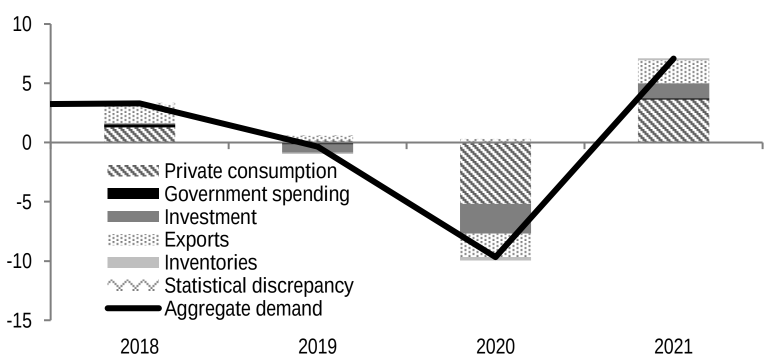
Aggregate supply and demand – Ending last year on a weak note

- **Aggregate supply and demand (4Q21): 3.0% y/y (nsa); Banorte: 3.5%; consensus: 3.6% (range: 3.4% to 5.1%); previous: 8.1%**
- **As a result, aggregate demand grew 7.1% in full-year 2021. This was led by investment (10.0%), albeit only after a deep contraction last year. Consumption picked up 7.4% and exports 6.9%**
- **All components kept growing relative to 2020, albeit more modestly except for exports as base effects became more challenging despite one more working day in the annual comparison**
- **Sequentially, it rose 0.1% q/q despite barely unchanged GDP in the period. Inside, we note the rebound in consumption (1.4%), probably helped by better epidemiological conditions. Moreover, exports (3.5%) stayed resilient, while investment (-0.2%) was mainly dragged by the public sector**
- **We maintain our 2.4% GDP forecast for this year. Nevertheless, recent geopolitical and economic events suggest that the balance of risks has tilted further to the downside**

Aggregate supply and demand moderated in 4Q21. These grew 3.0% y/y, lower than our forecast (3.5%) and consensus (3.6%). The annual rate kept moderating as base effects are increasingly challenging, more than compensating for one more working day in the annual comparison. In the former, GDP grew 1.1% y/y in the period. Meanwhile, imports boosted the result as they were up 8.2%, with goods (7.6%) below services (26.9%), as seen in Table 1. On demand, exports picked up (Chart 4), reinforcing the bias since the recovery began of more dynamism in the external front. Domestically, consumption (5.7%) and investment increased (6.7%), while government spending was more stable, at 0.6% (Chart 3). With these results, aggregate supply and demand grew 7.1% in full-year 2021, although still 3.3% below the level in 2019, before the pandemic. As has happened since the reopening started, trade has been more dynamic, with imports up 13.7% and exports advancing 6.9%. Demand was led by investment (10.0%), albeit only after a deep contraction last year. Lastly, consumption picked up 7.4% and government spending by 1.0%.

Aggregate Demand
Contribution to the annual comparison



Source: INEGI, Banorte.

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Sequential moderation despite better COVID-19 dynamics. Aggregate supply and demand picked up 0.1% q/q, virtually matching 3Q21 (Table 2). This marks the sixth consecutive quarter of the recovery, albeit decelerating at a relatively strong pace in the second half of the year. This is particularly relevant considering that COVID-19 dynamics were better during the full period. Specifically, the 'delta' wave started to recede by the end of August, while the 'Omicron' variant hit our country more clearly until early January. This was also seen in the 'traffic light' indicator, which in our view kept serving as a useful indicator for the population regarding the risks related to the pandemic.

Within demand, consumption expanded 1.4%, with some tailwinds from the pandemic and a relatively easy base effect. The former can be seen more clearly with the +2.1% of services. Moreover, it likely also helped a relative normalization in supply chains, with the imported goods component up 3.4%, stronger than the +0.8% in the domestic front (Chart 5). In our view, overall performance was positive considering elevated consumer prices that put a dent on real incomes.

Despite of this, domestic demand was dragged by investment, which fell 0.2%. This was explained by a heavy 4.6% contraction in public investment, in turn affected by the +5.1% of the previous quarter. We also do not rule out some issues from accounting methods, with the government possibly accruing expenditures with anticipation because of the end of the fiscal year. Private investment was also muted, at -0.1% (Chart 6), with monthly data showing weakness in construction. Moreover, government spending contracted 0.6% (see Chart 7). In turn, exports remained vigorous at 3.5%.

