BBVA | RESEARCH

Mexico Weekly Flash
17 July 2015

Economic Analysis

We estimate that the services sector is likely to have helped activity to grow in May

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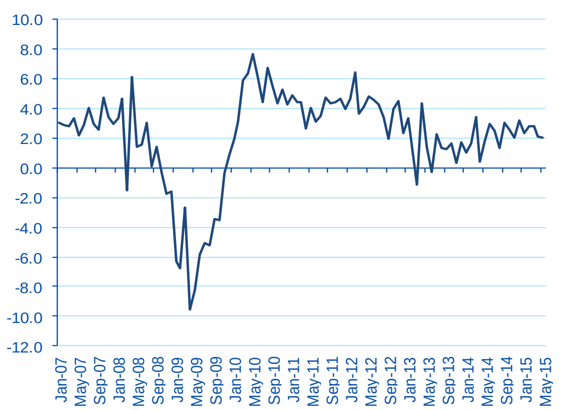
What happened this week…

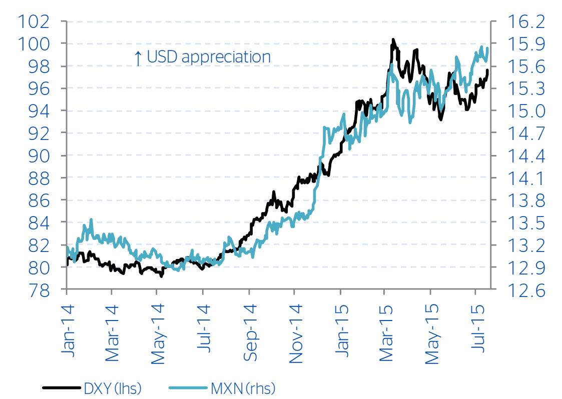
The trend of dollar appreciation persists even though global risks have moderated, while fixed-income markets remain unaffected. Stock markets have reacted positively to the third Greek bail-out. After the Greek parliament backed the measures demanded by the European creditors, the European Union reached an agreement in which EUR7.16bn is being provided in a three-month bridging loan, paving the way for Greece to settle its arrears with the IMF and pay off Greek bonds that are both due and in the hands of the ECB until a three-year bail-out package takes shape. Added to this, the new measures established by the Chinese authorities and the positive surprise from China's Q2 figures for GDP were also instrumental in driving positive equity market performances. Overall, and given the lower perceived risk from Greece and China, implied volatility diminished across all asset classes. On the other hand, Federal Reserve Chair Janet Yellen appeared to be more upbeat about developments in the US economy justifying a start to the normalisation process for monetary policy before the year is out. House-building figures ahead of initial expectations, together with a rise for YoY core inflation from 1.7% in May to 1.8% in June, supported this view. This seems to have already been discounted by the markets, judging by the movements along the US rate curve, as 2-year bond yields alone rose after Yellen's comments, while 10-year yields shed 5 basis points on the week. Emerging economy fixed income markets are holding stable in spite of the recent macroeconomic risks (e.g. in China and Greece).

Figure 1
Global Economic Activity Index (IGAE) (YoY % change, seasonally adjusted)



Source: BBVA Research with INEGI data

Figure 2
Exchange rate and DXY index (USD/MXN and dollar index against major currencies)



Source: BBVA Research with Bloomberg data

The virtually negligible reaction to these events, and even the recovery by fixed-income assets in emerging markets, might possibly be attributable to market expectations of a path of very gentle hikes by the Federal Reserve, which would provide some scope for many central banks to extend their accommodative monetary policies for longer. Meanwhile, the USD moved firmer against the key currencies, with the dollar index rising 1.7% over the week (see Figure 2), while emerging currencies continued their depreciating trend against their US counterpart. The Mexican peso weakened 1.3% during the week and closed at dollar levels above MXN15.9. On the commodity markets, oil prices came down by around 4% in response to the agreement with Iran, which opens the door to an additional rise in the oil supply in a market which is already betraying signs of oversupply.

…What to expect next week

We estimate that the Global Economic Activity Index (IGAE) figure for May, which INEGI is due to publish on 24 July, will show monthly growth in its seasonally-adjusted (sa) series of 0.2%. Taking into account a monthly growth rate of 0.2%, the annual growth rate for the May series (sa) would be 2.3%. Within this indicator, we expect secondary sector activity to indicate a decrease of 0.4% MoM, sa, while the tertiary component should have grown by 0.4% MoM. Looking at the IGAE in its original terms, we estimate 2.0% annual growth rate for it in May.

We forecast that annual inflation will have remained relatively stable in the first fortnight of June compared to the previous half-month (an estimated 2.89%, against 2.87% in the second fortnight of June). For the first two weeks in July, we estimate a fortnightly rise of 0.22% for headline inflation and of 0.12% for core. If our predictions prove right, in annual terms headline inflation would be 2.89%, whereas core would have eased down to 2.33% (compared to 2.35% for the previous fortnight). We still expect the exchange rate pass-through to inflation to remain minimal, largely because of the flatness of domestic demand, and that the rise in goods inflation will continue to be offset by a decent performance by the services component. Over this fortnight, the seasonal rise for tourist services due to the summer holiday peak period will be partly offset by a drop in the other services component associated with the summer sales. As regards the non-core component, our price-monitoring suggests substantial rises in tomato prices within the fruit and vegetables sub-index, while for the livestock prices component a further fall is anticipated in the egg price, although this will be compensated by price rises for chicken, beef and pork.

