economic recovery in Mexico in the fourth quarter**

This coming Thursday sees the release of industrial output figures for October. Despite the recent uptick in manufacturing output in the US, the weakness of the construction sector and the slowdown in the mining sector leads us to forecast industrial output in Mexico for October will remain weak (see next page). Nonetheless, the positive US job creation figures for November in the manufacturing sector (27,000) point to the sector continuing to enjoy the improvement that started in August. This means we could also expect to see an uptick in manufacturing output in Mexico in the last months of the year which would have a positive knock-on effect for industrial output in the last two months of the year.

US job figures do not substantially change expectations with regard to the tapering in asset purchases although they do strengthen the outlook for an improvement in the cycle

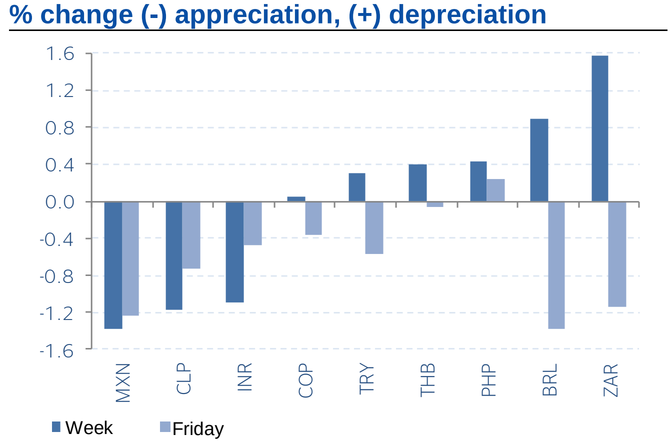
US economic indicators saw a surprise upswing this week. The job creation figures for November were especially important. 203,000 new jobs were created (vs. the forecast 185,000) and the figures for October were revised to 200,000 meaning the highest job creation was seen in two months since February-March. The long-term US interest rates increased 11bp over the week while the 10-year bond in Mexico also rose 16bp meaning the moves in US rates continue to be the key factor for those in Mexico. Nevertheless, the performance on the currency market was positive in comparison to bonds. This could partly be down to lower inflation in the US (especially core inflation) pointing to the tapering in quantitative easing may not be imminent, although it is mainly due to the recent success at the Fed in explaining the separation between conventional policies (i.e. exceptionally low interest rates over a prolonged period) and unconventional ones (i.e. the coming reduction in asset purchases); it could also be due to the continued strengthening in the global economic cycle that may favor inflows to stock markets in emerging economies. In this scenario, on Friday the peso was one of the strongest currencies, possibly due to Mexico being the main beneficiary of stronger US economic output.

Chart 1
Industrial output in Mexico and the US and IMEF manufacturing index, % change y/y and index, CSV



Source: BBVA Research with INEGI and Bloomberg data. CSV=Corrected for Seasonal Variation.

Chart 2
Trading in emerging currencies over the last week, % change (-) appreciation, (+) depreciation



Source: BBVA Research, INEGI.

Calendar: Indicators

November inflation (December 9)

Forecast: 0.90% (3.59% y/y)	Consensus: 0.92%	Previous: 0.48% (3.36% y/y)

On Monday, the inflation figures for November will be released which are set to continue to show no demand pressures. High monthly inflation is expected due to the seasonal adjustment in electricity prices and the major hike in agricultural prices seen in the first two weeks of the month. In monthly terms, we expect an increase in headline inflation of 0.90% and 0.14% for core inflation, representing year-on-year increases of 3.59% and 2.57% respectively (vs. 3.36% and 2.48% in October). In implicit terms, we forecast a 0.02% bi-weekly decline for core inflation due to the expectation of a positive performance in the goods sub-index after the "good end" offers and the services sub-index in light of a possible downward adjustment in cell phone prices after the increases seen in October. In December, the announced 3 to 5 peso rise in the metro price (starting from December 13) will lead to an increase of around 0.12pp in monthly inflation in December. This means we expect headline inflation to end the year at 3.7%.

Workers insured in the IMSS in November (December 10)

On December 10, the STPS is set to release the figures for the number of workers insured in the IMSS in November. The figure for new insured workers in October hit 143,591. Attention needs to be paid to this indicator since it will provide clues on whether economic output in Mexico is seeing a steady recovery in the fourth quarter of the year.

