Weekly Watch

Mexico

February 3, 2012

Economic Analysis

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Next week...

Important information on the Mexico jobs market. Banxico minutes with no significant new additions.

This week sees the release of labor market data: structural data on activity and employment from the National Occupation and Employment Survey (ENOE) for 4Q11 and the performance in formal private employment (IMSS) in the first month of the year. In the first quarters of last year, the change in employment was in line with the economy. Therefore, we expect this growth to have moderated in the last part of the year. We will also find out the breakdown of the jobs market and the features of the workforce in underemployment and unemployment. It should be stated that to 3Q11, the jobless rate ran to 2.76 million people, 1.8% more than in the same period the previous year. 65.5% of the 46.8 million in employment received income between zero and up to three times the minimum salary - a proportion which saw constant increases in the first three quarters of the year

(continued on next page...)

Market Analysis

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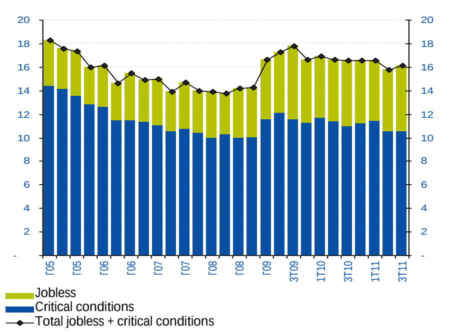
Finally, this Friday Banxico released its minutes of the monetary policy meeting on January 20. Debate continues among Board members on the balance of inflationary risks, although most recognize the recent shock is non-core. With regard to a knock-on effect from the exchange rate on inflation, most recognize it was limited and expect the devaluation to be temporary. Lastly, the debate surrounding the credibility on hitting the 3% target stands out in a scenario of inflation coming in and forecasts for above the target, even though most believe the current monetary stance is appropriate for achieving said target.

Global economic data again drive the appetite for risk

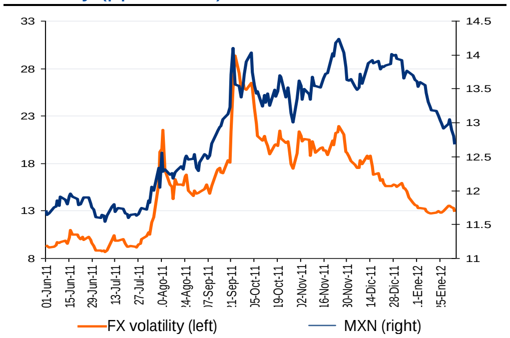
After showing some profit-taking on Monday and Tuesday, the MXN closed the week up around 2%. This move was in line with most emerging currencies. In turn, the Mexican stock market saw a weekly gain which was one of the lowest in the region and just above the US. Attention will be focused on corporate reports these weeks. Growth thus far comes in at 16.6% in sales, 15.5% in EBITDA and net profits substantially better taking into account the net loss at Cemex was lower than expected.

Chart 1
Job market indicators (as a % of EAP)



Source: BBVA Research and INEGI

Chart 2
Mexico: MXN/USD and implied 1-month volatility (ppd and %)



Source: BBVA Research and Bloomberg

Calendar: Indicators

Economic Analysis

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Formal Employment in the private sector (over the week, January)

Forecast: 0.43% m/m 4.16% y/y	Consensus: N.A.	Previous: 0.45% m/m (4.02% y/y)

the same as employees without access to health services (64.4% of those in employment). 8.9% of those in employment, around 4.1 million people, were classified as underemployed in the sense that they stated they needed and were available to work more hours than they currently do. In turn, the employment rate in critical conditions - the percentage of the employed population working under 35 hours a week due to market forces, plus that working over 35 hours but with monthly income below the minimum salary level and that working over 48 hours and earning up to twice the minimum salary - came in at 11% of those in work. It should be stated that this level, as with the unemployment rate (5.2% of the EAP on average in 2011), has not reached the percentages from before the 2009 crisis.

