

Ahead of the Curve

August 30, 2019

Positive remittances, but plunging investment

- Remittances (July).** We expect remittances at US\$ 3,011.2 million, up 5.4% yoy and accelerating relative to the 0.7% decline of the previous month, which was influenced by a difficult base effect. Broadly speaking, we anticipate flow dynamics to remain positive, a factor that continues to be of some support for domestic demand. We highlight that a very relevant development during the period was the announcement of widespread raids targeting immigrant families in the US, which in our view could have induced above-average flows. With this result, remittances would add up to US\$ 19,857 million so far in 2019, 4% above the same period of 2018
- Gross fixed investment (June).** We anticipate GFI at -9.9% yoy, below the -7.4% of the previous month. With this, investment would have plunged 7.7% in 2Q19 and -4.3% during the first half of the year. Using seasonally adjusted figures, we anticipate a second consecutive month in negative territory, at -1.3%. Both sectors would decline in the annual comparison, with the steepest fall in machinery and equipment (-14% yoy) on the back of a contraction in the imported component. On the other hand, construction would fall 6.7%, with the sector still facing a difficult environment in coming months despite possible support from higher government spending in the rest of 2019.

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Document for distribution among the general public

Mexico weekly calendar

DATE	HOUR (ET)	EVENT	PERIOD	UNIT	BANORTE	CONSENSUS	PREVIOUS
Mon 2-Sep	10:00am	Family remittances	Jul	US\$ mn	<u>3,011.2</u>	3,023.0	3,119.0
Mon 2-Sep	10:00am	Banxico's survey of economic expectations	Aug				
Mon 2-Sep	1:00pm	PMI's survey (IMEF)	Aug				
		Manufacturing		index	<u>49.0</u>	49.2	49.6
		Non-manufacturing		index	<u>47.8</u>	47.7	47.1
Tue 3-Sep	10:00am	International reserves	Aug-31	US\$ bn	--	--	180.3
Tue 3-Sep	12:30pm	Government weekly auction: 1-, 3-, 6-month CETES; 5y Mbono (Sep'24); 10y Udibono (Nov'28)					
Thu 5-Sep	7:00am	Consumer confidence	Aug	index	<u>102.8</u>	103.9	105.1
Thu 5-Sep	4:30pm	Citibanamex bi-weekly survey of economic expectations					
Fri 6-Sep	7:00am	Gross fixed investment	Jun	% yoy	<u>-9.9</u>	-8.9	-7.4
		Machinery and equipment		% yoy	<u>-14.0</u>	--	-5.4
		Domestic		% yoy	<u>-15.0</u>	--	-5.7
		Imported		% yoy	<u>-22.5</u>	--	-5.2
		Construction		% yoy	<u>-6.7</u>	--	-9.1

Source: Banorte; Bloomberg

Proceeding in chronological order...

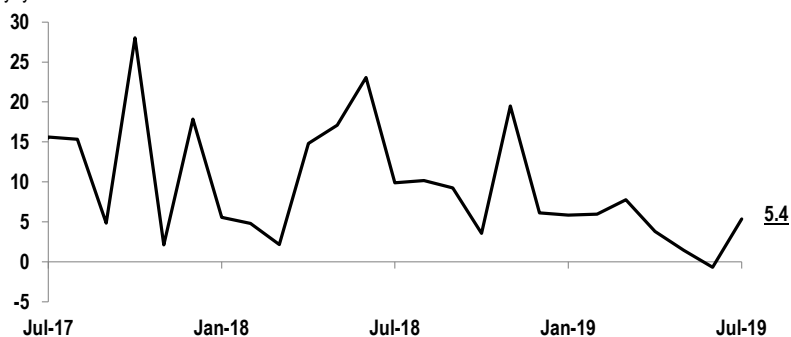
Remittances facing a challenging base effect in July. We expect remittances at US\$ 3,011.2 million, up 5.4% yoy and accelerating relative to the -0.7% of the previous month, which was influenced by a difficult base effect. Broadly speaking, we anticipate flow dynamics to remain positive, a factor that would keep providing some support to domestic demand.

