Macroeconomic Analysis

We estimate that industrial production in July will post annual growth of 2.2%, seasonally adjusted

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What happened this week …

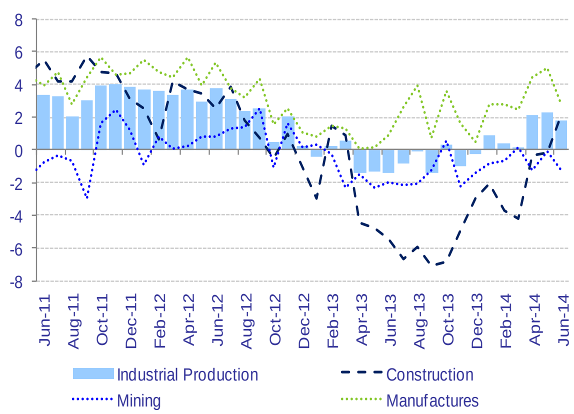
Monetary policy rate unchanged at 3.0%. The statement on increased inflation risks in the short term, in view of the hike in agricultural product prices, was neutral in tone. Banxico's tone was more neutral than previous statements, based on an improved balance of risks in activity and deteriorating prospects of short-term inflation. The central bank revised its headline inflation outlook to the upside. Whereas the last inflation report indicated that inflation would close 2014 below 4.0%, it is now expected to come in at around 4.0%. We now expect inflation to be close to 3.0% in the first half of 2015, and not by January, as indicated in the June statement. The statement's more neutral tone, together with the expectation that the real rate will stay in negative territory for longer than formerly estimated, supports our argument of a monetary pause for the rest of the year.

Producer and consumer confidence indicators showed mixed signals. In August, the Producer Confidence Index (PCI) jumped considerably (1.4% MoM, sa), but the Consumer Confidence Index (CCI) surprised to the downside (-0.3% MoM, sa). In line with our forecast (BBVA Research: 52.1 points, sa), the PCI posted 52.5 points in August, sa. Meanwhile, the CCI reached 87.9 points, sa. The latter was equivalent to a level of 89.7 points with original series, which was below both our estimate and that of the consensus (BBVA Research: 90.8 points, consensus: 91.0 points). All in all, there is a prevailing perception on the part of producers of an improvement in economic activity, but not on the part of consumers.

Remittances to Mexico grew 8.4% in July, marking 12 months in a row of gains. Remittances to Mexico reached USD1.996bn in July, an 8.4% jump in annual terms, in line with BBVA Bancomer expectations (USD1.982bn) and slightly higher than the market consensus (USD1.954bn). All this YoY growth is accounted for by the increase in the number of remittance transactions, which reached 6.78 million operations in July. The average remittance amount showed no significant change. The absolute and relative increase in employment of Mexican migrants in the US and the fall in the percentage of jobs that were only part-time because of employee restraints in the last few months have had a positive impact on the growth of remittances.

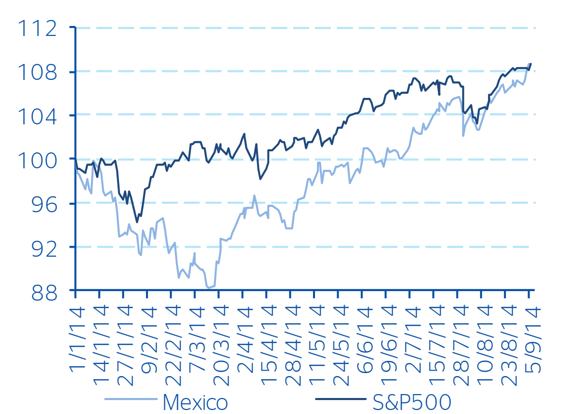
In line with the IMEF, the manufacturing and non-manufacturing performance indicators posted a significant rise in August. The IMEF Manufacturing index rose from 49.1 points in July to 51.6 points in August, returning to expansive territory, with seasonally adjusted figures (sa). The non-manufacturing index for August also rose significantly, coming in at 52.7 points, up from 50.1 points (sa) the previous month. These expectations were higher than BBVA Research estimates (49.8 points for the manufacturing index and 50.5 points for non-manufacturing) and also above the consensus (50.5 points for the manufacturing index and 50.8 points for non-manufacturing), so we may be seeing the first signs of the economic recovery expected for the second half of the year.

Figure 1
Industrial production and its components (% var., YoY, sa)



Source: BBVA Research with data from I INEGI. sa = seasonally adjusted.

