

Ahead of the Curve

Aggregate demand to fall 1.2% yoy in 2Q19

- **Aggregate supply and demand (2Q19).** We anticipate a strong moderation to -1.2% yoy from 1.4% in the previous quarter. The main drivers would be weakness in consumption and government spending along less dynamism in consumption. It should be remembered that 2Q19 GDP stood at -0.8% yoy, distorted by the timing of the Holy Week which subtracted labor days.

In consumption, we estimate a 0.1% advance, with a weak performance of durable-goods, consistent with high uncertainty. In investment, we anticipate -7.3%, affected by low public spending and idiosyncratic shocks such as the suspension of construction projects in Mexico City. Government expenditures would stay negative at -1.2%. This is weaker than the start of at least the three previous administrations, with austerity measures still in place. Lastly, exports would grow 4.7%, helped by a strong auto sector; while imports likely declined 2.4%, mainly impacted by plunging capital goods imports.

We maintain our full-year GDP forecast at 0.8%, with downside risks and slightly stronger than market expectations around 0.5%. In our view, economic activity will strengthen during the second half, particularly consumption, while exports would stay resilient. Despite its strong fall during the quarter, investment will likely remain as the weakest component of aggregate demand, only expecting a gradual improvement by the end of the year.

September 13, 2019

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Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Tue 19-Sep	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 3y Mbono (Dec'21); 3y Udibonos (Jun'22)					
Wed 19-Sep	10:00am	International reserves	Sep-13	US\$ bn	--	--	180.5
Fri 20-Sep	7:00am	Aggregate Demand	2Q19	% yoy	<u>-1.2</u>	--	1.4
		Private consumption		% yoy	<u>0.1</u>	--	1.1
		Government consumption		% yoy	<u>-1.2</u>	--	-0.8
		Gross-fixed investment		% yoy	<u>-7.3</u>	--	-0.9
Fri 20-Sep	3:30pm	Citibanamex bi-weekly survey of economic expectations					

Source: Banorte; Bloomberg

Proceeding in chronological order...

Weekly government bond auction. The Ministry of Finance (MoF) –via Banco de Mexico as its financial agent, will offer 3-year fixed-rate Mbonos (Dec’21), and 3-year Udibonos (Jun’22), in addition to the 1-, 3-, and 6-month zero-coupon Cetes (see following table). As usual, results will be released at 12:30pm (ET).

Auction specifics (Tuesday, September 17th, 2019)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²
Cetes				
1m	17-Oct-19	--	6,000	7.72
3m	19-Dec-19	--	10,000	7.73
6m	12-Mar-20	--	14,500	7.62
M Bono				
3y	09-Dec-21	7.25	10,500	7.12
Udibono				
3y	09-Jun-22	2.00	UDIS 1,125	3.49

Source: Banorte with data from Banco de México 1. Except for Udibonos, which are expressed in UDI million, everything else is expressed in MXN million. 2. Yield-to-maturity reported for Cetes, Mbonos and Udibonos

Weekly international reserves report. Last week, net international reserves increased US\$79 million, closing at US\$180.5 billion. According to Banxico’s report, this figure comes mainly from a positive valuation effect in central bank assets. In this context, the central bank’s international reserves have increased US\$5.7 billion during 2019 (please refer to the following table). Due to the holiday on September 16th, the report will be released until Wednesday.

Banxico's foreign reserve accumulation detail
US\$, million

	2018	Sep 6, 2019	Sep 6, 2019	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	174,793	180,456	79	5,663
(B) Gross international reserve	176,384	188,413	-939	12,029
Pemex	--	--	82	100
Federal government	--	--	-912	6,407
Market operations	--	--	0	0
Other	--	--	-108	5,522
(C) Short-term government's liabilities	1,592	7,957	-1,018	6,365

Source: Banco de México

Aggregate demand in 2Q19 dragged by investment and less dynamism in consumption. We expect a 1.2% yoy contraction in aggregate supply and demand, considerably below the +1.4% of the previous quarter. The most relevant factors behind this should be weakness in investment and government spending –in a context of the first year of a new federal administration– and less dynamism in consumption. It should be noted that 2Q19 GDP stood at -0.8% yoy, distorted by the timing of the Holy Week which subtracted labor days in the annual comparison.

