

Economic Analysis

Industrial activity has started off slowly in Q2 and inflation is at a historical low

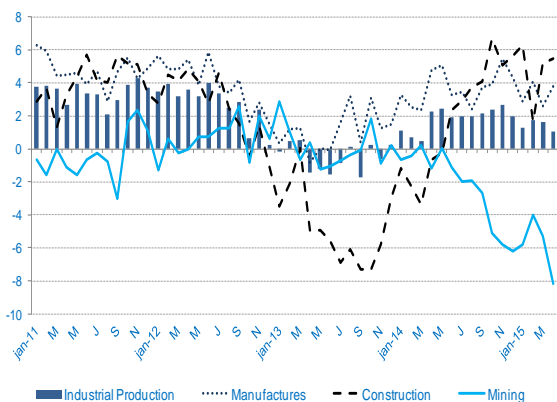
Arnoldo López / Javier Amador / Iván Martínez / Javier Morales

What happened this week...

Industrial production for April 2015 contracted by 0.1% in the month, due to the adverse mining sector performance and the lack of construction sector dynamism, leaving the industrial production AGR at 1.1%. The substantial MoM growth of 2.0% by the manufacturing industry suggests that external demand is picking up, although oil production continues to deteriorate, which can be seen in a weak industrial production figure in aggregate terms.

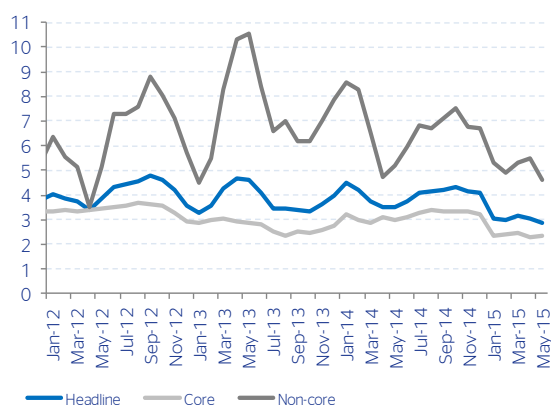
Annual inflation fell to a historical low in May of 2.88% after 3.06% in April, as headline inflation marked -0.50% MoM in May, helped by lower-than-expected inflation in the second fortnight of the month (0.04% QoQ). The surprise with respect to our forecast mainly came from a heavier-than-expected fall in the components of fruit and vegetables, and livestock. Core inflation was 0.12% MoM, which was in line with consensus estimates (BBVAe: 0.14%, consensus: 0.12%), and in annual terms, it edged up to 2.33% from 2.31% the previous month. All the underlying components rose in line with our forecasts, with the exception of the “other goods” item, which surprised on the downside. After these figures, we anticipate that headline inflation will remain below 3.0% over the rest of the year and we are revising our year-end forecast down to 2.65% from 2.75%.

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



Source: BBVA Research with INEGI data.

Figure 2
Inflation and components (YoY % change)



Source: BBVA Research with INEGI data.

We also expect core inflation to be lower than we had forecast earlier, and we now see it closing the year at 2.5% (2.6% previously). These forecasts also leave some margin to soak up any pressures that might arise due

to a transmission effect from the higher exchange rate and potential supply-side shocks over the remainder of the year (e.g. a possible reversal of perishable food prices).

The MXN was among those currencies which appreciated the most over the week, as the markets await an announcement from the FOMC (Federal Open Market Committee) on Wednesday. The MXN appreciated by around 2.0% over the week, which took its dollar rate to around MXN15.40. This was the second largest appreciation among the currencies of the emerging economies, behind only the Colombian peso (COP), which rose 3.82%. The gains made by the MXN over the week were influenced by the rising oil price, which, in the case of Mexican mix, was 4.0% higher, as well as by relative dollar weakness against several of the currencies of developed countries after the narrowing of the interest rate differential. In the fixed income market the redemption yield on the 10-year Mbono was trimmed by 8bp during the week and closed at around 6.20%, which was a heavier fall than was experienced by the T-bond that matures on a similar date. Meanwhile, on the equity markets, the Mexican IPC index advanced by 0.29% while the S&P 500 closed the week showing a rise of less than 0.1%. This week market attention will focus on any information it can glean on the process of monetary policy normalisation in the United States following the FOMC's monetary policy statement and the revised forecasts of the committee members, as well as the press conference to be given by the Fed chair.