Figure 2
Stock markets (1 Jan 2014 index=100)



Source: BBVA Research with data from Bloomberg

Lower-than-expected growth figures in the US non-farm payroll influence the appreciation of the peso and stock market gains. The US non-farm payroll rose by 142k jobs in August, well below the 230k expected by analysts, representing the lowest growth of the year. The unemployment rate decreased to 6.1%, as a result of the fall in the participation rate. In the light of these US labour market figures, the likelihood of an early start to the cycle of federal fund rate hikes was reduced. In this context, the peso appreciated 0.9% on Friday, the second biggest appreciation of all the emerging currencies, which impacted on the overall weekly appreciation of 0.4%. In the sovereign rate market, yields on the 10-year Mbono fell 4bp, closing at 5.74%, while the Treasury bond closed the week without important changes after having fallen 6bp on the intraday. There were record highs on the stock markets, on both the S&P500 and the IPC over the week.

…What is coming up next week

We anticipate that annual inflation will reach 4.1% in August. We expect monthly rises of 0.31% and 0.18%, respectively, for headline and core inflation during August. Should these forecasts prove correct, in YoY terms headline inflation will be 4.10% (compared to 4.07% in July) while core will come in at 3.34% (compared to 3.25% in July). When it comes to core inflation, we anticipate a monthly fall in the services sub-index (BBVAe: -0.07% MoM) resulting from a major increase in the education component (BBVAe: 0.90% MoM) which will be more than offset by an estimated fall of 0.57% MoM in the other services sub-index, mainly accounted for by the end of the summer holidays. For the merchandise sub-index, we estimate an increase of 0.49% MoM. Meanwhile, we anticipate an increase in the four main components in the agricultural sub-index and significant pressures on fruit and vegetable prices over the second half of the month. In terms of our outlook for the year, as we had forecast, inflation has posted higher than the upper limit of Banxico's tolerance threshold since July, and we forecast that it will remain over that level until October, before falling to 3.8% in November and to 3.7% by year-end. This scenario does not anticipate major supply-side shocks in perishable goods prices. Considering that the performance of the fruit and vegetable component has been very favourable so far this year (-13.8% aggregate up to the first half of August), an uptick in these prices in the next few months would pose a risk to the upside on our current forecast. For core inflation, we forecast that it will remain relatively stable at 3.3% for the rest of the year.

On 10 September the INEGI will publish the monthly gross fixed investment indicator figures for June 2014. This indicator deteriorated significantly in 2013, with an average annual negative growth rate of 1.7%. For the first seven months of 2014, the average annual growth rate shows less of a fall, at -1.1%, with the May 2014 figure even posting positively YoY, at 0.4%. Note here that in May the annual growth rates of the Construction and Machinery and Equipment components were -2.2% and 4.5%, respectively. For June we expect the annual growth rate of total gross fixed investment to be 1.8%, with that of its components recording 0.5% in the case of Construction and 4.7% for Machinery and Equipment. The positive YoY growth rate in construction investment that we forecast for June 2014 is to a large extent a mirror of the 2.2% positive growth rate which the global economic activity index (IGAE) of the construction industry posted that same month.

We expect July industrial production to increase 2.2% YoY, seasonally adjusted (sa). This estimate takes into account the close relationship that this variable has with the performance of the US Industrial Production monthly indicator in July (0.4% MoM, sa). In June this indicator grew 1.8% YoY in Mexico, sa (see Figure 1), but in monthly terms it fell 0.2%, linked to a fall in manufacturing (-0.7% MoM, sa). In original series we expect industrial production to increase by 2.5% YoY.

Calendar of indicators

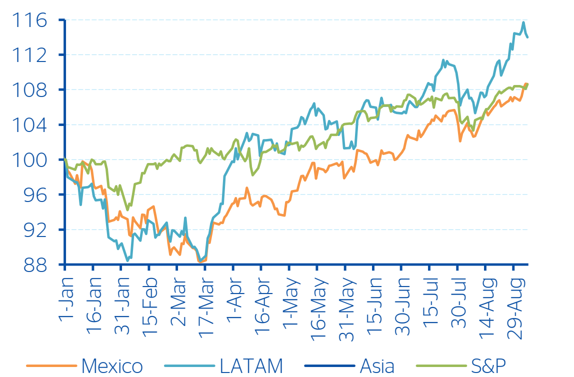
Mexico	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Headline inflation (MoM % change)	August	9 Sept	0.31	0.30	0.28
Headline inflation (YoY % change)	August	9 Sept	4.10	4.09	4.07
Core inflation (MoM % change)	August	9 Sept	0.18	0.20	0.19
Core inflation (YoY % change)	August	9 Sept	3.34	3.36	3.25
Fixed gross investment (YoY % change)	June	10 Sept	1.8	2.7	0.4
Industrial production (YoY % change, sa)	July	11 Sept	2.2	--	1.8

