Economic Analysis

The peso's dollar rate is returning to MXN16, influenced by lower figures than expected in the United States and the increase in the amount of dollars auctioned

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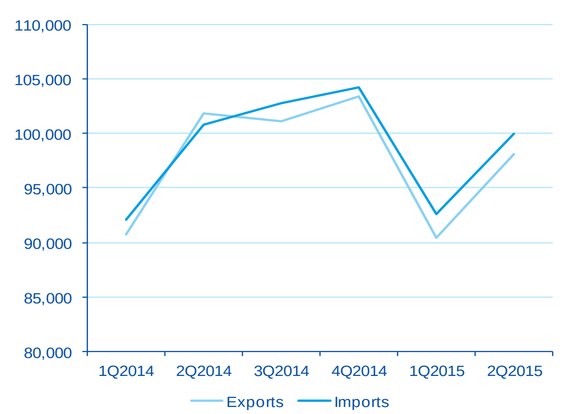
What happened this week…

As was expected, the balance of trade revealed a deficit in June that was slightly over USD700mn, which was in line with our estimates (BBVAe: -USD725mn, reported: -USD749mn). Manufacturing exports are showing a mild recovery, with an annual growth rate (AGR) of 6.5%, while oil exports continued to fall, doing so by more than 40% YoY.

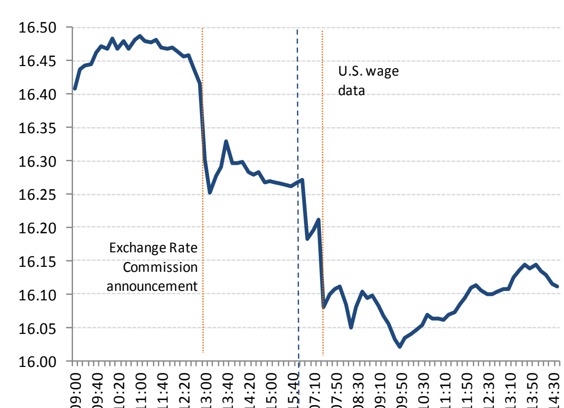
Benchmark rate unchanged. A less restrictive tone which will have a bearing on the pace of the hike cycle. The statement by the central bank had a less constrained tone to it, as it pointed out an overall deterioration as regards the risks to growth and an improvement in the assessment of risks for short-term inflation. It nonetheless said that monetary policy action by the Federal Reserve (Fed) constitutes the major risk to the consolidation of the convergence of inflation towards the target rate. As a result, we maintain that the first upward move will take place in harmony with the Fed and we expect this to happen in September. As for the less restrictive tone owing to domestic conditions, we consider that this will be influential, not only in connection with the beginning of the rate hikes but also as regards their momentum in 2016. This is provided that the reference rate adjustment manages to anchor inflation expectations and permits orderly behaviour in the financial markets.

Figure 1
Goods exports and imports by Mexico (USD mn, cumulative QoQ)



Source: BBVA Research with INEGI data

Figure 2
Intra-day exchange rate, 30 and 31 July 2015 (USD/MXN)



