BBVA Research

Mexico Economic Outlook

Third quarter 2018

Mexico Unit

Creating Opportunities

BBVA Research

Contents

Closing date: **3 August 2018**

1. Summary

According to early INEGI (National Statistics Institute) figures, in 2Q18 the economy shrank by -0.1%, which represents a 1.2 pp difference compared with the figure reported in 1Q18. By components, primary activities showed the biggest dip, with a YoY percentage change of -2.1% (vs. 0.9% in the previous quarter), while the industrial sector contracted by -0.3% (vs. 0.9% in the previous quarter). The tertiary sector surprised on the low side, with only modest growth of 0.3%, which contrasts with the 1.1% growth seen in the first quarter of the year. While the primary sector performance is prone to higher volatility owing to the nature of production in it, industry's less spirited showing is likely to be associated with a slowdown in the manufacturing sector and construction, as is evidenced by the manufacturers' orders indicator, which fell by an average of -0.4% in 2Q18 with respect to the previous quarter, and the aggregate trend indicator for the construction sector, which showed zero growth on average in 2Q18 compared with the previous quarter.

In the first half of 2018, the public sector's primary balance showed a total of 121.1 billion pesos vs. 412.9 billion in the same period of 2017. The primary surplus was largely due to the balance of institutions under indirect budgetary control as well as that of the IMSS (Mexican Social Security Institute). If disciplined management of the public finances continues over the second half of 2018, it will be possible to achieve the primary surplus target of 188.1 billion pesos (0.8% of GDP) for the entire public sector. The Historical Balance of Public Sector Borrowing Requirements (HBPSBR) stood at 44.6% of GDP at the end of June 2018. We expect fiscal consolidation efforts and the peso's appreciation to be reflected in a marginal reduction of the HBPSBR (as a % of GDP) from 46.2% in 2017 to 45.8% in 2018.

The trade deficit surged to US$2,773 million in 2Q18 from US$302 million in 2Q17. One factor behind this increase was the deterioration in the balance of oil trade (with a deficit of US$5,497 million in 2Q18 vs. US$3,826 million in 2Q17). We expect the trade deficit for 2018 to come in at US$12.8 billion. We foresee the current account deficit closing this year at roughly US$24 billion (2% of GDP).

In the opening months of the year inflation eased considerably. Nonetheless, in May headline inflation fell by less than we were predicting and from June it returned to an upward path which, due to its nature, we envisage as being only temporary. This rise originated from bigger than expected upturns in energy prices, mainly those of petrol (gasoline) and liquefied petroleum gas (LPG), which was reflected in substantial increases in non-core inflation. This change in relative prices has not affected core inflation, which continues to behave well and remains on a downward trend. Going forward, it appears inevitable that this change in relative prices on account of the above-mentioned supply shocks will affect the speed at which inflation moves towards its target level. We thus expect inflation to end the year at a shade over 4% (at 4.1%). This means that inflation will definitively reach the 3% target at a slower pace than was thought three months ago, when we were forecasting that it might end the year at slightly under 4% (at 3.8%). In contrast with this, as regards core inflation we still foresee an unbroken falling trend. Our projections suggest that core inflation is likely to settle at around 3.6% in the short term, before declining even further in the last two months of the year, reaching 3.4% at year-end.

Against this backdrop we predict a pause on the monetary front for the rest of the year. The tone of the last statement was less restrictive than it had been in previous communications and offered signs that, in the absence of further deterioration in the balance of risks for inflation, a monetary pause was the most likely scenario in the coming quarters. Moreover, the two rate hikes already seen this year have taken the real rate to a restrictive level. We predict that with a nominal rate at 7.75% over the rest of the year, the ex-ante real rate will be at over 4% on average, which is a high level by historical standards and significantly higher than a neutral rate of 2%. In 2019, with inflation at levels below 4% and gradually moving towards the target, Banxico will be able to calmly consider a gradual move of the MPR towards its neutral level (around 5.5%). We therefore foresee a 75 bp cut in the policy rate to 7% in 2019.

Over recent months the chief factor behind movements in domestic asset prices has been the escalation of trade tensions. On top of the renegotiation of NAFTA, the break-up of which remains the stand-out idiosyncratic risk, several countries have imposed various tariff measures. Investors are trying to weigh up to what extent such measures (especially those between the United States and China) are jeopardising world economic growth, and it is in the context of this mulling process that several bouts of risk aversion have been prompted. Movements in the principal financial variables in Mexico have in fact closely shadowed the ups and downs of trade-related matters, from the failed attempt to seal a preliminary accord on NAFTA over April and May through to the various nuances experienced in the tit-for-tat of tariff measures between China and the United States. In this context the outcome of the presidential election in Mexico and the initial messages from the winning candidate had a favourable effect on Mexican assets at a time that coincided with an easing of tensions worldwide.

Looking ahead, with high expectations of the renegotiation of NAFTA being concluded by 2019, and with the markets having given a favourable reception to the conciliatory message of the incoming administration, the potential imposition of a 25% tariff on cars imported to the US constitutes the main risk factor for financial variables in the short term.

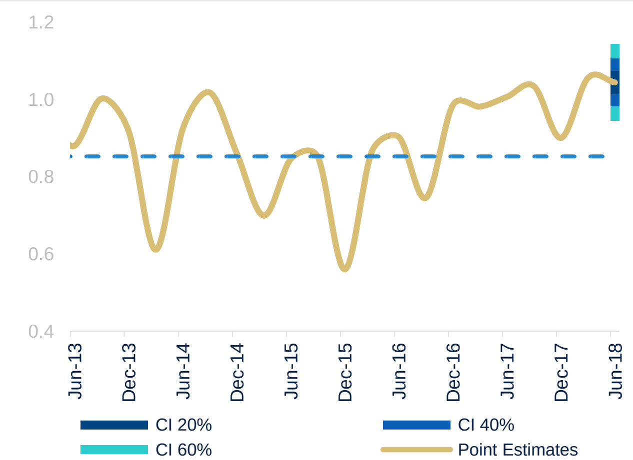
2. Global economy: robust growth but with certain signs of moderation and intensification of risks

The international economy continues to be subject to tensions of disparate forces between the good economic performance in recent quarters, now prolonged by the fiscal stimulus of the US economy and the stability of the Chinese economy, and several potentially negative factors that have been generated gradually in the first half of this year but which so far have not been directly reflected in activity. Both the Federal Reserve (Fed) and the European Central Bank (ECB) have taken a further step towards normalisation of monetary policy, which suggests somewhat less accommodative conditions, although the increasing financial tensions that have been generated in emerging economies as a result of the appreciation of the dollar seem to correspond more to a reassessment of risk than to a systemic threat. Oil prices have stabilised after a marked increase so far this year. The main risk is protectionism, which has increased in recent weeks with the measures and countermeasures that have been announced, and whose effect on activity could manifest in the second half of the year.

Stable growth in the first half of 2018, although with doubts about its persistence and with differences between the main areas

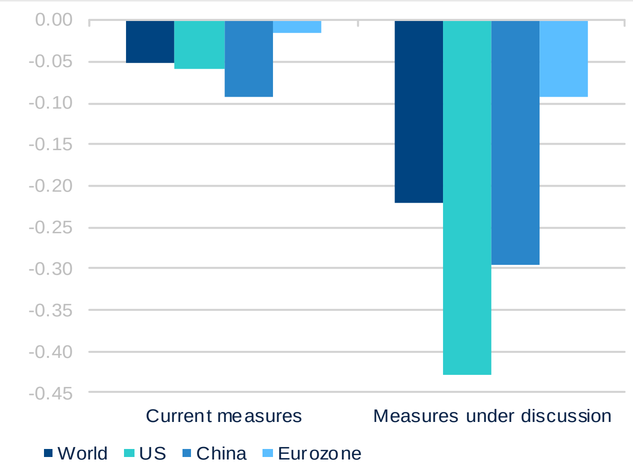
Data available up to May suggest that **global growth could have slowed slightly in the second quarter of the year** (BBVA-GAIN: 1% quarterly after 1.1% in 1Q18) (see Figure 2.1) and show **mixed signals for both areas and sectors**. Although the pace of expansion remains solid, it is occurring in a **less synchronised** manner, with accelerating growth in the US that contrasts with certain signs of moderation in China and some emerging economies and in a more pronounced way in the Eurozone.

Figure 2.1 World GDP growth (QoQ, %)



Source: BBVA Research

Figure 2.2 Effect on GDP growth due to US tariff hikes and the response of other countries (2018-19, pp)



Source: BBVA Research

The trend in the **industrial sector continues to cause concern**, as its activity has not recovered from the poor performance recorded at the beginning of the year, especially in emerging economies and **despite the positive data in global trade up until May**. However, these data do not yet reflect the possible negative effects of the protectionist escalation in recent months, unlike the confidence data for the industrial sector, which continued to deteriorate up until June. All this information points to **an ongoing recovery of the industrial sector, but at a more moderate pace, and it will be difficult to see it gaining traction in the coming quarters**.

The **confidence of the service sector has been more resilient**, with an increase in the emerging economies (especially those in the Asia Pacific region) that offsets a somewhat more disappointing trend in the developed economies. However, the trend in other indicators of domestic demand is more moderate, such as the **poor performance of retail sales up until May in the emerging economies that contrasts with a tentative recovery in the developed economies.** In any case, they suggest that the support from one of the main drivers of recovery in recent years could be stabilising or moderating.

In this context, **core inflation has risen very gradually in developed economies and has tended to stabilise in emerging economies** beyond the general rise in headline inflation, as a result of the increase in energy prices.

The oil supply shock and the first protectionist measures have led to an increase in uncertainty

The **increased growth of the US economy,** driven by fiscal measures **and the recovery of global trade** at the beginning of the year, continues to sustain the strength of the global recovery. **However, some of the supports** to growth have been fading in the last few years, **while uncertainty has increased**.

