

# Mexico Weekly Flash

## Next week...

- **More information on the performance for economic output in the third quarter.**

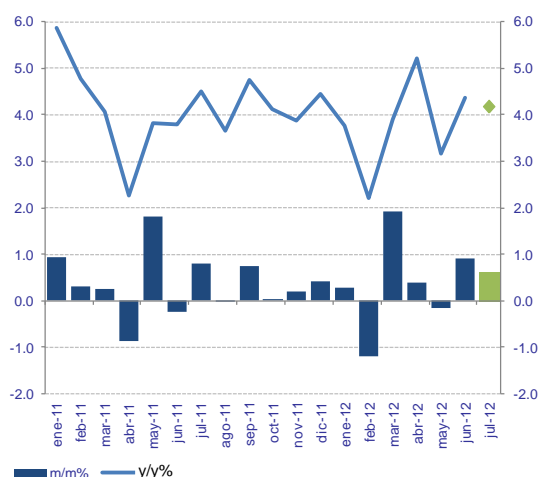
This week sees the release of the IGAE indicator performance in July. With the figures for industrial output in the same month being known, we are missing the performance in services and agriculture. It should be stated that manufacturing expanded in July by 0.5% m/m meaning the annual growth rate came in at 4.5%. The two main components, manufacturing and construction, saw good progress over the previous month (0.5% and 0.8%, respectively). In turn, output indicators linked with the tertiary sector such as the performance at retail establishments and the services indicator showed contrasting performances in July, with the services indicator seeing 2.8% growth while retail sales contracted (-)1.4% (0.8% and 1.8% m/m respectively in June). We believe the IGAE in July will have seen 0.6% monthly growth, 4.2% y/y seasonally-adjusted. Nonetheless, it should be stated that some released indicators for August point to a slight slowdown for the period, such as the confidence indicators (produced, consumer and automotive production), all three seeing a slight contraction over the previous month. In short, released indicators for the third quarter point to output continuing at a good rate, with slightly slower progress than in the second quarter.

- **Stable performance for interest rates**

Interest rates saw stable performance with a downward trend where the flattening of the Mbond and TIEE curves dominated. Investors are starting to take in a new prolonged scenario of low rates but given the current situation of extremely low curves, the taking of positions is slow. Foreign investment flows continue to dominate the curve in Mexico.

Chart 3

**IGAE (% change, y/y and m/m)**



Source: BBVA Research with INEGI data

# Calendar: Indicators

## IGAE in July (September 25)

Forecast: 0.6% m/m (4.2% y/y)

Consensus: N.A.

Previous:

0.9% m/m (4.4% y/y)

## Inflation for 1st two weeks in September (September 24)

Forecast: 0.22% bi-weekly (4.7% y/y)

Consensus: 0.32% bi-weekly

Previous:

0.3% m/m 4.57% y/y

Next Monday see the release of inflation figures for the first two weeks of September. We expect inflation to continue to rise at an annual rate and to come in around 4.7%. This increase in inflation is due to livestock products, energy and processed food prices continuing up thanks to the high global grain and oil prices and the bird flu outbreak in the west of the country, although this last shock will exercise much lower pressure than in the previous two months. In turn, core inflation will remain stable at around 3.7%, although the effects on the food component will continue. We believe the prices of other goods will start to curb the increase seen since December while services will continue to see low inflation in line with the slow but continual economic recovery. We estimate inflation in September will hit its yearly high and, in the absence of new supply shocks, will slow down markedly in the last quarter of the year to some in very near 4%.