USA	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Net total consumer credit, Federal Reserve (USD billion)	July	8 Sept	18.10	17.00	17.26
NFIB Small business optimism index (index)	August	9 Sept	95.5	96.0	95.7
Adjusted retail and food sales (MoM % change, sa)	August	12 Sept	0.30	0.55	0.00
Consumer confidence index, University of Michigan (index, sa)	September[p]	12 Sept	82.90	83.50	82.50

Source: BBVA Research with data from Bloomberg. YoY = annual rate of variation. sa = seasonally adjusted. MoM = monthly rate of variation MoM. [P] = provisional.

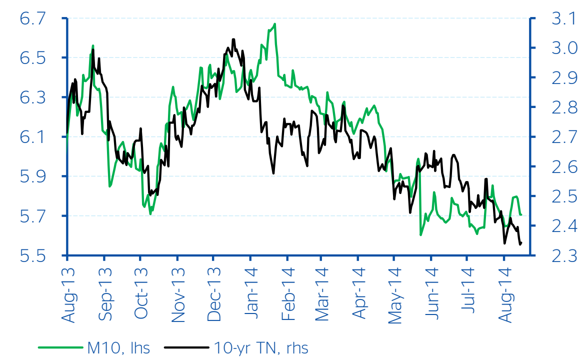
Markets

Figure 3
MSCI stock market indices (Index 1 Jan 2014=100)



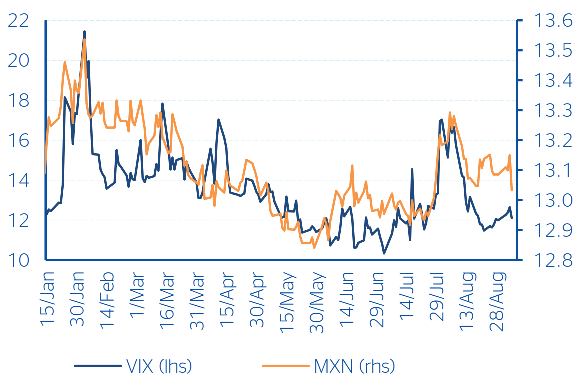
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



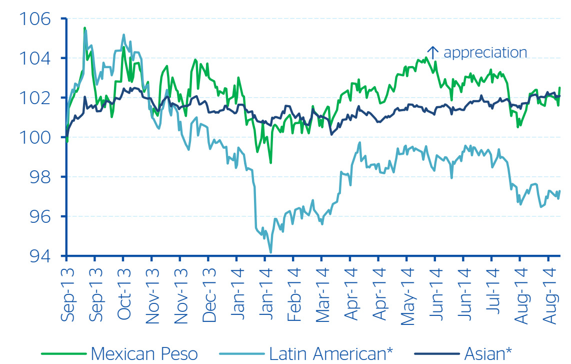
Source: BBVA Research, Bloomberg

Figure 5
Global risk and exchange rate (VIX index and USDMXN)



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD (5 Aug 2013 index=100)



* JP Morgan indices of Latin American and Asian currencies vs. USD; weighted averages by trade & liquidity.
Source: BBVA Research, Bloomberg

Annual information and forecasts

	2012	2013	2014
Mexico GDP (YoY % change)	4.0	1.1	2.5
General inflation (%, average)	4.1	3.8	3.9
Core inflation (%, average)	3.4	2.7	3.2
Monetary Policy Rate (%, average)	4.5	3.8	3.2
M10 (%, average)	5.7	5.7	6.1
US GDP (YoY % change)	2.8	1.9	2.0

Source: BBVA Research

Recent publications

Date		Description
1 Sept 2014	➡	Mexico Migration Flash. Remittances to Mexico grew by 8.4% in July, making twelve consecutive months of rises
1 Sept 2014	➡	Mexico Banking Flash. Credit to the private sector: moderation in growth continues, with a rate of 8.3% in July
5 Sept 2014	➡	Banxico Flash. Monetary rate unchanged at 3.0%. Neutral tone as short term inflation risks rose
5 Sept 2014	➡	Mexico Flash. The tax authority publishes its 2015 macroeconomic and fiscal framework