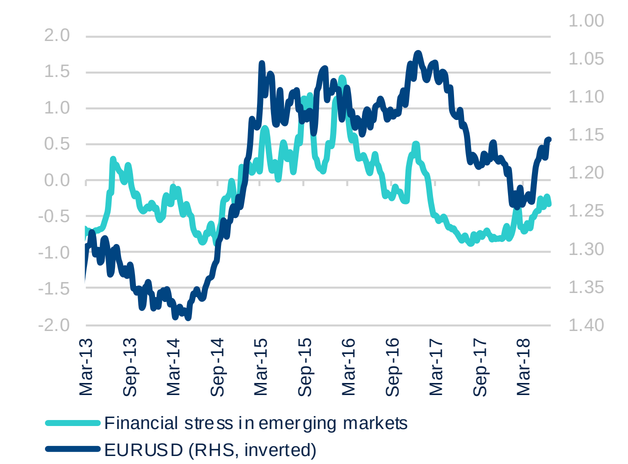
The first factor is the withdrawal of the United States from the nuclear agreement with Iran, which caused a supply ***shock* in the oil market that has increased the price of oil** by around 20% so far this year. Although prices seem to have stabilised in the wake of the increase in production by the OPEC countries, we now expect them to stabilise around US$70 per barrel in the forecast horizon, which suggests an upward revision in the forecasts of the oil price of around 10% this year and next with respect to those considered in the last quarter.

This will **place additional upward pressure on inflation and has already encouraged the central banks to take another step towards the normalisation of monetary policy**. This is particularly the case with the Fed, which so far this year has accumulated a rise of 50 basis points in its reference rates to reach 2% and plans to raise them to 2.50% by the end of the year and to 3.25% by the end of 2019. The interest rate differential and favourable growth in the US compared to the rest of the world has resulted in a **widespread appreciation of the dollar**.

An additional factor of uncertainty during the last few months is associated with the increase in trade tensions. It is still too early to know which measures will finally prevail of those already approved by the US administration and those that were previously announced, and the possible countermeasures from their trading partners. Nor is it easy to discern their impact on trade and activity. In principle, **the direct effect through the trading channel of the measures announced until now would be limited**. In particular, the increase in tariffs on imports of steel, aluminium and on those on a long list of Chinese exports covering US$50 billion, together with the countermeasures announced by the affected countries, is expected to yield a negative impact of **less than 0.1 pp on global growth** (around 0.1 pp on China's growth and virtually zero in the US and the Eurozone). Nevertheless, additional measures by the US are currently being discussed: on the one hand, the imposition of much higher tariffs on imports from the automotive sector, with tariffs of between 20% and 25%; on the other, the extension of tariffs on imports of Chinese products up to a value of US$200 billion (or more). This protectionist escalation, together with possible retaliation for similar amounts by the trading partners, would have a significant negative effect on the growth of both the US (-0.4 pp of GDP) and China (-0.3 pp). This effect would be somewhat lower in the Eurozone (-0.1 pp) although it differs per country, with Germany and the Central European countries being the most affected. Taken together, **the direct effect of these measures under discussion could subtract around 0.2 pp from global growth** (see Figure 2.2), **to which we should add potential indirect effects on the confidence of financial markets and economic agents** as a function of the magnitude of the trade conflict.

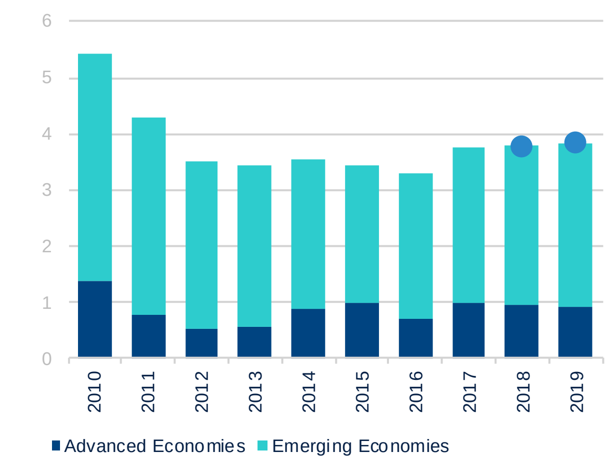
As a consequence of these uncertainties, there has already been a **readjustment in the perception of global risk, especially in the emerging countries**. Financial tensions in emerging countries have widespread (see Figure 2.3), due to the depreciation of currencies and the widening of risk premiums, although countries with higher external financing needs have been the most negatively affected. For this reason, the central banks in many of these economies (with the exception of China) have also tightened their monetary policies to avoid the depreciation of their currencies. **In Europe, the political risk in Italy** has resulted in a notable increase in the Italian risk premium (up to 250 basis points) but with a limited contagion to the rest of the peripheral countries. In addition, **uncertainty over protectionist measures has begun to have an impact on equity markets**, especially in Asian countries with China at the forefront, and on the demand for safer assets (US and German treasury bonds).

Figure 2.3 Euro-dollar exchange rate and BBVA index of financial tensions in emerging markets



Source: BBVA Research a partir de Bloomberg

Figure 2.4 World GDP growth forecasts (% YoY)



Source: BBVA Research

The ECB is wrapping up the asset purchase programme in December and will not raise rates at least until the second half of 2019

As expected, **the ECB** at its meeting in June **announced that the asset purchase programme** (APP) **will be concluding in December** of this year given the progress towards a sustained adjustment of the inflation path, while at the same time **strengthening the anchoring of expectations regarding interest rates.**

The ECB reiterated that the bond purchase programme will remain active, at a monthly pace of €30 billion per month until September, and €15 billion between October and December, when the net purchases of assets will end. With regard to interest rates, the monetary authority is maintaining the reference rate at 0% and the deposit rate at -0.40% but announced that the reference rates will remain unchanged at least until the summer of 2019, which is longer than expected**.** In this context, our expectation of the first hike in interest rates is being delayed, with a **first increase of the deposit rate in September and the official reference rate in December 2019.**

In summary, the ECB at this meeting adopted important measures for the process of normalisation of its monetary policy. Once the end of the asset purchase programme has been approved, the phase of emergency measures will be **gradually closed in order to make way, once again, for a more conventional monetary policy, more focused on interest rates.** The focus in the coming months will be on knowing when and at what pace rates will rise.

World growth forecasts remain unchanged, supported by solid US growth despite the slowdown in other areas

The global forecasts for the next two years remain at 3.8% (see Figure 2.4). Nevertheless, the lower degree of synchronisation observed recently is reflected in a **downward revision in the growth expected for 2018-19 for both the Eurozone and South America** (mainly Argentina and Brazil), while we **maintain the forecasts for the coming years in US and China**, after recording a good economic performance in the first part of the year and with the fundamentals still being solid for domestic demand.

In the Eurozone, after the negative surprise in GDP growth in the first quarter, we now expect a faster convergence towards more moderate growth rates. In particular, we revised the growth forecast for 2018 downwards by 0.3 pp to 2%, while we continue to expect a moderation of the cyclical momentum in 2019, reaching 1.7%. This downward revision in the forecasts is mainly explained by lower trade and higher inflation (due to the rise in the price of oil), to which we must add the growing political uncertainty. However, despite the above, domestic demand will continue to contribute to growth both this year and next, supported by employment growth, a still accommodative monetary policy, and a slightly expansive fiscal policy.

The downside risks linked to political uncertainty, vulnerabilities in emerging economies and above all protectionism are intensifying

The global scenario continues to be subject to mostly negative risks, which in recent months have increased. On the one hand, **the risk of a trade war has intensified** in the wake of the latest measures adopted by the United States and the response from China, mainly, and to a lesser extent, the rest of the countries affected. Added to this are new protectionist threats that would involve the interests of important sectors in other regions, such as the automobile sector in Europe, Mexico, Canada or Japan. While the direct impact of the measures, as discussed above, would be limited, **the risk of a trade war could act as a drag on confidence, increase risk aversion in the markets and curb global flows of direct investment**, with the consequent impact on the potential of global growth.

In addition, **in a more volatile financial environment, systemic risk would increase in emerging economies**. The combination of a greater protectionist risk added to those posed by a more accelerated normalisation of monetary policy in the United States and a possible slowdown in the global economy could trigger the perception of risk in emerging financial markets, raising the likelihood of a *sudden-stop* of capital flows. In this context, the risk of an abrupt adjustment in the Chinese economy remains, since some measures to respond to a possible trade war could limit and delay the process of deleveraging and restructuring the Chinese economy.

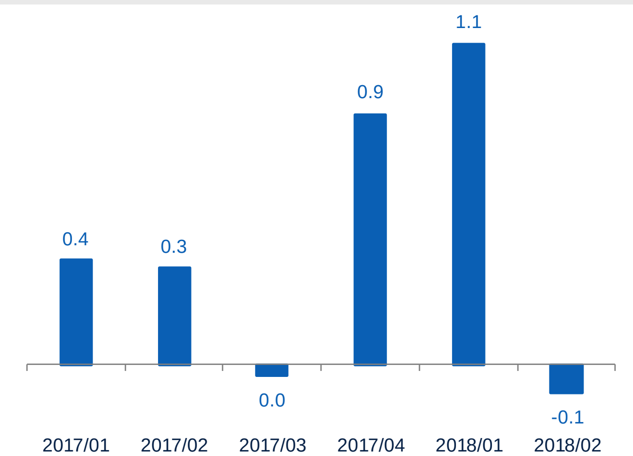
Lastly, **political risks in Europe have also intensified**. To the risks in Italy, we need to add those of governance in Germany, with potential direct consequences on the integration process of the Eurozone.

3. In the first half of the year the economy grew by 2.1% relative to the first half of 2017

In the first half of 2018 the economy grew at a YoY rate of 2.1%, below the clip of 3% observed last year. This modest performance arose from a mixed showing between the first two quarters of the year. At the March close economic activity benefited from the boost from the tertiary sector, construction, and electricity, water and gas supplies, which are sectors that showed signs of picking up, probably as a result of reconstruction work following the earthquakes and the re-establishment of supply activity for these services. In 1Q18, the tertiary sector posted a real YoY percentage change of 1.1%, thus keeping up the growth seen at the end of 2017, this being boosted by the professional and corporate services sector. In the same period secondary activities grew by 0.9% (vs. 02% in the previous quarter), driven by construction and electricity, water and gas supplies. Manufacturing failed to show any further growth progress (0%), while the mining sector reported a drop of -0.9%, which marks its third fall in a row in the past three quarters.