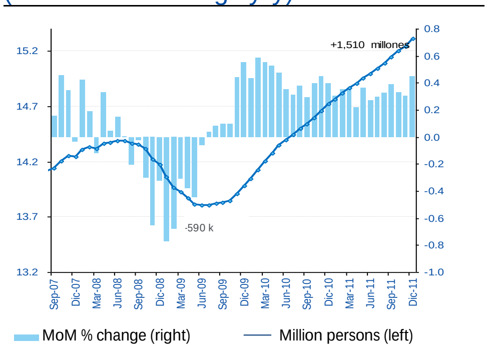
Further, formal private-sector employment progress in the first month of the year will also be released. We expect this indicator, influenced by the recent bounce in US manufacturing output which should have a knock-on effect for Mexico with a slight manufacturing output improvement, to have maintained its growth rate from recent months. In this sense, the number of workers insured in the IMSS should come in at around 15.4 million, around 32% of all those in work.

January inflation (Thursday 9 February, 8am)

Forecast: 0.82% m/m 4.16% y/y	Consensus: 0.65% m/m	Previous: 0.82% m/m (3.82% y/y)

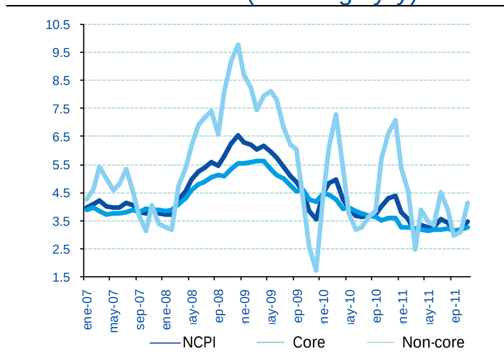
Next week sees the release of inflation figures for January. We estimate inflation will have continued its annual increase, mainly due to non-core pressures where prices for agricultural, livestock and electricity products continued to rise as in recent weeks. Agricultural prices normally rise at this time of the year since we are between harvests and the availability of different products is lower. However, livestock products and electricity are suffering from the prevailing high prices on international grain and oil markets. Core inflation will remain stable in annual terms at around 3.3% thanks to upward pressure on goods prices being compensated by the lack of demand pressure affecting services prices. We estimate core prices to have increased 0.43% m/m.

Chart 3
Formal Private-sector Employment (Level and % change y/y)



Source: BBVA Research with INEGI data

Chart 4
Inflation breakdown (% change y/y)



Source: BBVA Research with INEGI data

Markets

Market Analysis

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Global economic data again drive the appetite for risk...

A week of risk appetite favored by macro data and forecasts for an agreement on Greece. In general, manufacturing output data in all areas (including Europe) followed by US employment figures stood out. Sentiment, however, continues to revolve around Europe where forecasts for an agreement between Greece and its creditors (with the latest information pointing to a coupon cut from 4.0 to 3.6%) seem to be mostly discounted and the way to a second aid package being opened. China's statement of support for SMEs, showing its ability to stimulate the economy and prevent a hard landing, and its possible participation in financing the European crisis (always dependent on Europe getting its house in order) were also an element of support.

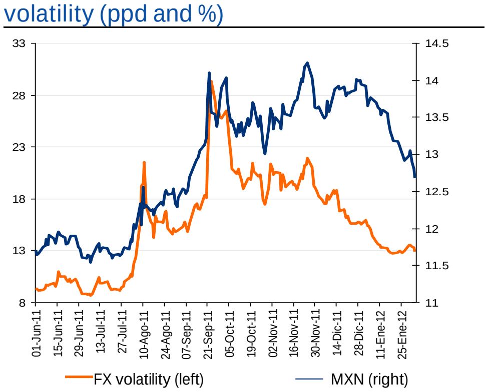
...with the MXN continuing to strengthen...

After showing some profit-taking on Monday and Tuesday, the MXN closed the week up around 2%. This move was in line with most emerging currencies and responded to the series of above-expectation economic data in the US, China and EMU. In turn, Bank of Mexico minutes released on Monday underlined forecasts pointing to a stronger MXN at *fair-value* levels. In this sense, the crossover broke down through the reference support level at 12.74 (200-day rolling average), making space for wider gains as long as there are no negative surprises in EU or European indicators/news. In any event, the market has not yet given signals of risk appetite running out.