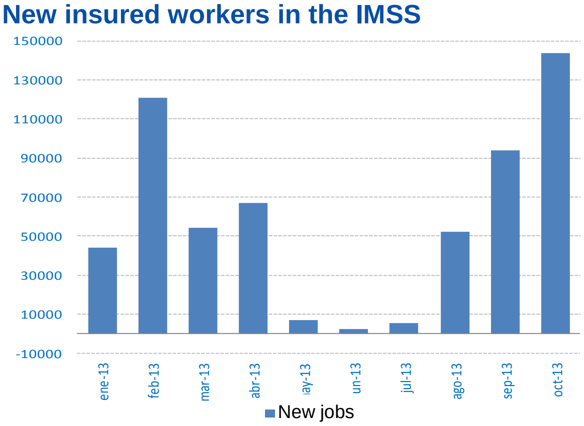
Industrial Output, October (December 12)

Forecast: -0.72% y/y, 0.0% m/m, CSV	Consensus: N/A	Previous: -1.65% y/y, -1.15% m/m, CSV

This coming Thursday, December 12, INEGI is set to release the performance in industrial output for October 2013. Industrial output in Mexico fell for the sixth month in a row in September in year-on-year terms (y/y), coming in at -1.65% (corrected for seasonal variation - CSV), declining (-)1.15% compared to the previous month (m/m). The decline in industrial output was due to the contraction in construction (-7.9% y/y, CSV) and mining (-1.1% y/y, CSV). Electricity, gas and water saw a minor rise of 1.0% y/y CSV and manufacturing increased 0.6% y/y CSV. In turn, the IMEF manufacturing indicator declined (-)2.3% m/m in October. In line with this performance and thanks to a slowdown in monthly growth for US industrial output in October (-0.1% m/m), we expect the industrial output indicator for Mexico to show monthly growth of 0.0%. This would represent an annual decline of (-)0.72%, CSV.

Chart 3

New insured workers in the IMSS

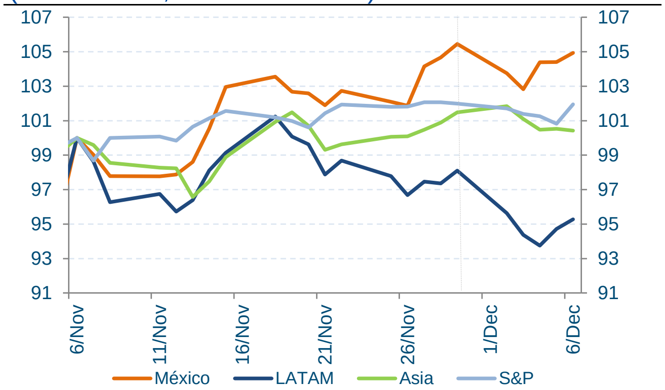


Source: BBVA Research, with Federal Mortgage Society (STPS) data.

Markets, activity and inflation

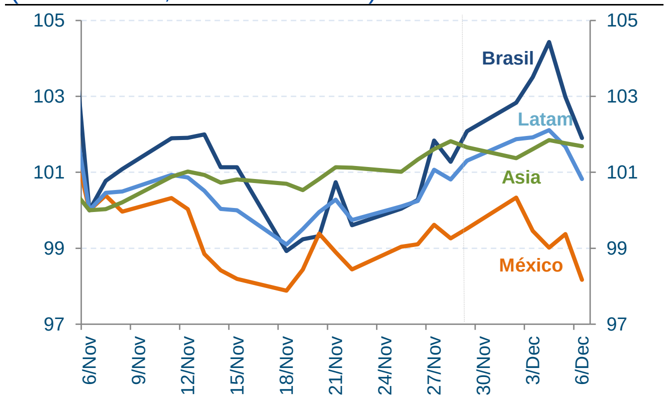
- Supported by the recent FED statement, the better-than-expected US job figures focused markets on economic recovery and outweighed attention on the upcoming asset purchase tapering. This led to gains on stock markets and stronger emerging currencies.

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



Source: BBVA Research with data from Bloomberg

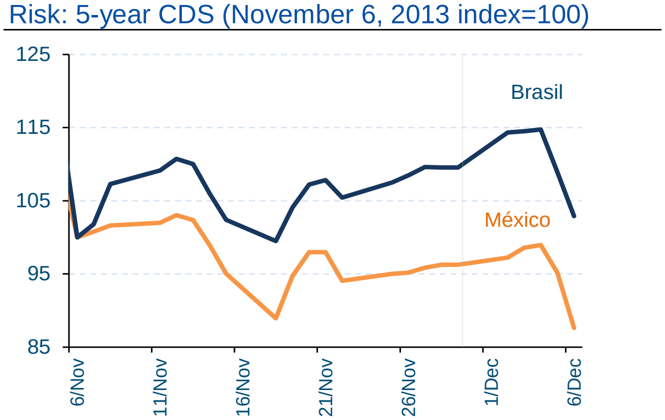
Chart 5
Foreign exchange: dollar exchange rates (November 6, 2013 index=100)



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.