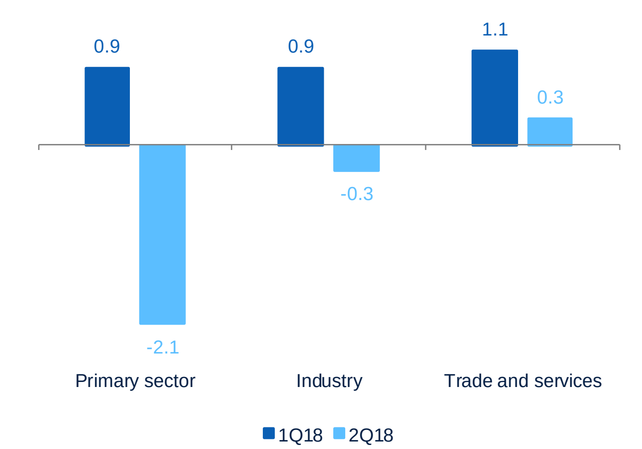
On the other hand, according to early INEGI figures, in 2Q18 the economy shrank by 0.1%, which represents a 1.2 pp difference compared with the figure reported in 1Q18. By components, primary activities showed the biggest dip, with a YoY percentage change of -2.1% (vs. 0.9% in the previous quarter), while the industrial sector contracted by -0.3% (vs. 0.9% in the previous quarter). The tertiary sector surprised on the low side, with only modest growth of 0.3%, which contrasts with the 1.1% growth seen in the first quarter of the year. While the primary sector performance is prone to higher volatility owing to the nature of its production, industry's less spirited showing is likely to be associated with a slowdown in the manufacturing sector and construction, as is evidenced by the manufacturers' orders indicator, which fell by an average of -0.4% in 2Q18 with respect to the previous quarter, and the aggregate trend indicator for the construction sector, which showed zero growth on average in 2Q18 compared with the previous quarter.

Figure 3.1 GDP (QoQ %, SA)



Source: BBVA Research / INEGI (National Institute of Statistics and Geography)

Figure 3.2 GDP by economic sector (QoQ %, SA)

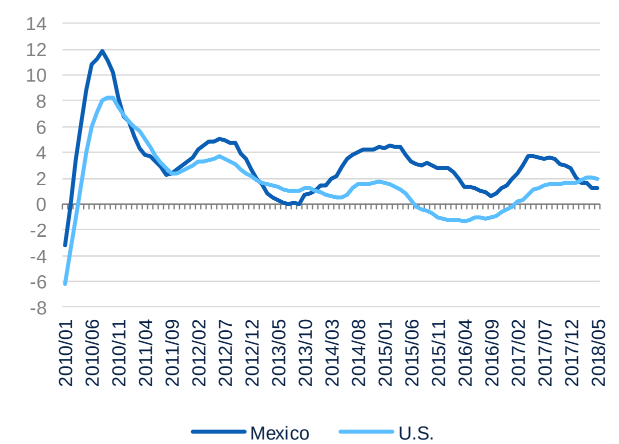


Source: BBVA Research / INEGI

Albeit to a limited extent, the slowdown in the manufacturing sector in 2Q18 is probably partly associated with the tariffs imposed by the United States on imports of steel (25%) and aluminium (10%), which, besides affecting Mexican companies geared to producing and exporting these raw materials, are likely to have an impact on economic activities linked to the same value chain. According to the Industrial Activity Indicator, in May basic metal industries showed the biggest reduction in growth within the secondary sector, surpassed only by the manufacture of petroleum and coal derivative products. In May the indicator for basic metal industries recorded a YoY percentage change of -2.4%, which represented a fall of 3.2 pp relative to April.

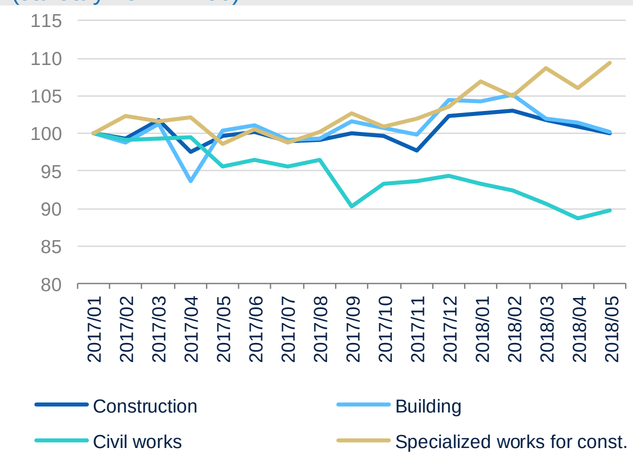
Although US manufacturing production has kept up a sound pace of growth in recent months, the figure for 2Q18 (0.5% QoQ), which is unchanged from the growth posted in 1Q18, points to a growth rate which, while still positive, is slowing. In the medium term US industry could report lower growth rates if the trade war which its government has begun becomes more intensive. As Figure 3 illustrates, the industrial sectors in the United States and Mexico are closely linked.

Figure 3.3 Manufacturing production index for the U.S. and Mexico (6-month moving average, MoM %, SA)



Source: BBVA Research / INEGI

Figure 3.4 Industrial Activity Indicator. Construction Sector (January 2017 = 100)



Source: BBVA Research / INEGI

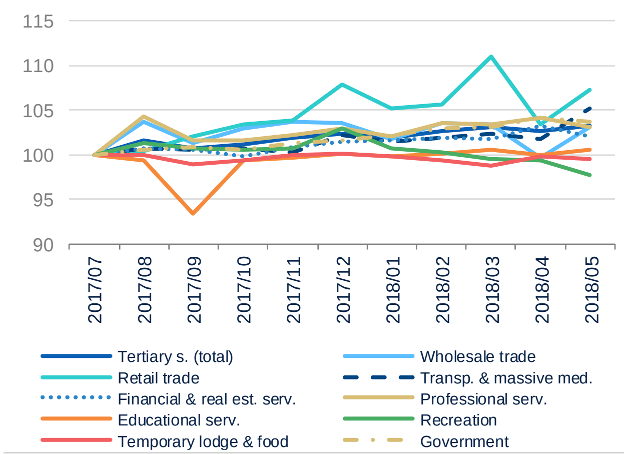
Moving to construction, the figures from the Industrial Activity Indicator suggest a weakening of the building work segment following an upturn in the first quarter of the year. Civil engineering work, for its part, continues to exhibit the poor performance it has put in since the second half of 2017. The specialist work for construction segment is the only one of the sector's components to have shown relatively steady growth since 3Q17, which is very possibly linked to the repair efforts after the September earthquakes. Over April and May the industrial activity indicator for the building work segment showed a fall of 3.8% relative to the first two months of the previous quarter (January-February), while the civil engineering segment showed a YoY percentage change of -3.9% in the same period (vs. -0.6% for the previous quarter). The indicator for specialist work for construction presented growth of 1.7% (vs. -4.5% the previous month).

For its part, the modest growth of the tertiary sector is very possibly attributable to less vigorous household spending bearing in mind the slowdown experienced by retail trade and leisure services in April and May (in cumulative terms). Over this period the IGAE (Global Economic Activity Index) for the retail sector showed zero growth (vs. 1.7% for January-February), while leisure, cultural and sports services exhibited a -1.9% decrease (vs. -0.1% in the previous quarter). Along with retail trade, wholesale trade also suffered a setback as it posted a YoY percentage change of -

1.3% in April-May (cumulative figure) vs. -0.6% for the first two months of the previous quarter. The other components of the tertiary sector continue to reflect a positive trend, and among these transport and mass media information services represent the segment with the biggest gain (putting in growth of 1.8% in the April-May period, vs. 1.2% in January-February).

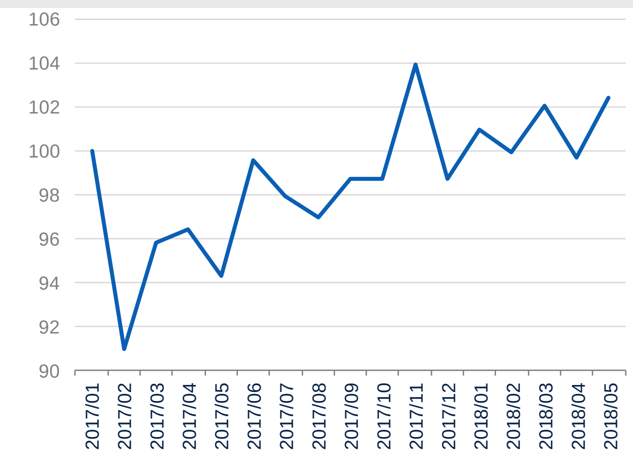
Lastly, the heavy fall for the primary sector in 2Q18 points to a negative performance by the agricultural and livestock sector in June, after growth of 2.7% in May, according to the IGAE for this segment. The low production level of this economic activity probably reflects the effects of the intense heat waves experienced in various Mexican states, which had an impact on crops and the output of dairy products. If adverse weather conditions continue, we could expect decreased agricultural and livestock activity in 3Q18 as well.

Figure 3.5 IGAE. Tertiary sector (July 2017 = 100)



Source: BBVA Research / INEGI

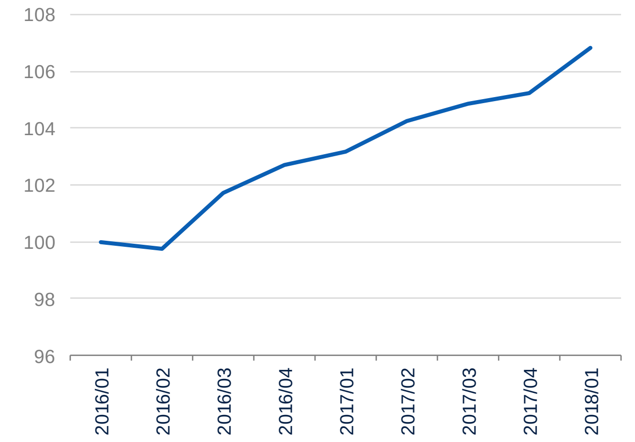
Figure 3.6 IGAE. Primary sector (January 2017 = 100)



Source: BBVA Research / INEGI

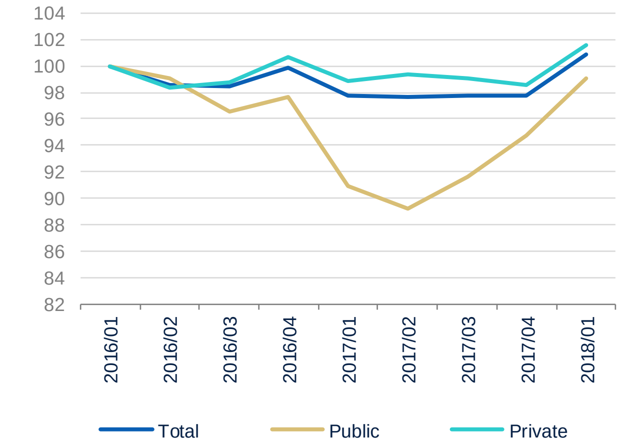
With regard to economic activity on the demand side, the main driver of growth continues to be private consumption (67% of GDP), which, according to the latest figure published by INEGI, grew by 1.5% in 1Q18 and therefore accounted for 60% of GDP growth in that quarter (1.1%, QoQ, SA). We expect real wages to recover over the rest of the year in a setting of lower inflation, albeit at a slower pace than was previously envisaged. Even though consumer confidence improved in July, the pattern of household spending could be affected in the coming quarters by a change in expectations in view of the uncertainty associated with the economic and social policies of the future administration, although the effect would only be temporary. Looking ahead, we expect private consumption to maintain positive growth rates and to consolidate growth in the second half of 2019, driven by greater purchasing power of households and companies deriving from lower inflation and certainty surrounding the accomplishment of NAFTA 2.0.

