

GFI fell 7.6% yoy in July, with broad weakness still prevailing

- **Gross fixed investment (July): -7.6% yoy (nsa); Banorte: -7.9%; consensus: -7.8% (range: -10.5% to -4.4%); previous: -8.7%**
- **Once again, the fall was explained by a contraction in most sub-indices, with machinery and equipment down 9.5% while construction fell 6.1%**
- **In seasonally adjusted terms, GFI fell 0.7%, with domestic facing sectors reversing some of last month's positive figures**
- **Today's report inserts additional and relevant risks to the downside to our full-year forecast for investment to drop 2.9% yoy despite some tentative signs that activity may have bottomed out**

GFI falls 7.6% yoy in July. GFI contracted for a sixth month in a row in annual terms, at -7.6% yoy, higher than both consensus (-7.8%) and our -7.9% forecast. The result is weak, with the print above the -8.8% observed in July to some extent explained by the fact that the period had one more working day in the annual comparison. Overall, this portrays a difficult start for the quarter. On a year-to-date basis, investment has declined 4.6%. Some of the persistent drivers behind this have been the impact of lower spending by the Federal Government, with capital outlays in the month down 6.5% in real terms according to budget figures, along high uncertainty and other idiosyncratic shocks, with one of the most relevant being the suspension of building projects in Mexico City.

By sectors, construction fell 6.1% yoy, worsening relative to the previous month (-4.5%) but in line with IP figures. Inside, both sectors posted a similar dynamic, with the residential sector -6.8% from -5.9% in June, while the non-residential sector was down -5.4% (previous: -3.3%). Machinery and equipment remains a drag (-9.5%), with the two sectors still declining, albeit with different narratives. The imported component fell at a double-digit pace for the second month in a row (-14.0%). In this respect and according to the trade balance report, capital goods imports fell 16.5%. On the contrary, the domestic component moderated its decline at -1.7%, helped to some extent by a base effect but also with transportation equipment remaining as a relatively bright spot within this category, up 3.5%.

Overall, the report does not provide enough light on the possibility of a recovery in the sector. News reports suggest that some efforts by the Federal Government are being made to kick-start construction, including in Mexico City. Nevertheless, in a best-case scenario, this probably will be reflected until September. We believe the private sector is not likely to pick-up the slack that has accumulated from the slowdown in public investment, at least in the short term. However, some signs of a gradual recovery, at least in terms of confidence levels, have started to emerge according to the most updated figures available.

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Gross fixed investment

% yoy, nsa

	Jul-19	Jul-18	Jan-Jul'19	Jan-Jul'18
Total	-7.6	4.6	-4.6	2.5
Construction	-6.1	2.7	-3.2	1.1
Residential	-6.8	6.0	-2.6	4.4
Non-residential	-5.4	-0.5	-3.7	-1.9
Machinery and equipment	-9.5	7.0	-6.5	4.5
<i>Domestic</i>	-1.7	-4.3	-4.3	-2.0
Transportation equipment	3.5	-6.9	3.3	-5.9
Other machinery and equipment	-9.5	-0.1	-15.1	4.2
<i>Imported</i>	-14.0	15.0	-7.9	9.0
Transportation equipment	0.3	14.8	-0.3	5.2
Other machinery and equipment	-16.2	15.0	-9.2	9.6

Source: INEGI

Seasonally-adjusted figures show a slow-down in domestic facing sectors, contrasting with the previous month. In particular, GFI declined 0.7% m/m, its third consecutive decline but improving on the margin relative to the -0.8 of the previous month. Nevertheless, activity levels –as measured by the level of the seasonally adjusted index– now stand at a new low since January 2014. Inside, domestic facing sectors posted contractions, with construction and domestic M&Eq. down 1.5% and 2.4%, respectively, with the former partially reversing the 4.0% expansion seen in the previous month. In this context, additional information in the following months will be key in order to assess if there have been any improvements due to the efforts led by both the Federal and Mexico City’s governments. Within the latter, sectors were mixed, with transportation down sharply (-6.7%) while ‘others’ bounced back considerably (+5.2%). On the contrary, imported M&Eq. edged-up 2.8%, with transportation leading the improvement (+7.7%). Considering the latter figures, the 3m/3m saar rate moderated its pace of decline relative to the previous month, standing at -13.4% from -14.7%. Nevertheless, part of the improvement is explained by a favorable base effect, as January –which was a positive print– was eliminated.

Gross fixed investment

% m/m sa, % 3m/3m saar

	% m/m			% 3m/3m saar	
	Jul-19	Jun-19	May-19	May-Jul'19	Apr-Jun'19
Total	-0.7	-0.8	-2.5	-13.4	-14.7
Construction	-1.5	4.0	-5.6	-14.7	-17.0
Residential	-0.1	4.4	-7.5	-19.1	-22.2
Non-residential	-3.7	5.6	-4.3	-8.3	-10.5
Machinery and equipment	-0.7	-5.4	-0.9	-17.2	-12.4
<i>Domestic</i>	-2.4	0.0	-1.7	0.2	13.8
Transportation equipment	-6.7	0.8	-1.9	11.6	50.9
Other machinery and equipment	5.2	-1.6	-1.9	-16.9	-26.9
<i>Imported</i>	2.8	-11.3	1.8	-25.3	-27.1
Transportation equipment	7.7	-8.0	15.2	4.0	-23.9
Other machinery and equipment	3.1	-12.9	0.2	-30.4	-29.8

Source: INEGI

Tentative signs that investment may have bottomed-out may have started to surface. As mentioned above, today's report does not suggest an improvement in investment at the start of 3Q19. In this respect, we continue expecting investment in full-year 2019 at -2.9% yoy, although with today's print inserting additional and relevant risks to the downside, reaffirming this component of aggregate demand as the weakest link in terms of GDP growth for this year.

However, some positive signs have started to emerge, particularly in terms of business confidence, with all four sectors (construction, commerce, non-financial services and manufacturing) increasing in September. In the news front, the Federal Government reached an agreement with the four companies (Grupo Carso, IEnova, TC Energy, and Fermaca) in charge of constructing gas pipelines for the state-owned utility, CFE. More recently, the Ministry of Finance (MoF) and Mexico's leading business chamber, *Consejo Coordinador Empresarial*, said that President Lopez-Obrador will provide details about 100 projects of the National Infrastructure Plan that will be offered in private-public partnerships in coming weeks. On the external front, Mexico's Undersecretary of Foreign Relations, Jesús Seade, said last week that they expect that US Speaker of the House, Nancy Pelosi, to give approval for a debate and eventual vote on the USMCA by the end of this month or on early November. According to him, the window to approve the deal is open until early 2020 as it would get harder to do so before the presidential election, with the impeachment process not putting the agreement at risk. The latter, coupled with the recent plan by the MoF to accelerate government expenditures, seems to suggest that the government is more keenly aware of the need to restart investment projects, a situation that could help reduce uncertainty and reinsert more dynamism into the sector.

Despite of the latter, it is our take that a cautious stance might still prevail, especially on private-sector investment. First, economic activity remains stagnant, providing less incentive for firms to engage in new investment projects, particularly in an environment in which marginal data suggests that global activity has decelerated further, particularly in manufacturing. However, some cushion may come from lower financing costs, as we believe Banxico will continue lowering its reference rate this year and next, within an easing cycle that we estimate could accumulate 225bps by the end of next year, with the rate ending 2020 at 6.00%.

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