Source: BBVA Research with Bloomberg data

The peso's dollar rate is coming back to the MXN16 level, influenced by lower figures than expected in the United States and the increase in the amount of dollars being auctioned off. Expectations over the start of the monetary normalisation process in the United States put substantial pressure on the peso during the week, although fresh intervention by the Currency Commission and overly timid wage growth in the United States were factors that caused the peso to appreciate towards the end of the week. On Wednesday, the changes in the FOMC's message kept expectations alive that the first move by the Fed could take place in September, which were heightened just one day later, when it emerged that the US economy had grown by 2.3% YoY in Q2 and 0.6% over the first three months, following a revision of the figures. In this context, the peso's dollar rate depreciated to around MXN16.49, just before the Currency Commission announced a rise in the figure for the daily auctions from USD52mn to USD200mn, up until 30 September. On top of this, the Currency Commission cut the minimum intraday depreciation level required to trigger the auctioning of a further USD200mn from 1.5% to 1.0%. After the announcement of these measures, the peso appreciated to MXN16.20 and then later closed at MXN16.26. The appreciation finally consolidated at around MXN16.10 on Friday, influenced by wage growth in the United States that showed a meagre 0.2% for the first quarter, its smallest rise since 1982, which sowed doubts among market participants over whether the Fed will have sufficient justification to raise the federal funds rate in September. In the fixed income market, the yield on the 10-year M-bond was pared down by 9bp during the week to 6.05%, a move which was in the same direction as the T-bond with a similar maturity, where the latter's yield was whittled down by 7bp over the week, closing at 2.19%. In the stock markets, the IPyC and the S&P 500 moved up by 1.01% and 1.33% respectively, influenced by the corporate reporting season.

…What to expect next week

INEGI is set to publish the monthly gross fixed investment figure for May on 4 August, and we expect YoY growth for the initial series for this index to be 2.5%. This AGR estimate is based on expected growth for its components of 1.5% for construction investment and 4.6% for machinery and equipment investment. It should be remembered that the 5.3% AGR for gross fixed investment in April was ahead of estimates, given a substantial improvement in both components (construction, 4.2%; machinery and equipment, 7.2%).

We estimate that annual inflation will have sunk to a new historical low in July (2.75% forecast, compared to 2.87% in June). We predict a MoM increase of 0.16% for headline inflation and also of 0.16% for core. Should our forecasts prove to be correct, in annual terms core inflation would have dropped back a little to 2.30%, compared to 2.33% in June, and reached a low point for the year. As we had been anticipating, and the figures for the first fortnight of the month confirmed, the behaviour of core prices will be typically seasonal, with a spike in the "other services" sub-index (BBVAe: 0.60% MoM) arising from the rise in prices associated with tourism due to the summer holiday season, which will be partly offset by the fall in non-food goods prices (BBVAe: -0.20%) on account of the summer sales. With regard to non-core inflation, we anticipate that a sharp monthly rise in fruit and vegetable prices will be offset by the fall in livestock prices, chiefly driven downwards by plunging egg prices. We forecast that annual core inflation will hit lows this month and then embark on an upward trend from August onwards. We predict that it will close the year at 2.50%. Moving to headline inflation, we think that this will come down in the last few months of the year, thanks to a favourable basis for comparison, and then end 2015 at around 2.50%. The strong additional peso depreciation in recent weeks gives our core inflation forecast upside risk since, although it did take account of a little more exchange rate pass-through to goods prices, it did not factor in the levels attained after the sharp further depreciation observed in the past few weeks. Whatever the case, we are confident that the consensus will continue to revise its year-end headline inflation forecast (2.9%) downwards, and that this will gradually continue to move more closely into line with our own.

Remittance inflow into Mexico could have risen 5.5% YoY in June, which would represent USD2,156mn. The cumulative remittance flow for the first five months of 2015 reached USD9,928.1mn, showing growth of 3.6% YoY. Although growth was below the level registered over the same period in 2014, remittances have stuck to a trend of moderate growth in 2015. The latest estimates from the US Bureau of Labor Statistics confirm the healthy rhythm of employment among the population of Mexican origin in the United States, from where c.98% of all remittances received in Mexico comes, with an unemployment rate of 6.3% (seasonally adjusted) for 2Q15, which is 0.7 percentage points below the figures recorded in the same quarter of 2014. Remittances for the month in June could have grown by 5.5% YoY, pointing to a level of USD2,156mn, which would break through the USD2bn barrier for the fourth time so far this year.