Figure 3.7 Private consumption (Index 1Q16 = 100, SA)



Source: BBVA Research / INEGI

Figure 3.8 Investment (Index 1Q16 = 100, SA)

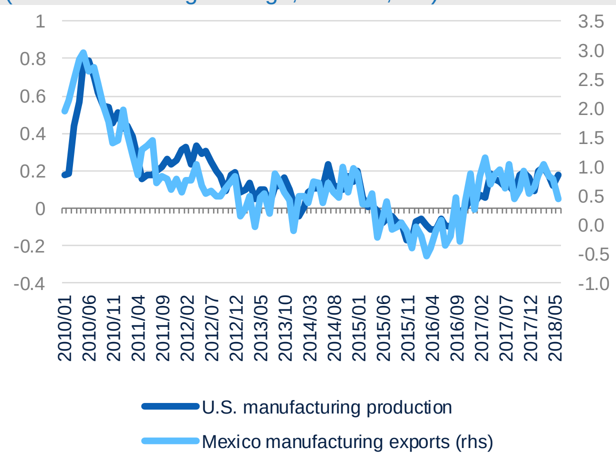


Source: BBVA Research / INEGI

Investment for its part (21% of GDP) surprised on the high side in 1Q18 by showing a YoY real growth rate of 3.2% (vs. 0% in the previous quarter), spurred by both of its private and public components (18% and 3% respectively of GDP). In 1Q18 private investment grew by 3%, marking a difference of 3.5 pp relative to the rate posted at the close of 2017, whereas public investment grew by 4.6%, representing a difference of 1.2 pp compared with 4Q17. According to the Gross Fixed Investment Indicator, investment in machinery and equipment was the most vigorous component in the first quarter of the year with a YoY percentage change reading of 2% (monthly average), while construction sector investment fell by -1% (monthly average) in the same quarter. The same indicator points to a weak start to 2Q18, with negative growth rates for both segments in April (-2.2% and -0.8% respectively). Added to this is the uncertainty over the renegotiation of NAFTA, which we suspect has prompted delays to the investment plans of many companies, especially those involved in the value chain of the automotive industry, which has a strong export orientation. We predict that the recovery of private investment will take place in the second half of 2019, assuming that the signing of the agreement is successfully concluded in the first quarter of the year. With respect to public investment, we expect less lively activity in 2H18 and increased growth towards the close of 2019 once investment projects begin to be implemented.

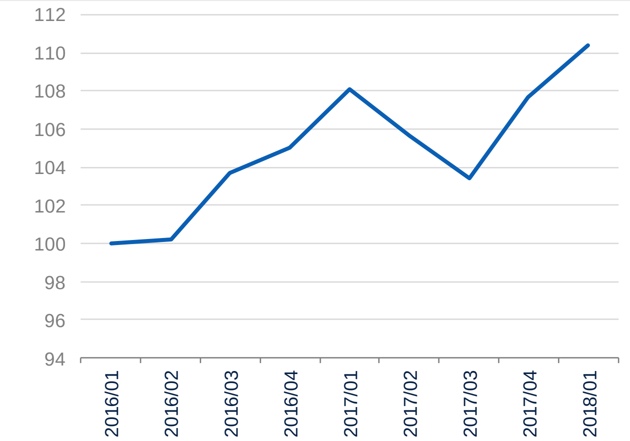
Turning to exports (36% of GDP), these kept up momentum in 1Q18, recording a YoY change of 2.5% in constant peso terms, while in dollar terms growth was 4%. Despite this, the balance of trade shows deterioration in 2018, particularly of both extractive and automotive industry exports. In 2Q18 automotive industry exports fell by -1.3% (vs. growth of 3.5% in 1Q), a figure which was accompanied by a drop of the same magnitude in exports by the extractive industries. It could be that exports by the latter industries have been hit by the steel and aluminium tariffs imposed by the US government, while the balance of automotive industry trade might be echoing the effects of the trade war declared by the Trump administration on China and the European Union. Although tariffs do not affect Mexico directly for the time being, they could have effects on manufacturing activity in the United States as a whole, which is the main destination for Mexican exports. As Figure 9 shows, Mexico’s manufacturing exports are closely linked to US manufacturing output. Although we foresee positive yet modest growth rates for the industrial sector in the United States, there is still a risk of a further deepening of the trade war in the United States, which would provoke a greater deterioration of the balance of trade in Mexico.

Figure 3.9 Index of US manufacturing output and Mexican manufacturing exports
(12-month moving average, MoM %, SA)



Source: BBVA Research / INEGI

Figure 3.10 Exports
(Index 1Q16 = 100, SA)



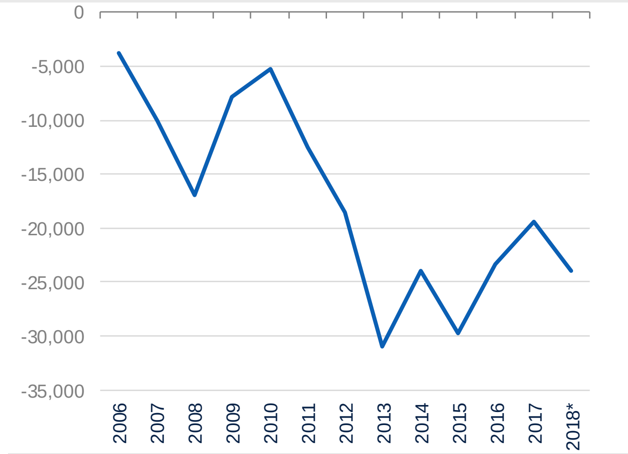
Source: BBVA Research / INEGI

Our growth forecast for 2018 is being held unchanged at 2.6% (SA), with downside bias stemming from the uncertainty generated by US trade policy, expectations associated with the mechanisms for implementing the new government's social and economic policies, and the adverse effects of the extreme weather conditions which agricultural and livestock production is having to face. We expect domestic consumption to continue to post positive changes, whereas investment will probably show some deterioration given the context of uncertainty, which we see being dispelled in the second half of 2019.

The current account deficit was significantly pared down in the first quarter of 2018 vs. the same period of the previous year, mainly due to the lower primary income deficit and the higher non-oil product surplus

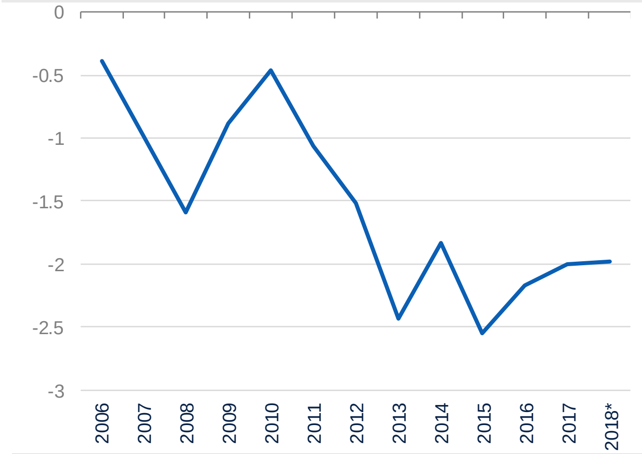
Having shown a reading of US$23.3 billion in 2016, the current account deficit narrowed to US$19.4 billion in 2017 (Figure 1). In terms of GDP, the current account deficit moved from 2.2% to 2% (Figure 2). The information for the first quarter of 2018 indicates that the current account deficit was US$ 6.9 billion, the annualised figure for which equates to 2.3% of GDP. For 2018 we predict that the current account deficit will be roughly US$24 billion, or 2% of GDP.

Figure 3.11 Current account (US$ millions)



* Forecast
Source: BBVA Research based on Banxico figures

Figure 3.12 Current account (% of GDP)



* Forecast
Source: BBVA Research based on Banxico figures

On analysing the behaviour of the current account deficit in the first quarter of 2018, we see that it grew relative to the figure from the fourth quarter of 2017 (Table 1). This is mainly due to a bigger primary income deficit.

Table 3.1 The current account and its components in the fourth quarter of 2017 and the first quarter of 2018 (US$ millions)

	Oct-Dec 17 (A)	Jan-Mar 18 (B)	Difference (B-A)
Current account	**-2,872**	**-6,941**	**-4,069**
Bal. on goods and services	-3,950	-3,492	458
Bal. on goods	-1.873	-1.814	59
Bal. on oil products	-5.046	-4.790	256
Bal. on non-oil goods	3.200	3.013	-187
Bal. on goods procured in ports by carriers	-27	-37	-10
Bal. on services	-2.076	-1.678	398
Bal. on primary income	-6.185	-10.245	-4.060
Bal. on secondary income	7.262	6.796	-466

Source: BBVA Research based on Banxico figures

Table 3.2 The current account and its components in January-March 2017 and 2018 (US$ millions)

	Jan-Mar 17 (A)	Jan-Mar 18 (B)	Difference (B-A)
Current account	**-10,384**	**-6,941**	**3,443**
Bal. on goods and services	-4.845	-3.492	1.353
Bal. on goods	-2.739	-1.814	925
Bal. on oil products	-4.372	-4.790	-418
Bal. on non-oil goods	1.601	3.013	1.412
Bal. on goods procured in ports by carriers	31	-37	-68
Bal. on services	-2.105	-1.678	427
Bal. on primary income	-12.029	-10.245	1.784
Bal. on secondary income	6.490	6.796	306

Source: BBVA Research based on Banxico figures

When we compare how the current account deficit performed in January-March 2018 vs. the same period in the previous year, we can see that its US$3.4 billion decrease is mainly due to the smaller primary income deficit as well as the larger non-oil product surplus (Table 2). The latter is substantially due to developments in connection with both the manufacturing trade deficit and the agricultural and livestock product trade surplus. In the first quarter of 2018, the former shrank by US$692.3 million, while the latter grew by US$500.5 million relative to the figures for the first quarter of 2017.

