Weekly Flash

Mexico

February 10, 2012

Economic Analysis

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Market Analysis

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Next week...

4Q11 GDP, forecast slowdown

This week sees the release of economic output performance for the end of last year with 4Q11 GDP and industrial output for December.

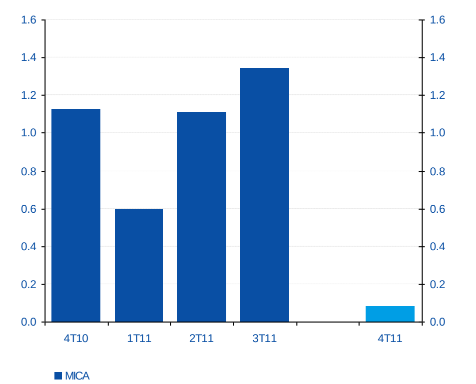
Several indicators, from production to retail sales, employment and confidence, coincide in showing a slowdown for economic growth in the last quarter of 2011 in comparison to the previous. For example, the IGAE (Global Economic Activity Indicator) contracted by (-)0.2% on average per month in the last quarter (to November). Meanwhile average monthly growth in the previous quarter had come in at 0.5%.. The main slowdown came in the manufacturing sector, (-)0.1% in the last part of the year vs. 0.3% in 3Q11. In turn, services continued to see growth, albeit slightly lower than in the July-September period (0.2% vs. 0.5%).

After quarterly GDP growth of 1.3% in the second and third quarters of the year, the fourth could come in much lower at around 0.1%.

Markets move with news from Europe

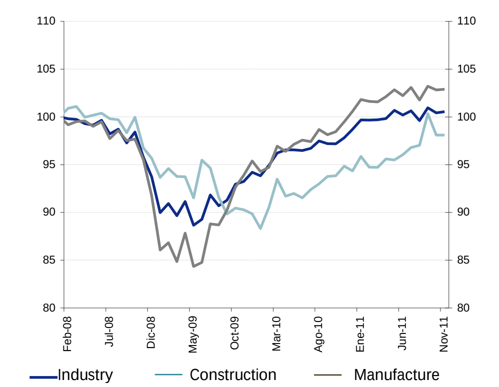
Last week saw profit-taking in risk assets such as stocks and the MXN given negative news from Greece regarding the sovereign debt bailout talks. Greece looks set to continue to dominate market performance over the coming week, as will volatility in Mexican assets after the rally over previous weeks.

Chart 1
GDP Mexico (q/q % change, MICA BBVA Research estimate)



Source: BBVA Research and INEGI. MICA model includes activity, expenditure, expectations and the financial sector variables and is estimated weekly.

Chart 2
Industries: Construction and Manufacturing (Jan 2008 = 100)



Source: BBVA Research with INEGI data

Calendar: Indicators

Economic Analysis

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Industrial Output (Monday, February 13, December)

Forecast: 0.02% m/m 1.9% y/y | Consensus: N.A. | Previous: 0.11% m/m (2.8% y/y)

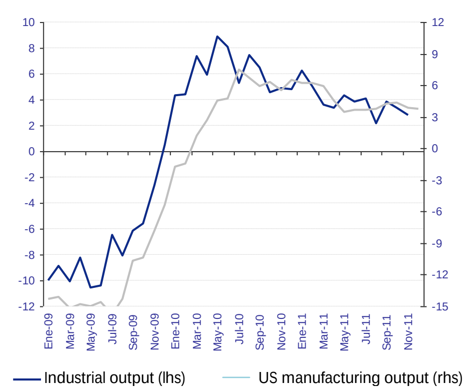
GDP (Thursday 16 February, 4Q11)

Forecast: 0.1% q/q 3.3% y/y | Consensus: N.A. | Previous: 1.3% q/q (4.4% y/y)

We estimate industrial output for December continued up albeit at a slower rate. This has been the case in trend terms in recent months and due to US manufacturing performance. It should be stated however that the slowdown was lower-than-expected than a quarter ago when indicators pointed to a decline in manufacturing at the end of the year.

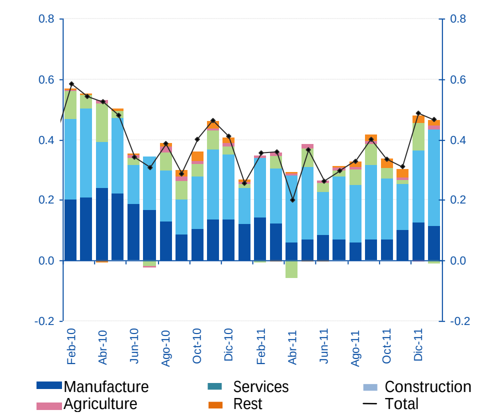
Finally, data were less gloomy than expected a few months ago thanks to the good performance in formal private employment both in manufacturing and more recently in services. In this sense, with information to January the employment creation rate remained stable at around 0.4% per month in the November-January quarter with a better performance in manufacturing and services jobs (0.3 in the August-October period, 0.4% November-January, 0.3% vs. 0.4% in the tertiary sector). This is in contrast with much slower performance in employment in construction and agriculture.