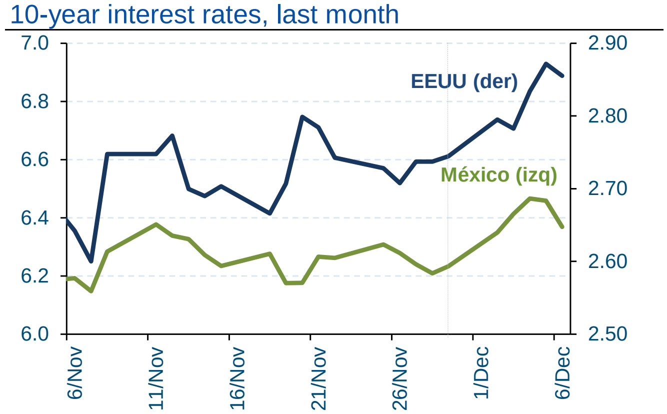
- Fall in global risk in light of better expectations for the US economy. Rates in Mexico declined at the end of the week in line with US rates.

Chart 6
Risk: 5-year CDS (November 6, 2013 index=100)



Source: BBVA Research with data from Bloomberg

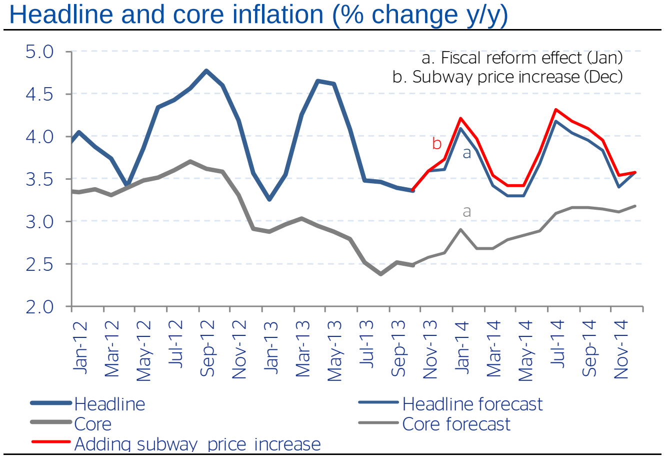
Chart 7
10-year interest rates, last month



Source: BBVA Research with data from Bloomberg

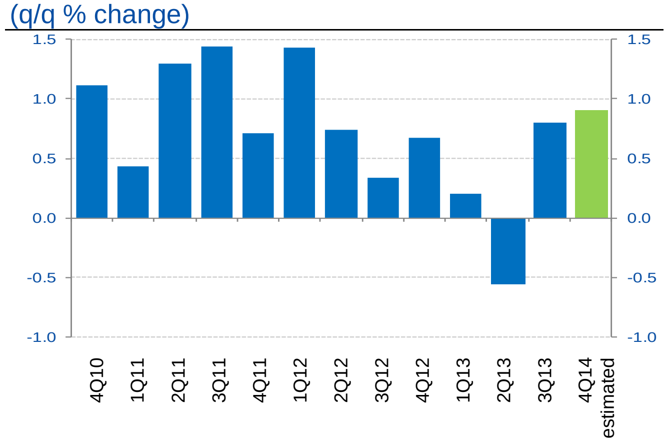
- Inflation will end the year at 3.7% after the announcement of higher metro prices from December 13.

Chart 8
Headline and core inflation (% change y/y)



Source: INEGI, BBVA Research

Chart 9
Observed and estimated GDP 4Q13 (q/q % change)



Source: BBVA Research with INEGI data.

Arnoldo López Marmolejo
arnoldo.lopez@bbva.com

Juan Carlos Rivas Valdivia
Juancarlos.rivas.valdivia@bbva.com

Iván Martínez Urquijo
ivan.martinez.2@bbva.com

Javier Amador
javier.amadord@bbva.com

BBVA | RESEARCH | Av. Universidad 1200, Col. Xoco, Mexico 03339 D.F. | researchmexico@bbva.bancomer.com | www.bbvaresearch.com