Calendar of indicators

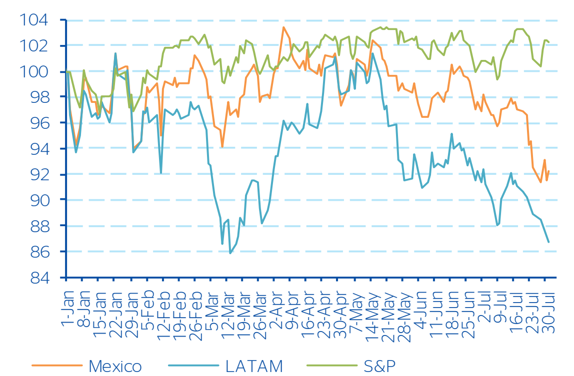
Mexico	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
Headline inflation (MoM % change)	July	8 August	0.16%	0.16	0.17%
Core inflation (MoM % change)	July	8 August	0.16%	0.17	0.21%
Headline inflation (YoY % change)	July	8 August	2.75%	2.75	2.87%
Core inflation (YoY % change)	July	8 August	2.30%	--	2.33%
Gross fixed investment (YoY % change)	May	4 August	2.5%	2.8	5.3%
Remittances (USD millions)	June	3 August	2,156	2,130	2,198

United States	Indicator period	Publication date	BBVA estimate	Consensus	Previous figure
ISM Manufacturing PMI (sa, index)	July	3 August	53.9	53.5	53.5
Employees on Nonfarm Payrolls Total (MoM net change, thousands, sa)	July	29 July	235	225	223

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

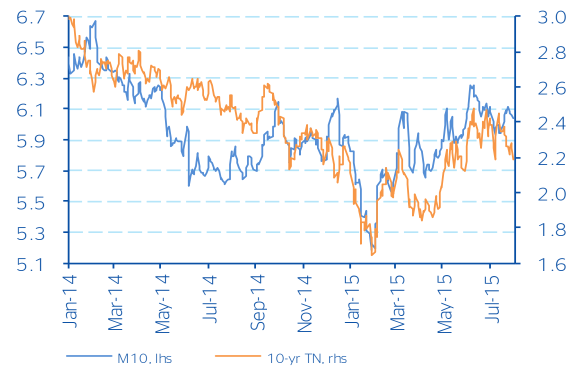
Markets

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



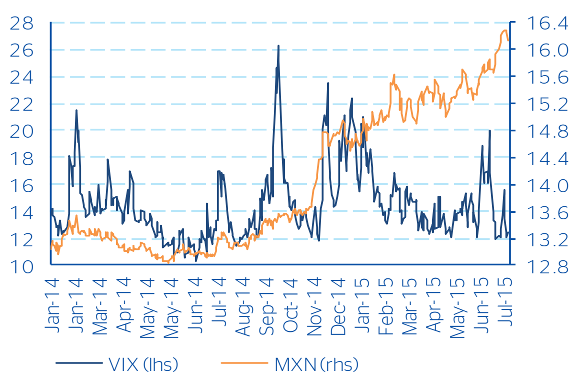
Source: BBVA Research, Bloomberg

Figure 4
10-year government bond yields (%)



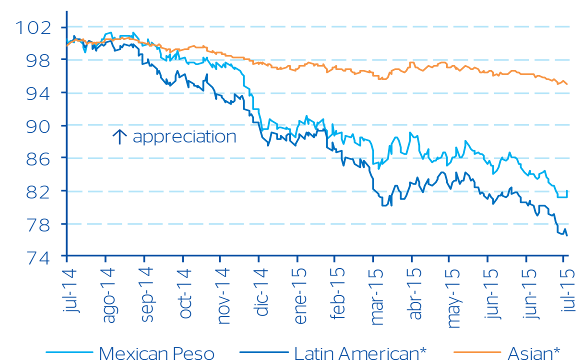
Source: BBVA Research, Bloomberg

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



Source: BBVA Research, Bloomberg

Figure 6
Currencies vs. USD (31 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	2.8
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
22 Jul 2015	➡	Mexico Real Estate Flash. As of May, mortgage loans have advanced 20%
22 Jul 2015	➡	Mexico Banking Flash. Banking deposits: recovering momentum, led by term deposits