## August Trade Balance (September 26)

Forecast: -986 md

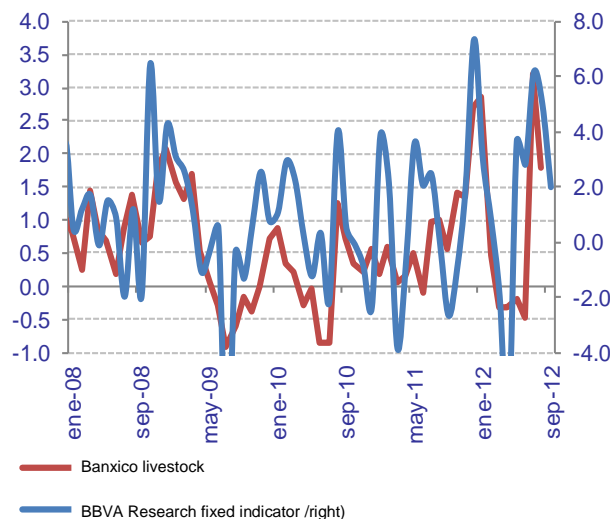
Consensus: -893.5

Previous: -427 md

Next week sees the release of the trade balance in August which we believe will be in deficit of around 900 md. We see the trade balance continuing to be negative in the remaining months of the year due to Mexican companies importing larger amounts of commodities to produce manufactured goods which, in turn, will be exported in coming months and to domestic demand for imported consumer goods increasing thanks to the continued economic recovery; linked to no surprise expected increases in economic output by our main trading partners, this will mean the trade balance returns to negative territory. Nevertheless, it is important to state that for the third year in a row, this deficit will be limited and easily financed at the end of the year.

Chart 3

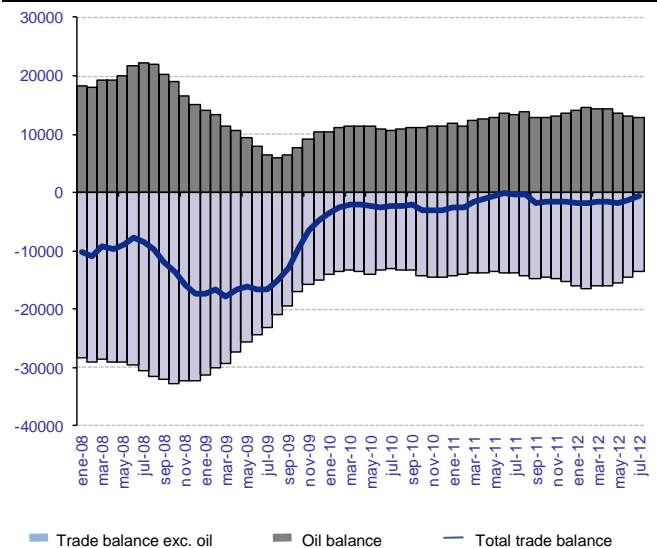
### CPI livestock prices and BBVA Research Livestock Monitoring (% change m/m)



Source: BBVA Research with INEGI data

Chart 4

### Trade balance by components (12-month rolling total, millions of dollars)



Source: BBVA Research with INEGI data

- **MXN trading in a narrow range and reducing appreciation room**

After the over 4% appreciation seen in the days approaching the Fed meeting, the MXN corrected part of the gains over last week by falling around 1.2%. The run of negative surprises in global output indicators led markets to renewed concerns over the global economic cycle, as well as the EMU issuing no more news that had resulted in a fall in risk premiums. In short, the currency traded in a limited range which we believe will continue to be the case in the short-term. On the one hand, the cyclical risk added to technical factors and positioning reduces the room for short-term strengthening. On the other, the injection of Fed funds should provide major resistance around the 13.0 zone. Economic data are set to be the main focal point this week.

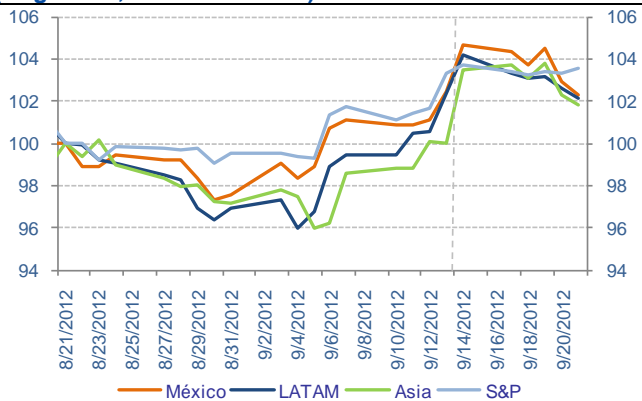
In the same vein, interest rates saw stable performance with a downward trend where the flattening of the Mbond and TIEE curves dominated. Investors are starting to take in a new prolonged scenario of low rates but given the current situation of extremely low curves, the taking of positions is slow. Foreign investment flows continue to dominate the curve in Mexico. To date in September, we estimate an inflow of around USD3.0bn.

