

Economic Watch

Mexico

May 30, 2011

Economic Analysis

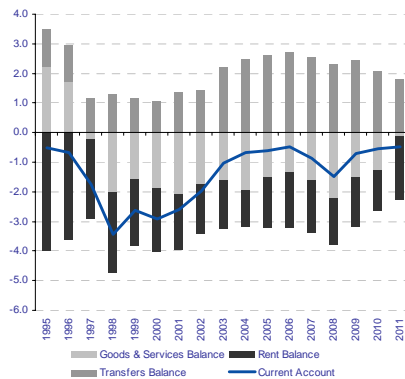
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Limited trade deficit, a sign of limited demand pressure and no excessive strengthening of the exchange rate

Balance of payments 1Q11

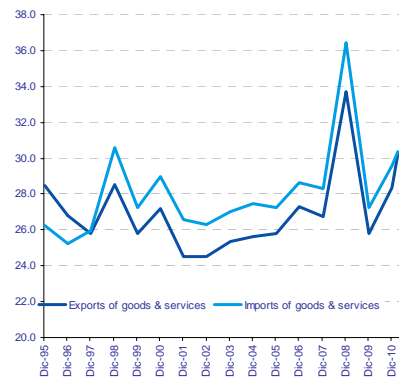
- The Current Account recorded a deficit of -1.375 millions of dollars (md) around -0.5% of GDP, thanks to a quicker recovery in foreign over domestic demand.
- Trade in goods continued to increase to high rates while overseas trade in services slowed.
- The Financial Account saw a surplus of 13.842 md (4.8% of GDP) thanks to portfolio investment driven by high global liquidity.

Chart 1
Current Account and Components (% of GDP, 2011=1Q11)



Source: BBVA Research with Banxico data

Chart 2
Exports & Imports of goods and services (% of GDP)



Source: BBVA Research with Banxico data

The Current Account in the first quarter saw a 1.376 md deficit (0.5% of GDP) comprising a surplus in the balance of goods of 2.018 md, a deficit in the balance of services of -2.339 md, a deficit in the income balance of -6.124 md and a surplus in the transfer balance of 5.069 md. The Current Account deficit can easily be financed with the Capital Account which saw a 13.842 md surplus thanks to positive FDI net inflows of 4.242 md, portfolio investment of 9.425 md and other investment of 175 md. The gross international reserves ended the period with a balance of 128.261 million dollars.

The Current Account balance was affected in the 1Q11 by the continuing recovery in the US economy, supporting export increases of 22.8%, imports of 20.6% and remittances of 5.5%. With regard to the exchange of services, income fell by 7.1% due to reductions in tourist and traveler inflows of -8.9% and 9.9% respectively. This performance may be due to the higher exchange rate (making Mexico more expensive for foreigners) and the slow recovery in foreign demand.

In a setting where the global economy continues to recover and there is abundant global liquidity thanks to an expansive monetary policy in developed economies, the financial account showed easy financing of the overseas deficit with FDI; additionally portfolio inflows continued, especially in the local public debt market taking advantage of the rates differential, this scenario meant international reserves continued to rise. In the 1Q11, FDI to Mexico saw inflows of 4.788 md, an 8% y/y fall. However, the net FDI balance increased 72.2% since Mexican investment overseas fell by -80.1%.

Conclusion: the Mexican economy continues to show a wide margin in the overseas sector thanks to domestic demand still not having sufficient strength for imports to rise enough to increase the trade deficit. In addition, global liquidity conditions and confidence in the country are being used advantageously with major portfolio investment inflows being received; this has driven up the exchange rate but, until now, the competitiveness of goods exports has not been affected. Although portfolio investment inflows will surely reverse somewhat and the currency might fall when global liquidity gradually dissipates, this should not be a problem for the country and, in any case, could lead to an underpinning of the export sector when recovery in domestic demand takes a leap forward.

Table 1

Current Account (md and % of GDP)

| | 2010 millions of dollars (md) | | | | 2010 % of GDP | 2011 md | 2011 % of GDP |
|--------------------------|-------------------------------|----------|----------|----------|---------------|----------|---------------|
| | 1Q10 | 2Q10 | 3Q10 | 4Q10 | | | |
| Current Account | 436.0 | -702.7 | -1,869.1 | -3,490.5 | -0.5 | -1,375.9 | -0.5 |
| Goods & Services Balance | -964.4 | -2,746.2 | -5,353.0 | -4,103.9 | -1.3 | -320.8 | -0.1 |
| Goods | 324.9 | -101.5 | -2,201.1 | -982.2 | -0.3 | 2,017.9 | 0.7 |
| Merchandise | 371.9 | -83.4 | -2,251.1 | -1,046.0 | -0.3 | 1,910.5 | 0.7 |
| Exports | 66,596.6 | 74,641.4 | 75,589.8 | 81,645.3 | 28.6 | 81,803.2 | 28.4 |
| Imports | 66,224.8 | 74,724.9 | 77,841.0 | 82,691.3 | 28.9 | 79,892.7 | 27.7 |
| Bought at Ports | -46.9 | -18.1 | 50.0 | 63.7 | 0.0 | 107.4 | 0.0 |
| Services | -1,289.4 | -2,644.7 | -3,151.9 | -3,121.6 | -1.0 | -2,338.6 | -0.8 |
| Rent | -3,455.1 | -3,853.8 | -2,130.4 | -4,523.7 | -1.3 | -6,124.1 | -2.1 |
| Transfers | 4,855.6 | 5,897.3 | 5,614.3 | 5,137.0 | 2.1 | 5,069.0 | 1.8 |

