

Mexico Weekly Flash

Next week...

- **Confidence indicators in September set to provide clues on output performance in 3Q12**

Taking into account recent output indicators that point to lower growth rates linked to the cycle overseas, focus will need to be on indicators being timely released on manufacturing and consumer confidence in Mexico. It should be stated that domestic manufacturing exports, US industrial output and the ISM indicators continued to slow down in August, which could be an alert on a lower growth rate in Mexico toward the end of the year.

- **Economic uncertainty and an appetite for safe-haven assets set the pattern for domestic assets**

The MXN depreciated around 0.3% and, with this, lost nearly all the gains made on Thursday. In view of US economic indicators, we believe the MXN showed a certain resistance despite the devaluation. Economic data are set to be the focal point this coming week, starting with the PMI in different countries on Monday. If these continue to show high risks of a slowdown, the USDMXN will undoubtedly continue to fluctuate around 13.00, the upper part of the current range.

Nominal curves end the week with an average 4bp upturn. Nonetheless, an average 14bp rally in the Mbond curve was seen over the week. As we stated, domestic curves continue to be in demand as a favorable scenario for UST purchases is being perceived. In our opinion, beyond news from Europe, demand for curves will continue. The moderation in risk aversion is likely to lead to a correction but domestic curves continue to have support, especially in short maturities (risk hedging, positive carry and bias for economic weakness) and long maturities (constructive outlook for Mexico, monetary pause throughout 2013 and gradual investor appetite in the face of economic weakness and continuous unraveling regarding Europe). Overseas investors accumulated an inflow in September (up to the 27) of USD 5.3bn, a clearly high amount. 78% of this inflow was seen in the short section of the curve, especially in the Mbond 2012.

Calendar: Indicators

Producer Confidence in September (October 3)

Forecast: 0.0% m/m (54.6 points)	Consensus: N.A.	Previous: 2.2% m/m (54.6 points)
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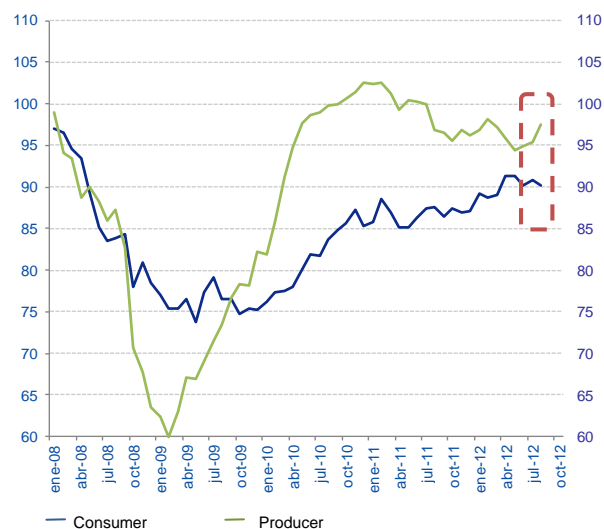
Consumer Confidence in September (October 3)

Forecast: -1.0% m/m (94.5 points)	Consensus: N.A.	Previous: -0.8% m/m (95.4 points)
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The performance of producer and consumer confidence indicators for September will be published this week. It should be recalled that both indicators saw divergent moves in recent months: on the one hand, producer confidence showed optimism among manufacturers regarding the future economic situation in coming months. Specifically, the optimism in indicators on the right moment for investing and the positive opinion regarding the country's current economic situation stand out. With regard to business perception of domestic or foreign demand for products, opinions saw greater variation, with a slight trend to optimism about the future. We believe for September, however, manufacturers' sentiments could start to moderate slightly due to the uncertainty in the overseas cycle, partially reflected in indicators such as manufacturing output in the US where in August industry contracted (-)1.2% m/m, the change in Mexican manufacturing exports (-)4.9% m/m, and business sentiment indicators such as the ISM remaining in the contraction range in the last three months (June-August).

