Aggregate supply and demand – External shocks impacting both 4Q19 and the outlook

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Juan Carlos Alderete, CFA
Director of Economic Research
juan.alderete.macal@banorte.com

Francisco Flores
Senior Economist, Mexico
francisco.flores.serrano@banorte.com

- **Aggregate supply and demand (4Q19): -1.6% y/y; Banorte: -1.1%; consensus: -0.9% (range: -1.6% to -0.4%); previous: -0.2%**
- **As a result, aggregate demand in full-year 2019 fell 0.4% y/y, below last year's +3.1% and lowest since 2009 (-7.8%). Most of the weakness is explained by investment (contribution: -73bps), coupled with a steep deceleration in private consumption (+29bps)**
- **In the fourth quarter, investment was a heavy drag at -5.2% y/y, while exports (-2.8%) and imports (-4.5%) were impacted by the shock to the auto sector in the early part of the quarter. On the contrary, consumption was marginally better at 0.9%**
- **In seasonally adjusted terms we see a similar story, with exports at -4.6% q/q and investment extending its downward trend (-1.4%). On a positive note, government spending was the outperformer at 0.9%**
- **When adjusting for the external shock, figures seemed to show a slightly more positive outlook for the Mexican economy, setting a more favorable backdrop for 2020**
- **However, the effect from the Coronavirus outbreak in the global and domestic economy will probably more than fully reverse these gains, particularly in 2Q20 and despite some figures suggesting more favorable dynamics at the start of the year**

Aggregate supply and demand fell 1.6% y/y in 4Q19. This was lower than consensus (-0.9%) but closer to our -1.1% forecast. The main deviation relative to our expectation came from an underestimation of the impact the GM strike and stoppages in other auto plants had on the economy. This was reflected both on imports in the supply side, at -4.5% y/y, and exports on the demand side, at -2.8% (Chart 4). However, in the domestic front figures were more positive, with improvements in private consumption at 0.9% and government spending (-0.2%). Investment also improved, at -5.2% from -6.5% (Chart 3), but was still dragged down by the 12.8% contraction in public investment (Table 1).

With these figures, aggregate supply and demand edged-down 0.4% y/y in full-year 2019, weakest in a decade. Investment was the largest negative contributor at -73bps (-4.9% y/y), impacted by both the private (-50bps; -3.9%) and public sectors (-23bps; -10.8%). In our view, the former was heavily affected by uncertainty, driven by both external and domestic factors, as we previously stated. The latter is consistent with the deceleration in spending from the first year of a new administration, also exacerbated by some austerity measures undertaken by the Federal Government. Consumption moderated strongly, adding only 29bps (0.6%), lowest contribution since 2009. We highlight that all the positive impact from goods (+30bps) stemmed from non-durables (+42bps), with semi-durables flat (+1bp) and durables lower (-12bps), consistent with heightened levels of uncertainty and other adverse shocks.

Government spending subtracted 13bps, while exports added only 29bps (Chart 1). On the supply side, GDP subtracted 11bps and imports -29bps, with the latter impacted by lower investment and consumption.

The quarterly dynamic clearly reflected the shock to autos. In our view, the main evidence of the latter is in both imports (-2.4% q/q) and exports (-4.6%), as shown in Chart 8. In addition, investment moderated its pace of decline at -1.4%, while noting that most of brunt was due to the 5.7% contraction in the public component, lowest since 3Q16. More favorable though, private investment improved relatively to -0.6%, in our view signaling some willingness from businesses to restart halted or delayed projects (Chart 6). With these, total supply and demand fell 0.8%. Meanwhile, consumption was unchanged at 0.0%, with the imported component stronger (0.9%), which is very favorable after last quarter's 3.1% expansion. We believe this was partly explained by: (1) A renewed dynamism possibly related to holiday period shopping and discounts, as explained in previous publications; and (2) additional strength of the Mexican peso. However, the domestic component was weaker at -0.2% (Chart 5), mainly due to the 0.5% decline in goods, albeit the 0.3% uptick in services (Table 2).

Today's figures seemed to show a build-up in momentum for the start of 2020, but the outlook has drastically worsened. It is our take that, excluding the shock to the auto sector on external accounts, these figures suggested that the economy started to gain some momentum late last year. Consumption began to shake off some of the uncertainty, as evidenced by the improvement in the durable goods component. In addition, government spending picked up, also reversing some of the typical sluggishness in the first year of a new administration. On the contrary, the magnitude of the contraction in public investment remains worrisome, likely related to implemented austerity measures and very little fiscal room for the Federal Government. Regarding this, there was some private-sector optimism late last year on actions that could be taken to reactivate it. This comes on top of more recent figures which seemed to show an improvement on overall activity at the start of 2020, such as IP, retailers' advanced sales and soft data such as IMEF's indicators.