Going to supply, imports advanced 0.6% (Chart 8), explaining why our forecast was better than actual data. In our view, difficulties in inventory management and supply restrictions keep affecting performance. This is relevant as more timely data suggests that these issues are still lingering around, which could cap growth much of this year. In this sense, we flag that inventories fell 24.3% after surging 191.3% in the third quarter, a situation that may well explain a great deal of the results. Lastly, and as already reported, GDP was flat (0.0%) even after falling 0.7% in the previous quarter.

Downside risks have increased on geopolitical events and economic developments. We maintain our 2.4% GDP forecast for this year. Nevertheless, risks have been on the rise. First, high inflation is likely to prove an additional headwind –at least in the short term– as global commodity prices increase, affected by the war in Ukraine. Despite Mexico's limited trade exposure to the region and government measures to soften the impact, consumers are poised to face additional price increases, at least in energy. We will watch this week's inflation report carefully, which in our view will show pressures in LP gas and low-grade gasoline, among other goods. Although this would be more modest than implied by the adjustments in international markets, the rise in inflation has been quite persistent. As a reaction, global monetary policy is likely to keep adjusting towards a less accommodative stance. This includes Banxico, expecting a 50bps rate hike again on Thursday, to 6.50%.

Hence, a more adverse environment for consumption and investment is likely. We continue seeing more resiliency in the former, mostly on remittances, a gradual recovery in employment, more dynamism in banking credit and higher government spending in direct transfers from social programs, albeit possibly less so than previously envisaged.

On the other hand, we have had more warning signs regarding the pandemic. Although we are currently at a relatively good spot in new daily cases and deaths, the BA.2 variant, which appears to be closely related to 'Omicron' (itself known as BA.1), has likely driven a new surge in cases in countries such as China and in Western Europe. Moreover, preliminary data suggests it is more transmissible. In the former country, some regions have seen new restrictions that have affected manufacturing production, a situation that may strain supply chains further. In the US, NIAID director Anthony Fauci said they will likely experience higher cases in coming weeks. This is also highly probable to happen in Mexico. Although this may not be accompanied by higher hospitalizations and deaths, our country's recent experience suggests that an economic impact is still in the cards, especially as people needs to take a temporary leave from their jobs, care for relatives, or just are more cautious about going out. This would happen even if the government does not impose new restrictions, as has been the case since last year. Moreover, the effect may be compounded if it leads to new supply chain bottlenecks, in turn affecting inflation and the monetary policy outlook.

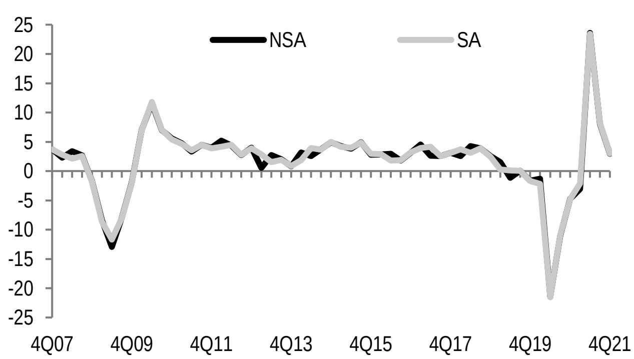
In the US, GDP growth expectations have been revised to the downside. In addition, the fiscal drag relative to the previous year is likely to stay in place as the Federal Government was not able to negotiate a larger budget for fiscal year 2022. The president signed a US$ 1.5 trillion budget, significantly below the original proposal. Considering ongoing problems in key export sectors such as autos –due to supply challenges, among other factors–, industrial activity is also likely to see limited upside. Lastly, other sectors, such as construction, are still facing difficulties because of the high levels of uncertainty, increased costs (including in funding) and dampened demand for durable goods. All these factors will keep impacting the private sector the most, with public investments not enough to compensate for it.