# Markets

- Concerns over whether the new ECB program is enough to alleviate the debt crisis in Europe reduced the strengthening effects and gains on currency exchanges and stock markets respectively, generated by the central banks' statements last week.

Chart 7

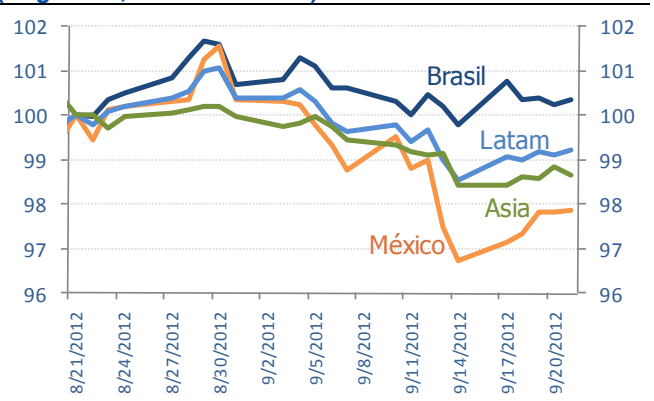
**Stock Markets: MSCI Indices**  
(August 21, 2012 index=100)



Source: Bloomberg & BBVA Research

Chart 8

**Foreign exchange: dollar exchange rates**  
(August 21, 2012 index=100)

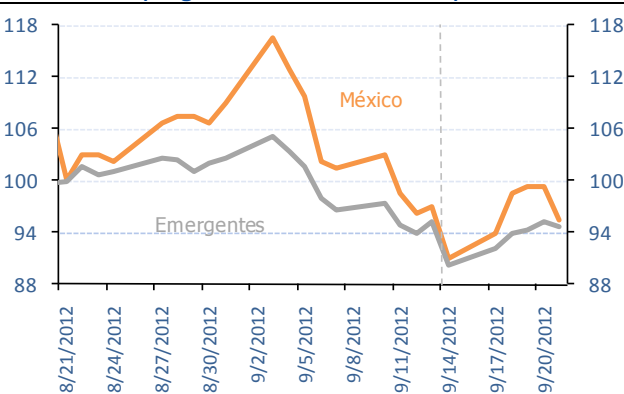


Source: Bloomberg and BBVA Research Note: LATAM includes Argentina, Brazil, Chile, Colombia and Peru. Asia includes the Philippines, South Korea, Taiwan, Singapore, Indonesia and Thailand. Non-weighted averages

- Slight upswing in risk aversion due to doubts surrounding the crisis in Europe.

Chart 9

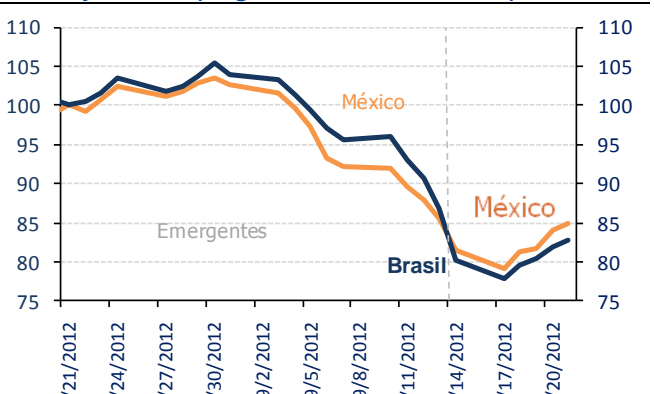
**Risk: EMBI+ (August 21, 2012 index=100)**