We highlight that a very relevant development during the period was the announcement of widespread raids targeting immigrant families in the US, eventually carried out in the middle of July. According to news reports, detentions did not pick-up significantly after this announcement. Nevertheless, we believe that since this piece of news hit the wires, higher uncertainty and an increased probability of being deported alone likely induced above-average flows. Going to other variables, the Mexican peso appreciated on average during the month, from 19.27 to 19.05 in July. Contrary to the previous month in which volatility was markedly higher, the MXN traded in a relatively tight range, between 18.91 and 19.18. This probably had an adverse effect on the overall flow, remembering that a stronger peso tends to discourage remittances as its purchasing power in local currency decreases.

With this result, remittances would add up to US\$ 19,857 million so far in 2019, 4% above the same period of 2018. We maintain our view that full-year growth will be more modest when compared to the 10.5% of the previous year, with greater headwinds in the second half as US economic activity keeps slowing gradually, eventually impacting dynamism of Mexican migrants' employment growth in that country.

Family remittances

% yoy



Source: Banxico

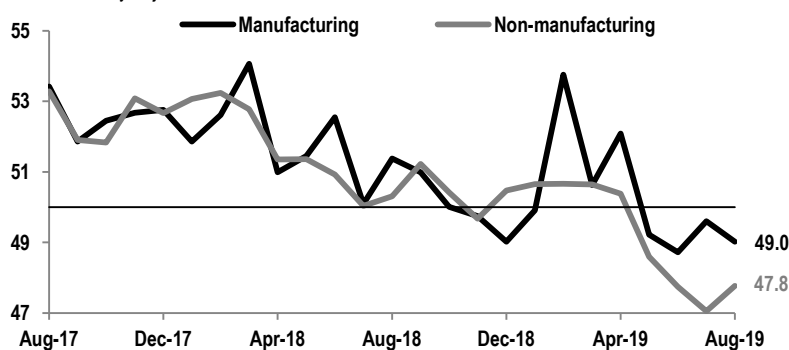
Banxico's survey of economic expectations. As usual, markets will focus on inflation forecasts. The median for 2019 is 3.66%, above our 3.3%. Moreover, the medium-term estimate remains above target, standing at 3.5%. In addition, estimates for the reference rate will be published. Our expectation is for Banxico to cut an additional 50bps through the remainder of the year, ending 2019 at 7.50% (consensus: 8.00%). GDP forecasts will also be released. In the last survey, economists' growth for 2019 stood at 0.8%, in line with our estimate. For 2020, it came in at 1.5% (Banorte: 1.4%). Finally, we could see an upward revision in the exchange rate, considering that the YE19 forecast stands at USD/MXN 19.70 (Banorte: 20.30), while spot is hovering near 20.00 per dollar.

PMI's still in contraction in August. We expect the manufacturing index at 49.0pts from 49.6pts sa in July, which would mark its fourth consecutive print in contraction territory. The main driver would be that industry remains challenged by global trade tensions, impacting demand. In this respect, the preliminary US manufacturing PMI dipped to contraction (49.9pts), for the first time since September 2009. According to *IHS Markit*, this mainly reflected a weaker contribution from new orders, falling for the second time in the past four months, while also signaling a steep reduction in export sales, which is negative for our country due to the integration of supply chains. This seems to confirm the signal provided by the ISM report for July, in which business imports were also contained and in contraction at 47.0pts, a new minimum in three years. Overall, the sector looks to be extending its soft patch, with US businesses' expectations of the year ahead taking an additional hit. On the other hand, we believe some of the negative impact from US conditions may have been at least partially compensated by the depreciation of the Mexican peso, which was pressured since the beginning of the month, going from 19.24 to around 20.00 per dollar currently (3.9%).