Table 1: Aggregate demand
% y/y nsa, % y/y sa

	% y/y nsa						% y/y sa	
	4Q21	3Q21	4Q20	3Q20	2021	2020	4Q21	4Q20
Aggregate supply	3.0	8.1	-4.8	-11.1	7.1	-9.7	3.0	-4.8
GDP	1.1	4.5	-4.4	-8.5	4.8	-8.2	1.1	-4.4
Imports	8.2	18.3	-5.8	-17.7	13.7	-13.7	8.1	-5.9
Goods	7.6	17.8	-4.2	-15.8	13.7	-12.6	--	--
Services	26.9	31.0	-38.2	-48.0	13.4	-35.6	--	--
Aggregate demand	3.0	8.1	-4.8	-11.1	7.1	-9.7	3.0	-4.8
Private consumption	5.7	8.8	-7.4	-12.6	7.4	-10.5	5.6	-7.5
Domestic	5.6	8.4	-8.0	-12.7	6.5	-10.8	5.6	-8.0
Goods	2.4	4.7	-2.2	-7.5	6.7	-7.7	2.3	-2.3
Services	9.1	12.3	-13.5	-17.5	6.2	-13.8	9.1	-13.5
Imported	17.5	25.8	-7.7	-18.3	23.5	-14.3	17.4	-7.8
Goods	17.0	24.9	-6.4	-16.4	23.3	-13.0	--	--
Services	51.5	85.3	-51.4	-67.6	36.6	-51.7	--	--
Government spending	0.6	1.4	-0.8	-0.4	1.0	0.1	0.7	-0.6
Investment	6.7	12.6	-12.8	-18.5	10.0	-17.8	6.8	-12.6
Private	6.8	12.3	-13.9	-19.7	10.8	-19.3	6.9	-13.8
Public	6.2	14.6	-6.2	-10.1	5.7	-8.0	6.3	-6.3
Exports	4.5	0.8	3.6	-2.7	6.9	-7.3	4.2	3.2
Goods	1.4	-2.5	6.7	0.5	5.2	-4.7	--	--
Services	78.9	103.4	-38.8	-51.3	46.0	-41.9	--	--
Inventories	265.1	388.1	-75.1	-77.3	150.4	-76.0	153.5	-65.6
Statistical discrepancy	-178.4	-447.0	-0.8	-130.1	-1.8	48.9	--	--