Source: Bloomberg & BBVA Research

Chart 10

**Risk: 5 year CDS (August 21, 2012 index=100)**

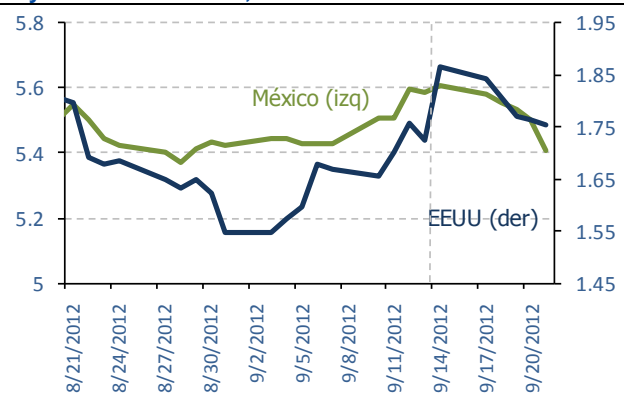


Source: Bloomberg & BBVA Research

- Fall in rates in the US due to slight increase in risk aversion. Rates in Mexico moved in line.

Chart 11

**10-year interest rates\*, last month**



Source: Bloomberg & BBVA Research

Chart 12

**Carry-trade Mexico index (%)**



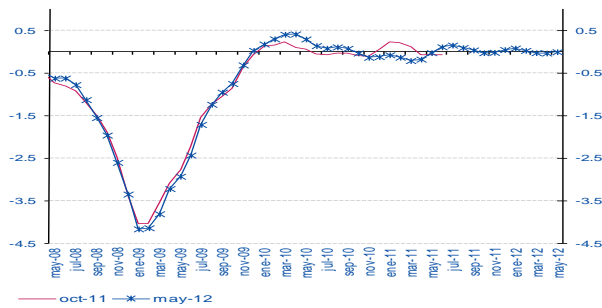
Source: BBVA Research with data from Bloomberg

# Activity, inflation, monetary conditions

- Output holds positive albeit moderate performance, situation indicators point to 3Q12 with quarterly rates above 0.5%.

Chart 13

## BBVA Research Synthetic Activity Indicator for the Mexican economy

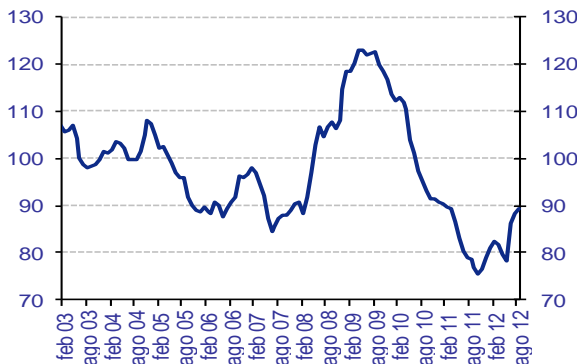


Source: BBVA Research with data from INEGI, AMIA and BEA  
Weighted sum of 21 different indicators of activity, expenditure and expectation, based on trend series.

- Recently we have seen upward surprises in inflation and output.

Chart 15

## Inflation Surprise Index (July 2002=100)

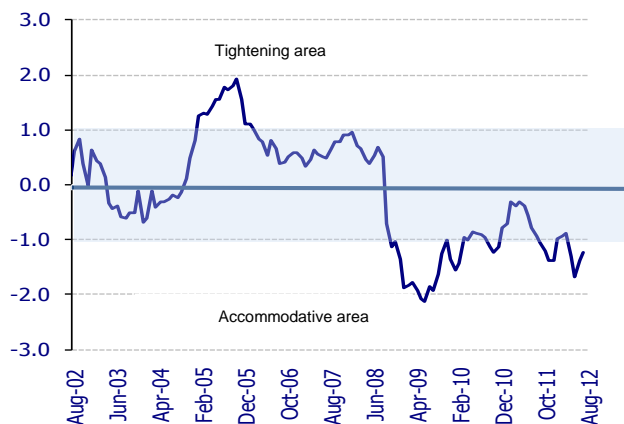


Source: BBVA Research with data from Banxico from the monthly surveys on the expectations of economic specialists in the private sector.

