Economic Analysis

Monetary policy rate unchanged at 3.0%

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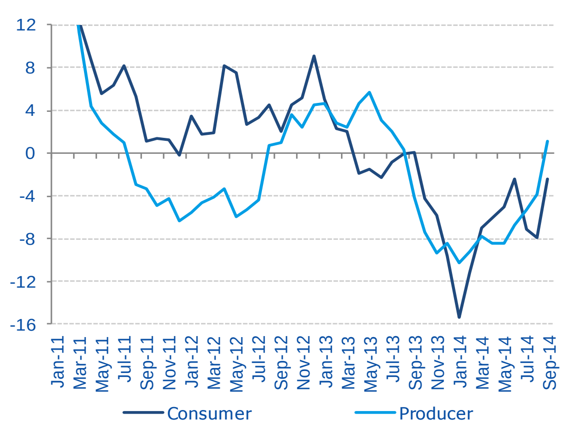
What happened this week…

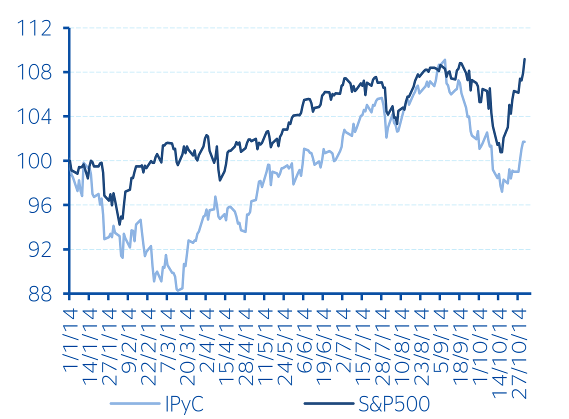
The central bank maintained a neutral tone. The favourable economic outlook from the US and the reforms offset the risks to the downside of world growth. On balance, inflation risks were unaffected. The language used by the central bank about its monetary policy decision today implied a degree of confidence that the positive figures on the US economy will impact on greater momentum in the domestic economy by the end of the year, leaving behind the negative shocks such as the one suffered in the first quarter. Caution remains as to price behaviour in the context of inflation above 4.0% and the presence of risks to the upside, particularly when convergence to 3.0% is expected for 2015. There was a reference to "recent events in civil society", such as the risk of a fall in inflation as a result of the effects which these might have on economic agents' expectations and, as such, on the vigour of economic activity. Based on the central bank's criterion for efficient convergence, we consider that the current outlook is consistent with keeping to the monetary pause for the rest of the year.

Figure 1
Producer and consumer confidence indexes, 2011-14 (YoY % change, 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

September's balance of trade surprised with a higher surplus than expected. According to INEGI data, the balance of trade in September 2014 was in surplus by USD590mn (BBVAe: USD100mn; consensus: USD-318mn). This is due to the fact that goods exports showed an annual rate of growth in September of 9.2%, while import growth came in at 9.6%. The growth of non-automotive manufacturing exports is responsible for this favourable performance in goods exports. In September their annual rate of growth rose to 11.7%, up from the previous month's annualised increase of 0.9% and the 10.3% growth rate in automotive exports. Provided that both automotive and non-automotive manufacturing exports continue to grow robustly in the near future, the country will have this element, which is vital for more vigorous economic expansion, to rely on.

Higher-than-expected growth in the US in 3Q and the optimistic tone around economic activity on the part of the Federal Reserve underpinned the gains on the stock markets. Over the week the Fed (Federal Reserve) finished its asset purchase programme and commented on the progress made in the labour market and the reduction in the US economy's slack capacity. Furthermore, the institution made it clear that the current economic conditions in the US are strong enough to move towards full employment with price stability. The YoY GDP growth figure of 3.5% in the third quarter confirmed the Fed's outlook published the day before, and was the spur for risk-taking on the financial markets. On this occasion, the growth figure and outlook outweighed speculation about the implications this figure will have on a possible early start to the cycle of monetary normalisation. Given this climate, there were weekly gains on stock markets, emerging currencies appreciated and the long-term interest rates jumped. In particular, the S&P 500 once again reached a record high, rising by 2.7% over the week, while the IPC rose by 3.1% over the same period. Expanded monetary stimulus in Japan gave a further boost to the demand for risk assets at the end of the week. The peso appreciated 0.58%, the second highest appreciation among emerging currencies, closing the week at USDMXN 13.48. On the government debt market, yields on the 10-year M-bond increased by around 2bp during the week, closing at around 5.88%, in line with the 6bp rise on the equivalent US T bond.

