4Q19 GDP – Industry shocks partially compensated by the rebound in services

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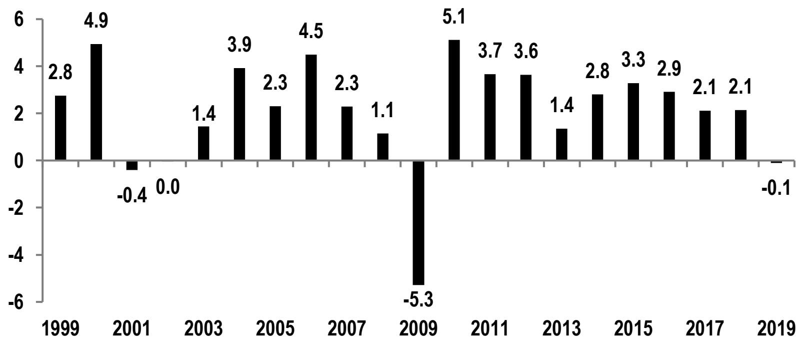
- **Gross Domestic Product (4Q19, nsa): -0.3% y/y; Banorte: -0.6%; consensus: -0.5% (range of estimates: -0.6% to 0.1%); previous: -0.3%**
- **Gross Domestic Product (4Q19, sa): 0.0% q/q; Banorte: -0.2%; consensus: -0.2% (range of estimates: -0.4% to 0.1%); previous: 0.0%**
- **As a result, full-year 2019 GDP declined 0.1% y/y from +2.1% in 2018. Primary activities were up 1.9%, industry contracted 1.7%, and services slowed down to 0.5%**
- **As expected, industry impacted growth the most in the quarter, declining 1.0% q/q, while primary activities stood at -0.9%. On the other hand, services rebounded 0.3%, best since 3Q18**
- **Taking into account that the monthly GDP-proxy, IGAE, stood at -1.0% y/y on average in October-November, today's print would imply an expansion of around 1.0% in December, with services surprising to the upside relative to available data released so far**
- **We expect a rebound in economic activity in 2020, maintaining our estimate of a 0.8% y/y expansion, with risks broadly balanced**
- **The revised figure will be published on February 25th**

Full-year 2019 GDP declined 0.1% y/y. This figure is lower than the +2.1% of the previous year and is the first contraction since 2009 (see chart below). Primary activities were up 1.9%, industry contracted 1.7%, and services slowed down to 0.5%. Broadly speaking, economic activity was impacted by several factors, including: (1) The typical deceleration during the first year of a new administration, impacting both public and private investment; (2) a series of temporary shocks –including delays in gasoline distribution, labor strikes both domestically and abroad, railway blockades in Michoacán, and the suspension of construction projects in Mexico City–; and (3) trade uncertainty that affected the manufacturing sector, in the midst of tensions between the US and China, renewed threats of tariffs to Mexico by the US, and challenges to the approval of USMCA.

GDP
% y/y nsa



Source: INEGI

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In particular, activity contracted 0.3% y/y in 4Q19. This figure was above our forecast (-0.6%) and consensus expectations of a 0.5% contraction. This is basically in line with the previous month's decline, with muted performance mainly explained by negative shocks in the industrial sector, highlighting the General Motors strike in the US, among others, which had a significant impact in our country. This sector posted a 1.8% y/y fall in 4Q19. Services inched higher by 0.2%. Finally, agricultural activities increased 1.9%, with two consecutive quarters showing strength.

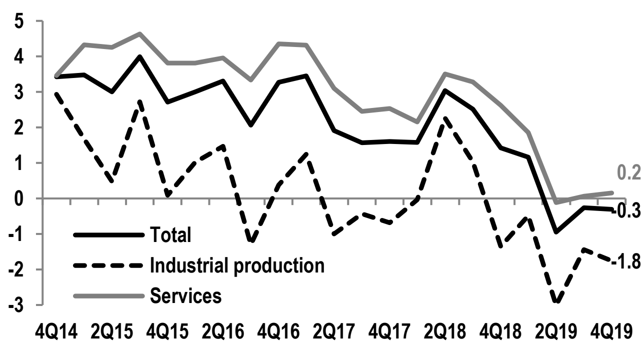
Activity remained flat relative to the previous quarter. Using seasonally-adjusted figures, GDP was unchanged (0.0% q/q) for second consecutive quarter, confirming that although the economy seems to have stagnated, it is not in recession. Moreover, and as previously mentioned, the main driver behind this performance was the deceleration in industry (-1.0%), with the relative recovery in mining more than compensated by temporary shocks in manufacturing, along persistently low dynamism in construction. On a more positive note and contrary to our expectations, services grew 0.3%, accelerating relative to sector's data already published as well as more timely figures for December, such as retail sales and non-oil consumption goods imports. Lastly, primary activities contracted 0.9%, although modest when taking into account the 3.3% surge observed in 3Q19.

