

Economic Analysis

We expect industrial production to have shown something of an improvement going into 2Q15

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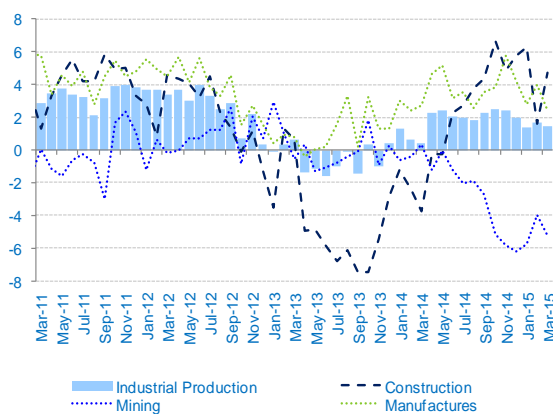
What happened this week...

The consumer confidence index (ICC) was better, moving up from 91.3 points in April to 92 points in May (BBVAe: 92.6 points), and notably also improved relative to May 2014 (90.7 points), although this was only slight. The rise in the ICC was only moderate because just one of its five components performed substantially better, whereas three only showed marginal improvements, and the reading for the fifth and final component actually indicated a deterioration.

The gross fixed investment indicator rose by 6.6% YoY in March 2015 according to its initial series, which was slightly better than we expected (BBVAe: 6.1%). The difference between estimated and actual growth was primarily due to the fact that construction investment, which has the biggest weight, increased more than forecast. This implies that growth in gross fixed investment in 1Q15 will be 5.4%.

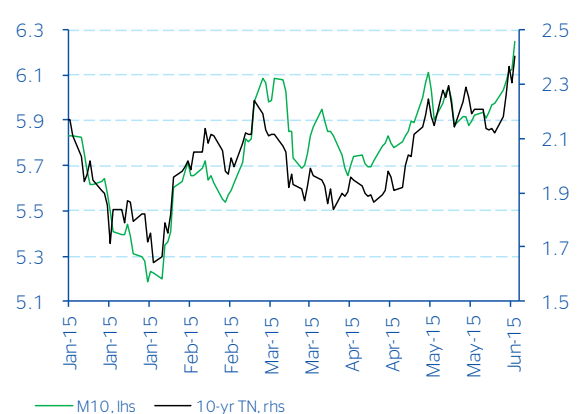
The central bank held its MPR unchanged at 3.0% and said in its statement that the balance of risks remains the same. According to the central bank, the potential monetary rate hike in the United States and its knock-on effect on the exchange rate is still the biggest threat to achieving and consolidating the convergence of inflation towards its target rate.

Figure 1
Industrial production and its components (YoY % change, seasonally adjusted)



Source: BBVA Research with INEGI data

Figure 2
Yield on government 10Y bonds (%)



Source: BBVA Research with Bloomberg data

The IMEF manufacturing indicator, which measures activity expectations for the sector, came in better in May, reaching 52.4 points, while the IMEF non-manufacturing indicator fell back to 51.1 points. Both indicators are above the threshold indicative of growth (50 points). These results suggest that manufacturing activity is showing a mild improvement in 2Q15 and that non-manufacturing activity growth is holding up, albeit at a slow pace.

Uncertainty and the fine job-creation figure in the United States are creating a stir among higher-risk assets, while the dollar exchange rate is hitting a historical high at MXN15.71. The rising trend in long-term bond yields in the major economies continued this week. Higher-than-expected inflation in the eurozone, allied with ECB toleration of the recent rise in bond yields were the factors behind the observed yield increases. In the United States, job-creation that beat expectations (280,000 vs. an expected 226,000) further underpinned the upward trend at the end of the week by pushing up federal funds rate futures, although market expectations still place the timing of the opening rate hike in 1Q16. Over the week, the IMF said that the Fed ought to put off raising rates until early in 2016, given the "significant uncertainty over the inflation outlook, the degree of slack and the neutral policy rate". We think that the better-than-expected employment growth is still not enough to offset the weak inflation in the Fed outlook and that the first Fed rate hike will take place in September this year. In the United States the yield on the 10-year treasury note rose 28bp on the week to 2.40%, a high for the last eight months. Higher bond yields in the key economies within a context where markets are already facing a strong dollar continued to stoke tensions among assets in emerging markets (EMs). On top of this there is renewed commodity price weakness at a time when greater jitters are more likely in the near future, given that the moment for the impending Fed rate rises is approaching. In this situation bonds in the EMs were swayed by US yields, and the 10-year Mbono yields flipped up by 27bp on the week to 6.25%, while EM currencies extended their depreciation against the USD. The MXN was among the worst-performing EM currencies over the week, probably affected by the lower oil price, as it slid 2.2%, taking the dollar exchange rate to a historical high of MXN15.71. As we have been arguing, the situation for higher-risk assets will remain difficult in the near future and no potential drivers have emerged on the horizon which might firm up the MXN significantly before the Fed begins its next cycle of hikes.

...What to expect next week

We expect industrial production in April to have shown an AGR of 1.9% in its initial series, and on 11 June INEGI is due to publish the official April 2015 figure for this index. The forecast AGR of 1.9% would be ahead of both the rate for the month before (1.7%) and that for the same month in 2014 (-0.9%). The main factor which is hampering vigour in the industrial sector is the mining and quarrying element, as this is still displaying negative growth rates after the slump in oil prices.