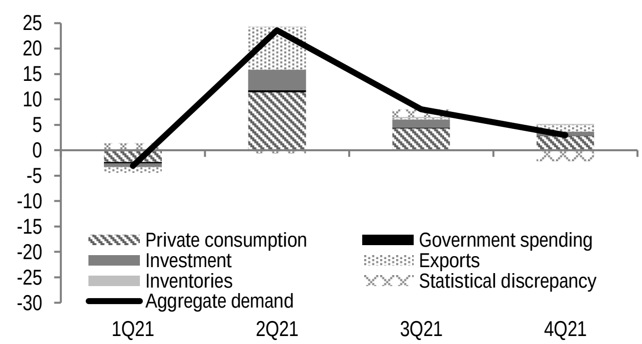
Source: INEGI

Chart 1: Aggregate demand
% y/y nsa, % y/y sa



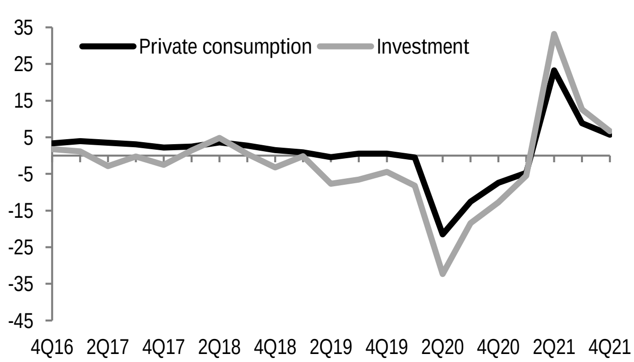
Source: INEGI

Chart 2: Aggregate demand
% y/y, contribution to the annual change, nsa



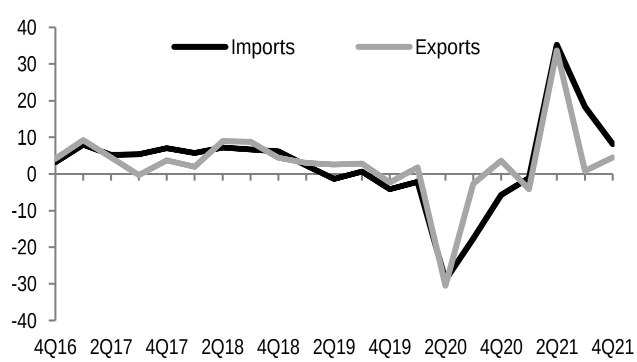
Source: INEGI

Chart 3: Private consumption and investment
% y/y nsa



Source: INEGI

Chart 4: Exports and imports
% y/y nsa



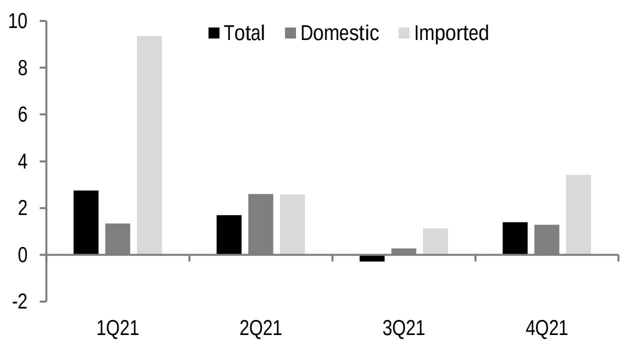
Source: INEGI

Table 2: Aggregate supply and demand
% q/q sa, % q/q saar

	% q/q sa				% q/q saar	
	4Q21	3Q21	2Q21	1Q21	4Q21	3Q21
Aggregate supply	0.1	0.1	1.1	1.7	0.6	0.2
GDP	0.0	-0.7	1.0	0.8	0.1	-2.8
Imports	0.6	1.9	0.1	5.3	2.5	8.0
Aggregate demand	0.1	0.1	1.1	1.7	0.6	0.2
Private consumption	1.4	-0.3	1.7	2.7	5.7	-1.1
Domestic	1.3	0.3	2.6	1.3	5.2	1.1
Goods	0.8	-0.6	0.7	1.3	3.4	-2.4
Services	2.1	1.5	3.7	1.6	8.6	6.1
Imported	3.4	1.1	2.6	9.4	14.4	4.6
Government spending	-0.6	-2.4	3.4	0.3	-2.3	-9.2
Investment	-0.2	1.0	1.2	4.8	-0.9	4.0
Private	-0.1	0.6	1.0	5.4	-0.3	2.4
Public	-4.6	5.1	4.4	1.5	-17.0	22.0
Exports	3.5	4.1	-0.6	-2.7	14.7	17.3
Inventories	-24.3	191.3	19.9	-4.1	-67.2	7,101.7

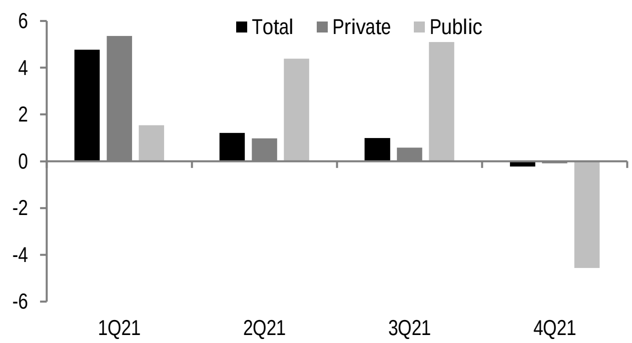
Source: INEGI

Chart 5: Private consumption
% q/q sa



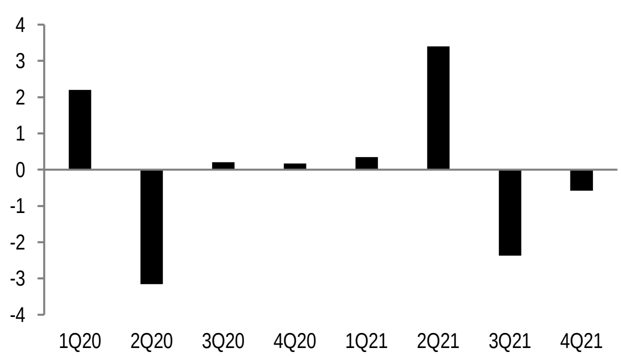
Source: INEGI

Chart 6: Investment
% q/q sa



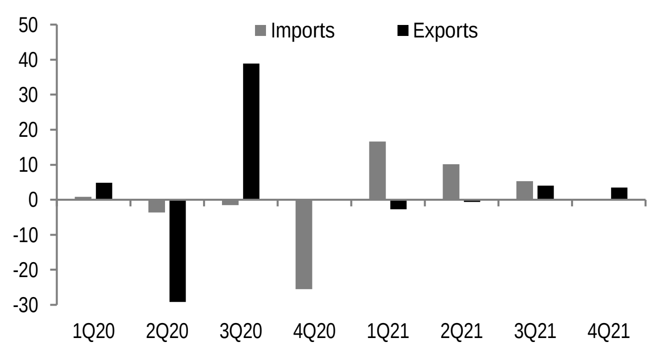
Source: INEGI

Chart 7: Government spending
% q/q sa



Source: INEGI

Chart 8: Exports and imports
% q/q sa



Source: INEGI

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