GDP
% yoy; % q/q

% y/y, nsa	4Q19	3Q19	4Q18	3Q18	2019	2018
Total	**-0.3**	**-0.3**	**1.4**	**2.5**	**-0.1**	**2.1**
Agricultural	1.9	5.4	0.9	1.0	1.9	2.4
Industrial Production	-1.8	-1.4	-1.4	1.0	-1.7	0.5
Services	0.2	0.1	2.6	3.3	0.5	2.9
% y/y, sa						
Total	**-0.3**	**-0.2**	**1.4**	**2.6**	**-0.1**	**2.1**
Agricultural	1.9	5.4	0.8	1.1	2.1	2.4
Industrial Production	-1.5	-1.5	-1.1	1.0	1.7	0.4
Services	0.1	0.1	2.5	3.4	0.5	2.9
% q/q, sa						
Total	**0.0**	**0.0**	**-0.1**	**0.4**	**--**	**--**
Agricultural	-0.9	3.3	2.1	-1.9	--	--
Industrial Production	-1.0	-0.1	-1.2	-0.4	--	--
Services	0.3	0.1	0.2	0.8	--	--

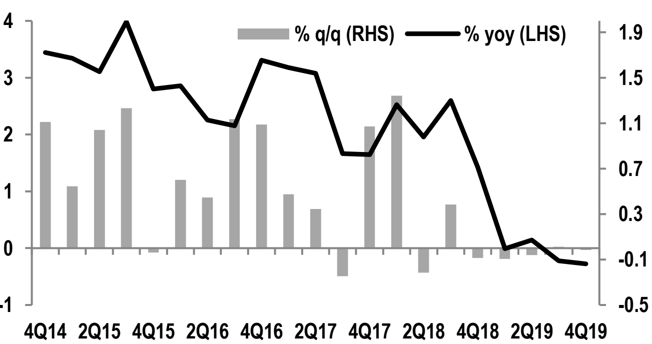
Source: INEGI

GDP
% y/y nsa



Source: INEGI

GDP
% y/y sa; q/q sa



Source: INEGI

Today's report suggests stronger activity in December. In particular, we estimate the monthly GDP proxy (IGAE) around 1.0% y/y in December (0.2% m/m, higher than the previous month and which would the highest since January 2019). This contrasts with other data such as IMEF indicators, with both the manufacturing and non-manufacturing in contraction and broadly unchanged to November. As already stated, ANTAD and Walmart sales also pointed to lingering weakness. On the contrary, others have been more favorable, highlighting the significant fall in the unemployment rate –to a new historical low– and the recovery of business confidence for all sectors except manufacturing. Today's performance provides more credence to the latter view, although cautiousness is still granted due to most recent economic dynamics.

We maintain our 2020 GDP forecast at 0.8% y/y, with risks broadly balanced. In our view, the surprise to the upside when compared to consensus and our expectations places the economy in a better footing into this year. In this respect, we reiterate our 0.8% GDP estimate, which remains slightly below market expectations at 1.0% according to the latest *Citibanamex* survey.

It is our take that the relative improvement to 2019 will be supported by several factors, including lower uncertainty –especially in trade after the ratification of USMCA in the US– that could help lift business confidence. Moreover, the first phase of the government's infrastructure plan could induce private investment to improve. The typical slowdown of the first year of the new administration will not be present, which would also be positive in terms of public infrastructure spending (including construction of some key projects). We expect consumption to accelerate modestly (1.2% y/y), helped by higher wages –taking into account the 20% minimum wage increase–, well-behaved inflation, and the consolidation of social programs, among the most relevant. On the other hand, we estimate net exports to contribute less than in 2019, with the US slowing down –affected to some extent by the global deceleration– while imports could accelerate after a tough year which will likely end in contraction territory in annual terms.

Last but not least, we see monetary and fiscal policy as less restrictive at the margin. We reiterate our view that Banxico will cut the reference rate three more times, each by 25 bps in February, March, and May, with the reference rate closing the year at 6.50%. In terms of fiscal policy, we believe room for stimulus is limited, although the government is aiming for a more modest primary surplus (0.7% from 1.0% expected in 2019). Nonetheless, some risks remain, particularly in terms of revenue given GDP growth forecasts and challenges to oil production, among the most relevant. Lastly, although we think uncertainty will decline, we cannot discard the possibility of renewed shocks, especially due to the US election but also taking into account other geopolitical risks, in a context of global economic deceleration.

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We, Gabriel Casillas Olvera, Delia Maria Paredes Mier, Alejandro Padilla Santana, Manuel Jiménez Zaldívar, Tania Abdul Massih Jacobo, Katia Celina Goya Ostos, Juan Carlos Alderete Macal, Víctor Hugo Cortes Castro, Marissa Garza Ostos, Miguel Alejandro Calvo Domínguez, Hugo Armando Gómez Solís, Gerardo Daniel Valle Trujillo, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Santiago Leal Singer, Francisco José Flores Serrano, Luis Leopoldo López Salinas, Jorge Antonio Izquierdo Lobato, Eridani Ruibal Ortega and Leslie Thalía Orozco Vélez, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

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