Regarding the non-manufacturing index, we expect a modest pickup from 47.1pts in July (lowest since February 2017) to 47.8pts. In particular, it is our take that this would be supported by positive inflation surprises, with the 1H-August at -0.08% 2w/2w vs. consensus at 0.14%. The production component would be the most supportive, expecting to rebound from a very depressed level of 45.0pts in the previous month. We anticipate a similar response in new orders. On the other hand, employment is likely to stay depressed, as the most recent data show that the persistent slowdown in formal job creation has extended, while the July unemployment rate increased to 3.58% (seasonally-adjusted), a high not observed since December 2016.

IMEF indices

Indices, seasonally-adjusted



Source: IMEF

Weekly international reserves report. Last week, net international reserves increased US\$20 million, closing at US\$180.3 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\$5.5 billion during 2019 (please refer to the following table).

Banxico's foreign reserve accumulation detail

US\$, million

	2018	Aug 23, 2019	Aug 23, 2019	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	174,793	180,263	20	5,471
(B) Gross international reserve	176,384	189,088	63	12,704
Pemex	--	--	72	170
Federal government	--	--	2	7,341
Market operations	--	--	0	0
Other	--	--	-11	5,193
(C) Short-term government's liabilities	1,592	8,825	42	7,233

Source: Banco de México

Weekly government bond auction. The Ministry of Finance (MoF) –via Banco de Mexico as its financial agent, will offer 5-year fixed-rate Mbonos (Sep'24), 10-year Udibonos (Nov'28), 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 3rd, 2019)

	Fecha de Vto.	Tasa cupón	Monto a subastar ¹	Tasa previa ²
Cetes				
1m	03-Oct-19	--	6,000	7.87
3m	05-Dec-19	--	9,000	7.82
6m	27-Feb-20	--	13,000	7.68
Bono M				
5 años	05-Sep-24	8.00	11,500	7.37
Udibono				
10 años	30-Nov-28	4.00	UDIS 950	3.46

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

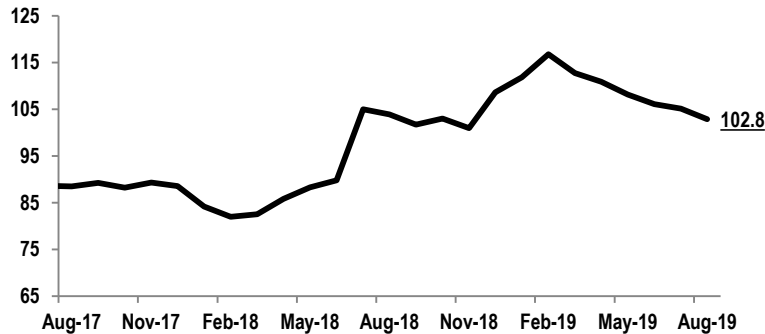
Consumer confidence to keep declining in August. We anticipate an additional decline, to 102.8pts (lowest since November) from 105.1pts in July, which would imply -1.0% yoy –first contraction since the election, as the base effect has become more challenging–. Despite of this, the level would stand about 13pts higher than immediately before this event. With seasonally-adjusted figures this would imply a 1.9% decline, sixth consecutive on the downside. In our view, this would be mostly due to the an impact in country conditions stemming from the strong depreciation of the peso, going from around 19 to 19.75 per dollar and climbing persistently in the month between the end of survey periods. Additionally, we believe downward revision in 2Q19 GDP could also have an impact, especially as news outlets debated the implications of a potential ‘technical recession’, which could have stoked stronger fears among the population.

On the other hand, we believe household’s current conditions and purchasing power components could have been supported by lower inflation pressures, as it has been coupled with strong nominal wage gains. Nevertheless, this could be somewhat limited by the deceleration in formal job creation, a situation that now seems to be impacting more clearly the unemployment rate. Last but not least, confidence may catch-up lower, at least to some extent, the recent fall in presidential approval ratings, as it has kept a relatively tight correlation in terms of direction but has lagged in terms of magnitude, with the latest print according to *Oraculus*’s poll of polls unchanged in the monthly comparison, with a net approval of 45%.