...and the Mexican stock market finally awoke from its lethargy at the start of the year

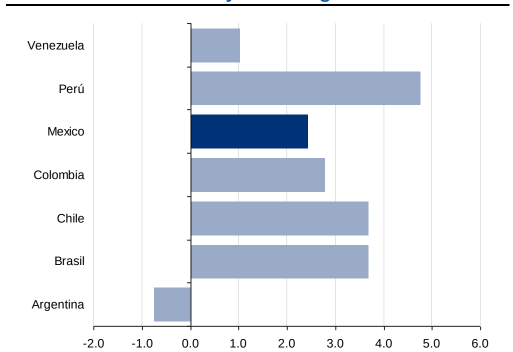
In this scenario of renewed risk appetite and after a strong close to 2011, the Mexican stock market finally came out of its lethargy although the weekly gain was one of the lowest in the region and just above the US. Five corporations under our cover in Mexico have reported, with a surprise upswing at Cemex. Growth thus far comes in at 16.6% in sales, 15.5% in EBITDA and net profits substantially better taking into account the net loss at Cemex being substantially lower than expected. Gmexico and Amx reports will be reporting this week.

Chart 5
Mexico: MXN/USD and implied 1-month volatility (ppd and %)



Source: BBVA Research and Bloomberg

Chart 6
Stock Markets: weekly % change



Source: BBVA Research and Bloomberg

Market Analysis
Equities

Technical Analysis
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Technical Analysis

IPC Stock Market Index

The IPC had a positive week and managed to close above 38,000pts for the first time in just over 12 months. This close sets the next short-term target at 38,700pts, matching the market's historical high. Several heavyweight issuers on the IPC (Amx, Tlevisa, Femsa) still have short-term upward leeway which could support a move toward this historical high.

Previous Rec.: A downward break through the 30-day rolling average could lead to a return toward 36,500pts (previous minimum) and then toward the 200-day rolling average, around 35,600pts. The main resistance sits at 38,000pts.

Source: BBVA, Bancomer, Bloomberg

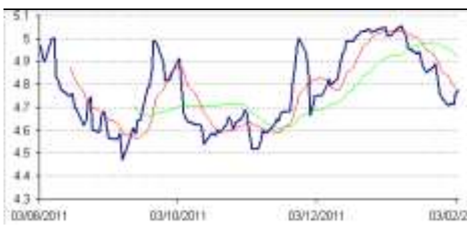
MXN

The dollar maintains the major negative trend and ends the week below the 200-day rolling average. This break sets the next target in the MXN12.55 zone. Over-sell readings remain very high.

Previous Rec.: Any close above MXN13.00 would point to a return to MXN13.40.

Source: BBVA, Bancomer, Bloomberg

3Y M BOND

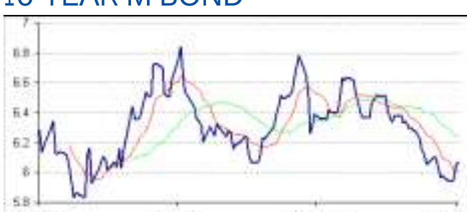


3-YEAR M BOND: (yield): Bounce over the week hitting an initial resistance at the 10-day rolling average (4.75%). Breaking through this level could drive the upswing toward (4.9%).

Previous Rec.: If the 4.7% range is not held, the next floor sits at 4.5%.

Source: BBVA, Bancomer, Bloomberg

10 YEAR M BOND



10-YEAR M BOND: (yield): Testing the 5.9% floor and bouncing to close the week above the 10-day rolling average. This break points to a move toward 6.3%.

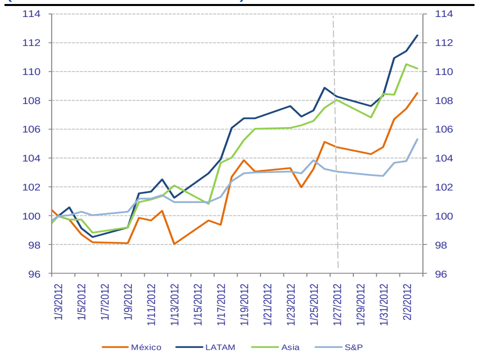
Previous Rec.: With this break, the next floor sits at 5.9%.

Source: BBVA Bancomer, Bloomberg

Markets

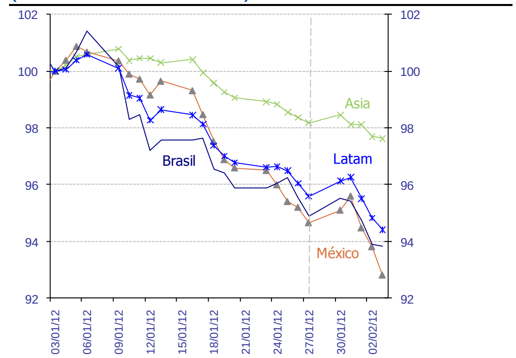
Upswing on stock markets and major strengthening against the dollar influenced by better-than-expected US manufacturing output and employment data.