Chart 3
Industrial Output and Manufacturing Output in the US (y/y % change)



Source: BBVA Research with INEGI data

Chart 4
Formal private-sector employment (components in growth % m/m)



Source: BBVA Research with INEGI data

Markets

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Risk appetite slows at the end of the week with doubts surrounding Greece...

After risk appetite continuing over most of the week, on Friday markets were much more cautious due to statements from Greek government representatives who stated they would not support the higher budget cuts demanded by the Troika. Meanwhile, Spain continues with its reform agenda, this Friday passing regulatory changes to the job market to provide companies with more flexibility for the internal organization of their job resources and setting salaries, and reducing the cost of dismissals - all in an attempt to favor job creation.

The market will be looking at how proposals go in the Greek parliament over the weekend.

The MXN closes the week with more than a 1% decline after the major rally over previous weeks. The long net position on the CME increases

The MXN ended Friday's session with a near 1.3% fall in response to global risk aversion due to the lack of agreement in the EMU on the Greek bailout and Lucas Papademos' threat to resign. The move in the MXN came after a week of erratic performance in most assets - a sign of caution.

There will be a series of meetings in Europe in coming days which could continue the drive for profit-taking. In our opinion, this should not represent a trend change (at least with negative surprises involving a lack of agreement meaning Greece defaults on its debt) but a chance to take new long positions in the MXN.

In turn, in line with the CFTC weekly report, the non-commercial net long position in the MXN increased by nearly USD 520mn. With this, it hit USD 1.3bn on Tuesday 7 February. The space for positions to continue increasing is wide (the maximum last year hit USD 5.8bn). However, this will depend on both the cyclical and sovereign series of risks.

Mexico compared negatively to developed markets but better than LatAm.

Stock market performance was somewhat based on corporate earnings (6 companies) where sales increased by 17.2%, EBITDA 9.9% and profits fell 5.4%. As in previous quarters, sales continued to show upward surprises, +5.8%. Meanwhile, EBITDA and net profits went in the same direction but at a much smaller scale in the face of commodity price pressures and, in some instances, the lower exchange rate.

Market Analysis
Equities

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Technical Analysis

IPC Stock Market Index

Source: BBVA, Bancomer, Bloomberg

The IPC maintains a forecast move toward 38,700pts which we mentioned last week. In a lateral week, it managed to stay above the 38,000pts level and, therefore, has not generated an exit signal. It is important to watch for any negative contagion which could lead to a downward break on the US market where over-buying readings are high. In this scenario, the relevant support comes in at the 30-day rolling average above 37,300pts.

Previous Rec.: Several heavyweight issuers on the IPC (Amx, Tlevisa, Femsa) still have short-term upward leeway which could support a move toward this historical high.

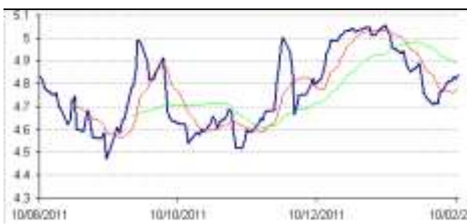
MXN

Source: BBVA, Bancomer, Bloomberg

The dollar maintains a lateral tone over the week with a slight bounce at the end. Oscillating indicators start to bounce up from the over-sell zone and the closes the week above the 10- and 200-day rolling averages. The close above MXN12.80 signals a move toward the resistances of MXN13.00 or even MXN13.28 where the 30-day rolling average sits.

Previous Rec.: Over-sell readings remain very high.

3Y M BOND

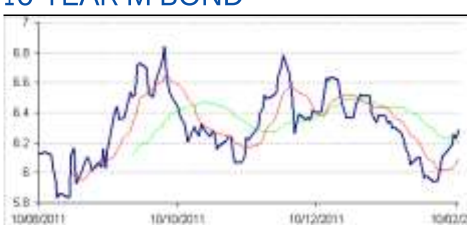


Source: BBVA, Bancomer, Bloomberg

3-YEAR M BOND: (yield): The upswing remains and sits above the 10-day rolling average. It could hit resistance at 4.9% although the position on oscillating indicators points to a move toward 5% where the 200-day rolling average sits.