…What is coming up next week

We expect the IMEF indicators on manufacturing and non-manufacturing performance expectations to remain unchanged. These indicators, published on 3 November, will give guidelines as to the expectations for the country's economic activity at the beginning of 4Q14. We forecast that the IMEF indicators will perform similarly to the month before, due to the expectation of sluggish industrial and services activity before the end-of-year buying spree.

We expect the producers' confidence indicator to continue improving in October and for consumer confidence to increase slowly. On 5 November the INEGI will publish the Producer (PCI) and Consumer (CCI) Confidence Indexes for October. We estimate that the PCI will reach at 54.5 points, seasonally adjusted (sa), from 53.2 points, sa, the month before, due to good recent performance from the manufacturing sector. In addition, taking the creation of formal employment during September (156,432 job positions) into account, we expect the CCI to reach 90.5 points, sa, compared to the previous month's 90.4 points. This is equivalent to 91.7 points with original series (see Figure 1).

Remittances in September are forecast at USD1.957bn, equivalent to an annual increase of 7.0%. Recent estimates using the Current Population Survey (CPS) indicate that the volume of Mexican migrants in the United States, the main source of remittances to Mexico, is still not showing sustained levels of growth. However, the reduction in the rate of overall unemployment in the neighbouring country to 5.9% in September may also have generated an increase in occupancy and an improvement in the labour conditions of Mexican migrants in the US. Thus, we estimate that September will see an increase in remittances of 7.0% compared to the same month the year before.

We forecast that annual inflation will be 4.31% in October. We anticipate monthly increases of 0.57% and 0.18% respectively for headline and core inflation in October. If our forecasts are correct, in annual terms headline inflation will post at 4.31% (compared to 4.22% in September) while core inflation will be 3.33% (compared to 3.34% in September). Although there was already a spike in the first half of the month, the main factor which will explain the sudden increase in inflation will be the beginning of the seasonal electricity tariff rise as the hot season subsidies come to an end. In the second half of the month, our price tracker indicates that the pressures on beef prices continued and it anticipates significant increases in the prices of fruit and vegetables.

For the end of the year, we hold to our estimate for headline and core inflation of 3.84% and 3.39% respectively, although if our forecasts are correct – with the return of price hikes on fruit and vegetables in the second half of the month and the persistence of price pressures on beef – the risks will once again be biased to the upside.

Calendar of indicators

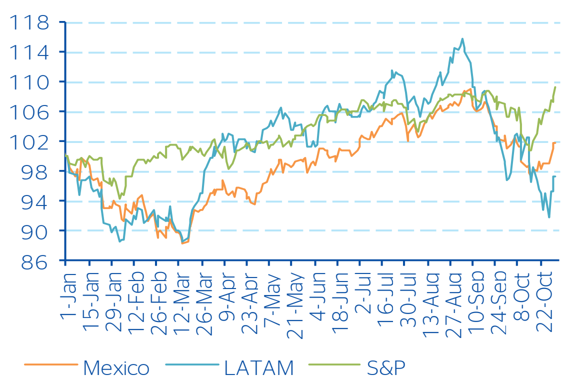
Mexico	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
IMEF manufacturing indicator (index, sa)	October	3 Nov	52.6	--	52.7
IMEF non-manufacturing indicator (index, sa)	October	3 Nov	51.6	--	51.8
Household remittances (USD mn)	September	3 Nov	1,957	--	2,010.4
Producer confidence (Index, sa)	October	5 Nov	54.5	--	53.2
Consumer confidence (Index)	October	5 Nov	91.7	--	91.8
Headline inflation (MoM % change)	October	7 Nov	0.57%	0.55%	0.44%
Headline inflation (YoY % change)	October	7 Nov	0.18%	0.18%	0.29%
Core inflation (MoM % change)	October	7 Nov	4.31%	4.30%	4.22%
Core inflation (YoY % change)	October	7 Nov	3.33%	3.33%	3.34%