In consumption, we estimate a 0.1% advance, much lower than the 1.1% observed in 1Q19. This would match the monthly indicator of domestic consumption, which declined relative to the 1.7% seen in the previous quarter. Domestically-produced durable-goods have been the most impacted (-11.7%) in the period, adding three quarters in contraction and consistent with high levels of uncertainty.

On the other hand, non-durables decelerated to 1.1% from 2.5%. In our view consumption could accelerate later in the year, supported by low inflation pressures, social programs by the Federal Government, and real wage gains. Nevertheless, the moderation in formal job creation and economic growth will likely limit put a limit on its potential upside.

We expect investment at -7.3% yoy, in line with the monthly GFI report, and below the -0.8% of the previous quarter. Performance was affected by low public spending but also by idiosyncratic shocks, such as the suspension of construction projects in Mexico City. Although investment could improve gradually, this will likely be modest as business confidence remains low, domestic and external uncertainty are high, and growth forecasts continue to weaken at the margin, among other factors.

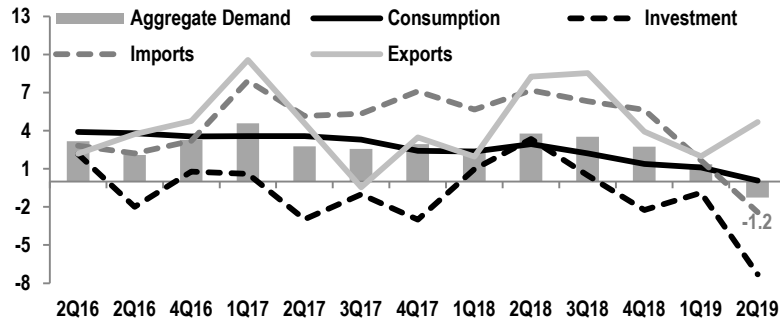
Government expenditures would stay negative at -1.2% yoy from -0.8%. According to public finance reports, spending contracted 3%, with austerity measures by the Federal Government still in place. The deceleration has been a stronger drag than the start of at least the last three six-year Presidential terms, with spending at 4.7% in 2Q13, 5.8% in 2Q07, and 8.5% in 2Q01. In contrast to the previous quarter, the base-effect is more challenging as this category grew 3% in the same period of 2018, likely related to electoral expenditures. We believe government spending will return to positive for the rest of the year, helped in part by the renewed push to accelerate investment (with infrastructure and private-public partnerships, among others) and consumption (accelerating loans to the private-sector).

Last but not least, exports would grow 4.7% while imports likely declined 2.4%, with the latter very weak according to trade balance figures as they fell 2%, impacted by the plunge of 11.1% in capital goods imports (related to investment spending). Imports of non-oil intermediate-goods, related to manufacturing, were also down slightly (-0.1%). Nevertheless, total goods exports accelerated to 4.7% yoy from 2.6%, with oil-related goods declining more (-13.6%) but with a relative rebound in non-oil exports, to 6.1% from 3.2%, with a particularly good performance in the auto sector.

We maintain our full-year GDP forecast at 0.8%, with downside risks and slightly stronger than market expectations around 0.5%. In our view, economic activity will strengthen during the second half, particularly consumption, while exports would stay resilient. Despite its strong fall during the quarter, investment will likely remain as the weakest component of aggregate demand, only expecting a gradual improvement by the end of the year.

Aggregate demand

% yoy (nsa)



Source: INEGI, Banorte

Citibanamex Survey. Markets will center on analysts' inflation forecasts for the first half of September (to be published on Tuesday, September 24th) along with the 2019 year-end estimate. It will be important to see monetary policy assessments, particularly when considering the timing of the next policy meeting, which will take place on September 26th. We will also pay attention to GDP growth and the exchange rate.

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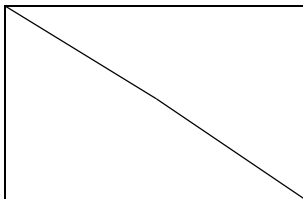
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