Chart 7
Stock Markets: MSCI Indices
(Jan 3, 2012 index=100)



Source: Bloomberg & BBVA Research

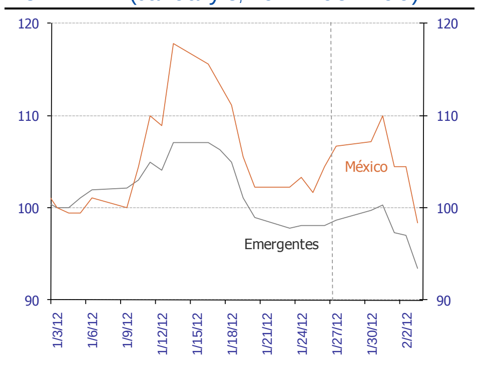
Chart 8
Foreign exchange: dollar exchange rates
(Jan 3, 2012 index=100)



Source: Bloomberg and BBVA Research Note: LATAM includes Argentina, Brazil, Chile, Colombia and Peru. Asia includes the Philippines, South Korea, Taiwan, Singapore, Indonesia and Thailand.
Non-weighted averages

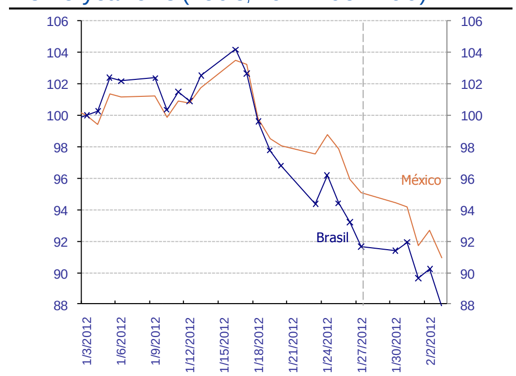
Fall in risk aversion after the release of US jobs figures which may point to a quicker-than-expected recovery

Chart 9
Risk: EMBI+ (January 3, 2012 index=100)



Source: Bloomberg & BBVA Research

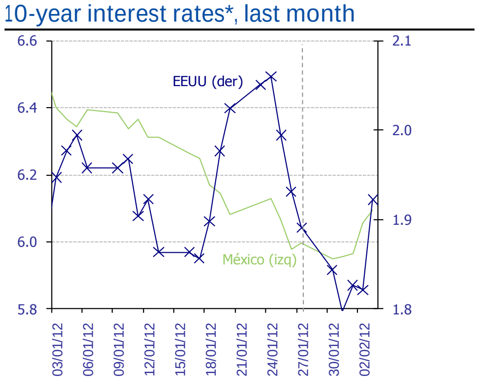
Chart 10
Risk: 5-year CDS (Feb 3, 2012 index=100)



Source: Bloomberg & BBVA Research

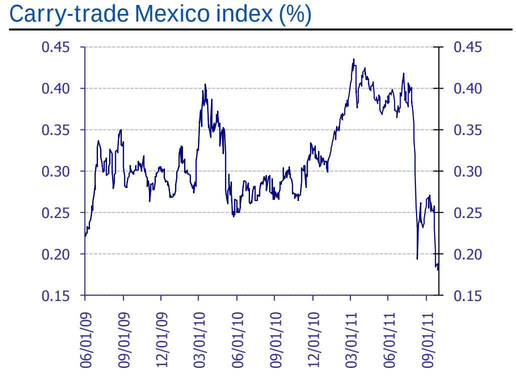
Rise in Mexican and US interest rates due to greater appetite for risk

Chart 11
10-year interest rates*, last month



Source: Bloomberg & BBVA Research

Chart 12
Carry-trade Mexico index (%)