We estimate that annual inflation will be 2.96% for May and are predicting a setback for the month of -0.42% for headline inflation and a rise of 0.14% for its core counterpart. Should our forecasts be confirmed, in annual terms headline inflation will have dropped back to 2.96% in May from 3.06% in April, whereas core inflation should rise slightly to 2.36%, after 2.31% in April. With regard to core inflation, we expect a less encouraging performance from fruit and vegetable prices in the second half of the month. We forecast that annual inflation will hold relatively stable until October, at between 2.9 and 3.0%, before retreating in the final two months due to base effects, thence closing 2015 at a shade under 2.8%.

Calendar of indicators

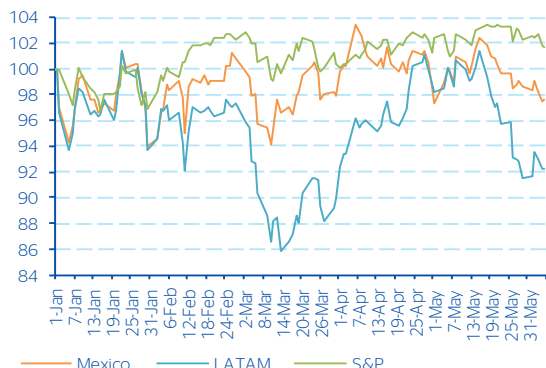
Mexico	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Headline inflation (MoM % change)	May	9 June	-0.42%	-0.49%	-0.26%
Core inflation (MoM % change)	May	9 June	0.14%	0.12%	0.16%
Headline inflation (YoY % change)	May	9 June	2.96%	2.90%	3.06%
Core inflation (YoY % change)	May	9 June	2.36%	2.34%	2.31%
Industrial production (YoY % change)	April	11 June	1.9%	1.3%	1.7%

United States	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Adjusted retail & food services sales total (MoM % change, sa)	May	8 June	0.4	1.2%	0.0%
University of Michigan consumer sentiment (Index)	June	12 June	93.3	91.4	90.7

Source: BBVA Research with data from Bloomberg. sa = seasonally adjusted. YoY = annual % change. QoQ = quarterly % change. MoM = monthly % change. P = preliminary

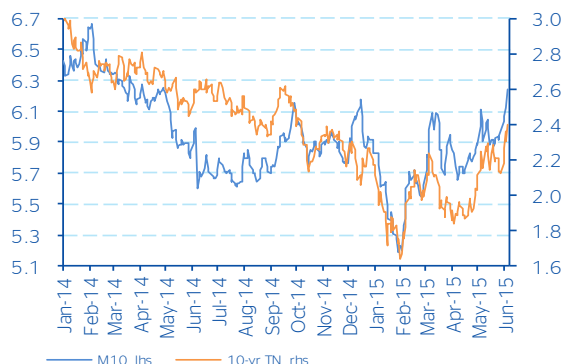
Markets

Figure 3
MSCI stock market indices
(Index 1 Jan 2015=100)



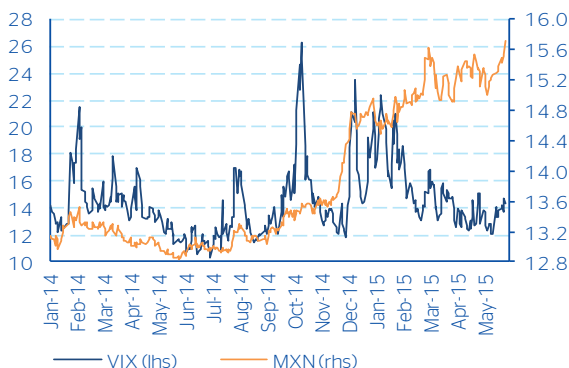
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



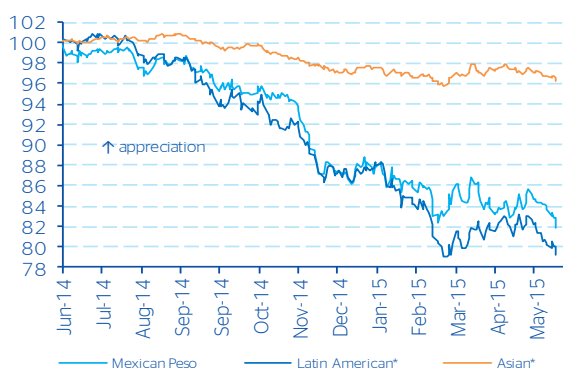
Source: BBVA Research, Bloomberg

Figure 5
Global risk and exchange rate:
VIX index and USDMXN



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD
(5 Jun 2014 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

	2013	2014	2015
Mexico GDP (YoY % change)	1.4	2.1	2.5
General inflation (% average)	3.8	4.0	3.0
Core inflation (% average)	2.7	3.2	2.4
Monetary Policy Rate (% average)	3.8	3.2	3.2
M10 (% average)	5.7	6.0	5.7
US GDP (YoY % change)	1.9	2.4	2.9

Source: BBVA Research.

Recent publications

Date	Description
3 Jun 2015	➔ Yearbook of Migration and Remittances. Mexico 2015
4 Jun 2015	➔ Mexico Migration Flash. Remittances show modest growth in April 2015, at 1.8% (YoY)
5 Jun 2015	➔ Mexico Banking Flash. Private sector credit: still trending positively after growing 10.9% in April

Disclaimer

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