- Monetary conditions slightly reduced their looseness after currency appreciation.

Chart 17

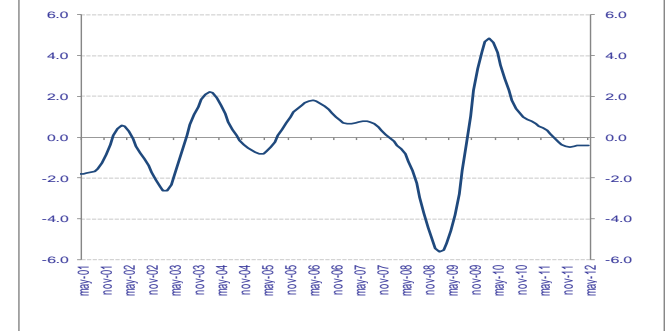
## Monetary Conditions Index



Source: BBVA Research

Chart 14

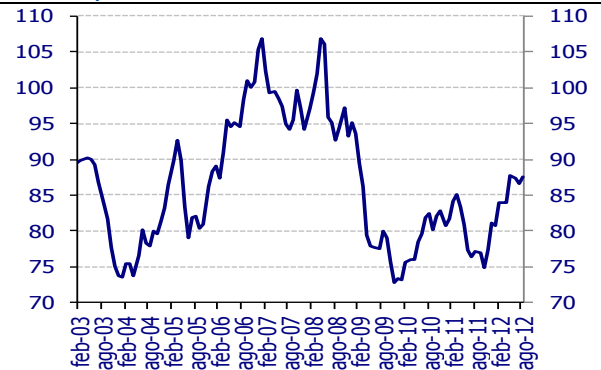
## Advance Indicator of Activity, trend (% change y/y)



Source: INEGI

Chart 16

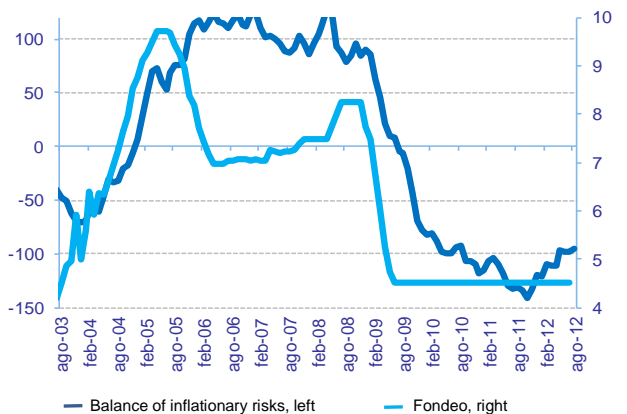
## Activity Surprise Index (2002=100)



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

Chart 18

## Balance of Inflationary Risks\* and Lending Rate (standardized and %; monthly averages)



Source: BBVA Research. \* Standardized and weighted index (of inflation and economic growth) based on economic indicators of economic activity and inflation. A rise in the IBR signals greater weight of inflationary risks over those of growth and, therefore, more likelihood of monetary restriction

Claudia Ceja  
claudia.ceja@bbva.bancomer.com

Pedro Uriz  
pedro.uriz2@bbva.com

Alejandro Fuentes Pérez  
a.fuentes@bbva.bancomer.com

Octavio Gutiérrez Engelmán  
o.gutierrez3@bbva.bancomer.com

Ociel Hernández  
o.hernandez@bbva.bancomer.com

Arnoldo López  
arnoldo.lopez@bbva.com

Iván Martínez  
ivan.martinez.2@bbva.com

Rodrigo Ortega  
r.ortega@bbva.bancomer.com

Cecilia Posadas  
c.posadas@bbva.com



| Av. Universidad 1200, Col. Xoco, Mexico 03339 D.F. | [researchmexico@bbva.bancomer.com](mailto:researchmexico@bbva.bancomer.com) | [www.bbva.com/research](http://www.bbva.com/research)

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