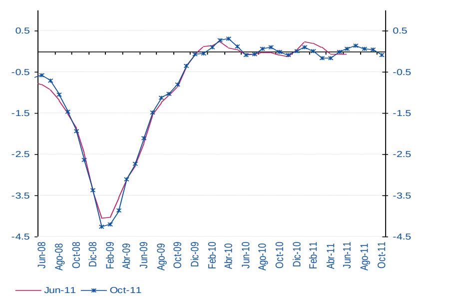


Source: BBVA Research with data from Bloomberg

Activity, inflation, monetary conditions

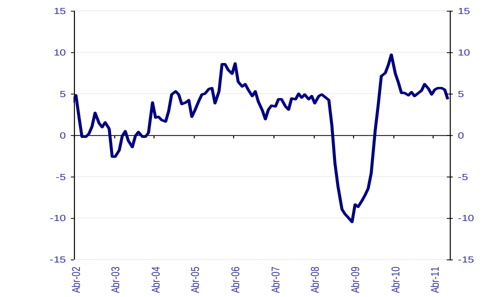
Output holds positive performance, situation indicators point to 3Q11 with quarterly rates around 1%

Chart 13
BBVA Research Synthetic Activity Indicator for the Mexican economy



Source: BBVA Research with data from INEGI, AMIA and BEA
Weighted sum of 21 different indicators of activity, expenditure and expectation, based on trend series.

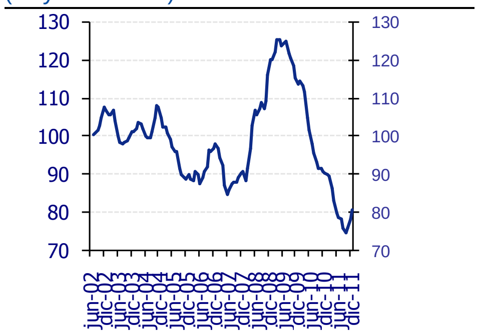
Chart 14
Advance Indicator of Activity (% change y/y)



Source: INEGI

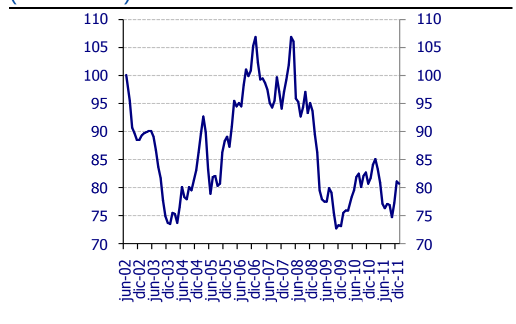
Recent inflationary surprises have been downward, while those concerning economic activity have been mixed.

Chart 15
Inflation Surprise Index (July 2002=100)



Source: BBVA Research with data from Banxico from the monthly surveys on the expectations of economic specialists in the private sector.

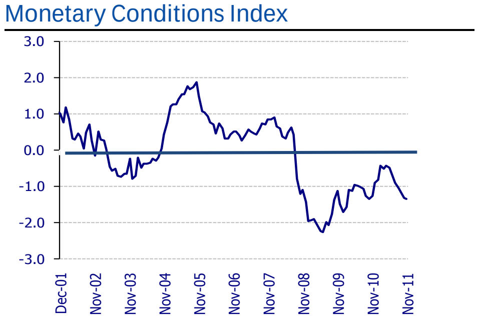
Chart 16
Activity Surprise Index (2002=100)



Source: BBVA Research with Bloomberg data. Difference between recorded data and the Bloomberg consensus for seven activity variables in Mexico. Standardized index. Rises (falls): positive (negative) surprises.

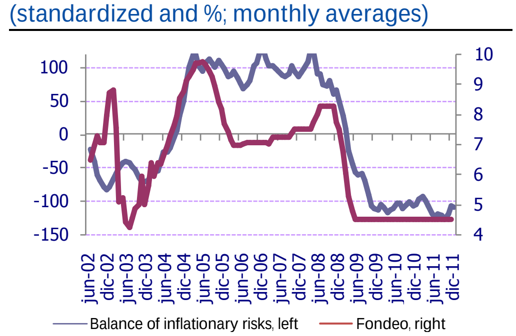
Monetary Conditions relax due to exchange rate depreciation.

Chart 17
Monetary Conditions Index



Source: BBVA Research

Chart 18
Balance of Inflationary Risks* and Lending Rate (standardized and %; monthly averages)



Source: BBVA Research. *Standardized, weighted index (between inflation and economic growth); uses economic indicators for activity and inflation. A rise in the index points to a greater weight of inflationary risks over growth risks and thus a greater likelihood of monetary restriction

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