Source: BBVA Research with Banxico data

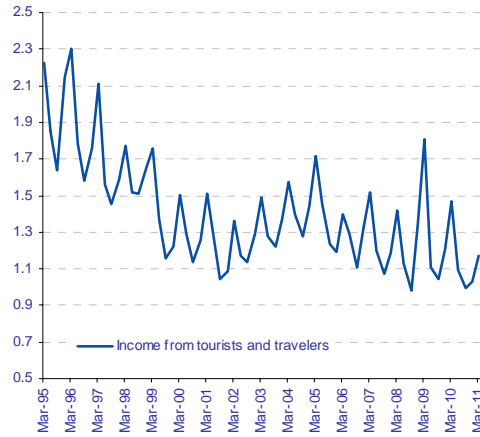
Table 2

Financial Account (md and % of GDP)

| | 2010 millions of dollars (md) | | | | 2010 % of GDP | 2011 md | 2011 % of GDP |
|---|-------------------------------|----------|----------|-----------|---------------|----------|---------------|
| | 1Q10 | 2Q10 | 3Q10 | 4Q10 | | | |
| Financial Account | 5,403.0 | 5,133.7 | 8,082.6 | 14,229.7 | 3.1 | 13,841.8 | 4.8 |
| Foreign Direct Investment | 2,463.0 | 834.5 | -1,035.5 | 2,072.7 | 0.4 | 4,242.2 | 1.5 |
| In Mexico | 5,204.0 | 7,642.1 | 2,477.6 | 3,355.6 | 1.8 | 4,787.7 | 1.7 |
| From Mexicans | -2,741.0 | -6,807.6 | -3,513.1 | -1,282.9 | -1.4 | -545.5 | -0.2 |
| Financial Investment | 10,163.0 | 4,136.8 | 12,846.8 | 12,264.4 | 3.8 | 9,424.6 | 3.3 |
| Liabilities | 9,761.3 | 6,166.8 | 9,620.6 | 11,553.1 | 3.6 | 15,235.5 | 5.3 |
| Public Sector | 6,178.2 | 742.1 | 9,465.3 | 11,711.8 | 2.7 | 13,084.9 | 4.5 |
| Private Sector | 3,583.1 | 5,424.7 | 155.3 | -158.8 | 0.9 | 2,150.6 | 0.7 |
| Assets | 401.7 | -2,030.0 | 3,226.2 | 711.3 | 0.2 | -5,810.9 | -2.0 |
| Other investment | -7,223.0 | 162.5 | -3,728.6 | -107.4 | -1.0 | 175.0 | 0.1 |
| Liabilities | -2,680.9 | 668.6 | 1,653.9 | 12,133.7 | 1.1 | -1,521.2 | -0.5 |
| Assets | -4,542.1 | -506.1 | -5,382.5 | -12,241.1 | -2.2 | 1,696.2 | 0.6 |
| Errors & Omissions | -4,130.5 | -508.9 | 1,898.2 | -3,866.3 | -0.6 | -4,918.6 | -1.7 |
| Change of International Reserves | 1,713.1 | 3,953.8 | 8,127.6 | 6,900.0 | 2.0 | 7,673.8 | 0.7 |
| Valuation Adjustments | -4.5 | -31.7 | -15.9 | -27.1 | 0.0 | -126.5 | 0.0 |

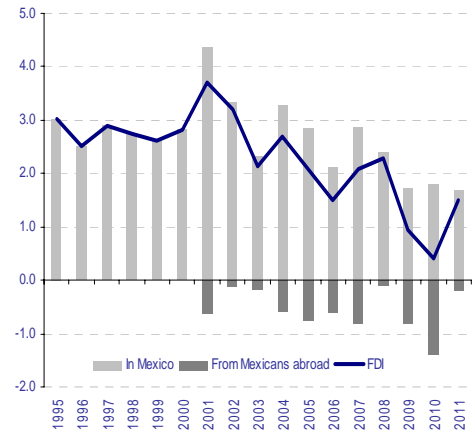
Source: BBVA Research with Banxico data

Chart 1
Income from tourists and travelers (% of GDP)



Source: BBVA Research with Banxico data

Chart 2
FDI flows (% of GDP, 2011=1Q11)



Source: BBVA Research with Banxico data

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