Public finances: total public sector revenue for the first half of 2018, excluding Banco de México's operating surplus from the previous year, registered a real YoY increase of 2.1%, while total net expenditure showed a real YoY rise of 4.9% in the same period

Total public sector budget revenue showed a real YoY decrease of 10.3% in the first six months of 2018. It is important to mention that this YoY comparison includes the amount of 321.7 billion pesos from the Banco de México operating surplus, which was transferred to the federal government in March 2017. If we excluded this component from budget revenue for January-June 2017, the real YoY increase would be 2.1%.

If we break down total budget revenue into components, non-tax revenue (including the federal government's oil revenue) showed a real YoY decrease of 46.7% in the January-June period of 2018. Excluding the central bank's operating surplus (transferred to the federal government in March 2017) would imply a decrease of 4.1% in this component in real YoY terms. On the other hand, there was a 1.1% real YoY increase in tax revenue in this period. Although VAT contributed 2.7 percentage points to the real YoY change in tax revenue, this positive contribution was frustrated by the 2.1 pp dampening effect on any tax revenue buoyancy of the excise tax (IEPS) on petrol (gasoline) and diesel. For its part, income tax (ISR) also made a positive contribution of 0.3 percentage points to tax revenue growth.

Income tax is an important component of tax revenue due to its weight in its overall structure (accounting for 56.3% in January-June 2018). Although income tax showed a real YoY change of 0.6% in this period, this compares unfavourably with real YoY growth of 3.2% observed in January-June 2017.

Table 3.3 Total public sector budget revenue in January-June (MXN billions)

	2017	2018	Real % ch.	Struc. %
Total	2,655.3	2,500.3	-10.3	100.0
Federal Government	2,128.4	1,927.1	-13.8	77.1
Tax	1,468.9	1,558.1	1.1	62.3
Income tax	830.5	876.8	0.6	35.1
VAT	400.0	460.9	9.8	18.4
Non-tax	659.5	369.0	-46.7	14.8
Budget controlled agencies and companies	174.8	191.7	4.5	7.7
State-owned productive enterprises	352.1	381.6	3.3	15.3
Pemex	182.0	210.3	10.1	8.4
CFE (state-owned electric utility)	170.1	171.3	-4.0	6.9
Total	2,655.3	2,500.3	-10.3	100.0
Oil revenue	417.2	475.7	8.7	19.0
Non-oil revenue	2,238.1	2,024.6	-13.8	81.0

Source: BBVA Research with SHCP (Secretariat of Finance and Public Credit) data

Table 3.4 Net public sector expenditure in January-June (MXN billions)

	2017	2018	% real ch.	Struc. %
Total	2,534.6	2,790.4	4.9	100.0
Projected expenditure	1,819.6	1,956.3	2.5	70.1
Current expenditure	1,439.3	1,616.4	7.0	57.9
Capital expenditure	380.3	339.9	-14.8	12.2
Non-projected	715.0	834.1	11.2	29.9
Funding for States	411.0	436.3	1.2	15.6
Borrowing Cost	279.6	331.7	13.1	11.9
Adefas* and other	24.4	66.1	158.5	2.4

* Spanish acronym for Debts from previous fiscal years
Source: BBVA Research with SHCP data

Public sector oil revenue accounted for 19% of total budget revenue in January-June 2018 (15.7% during the same period in 2017). It is important to note that this revenue item increased in YoY terms, with a real growth rate of 8.7% in January-June 2018.

As far as net public sector expenditure in January-June 2018 is concerned, this registered a real YoY rise of 4.9%. This was mainly due to non-projected expenditure (which represented 29.9% of total net public sector expenditure in January-June 2018), with a real YoY increase of 11.2% in the period. Within non-projected expenditure, debts from previous fiscal years and other expenditure showed a real YoY rise of 158.5%. At the same time the cost of borrowing showed a 13.1% increase in real YoY terms.

It is important to recognise that federal funding, public pensions, and the cost of public borrowing continued to place pressure on the public finances in January-June 2018. Nevertheless, our own calculations show that without financial investment and the expenditure items referred to, other expenditure saw a bigger rise, having shown a real YoY increase of 9.6% over the period.

The relatively greater YoY real increase experienced by this more limited expenditure item will imply an even greater effort on the part of the federal government to maintain a certain degree of financial discipline over the items that are more directly under its control. The federal government will have to step up its cost containment efforts in July-December 2018 to achieve its primary surplus target of 0.8% of GDP, particularly bearing in mind that the public finances have not been able to rely on support from Banxico's operating surplus on this occasion.

In the first half of 2018, the public sector's primary balance showed a total of 121.1 billion pesos vs. 412.9 billion in the same period of 2017. The primary surplus was largely due to the balance of institutions under indirect budgetary control as well as that of the IMSS (Mexican Social Security Institute). If the federal government's primary balance returns to a surplus and disciplined control of the finances of other state agencies and companies continues in July-December 2018, it will be possible to make the target of 0.8% of GDP for the primary surplus of the entire public sector achievable.

Table 3.5 Public sector expenditure indicators for January-June (MXN billions)

	2017	2018		
	Nominal	Nominal	Real	Real % ch.
Total net expenditure	2,534.6	2,790.4	2,659.2	4.9
Without financial investment	2,439.1	2,767.0	2,636.9	8.1
Without financial investment and state funding	2,028.1	2,330.7	2,221.1	9.5
Without financial investment, state funding and pensions	1,679.6	1,942.1	1,850.8	10.2
Without financial investment, state funding, pensions & cost of borrowing	1,399.9	1,610.4	1,534.7	9.6

Source: BBVA Research with SHCP data

Table 3.6 Financial position of the public sector in January-June (MXN billions)

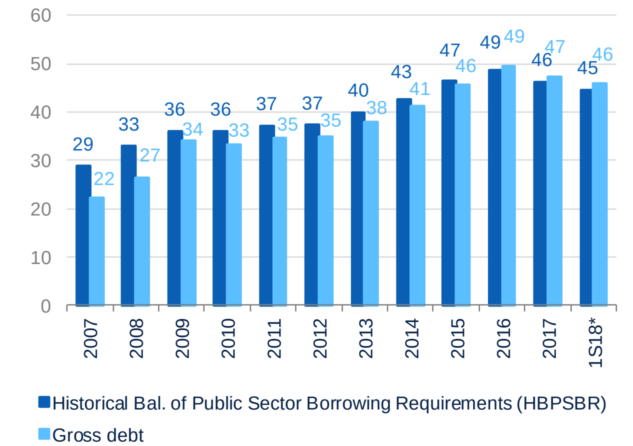
	2017	2018	% real ch.
Public balance	141.9	-206.7	n.s.
Public bal. w/o prod. investment	318.4	107.1	-67.9
Budget balance	120.7	-290.1	n.s.
Budget revenue	2,655.3	2,500.3	-10.3
Net budget expenditure	2,534.6	2,790.4	4.9
Federal Government balance	105.1	-276.1	n.s.
Agencies and companies balance	15.6	-14.0	n.s.
Primary balance	412.9	121.1	-72.1
Budget balance	400.3	41.6	-90.1
Federal Government	319.6	-24.1	n.s.
Agencies and companies	80.7	65.7	-22.5
Pemex	-18.3	19.4	n.s.
Other institutions	99.0	46.3	-55.4
Indirectly-controlled institutions	12.6	79.5	501.8

n.s.: not significant
Source: BBVA Research with SHCP data

Gross public debt stood at 45.9% of GDP at the close of June 2018. The debt level is 1.3 percentage points lower than the ratio of public debt to GDP seen at the close of 2017. As regards the proportions of the domestic and external components in this debt, external debt moved from 37.3% in 2017 to 37.5% at the close of June 2018.

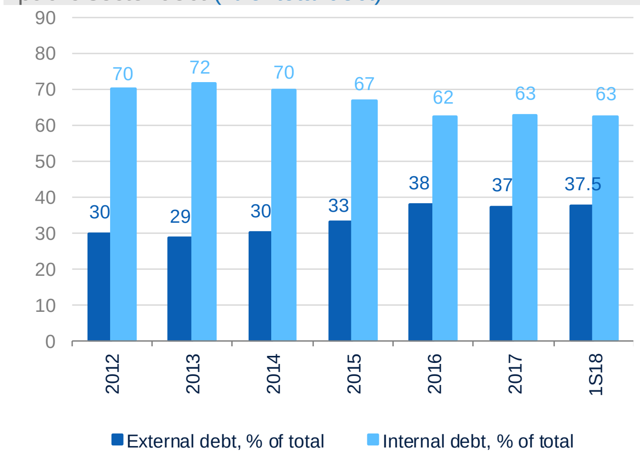
At the end of June 2018, the Historical Balance of Public Sector Borrowing Requirements (HBPSBR) was 15.8 pp of GDP higher than its level in 2007. This broad indicator of public debt stood at 44.6% and 46.2% of GDP at the end of June 2018 and December 2017 respectively.