USA	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
ISM Manufacturing PMI (Index, sa)	October	3 Nov	57.30	56.50	56.60
Manufacturers New Orders Total (MoM % change, sa)	September	4 Nov	-0.70	-0.45	-10.10
ISM Non-Manufacturing NMI (Index)	October	5 Nov	59.00	58.00	58.60
Employees on Nonfarm Payrolls Total MoM Net Change ('000s, sa)	October	7 Nov	224.00	230.00	248.00
Unemployment rate (%)	October	7 Nov	5.90	5.90	5.90

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

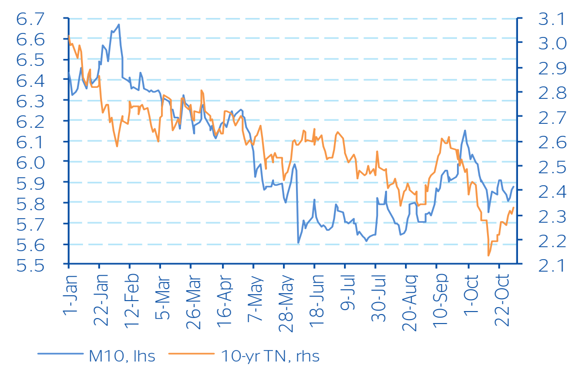
Markets

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



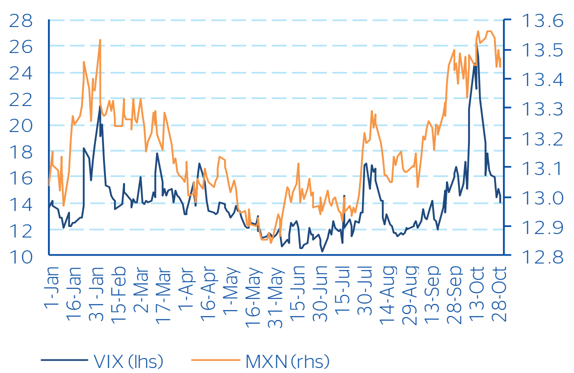
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



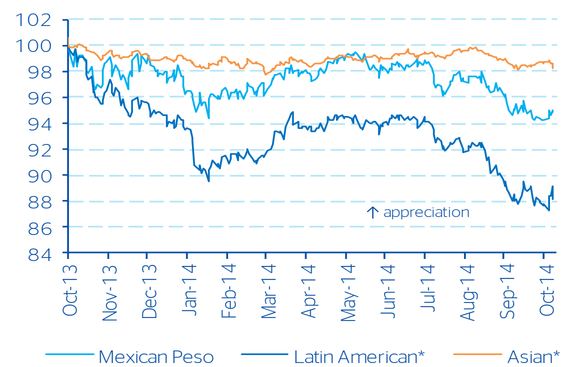
Source: BBVA Research, Bloomberg

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



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD (30 Oct 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
Headline inflation (%, average)	4.1	3.8	4.0
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	6.0
US GDP (YoY % change)	2.8	1.9	2.0

Source: BBVA Research

Recent publications

Date		Description
31 Oct 2014	➡	Banxico Flash. Fondeo rate unchanged at 3.0%. Neutral tone that denotes the pause will remain the rest of 2014
31 Oct 2014	➡	Mexico Banking Flash. Credit to the private sector: growth steadies at 7.7%, supported by credit to companies