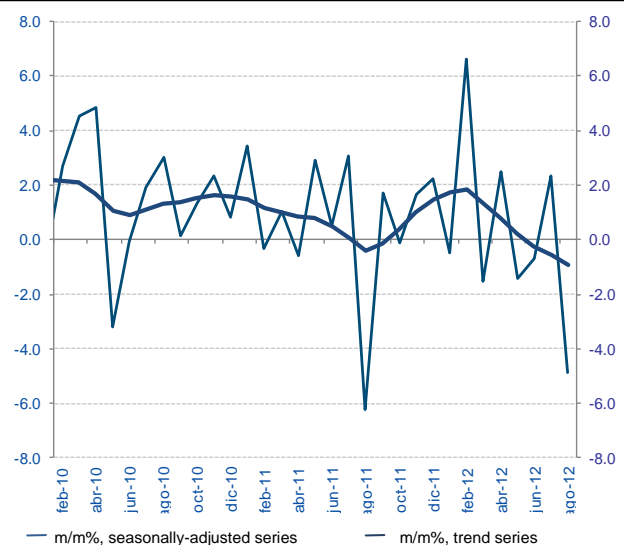
On the other hand, consumer confidence saw scant growth in recent months and we believe this situation is set to continue, even seeing some contraction in the September level in comparison to the previous month. It should be stated that although the employment level continues to expand at a good rate, the contribution of real wages to annual growth in wages was inexistent or slightly negative in recent months. We should also consider that the consumer confidence indicator level remains far below that seen before the 2009 recession.

Chart 3
Producer and Consumer Confidence Indicators (Jul07=100)



Source: BBVA Research with INEGI data

Chart 4
Manufacturing Exports (% change m/m)



Source: BBVA Research with INEGI data

Technical Analysis

IPC



Source: BBVA, Bancomer, Bloomberg

The IPC managed to move up over the week after testing the 30-day rolling average and 3 consecutive upward sessions. It did not manage to go above the 41,000pts barrier in recent week but we believe it could have the necessary momentum this time to break through this level and seek out the 41,500pts zone. With the RSI at 57pts, we are not concerned with a major decline for coming days. Last week we commented on the high over-selling we were seeing in the Amx (an issuer accounting for 25% of the IPC) which we finally started to see bounce over the week. We believe this issuer still has a lot of upward room and should help the market to at least hit a major floor in the 40,000/40,200pts zone.

Previous Rec. (9/24/12): The positive technical signal remains valid while the support is 40,200pts (30-day rolling average).

MXN



Source: BBVA, Bancomer, Bloomberg

Although the dollar tried an upward bounce over the week, it hit resistance at the MXN12.85 level. The dollar remained in the short-term downward channel and only an upward break through MXN13.00 would mark a trend change.

Previous Rec (9/24/12). For the moment, the main short-term trend continues to be negative and only an upward break through MXN13.00 would mark a trend change.

3Y M BOND



Source: BBVA, Bancomer, Bloomberg

3Y M BOND (yield): The bond maintained an adjustment move and hit the support at 4.7%. With the 30-day rolling average already passed and the RSI near 30pts, we believe it could see a bounce toward 4.8%. If it breaks down through 4.7%, the next floor is at 4.55%.

Previous Rec. (9/24/12). With the RSI at mid-channel, this break could indicate a return to the support at 4.7%.

10Y M BOND



Source: BBVA, Bancomer, Bloomberg

10Y M BOND (yield): Downward break through the support at 5.4%. It could maintain the adjustment toward a next floor at 5.2%. The 10-day rolling average crossed down through the 30-day meaning we could expect weakness. Resistencia en 5.45%.

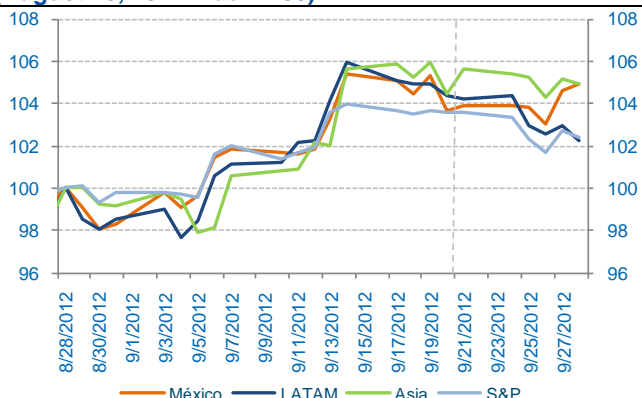
Previous Rec. (9/10/12). Maintaining position while there is no break of the 5.4% floor.

Markets

- Protests against the austerity measures in Spain and Greece led to increased risk aversion. At the end of the week, lower-than-expected economic data on consumer spending, manufacturing output and US consumer confidence led to slight falls on stock markets and in currencies.