Figure 3.13 Gross debt and the balance of public sector borrowing requirements* (% of GDP)



* To calculate the HBPSBR (Historical Balance of Public Sector Borrowing Requirements) and public debt we have used the SHCP's nominal GDP forecast for 2018.
Source: BBVA Research with SHCP data

Figure 3.14 Percentage structure of internal and external public sector debt (% of total debt)

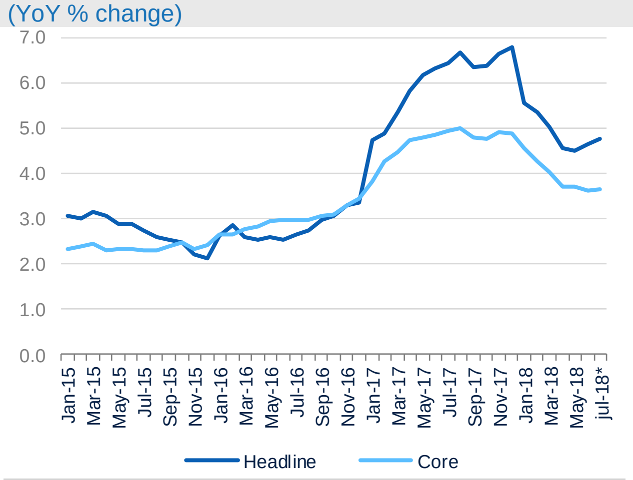


Source: BBVA Research with SHCP data

4. Inflation: abating in 2018, the spike in June-July will be only temporary

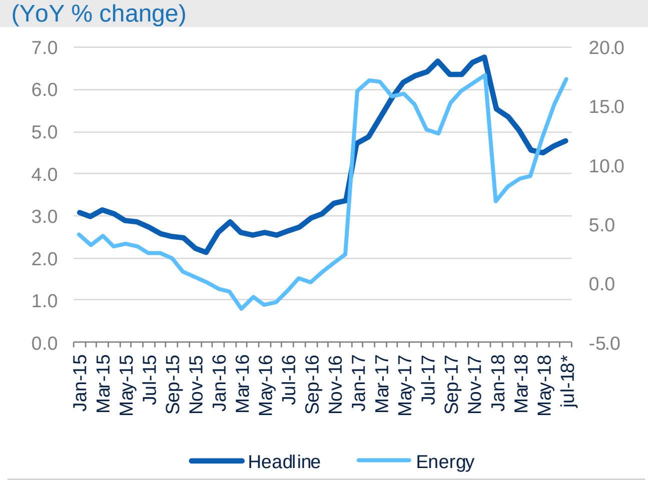
In line with our forecast, inflation eased significantly in the opening months of the year. After closing 2017 at 6.77%, the highest year-end figure since 2000, in January alone headline inflation came down to 5.55% and maintained its downward trend over the first five months of the year. Having averaged 6.59% in the fourth quarter of 2017, it averaged 5.31% in 1Q18 and 4.57% in 2Q18. This fall came as no surprise. As had been expected, the effect of the January 2017 increases in energy prices (mainly petrol (gasoline)) faded, as did the impact of the greater rate of exchange rate pass-through to core inflation, mainly during the first half of 2017 (see Figure 4.1). Nonetheless, in May headline inflation fell by less than we were predicting and from June it returned to an upward path which, due to its nature, we envisage as being only temporary. This rise originated from bigger than expected upturns in energy prices, mainly those of petrol (gasoline) and liquefied petroleum gas (LPG), which was reflected in substantial increases in non-core inflation that led to the aforementioned rebound in headline inflation (see Figure 4.2).

Figure 4.1. Headline and core inflation*
(YoY % change)



* The July figure is a forecast but is based on data available for the first half of the month.
Source: BBVA Research / INEGI

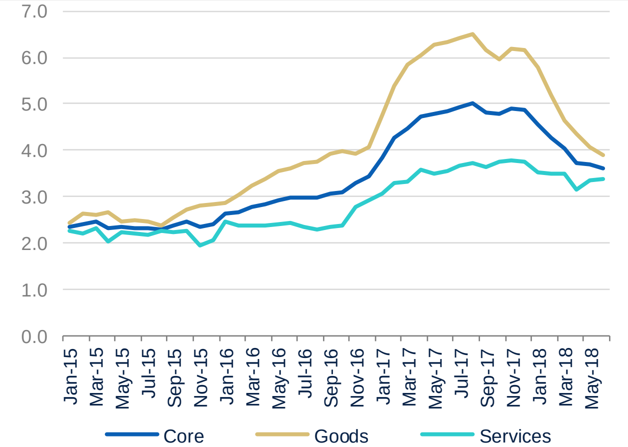
Figure 4.2. Headline and energy price inflation*
(YoY % change)



* The July figure is a forecast but is based on data available for the first half of the month.
Source: BBVA Research / INEGI

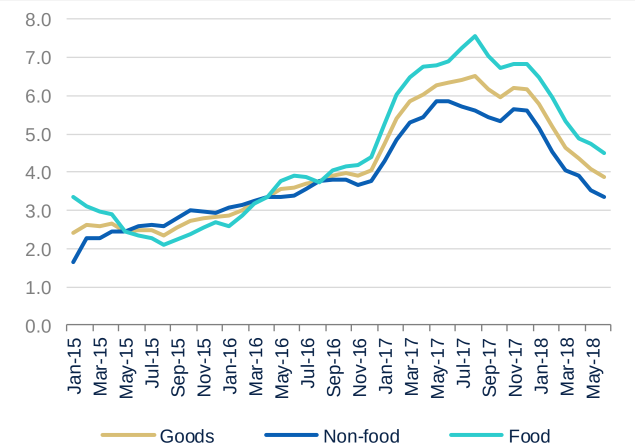
This change in relative prices has not affected core inflation, which continues to behave well and remains on a downward trend. Having averaged 4.85% in the fourth quarter of 2017, YoY core inflation fell to averages of 4.29% in 1Q18 and 3.67% in 2Q18. The favourable performance of core inflation is across the board (see Figure 4.3). Within core inflation, the goods index shed 2.3 percentage points between December 2017 and June 2018 (from 6.17% to 3.88%). Over the same period services inflation eased by 0.4 pp (moving from 3.76% to 3.38%). Looking more closely at goods inflation, both of its sub-indices have come down significantly as expected in 2018 as the effect of the greater rate of exchange rate pass-through to goods has worn off (see Figure 4.4). The foods sub-index eased from 6.82% in December 2017 to 4.49% in June, while the non-food goods sub-index fell by 2.3 pp (from 5.62% to 3.36%).

Figure 4.3. Core inflation and components
(YoY % change)



Source: BBVA Research / INEGI

Figure 4.4 Core goods inflation and components
(YoY % change)



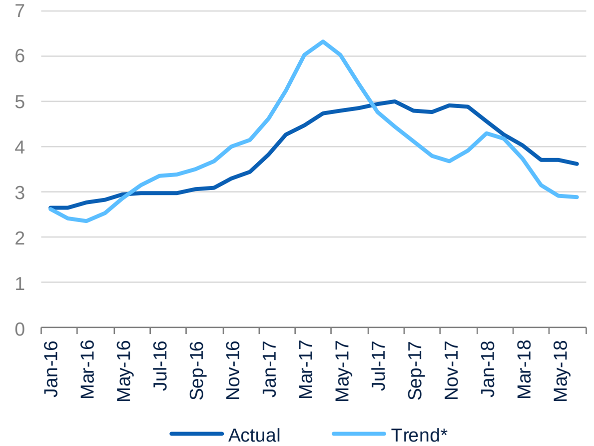
Source: BBVA Research / INEGI

A slower pace of approach to the 3% target

Headline inflation's recent upturn (i.e. in June-July) was in the main driven by surging energy prices. Core inflation is still charting a downward course. Going forward, it appears inevitable that this change in relative prices on account of the above-mentioned supply shocks will affect the speed at which inflation moves towards its target level. Although we expect the effect to be temporary, we also foresee headline inflation rising to 4.8% in July and showing some downside stickiness in August-October, when we anticipate that it will average 4.6%. For the last two months of the year we predict a major new fall, given that YoY inflation will benefit from two base effects in the shape of the substantial upturn in LPG prices late in 2017 and high core inflation over those same months. We thus expect inflation to end the year at a shade over 4% (at 4.1%). This means that inflation will definitively reach the 3% target at a slower pace than was thought three months ago, when we were forecasting that it might end the year at slightly under 4% (at 3.8%).

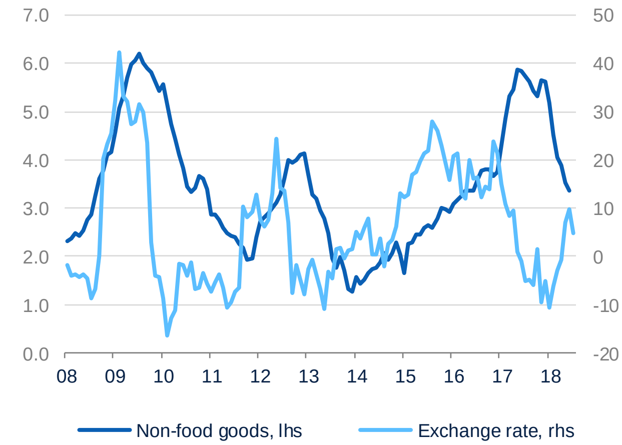
In contrast with this, as regards core inflation we still foresee an unbroken falling trend. Our projections suggest that core inflation is likely to settle at around 3.6% in the short term, before declining even further in the last two months of the year, reaching 3.4% at year-end. The significant weakening of the MXN that we saw between mid-April and the end of June ramped up the risks of a new round of pass-through, but July's marked improvement in the prospects for NAFTA 2.0 reducing these risks. Thus far the peso's weakness has not affected trends in goods inflation (see Figure 4.6) and its stronger performance of late is reducing the risk of this happening in the next few months.

Figure 4.5 Core inflation: actual and trend*
(YoY % change and annualised QoQ % change)



* Own calculations based on seasonal adjustment of the core inflation index.
Source: BBVA Research / INEGI

Figure 4.6 Non-food goods inflation and the exchange rate
(YoY % change)



Source: BBVA Research / INEGI

The risks for inflation continue to have upside bias, yet they are abating

Our inflation forecasts are subject to risks to both the downside and the upside, and on balance they still have upside bias, although these risks have been tempered by the recent strengthening of the peso and the brighter outlook for NAFTA, which suggests that the firmer peso could be an enduring phenomenon and we might even see further appreciation if the outcome is favourable.

Even so, there is still an underlying risk of a new bout of peso weakness, which could stem from either new setbacks in the process of renegotiating NAFTA or a potentially faster than expected pace in federal fund rate hikes with an impact on the valuation of risk assets. By the same token there is still a risk of supply shocks continuing to affect energy prices or of agricultural and livestock prices rising further than expected. The chief downside risk is of additional peso appreciation. All in all, even though risks have subsided, primarily due to a better performance by the peso in terms of both its observed and expected showing, they still have upside bias.