All in all, we continue to believe that confidence will keep declining gradually as political optimism fades away, eventually returning towards its long-term average, especially in a context of a slowdown and stagnation of activity.

Consumer confidence

Index, nsa



Source: INEGI

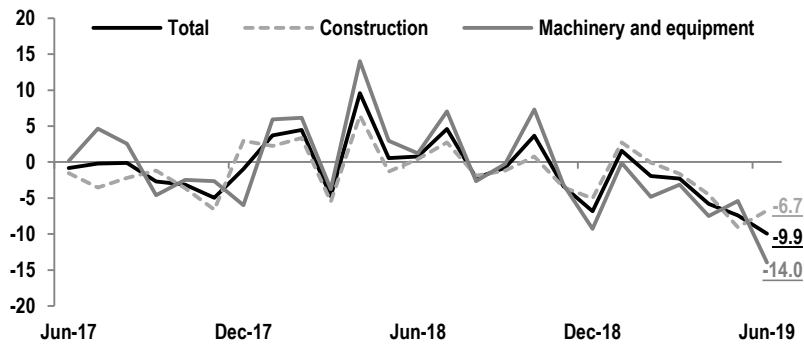
Citibanamex Survey. Markets will center on analysts’ inflation forecasts for August (to be published on Monday, September 9th) along with the 2019 year-end estimate. It will be important to see monetary policy assessments, particularly after the release of the latest *Quarterly Report* and monetary policy minutes. We will also pay attention to GDP growth and the exchange rate.

Gross fixed investment to plunge in June. We anticipate GFI at -9.9% yoy, significantly lower than the -7.4% of the previous month. As a result, GFI would have plunged 7.7% in 2Q19 and 4.3% during the first half of the year. If our forecast materializes, this quarterly performance would imply a downgrade to our estimate of -7.3%, with aggregate demand figures to be released on September 20th. Using seasonally adjusted figures, we anticipate a 1.3% contraction, adding two months in negative territory.

In particular, we forecast construction at -6.7% yoy, virtually in line with the -6.8% observed in the industrial production report. In the annual comparison the latter stayed deeply negative, with civil engineering at -5.3% (still impacted by austerity measures and the slowdown in expenditures during the first year of a new administration) and edification at -5.5%. Nevertheless, a rebound of 3.1% was observed in monthly terms, which despite being more favorable, it was not enough to reverse May’s 6.2% contraction. For details, see: “*Industrial production – Activity rebounds in June but challenges remain*”, August 9th, 2019, <[pdf](#)>. We continue seeing challenges for this sector in coming months despite potential support from higher government expenditures in the second half, as announced recently. Even if we observe an improving trend, we believe it would be modest as business confidence remains low in an environment of high local uncertainty. Overall performance is likely to be limited by some temporary shocks that could still be having an impact, highlighting the suspension of construction projects in Mexico City.

Moreover, we anticipate machinery and equipment (M&Eq) to fall 14%, which would be the weakest since late 2009 in the midst of the Financial Crisis. The result would be dragged by the imported component, estimated at -22.5%, consistent with the hefty decline in capital goods imports according to the trade balance. For details, see: “*Trade balance – Weakness across the board in June*”, July 26th, 2019, <[pdf](#)>. It should be mentioned that this latter component has stayed weak, confirming that investment remains as the worst link in Mexico’s growth story. On the other hand, we estimate the domestic component to pick-up modestly after declining 5.7% in May, albeit still in negative territory at -1.5% yoy.

GFI
% yoy



Source: INEGI, Banorte

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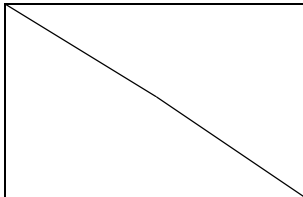
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