Chart 7

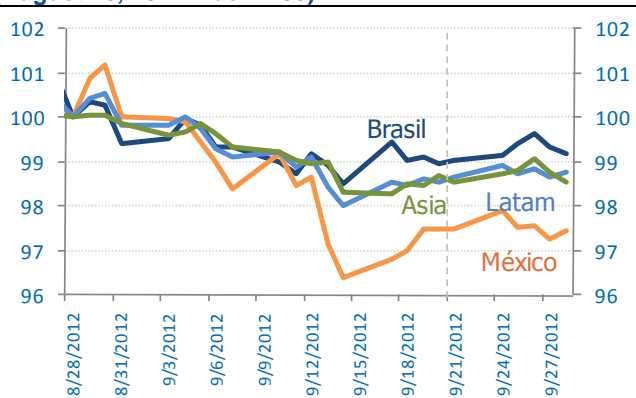
Stock Markets: MSCI Indices
(August 28, 2012 index=100)



Source: Bloomberg & BBVA Research

Chart 8

Foreign exchange: dollar exchange rates
(August 28, 2012 index=100)

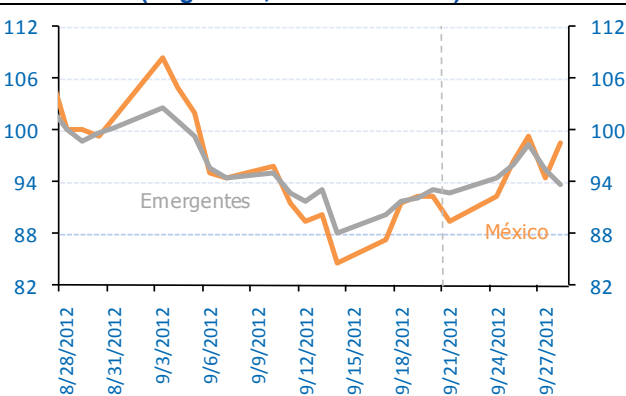


Source: Bloomberg and BBVA Research Note: LATAM includes Argentina, Brazil, Chile, Colombia and Peru. Asia includes the Philippines, South Korea, Taiwan, Singapore, Indonesia and Thailand. Non-weighted averages

- Protests in Spain and Greece again lead days of risk aversion.

Chart 9

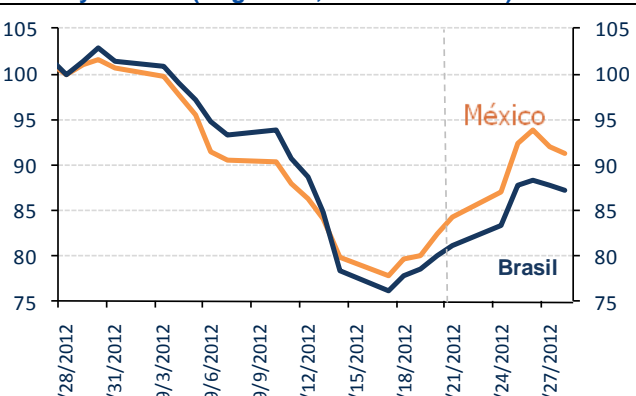
Risk: EMBI+ (August 28, 2012 index=100)



Source: Bloomberg & BBVA Research

Chart 10

Risk: 5 year CDS (August 28, 2012 index=100)

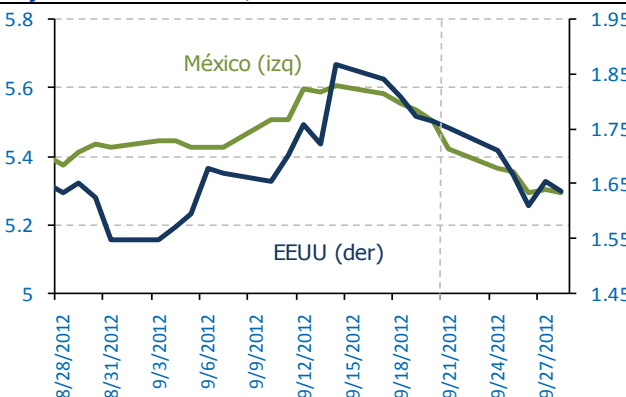


Source: Bloomberg & BBVA Research

- Fall in rates in the US due to some days with higher risk aversion. Rates in Mexico continue in high correlation with US Treasury bond rates.

Chart 11

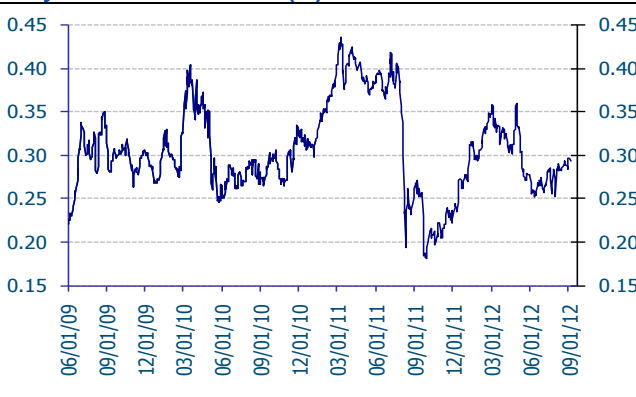
10-year interest rates*, last month



Source: Bloomberg & BBVA Research

Chart 12

Carry-trade Mexico index (%)