Monetary policy: on pause for the rest of the year

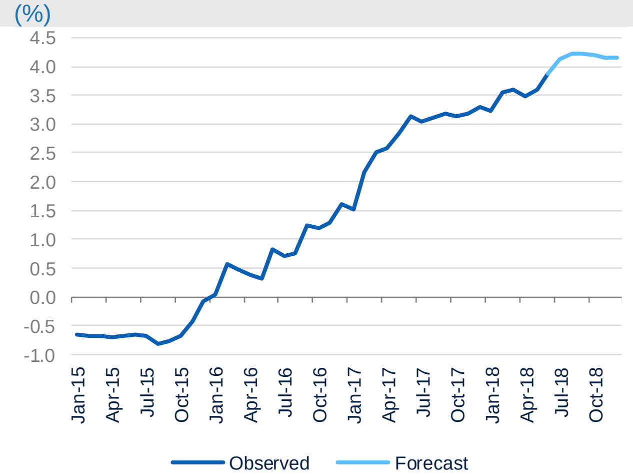
After two 25 bp hikes in the reference rate at the monetary policy meetings in February and June, at its last meeting (on 2 August) Banxico's governing board unanimously decided to hold the rate unchanged at 7.75%. Although Banxico is being cautious, the tone of its statement still being hawkish, and the door being left open to fresh hikes if necessary (monetary policy will be adjusted "in a timely and firm manner"), the tone of the latest statement is less restrictive than it has been on previous occasions and shows signs that, in the absence of any further decline in the balance of risks for inflation, a monetary pause is the most likely scenario in the coming quarters.

In particular, three changes in the statement suggest that there will be no further rate hikes over the rest of the year in the present context: i) despite the recent rally in headline inflation and expectations of a slower pace of movement towards the target level, Banxico signalled that inflation risks continue to have upside bias on balance, yet it omitted to make any mention of a deterioration in such risks as it had done in June, when it decided on a 25 bp hike; ii) the statement acknowledges the worse risk situation on balance for growth in a context in which the real rate is restrictive; and iii) the statement stresses that the recent upturn in inflation will be only temporary and that “the expected trend for core inflation remains downwards”. In short, Banxico is comfortable with both the current level of the reference rate and recent developments in inflation in spite of the temporary spike in headline inflation.

Moreover, the recent hardening of the peso given the improvement in prospects for NAFTA 2.0 should also contribute to a lowering of expectations of inflation from market measures, which have recently increased. Meanwhile the slight rise in long term inflation expectations on the part of analysts could be short-lived if we are right and inflation does not increase further after July. We still think that developments for the peso (MXN) will continue to be a key factor in future decisions. If, as we expect, the MXN does not weaken over the remainder of the year, we consider a further rise in rates to be unlikely, even if possible supply shocks slow down the pace at which inflation draws close to the 3% target even more. If the promising tone of NAFTA negotiations continues, the MXN will consolidate its recent appreciation. A positive outcome would lead to further strengthening. On the other hand, if negotiations become difficult again, a potential significant weakening of the MXN would re-open the door to possible additional rate hikes. We view the first scenario as the more likely and for that reason we see the rate holding at 7.75% over the rest of the year.

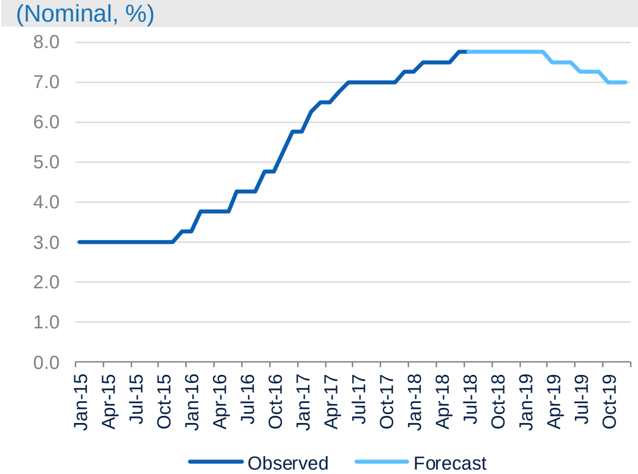
Moreover, the two rate hikes already seen this year have taken the real rate to a restrictive level (see Figure 4.7). We predict that with a nominal rate at 7.75% over the rest of the year, the ex-ante real rate will be at over 4% on average, which is a high level by historical standards and significantly higher than a neutral rate of 2%. In a context where we expect inflation to return to a falling trend, and assuming that the spread between Mexican and US rates will remain large, we would expect a sustained pause, which might run to the next three quarters. In 2019, with inflation at levels below 4% and gradually drawing close to the target, Banxico will be able to calmly consider a gradual adjustment of the policy rate to its neutral level (around 5.5%). We therefore foresee a 75 bp cut in the policy rate to 7% in 2019. This scenario is based not only on our forecasts for inflation, but also on the assumption that NAFTA will not collapse, which remains the chief risk to our scenario.

Figure 4.7 Ex ante real rate*
(%)



* Own calculations based on 12-month inflation expectations from the Banxico analysts’ survey and using our inflation expectations for projected data.
Source: BBVA Research / INEGI / Banxico

Figure 4.8 BBVA Research outlook for the MPR
(Nominal, %)



Source: BBVA Research / Banxico

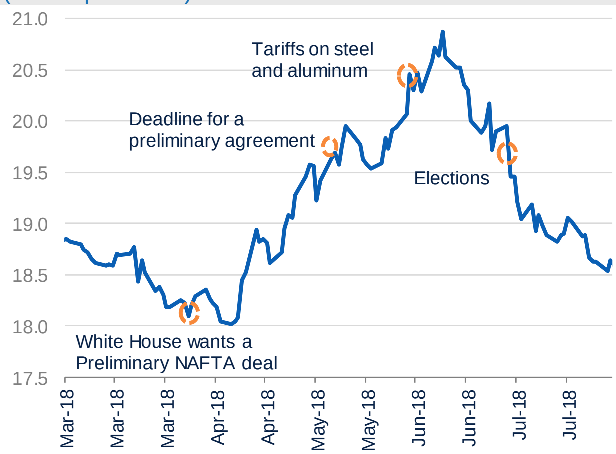
5. The easing of global trade tensions paves the way for gains for domestic assets given the temporary reduction in idiosyncratic risks

In recent months global financial asset prices have for the most part been influenced by two factors. Firstly the switch from growth which has been virtually across-the-board among the world's regions to one dominated by the US economy which reinforces the divergence among the monetary cycles of the major central banks. The most recent economic activity data suggests that the pace of growth in Europe and Asia has slackened relative to expectations at the beginning of the year, whereas the United States continues to show a labour market close to full employment that underpins quarterly growth rates of over 4%. This has prompted a shift in investment flows into US assets, particularly the dollar, given prospects of bigger returns. The second factor is the escalation of trade tensions. Investors are trying to weigh up to what extent the imposition of tariff measures (especially between the United States and China) are jeopardising world economic growth, and it is during this mulling process that several bouts of risk aversion have been prompted.

On top of the impact from this global environment, Mexican assets have been influenced by developments in renegotiating NAFTA and the election process, the two idiosyncratic risks that affect the national economy. It is actually instructive to trace the exchange rate performance in recent months, as this to a great extent reflects the changing presence of the above-mentioned factors. After the Trump administration sought a swift preliminary trade agreement in April so that it could be approved by the current Congress with a Republican majority, the issues surrounding the rules of origin for the automotive industry and the question of the sunset clause once again obstructed negotiations to the point where, in mid-May, the trade representatives of the three countries declared that it would not be possible to reach an agreement in the short term. Given these ups and downs for expectations regarding the trade agreement, the exchange rate moved within a range of 18 pesos per dollar (ppd), its lowest level in the year, to 19.9 ppd. After this new failure to reach agreement in the NAFTA negotiations, the Trump administration announced the imposition of tariffs on steel and aluminium imports, whereupon the peso saw further depreciation and, with an intensification of the trade dispute between China and the United States, the dollar hit a high for the year of MXN 20.88 on 14 June. Here it should be noted that all of this process of currency depreciation took place in an orderly manner in terms of liquidity.

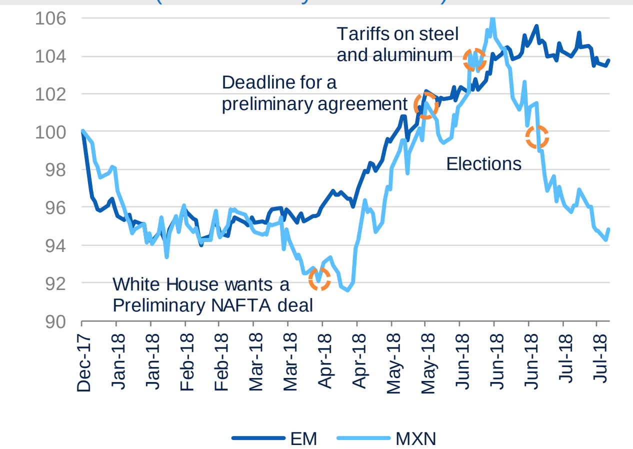
And just as intensification of these factors gave rise to depreciation, the easing of trade tensions worldwide began with a period of appreciation which became more pronounced given a favourable reaction by the markets to the conciliatory stance of Andrés Manuel López Obrador (AMLO) after he emerged as the clear winner in the presidential elections. Indeed, in initial speeches by AMLO and his team of associates they laid emphasis on fiscal discipline as well as respect for the independence of the central bank and free enterprise. Even though it remains unclear how these statements will be reconciled with his social welfare programmes which were the centrepiece of his election campaign, the markets seem to have given him the benefit of the doubt, with the result that in the short term one of the idiosyncratic risks for the country has been neutralised. In terms of magnitudes, the day before the election the exchange rate stood at 19.90 pesos to the dollar, while a couple of weeks afterwards the dollar was priced at MXN 18.88, making the peso the currency that appreciated the most in the first half of July. Essentially, in a more helpful environment on account of a relaxing of global trade tensions, the swift resolution of the election process and the prudent stance exhibited by the winning candidate produced a positive change for Mexico's currency. Towards the end of July renewed optimism over the renegotiation of NAFTA took the dollar to below 18.60 pesos, yet so far this appreciation does not seem to have any basis in tangible progress at the negotiating table.