Previous Rec.: Breaking through this level could drive the upswing toward (4.9%).

10 YEAR M BOND



Source: BBVA Bancomer, Bloomberg

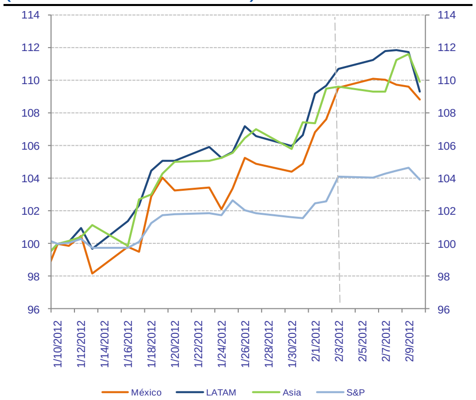
10-YEAR M BOND: (yield): The upswing remains and sits above the 30-day rolling average. We believe it could continue this trend toward 6.5% at the 200-day rolling average.

Previous Rec.: This break points to a move toward 6.3%.

Markets

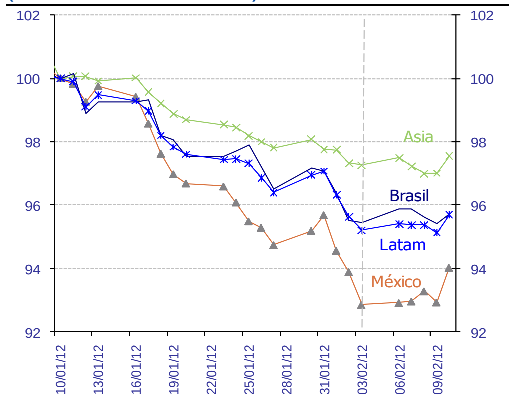
Falls on stock markets and a lower peso after EU finance ministers made the second bailout package for Greece conditional on additional spending cuts and making the austerity measures law.

Chart 7
Stock Markets: MSCI Indices (Jan 10, 2012 index=100)



Source: Bloomberg & BBVA Research

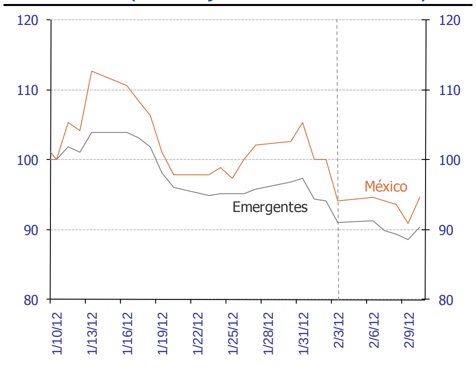
Chart 8
Foreign exchange: dollar exchange rates (Jan 10, 2012 index=100)



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

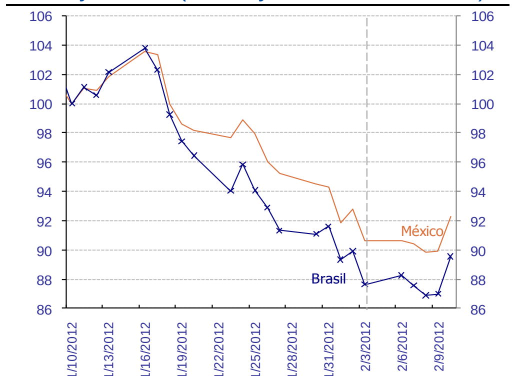
Upswing in risk aversion with the increased fears of a possible Greek default this coming March

Chart 9
Risk: EMBI+ (January 10, 2012 index=100)



Source: Bloomberg & BBVA Research

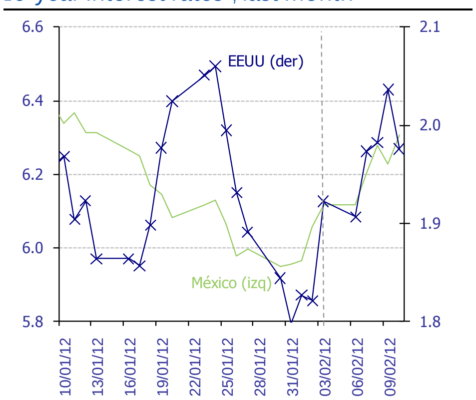
Chart 10
Risk: 5-year CDS (January 10, 2012 index =100)