...What to expect next week

The components of GDP for 1Q15 are due to be published, and on 19 June INEGI will release the Global Supply and Demand of Goods and Services at Constant and Current Prices for Q1. These indicators are of great significance, as they reveal contributions to growth of consumption and public and private investment, net exports and inventories, which tell us what the elements behind Q1 growth are.

The central bank will release the minutes from the last policy committee meeting of 4 June on Thursday. Even though the statement showed very few changes relative to the message in April, it will be worth noting whether any of the opinions expressed by members of the policy committee regarding a potential policy rate hike have changed following the narrowing of the forecast range for economic growth. Likewise, it will be useful to follow the debate on the risks of any transmission of exchange rate depreciation through to inflation expectations, given that these are essential to the debate after the central bank's recent statement.

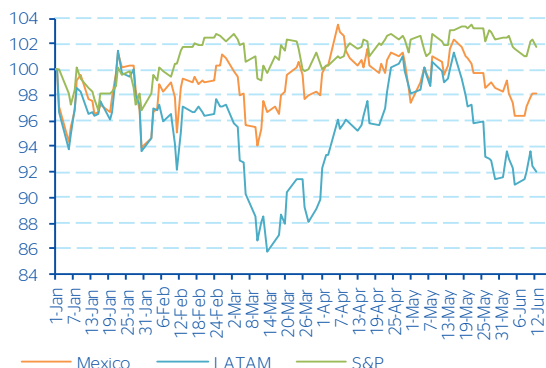
Calendar of indicators

United States	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Industrial Production (MoM % change, sa)	May	15 June	0.4%	0.2%	-0.3%
New Privately Owned Housing Units Started by Structure Total (thousands, saar)	May	16 June	1,120	1,100	1,135
Federal Funds Target Rate		17 June	0.00-0.25%	0.00-0.25%	0.00-0.25%
CPI Urban Consumers Less Food & Energy (MoM % change, sa)	May	18 June	0.2	0.2%	0.3%

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

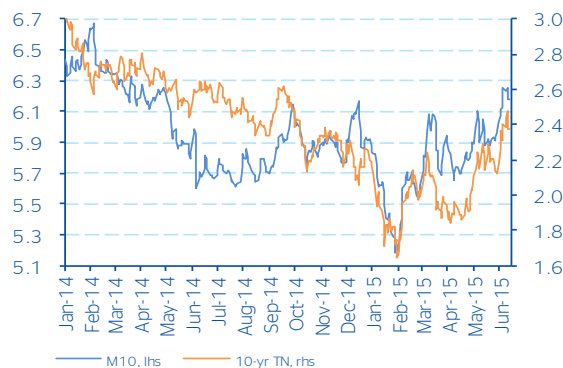
Markets

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



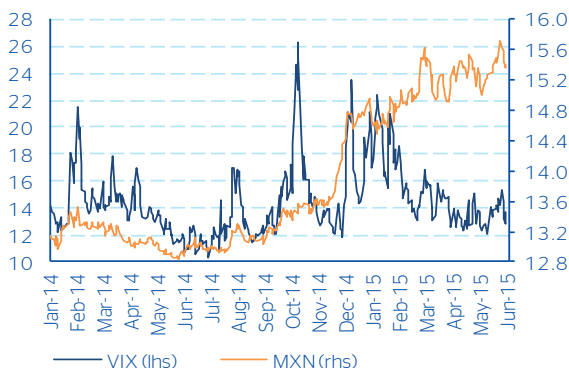
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



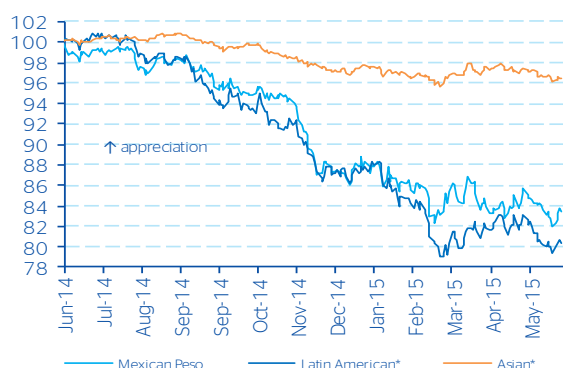
Source: BBVA Research, Bloomberg

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



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD
(12 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

Fuente: BBVA Research.

Recent publications

Date	Description
9 Jun 2015	➔ Banxico Flash. The central bank is holding the monetary policy rate unchanged at 3.0% and the risk assessment remains unaltered
9 Jun 2015	➔ Mexico Inflation Flash. Annual headline inflation is at a record low; we lower our year-end forecast to 2.65%

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