We estimate that May retail sales will reveal a YoY rise of 3.6%, sa. The result for this will be published by INEGI on 22 July and will be tied in with the ANTAD sales performance - which, for outlets overall, rose that same month by a real 6.2% YoY, sa - as well as with the poor figure for formal employment in May. It is worth recalling that in April retail sales grew by 4.2% YoY, sa.

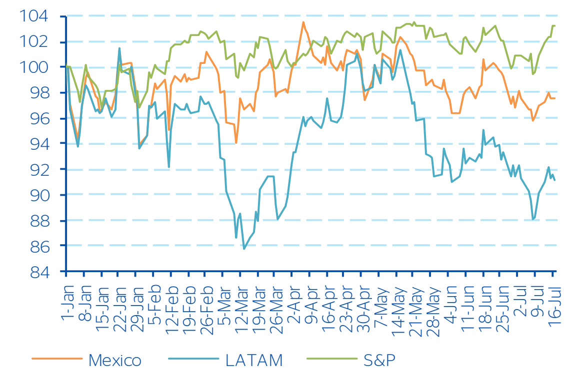
Calendar of indicators

Mexico	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
IGAE (MoM % change, sa)	May	24 July	0.2%	-	0.7%
IGAE (YoY % change, sa)	May	24 July	2.3%	-	2.4%
IGAE (YoY % change, original series)	May	24 July	2.0%	1.0	2.1%
Headline inflation (FoF % change)	1F July	23 July	0.22%	0.20%	0.03%
Headline inflation (YoY % change)	1F July	23 July	2.89%	2.87%	2.87 %
Core inflation (FoF % change)	1F July	23 July	0.12%	0.15%	0.08%
Core inflation (YoY % change)	1F July	23 July	2.33%	2.36%	2.35%
Retail sales (YoY % change, sa)	May	22 July	3.6%	5.0%	4.20%
Retail sales (MoM % change, sa)	May	22 July	0.3%	0.2%	0.4%
United States	**Indicator period**	**Publication date**	**BBVA estimate**	**Consensus**	**Previous figure**
Existing Homes Sales (saar, millions)	June	22 July	5.4	5.4	5.35
Chicago Fed National Activity Index	June	23 July	-0.08	-0.05	-0.17
Conference Board Leading Index (MoM % change)	June	23 July	0.3	0.1	0.7

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

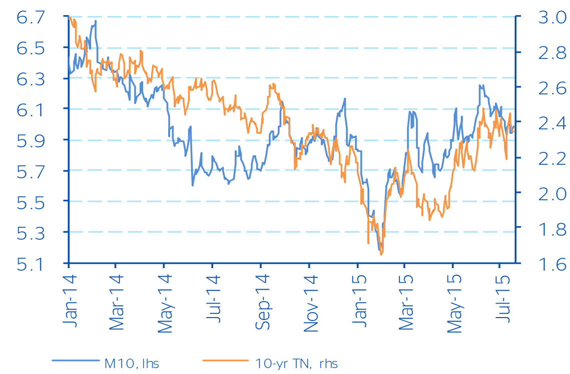
Markets

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



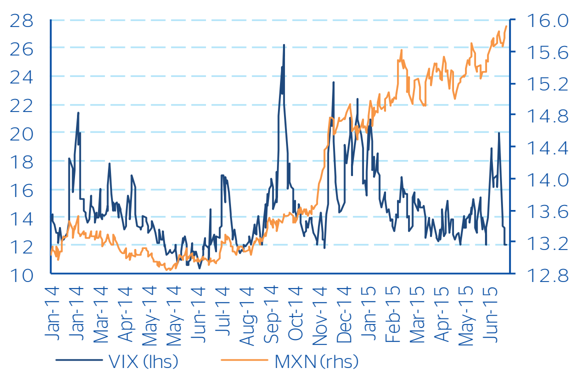
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



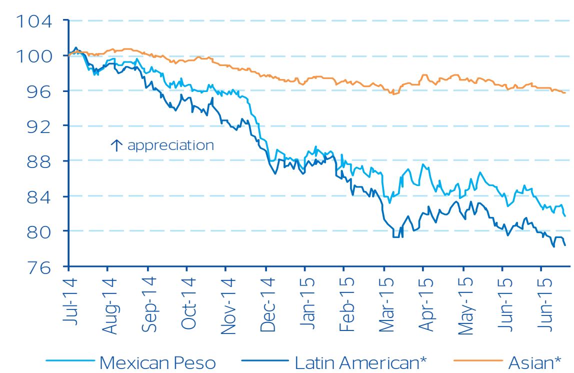
Source: BBVA Research, Bloomberg

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



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD (17 Jul 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	2.9
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	2.5

Source: BBVA Research.

Recent publications

Date		Description
14 Jul 2015	➡	Mexico Economic Outlook Second Quarter 2015