Source: Bloomberg & BBVA Research

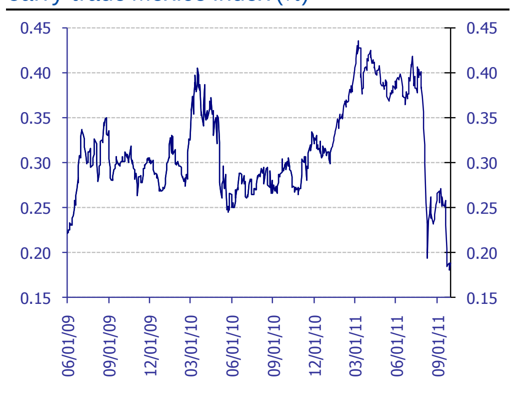
Higher Mexican interest rates and a fall in US rates at the end of the week due to the lower demand for risk assets

Chart 11
10-year interest rates*, last month



Source: Bloomberg & BBVA Research

Chart 12
Carry-trade Mexico index (%)

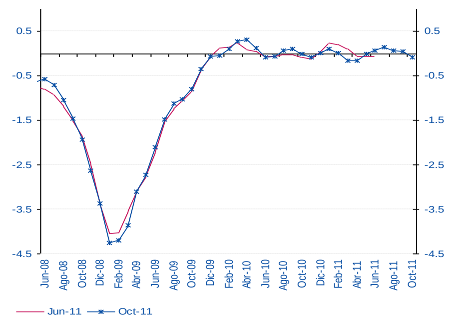


Source: BBVA Research with data from Bloomberg

Activity, inflation, monetary conditions

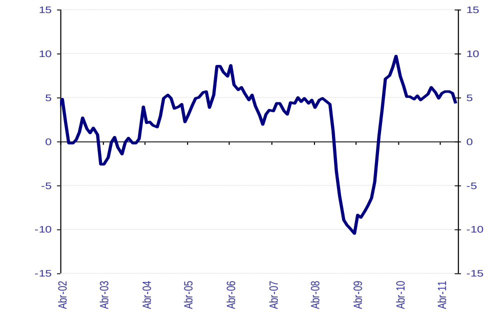
Output holds positive performance, situation indicators point to 3Q11 with quarterly rates around 1%

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.

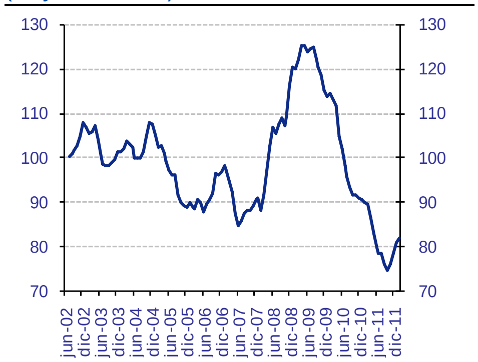
Chart 14
Advance Indicator of Activity (% change y/y)



Source: INEGI

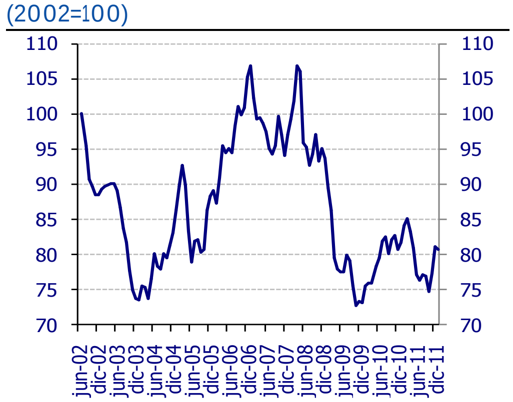
Both the recent inflation and output surprises continue to rise

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.

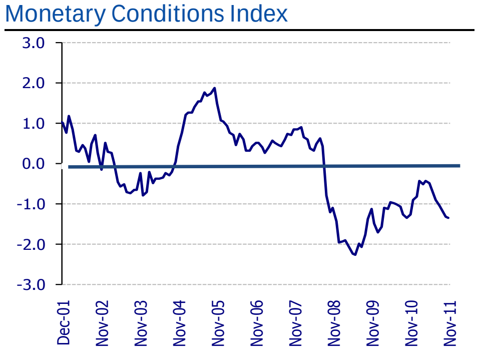
Chart 16
Activity Surprise Index (2002=100)



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.

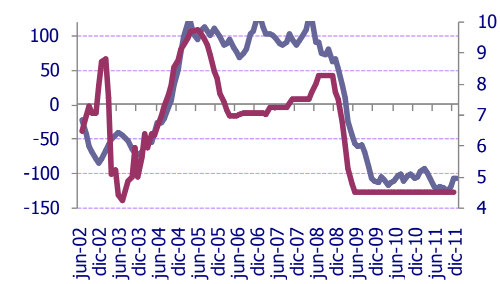
Monetary Conditions relax due to exchange rate depreciation.

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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