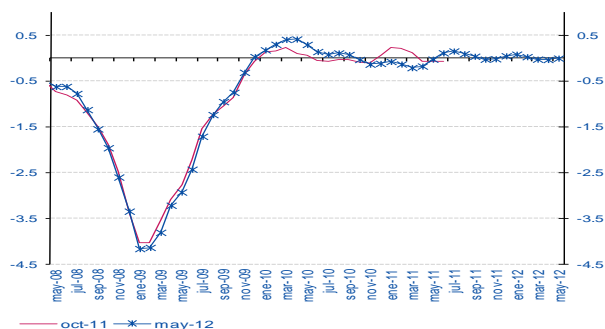
Source: BBVA Research with data from Bloomberg

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)

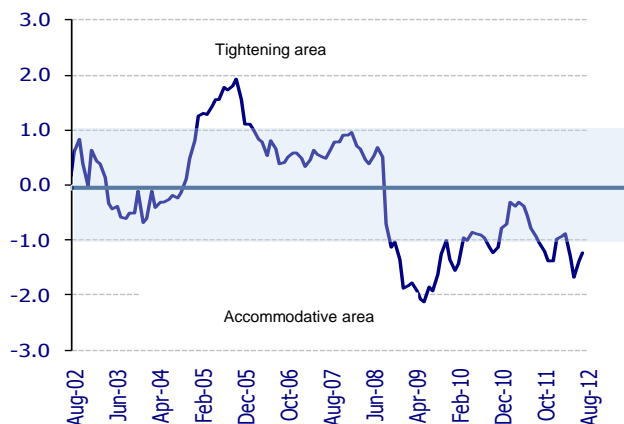


Source: BBVA Research with data from Banxico from the monthly surveys on the expectations of economic specialists in the private sector.

- Monetary conditions slightly reduced their looseness after currency appreciation.

Chart 17

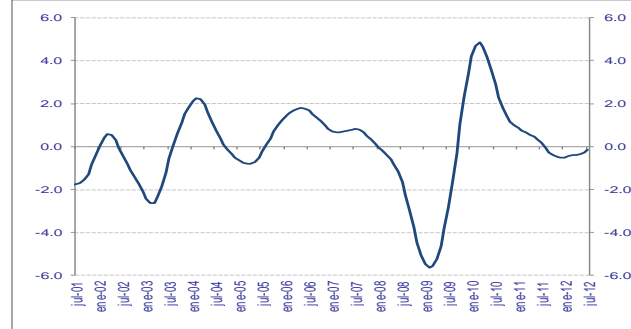
Monetary Conditions Index



Source: BBVA Research

Chart 14

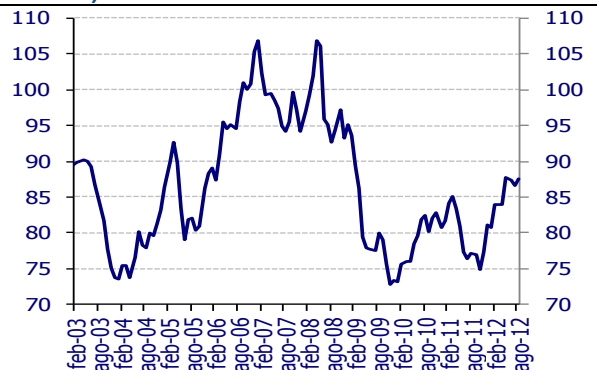
Advance Indicator of Activity, trend (% change y/y)



Source: INEGI

Chart 16

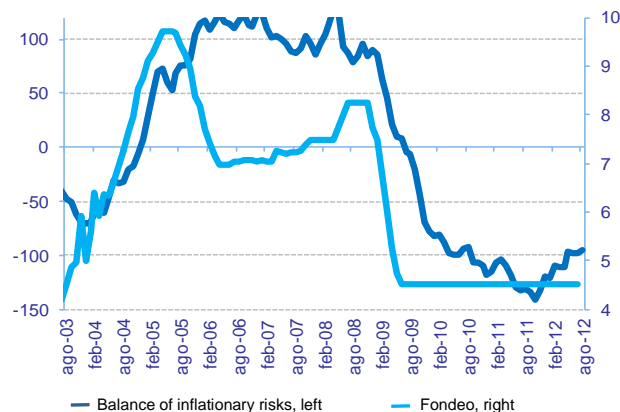
Activity Surprise Index (2002=100)



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

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