Figure 5.1 Exchange rate
(Pesos per dollar)



Source: BBVA Research based on Bloomberg data

Figure 5.2 Emerging market currencies and Mexican peso vs. the dollar (Index January 2018 = 100)



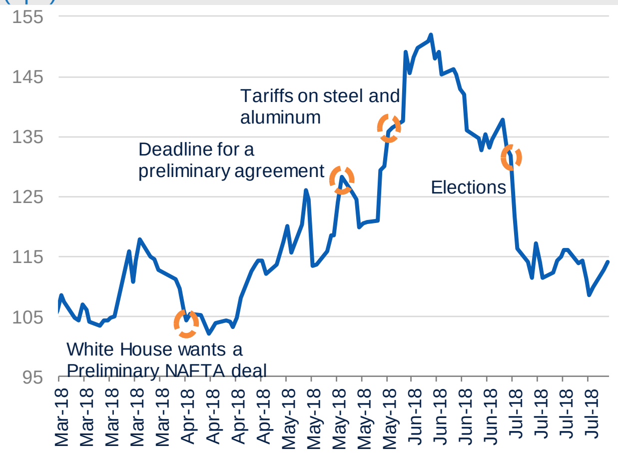
Source: BBVA Research based on Bloomberg data

The observed exchange performance was replicated in a substantial portion of market variables: Sovereign risk as measured by the spread of the 5-year CDS moved from 105 basis points (bps) at the beginning of April to 152 bps on 12 June, before ending July at around 114 bps after the risks abated. These movements in sovereign risk influenced movements in long-term interest rates. The yield to maturity of the 10-year M-bond peaked in mid-June, when it touched 8%, then shrank back to 7.76% in late July.

One variable which was notable for its performance over this recent period of volatility was foreign-held medium and long term bonds. Even given the uncertainty associated with renegotiation of NAFTA and the election, flows into bonds have stayed in positive territory since March after falling off slightly at the beginning of the year. Although there were dips in holdings in reaction to escalating trade tensions and in line with outflows from most emerging markets, the recovery in the last two weeks was enough for the change in holdings to marginally top US$1 billion at the end of the month. This performance becomes more significant if we bear in mind that, from March onwards practically, there have been outflows from emerging markets on the back of the rise in yields in the United States and greater risk aversion due to trade uncertainty. The fact is that, given Banxico’s restrictive policy and the recent reduction in both the implied volatility of the Mexican peso and the country risk, Mexico is managing to maintain attractive risk-weighted yields compared with its peers, which has meant that foreign-held M-bond holdings have risen by almost a cumulative US$4 billion in the first half of the year.

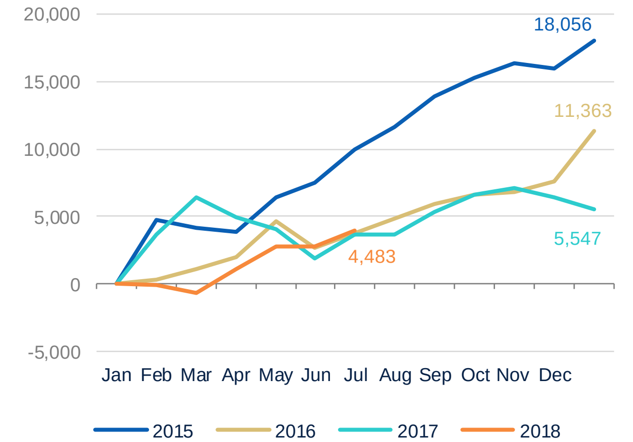
To summarise, the idiosyncratic risks that have been influential on domestic asset prices over a good part of the year have gone into a latent phase due to the absence of substantial progress in the renegotiation of NAFTA and the “benefit of the doubt” which the markets have given to the new government. Even so it is global factors that are expected to have the greatest influence in the coming months, above all the question of trade tensions. And in that regard we will have to monitor particularly closely the potential imposition of a 10% to 25% tariff on car imports by the United States, which would deal a serious blow to the Mexican automotive industry and could be used as a means of exerting pressure in the NAFTA negotiations. Taking these elements into account we expect the exchange rate to stand at around 18.80 pesos to the dollar at the end of the year and the yield to maturity of the 10-year M-bond to close 2018 at around 7.75%.

Figure 5.3. Sovereign risk. 5-year CDS spread (bps)



Source: BBVA Research based on Bloomberg data

Figure 5.4 Cumulative change in foreign-held M-bonds (USD million)



Source: BBVA Research based on Banxico figures

6. Indicators and forecasts

Table 6.1 Macroeconomic forecasts: Gross Domestic Product

	2015	2016	2017	2018	2019
United States	2.9	1.6	2.2	2.8	2.8
EMU	2.0	1.8	2.6	2.0	1.7
Germany	1.5	1.9	2.5	1.9	1.7
France	1.0	1.1	2.3	1.8	1.6
Italy	0.8	1.0	1.6	1.1	1.2
Spain	3.4	3.3	3.1	2.9	2.5
UK	2.3	1.8	1.7	1.3	1.4
Latin America*	-0.1	-1.0	1.2	1.4	2.1
Mexico	3.3	2.6	2.3	2.6	2.0
Brazil	-3.5	-3.5	1.0	1.6	2.4
Eagles**	4.8	5.2	5.5	5.4	5.3
Turkey	6.1	3.2	7.4	3.8	3.0
Asia-Pacific	5.7	5.7	5.7	5.5	5.5
Japan	1.4	1.0	1.7	1.0	1.2
China	6.9	6.7	6.9	6.3	6.0
Asia (exc. China)	4.6	4.7	4.6	4.8	5.0
World	3.4	3.3	3.8	3.8	3.8

* Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
** Bangladesh, Brazil, China, Egypt, Philippines, India, Indonesia, Iran, Malaysia, Mexico, Nigeria, Pakistan, Russia, Turkey and Vietnam.
Forecasts closing date: 13 July 2018.
Source: BBVA Research & IMF

Table 6.2 United States indicators and forecasts

	2016	2017	2018	2019	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
Real growth (%)	1.6	2.2	2.8	2.8	2.2	4.1	2.9	3.1	3.0	2.3	2.4	2.5
Personal consumption (real % change)	2.7	2.5	2.7	2.6	0.5	4.0	3.4	3.2	2.2	2.2	2.2	2.1
Govmnt. consumption (real % change)	1.4	-0.1	1.4	1.6	1.5	2.1	1.6	1.7	1.4	1.8	1.2	1.2
Gross fixed investment (real % change)	-1.3	4.8	4.2	4.6	9.6	-0.5	1.8	2.5	8.0	4.9	5.1	5.7
Construction[1]	6.5	3.3	1.1	4.3	-3.4	-1.0	3.4	3.4	5.8	5.3	4.4	4.5
Industrial prod. (real annual % change)	-2.0	1.6	3.7	2.6	2.3	5.9	2.8	2.0	2.6	2.5	2.3	1.8
Current account balance (% of GDP)	-2.3	-2.3	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5	-2.6	-2.6	-2.6
Final annual inflation	2.1	2.1	2.7	2.6	2.5	2.4	3.3	2.5	2.0	3.1	4.2	1.4
Average annual inflation	1.3	2.1	2.6	2.7	3.5	1.7	3.3	2.5	2.2	2.4	4.8	1.5
Primary fiscal balance[2] (% of GDP)	-3.1	-3.4	-3.9	-4.6	-4.7	-4.6	-4.1	-4.2	-4.5	-4.6	-4.6	-4.8

1: Residential investment
2: Fiscal balance (% of GDP)
Source: BBVA Research

Table 6.3 Mexico indicators and forecasts

	2016	2017	2018	2019	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
GDP (seasonally-adjusted)												
Real annual % change	2.6	2.3	2.6	2.0	2.3	1.9	3.0	3.0	2.1	2.6	1.9	1.5
Per inhabitant (US dollars)	8,790	9,356	9,608	10,392	9,893	9,578	9,308	9,850	10,100	10,122	10,656	11,304
US$ billions	1,075	1,156	1,198	1,308	1,227	1,188	1,155	1,222	1,253	1,256	1,322	1,402
Inflation (average, %)												
Headline	2.82	6.04	4.72	3.83	5.31	4.57	4.68	4.33	4.11	4.05	3.55	3.59
Core	2.97	4.68	3.77	3.44	4.29	3.67	3.64	3.49	3.43	3.50	3.47	3.36
Financial Markets (eop, %)												
Interest rates												
Bank funding	4.29	6.75	7.63	7.38	7.42	7.58	7.75	7.75	7.75	7.50	7.25	7.00
28-day Cetes	4.33	6.69	7.59	7.34	7.37	7.56	7.72	7.72	7.72	7.47	7.22	6.97
28-day TIIE	4.58	7.06	7.96	7.71	7.75	7.93	8.09	8.09	8.09	7.84	7.59	7.34
10-year Bond (%, average)	6.22	7.18	7.56	7.38	7.59	7.66	7.89	7.77	7.71	7.68	7.54	7.42
Exchange rate (average)												
Pesos per dollar	18.7	18.8	18.9	17.8	18.7	19.4	19.1	18.6	18.9	18.9	18.2	17.9
Public Finances												
FRPS (% of GDP)	-2.8	-1.1	-2.5	-2.5				-2.5				-2.5
External Sector[1]												
Trade balance (US$ billions)	-13.1	-10.9	-12.8	-16.3	-1.8	-2.8	-6.1	-2.2	-3.8	-2.2	-7.6	-2.7
Current account (US$ billions)	-22.7	-18.8	-24.0	-25.5	-6.9	-3.7	-5.6	-7.8	-7.7	-3.8	-5.8	-8.1
Current account (% of GDP)	-2.2	-1.9	-2.0	-1.9	-2.3	-1.3	-1.9	-2.5	-2.5	-1.2	-1.8	-2.3
Employment												
Formal Private (annual % chge.)	3.8	4.4	4.2	2.6	4.4	4.3	4.2	3.8	3.2	2.8	2.3	1.9
OUR (% active population)	3.9	3.4	3.4	3.8	3.1	3.1	3.5	3.6	3.8	3.8	3.8	3.8

1: Accumulated, last 12 months
FRPS: Financial Requirements of the Public Sector
OUR: Open Unemployment Rate
Source: BBVA Research with Banxico, INEGI & SHCP data

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