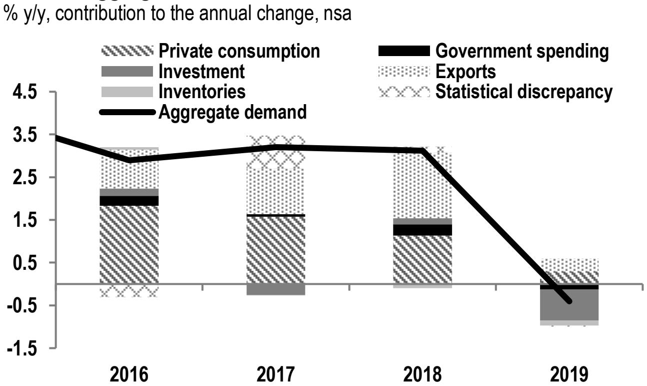
Nevertheless, the COVID-19 outbreak has drastically changed the outlook. Signs from China point to possible disruptions in supply chains as soon as February, awaiting confirmation from the upcoming trade balance report. Moreover, while so far we haven't seen a total shutdown of activities in our country, the stoppage of several plants in the US, particularly in the auto sector, will definitely hit this sector's output in Mexico, which can be highly relevant as seen in today's figures. Moreover, anecdotal evidence already suggests lower services activity, with people much more cautious and starting to work from home, while some businesses halt operations. This could be exacerbated if a generalized quarantine with stringent social-distancing measures is announced, similar to the one during the A(H1N1) outbreak in 2009. In this sense, we expect the brunt of the impact to be felt in 2Q20. However, its magnitude is still highly uncertain as it depends on the duration and evolution of the outbreak, measures to be taken by authorities and possible stimulus measures to be undertaken –both globally and domestically– that will try to stem the strong shock to growth because of the virus.

Table 1: Aggregate demand
% y/y nsa

	4Q19	3Q19	2Q19	1Q19	2019	2018
Aggregate supply	-1.6	-0.2	-1.0	1.3	-0.4	3.1
GDP	-0.5	-0.3	-0.9	1.2	-0.1	2.1
Imports	-4.5	-0.1	-1.3	1.8	-1.1	5.9
Goods	-4.1	-0.3	-1.1	2.6	-0.8	6.3
Services	-13.3	4.8	-5.8	-13.2	-7.0	-2.6
Aggregate demand	-1.6	-0.2	-1.0	1.3	-0.4	3.1
Private consumption	0.9	0.8	-0.2	0.9	0.6	2.3
Domestic	0.6	0.6	0.3	1.3	0.7	2.2
Goods	0.9	1.2	-0.2	0.8	0.7	1.3
Services	0.3	0.1	0.8	1.8	0.7	3.1
Imported	4.9	4.3	-2.0	1.8	2.3	2.9
Goods	5.1	4.8	-0.9	2.9	3.1	3.1
Services	-1.3	-8.9	-29.4	-26.0	-16.9	-0.9
Government spending	-0.2	-2.0	-2.9	-0.8	-1.5	3.0
Investment	-5.2	-6.5	-7.7	-0.2	-4.9	0.9
Private	-3.8	-5.9	-6.7	0.8	-3.9	1.2
Public	-12.8	-9.9	-13.9	-6.0	-10.8	-0.9
Exports	-2.8	2.8	2.0	2.8	1.1	5.9
Goods	-2.6	2.9	2.0	2.5	1.2	6.3
Services	-5.9	0.5	1.9	6.2	0.7	0.7
Inventories	-22.4	-16.2	-16.4	-30.2	-23.8	-15.4
Statistical discrepancy	-33.6	-17.9	15.4	-815.3	-3.7	33.5

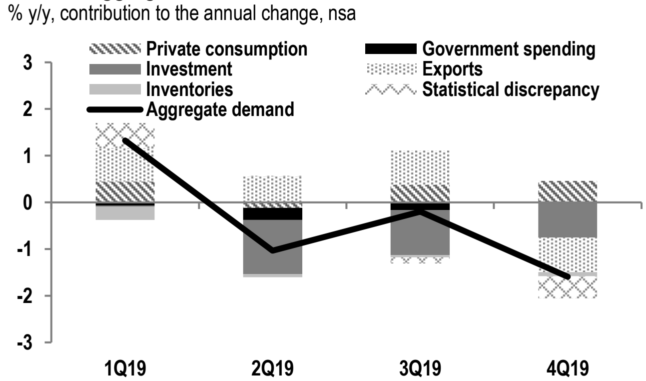
Source: INEGI

Chart 1: Aggregate demand
% y/y, contribution to the annual change, nsa



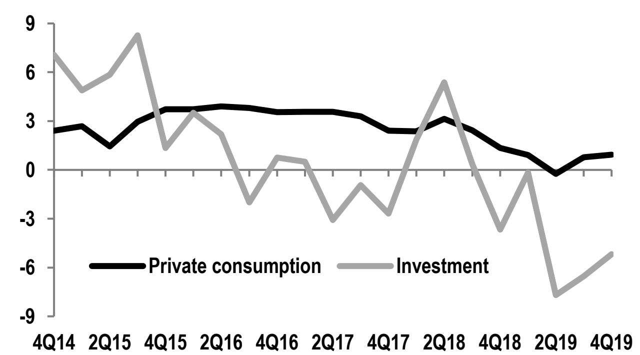
Source: INEGI

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



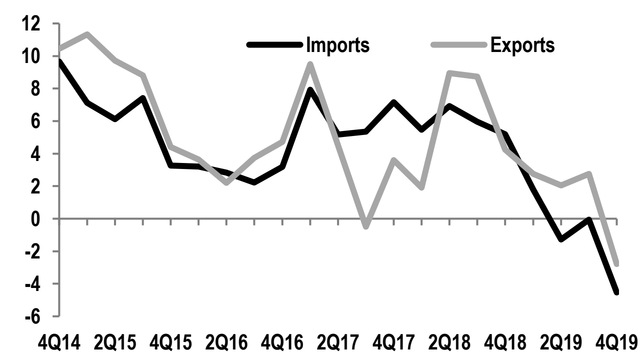
Source: INEGI

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



Source: INEGI

Chart 4: Exports and imports
% y/y nsa



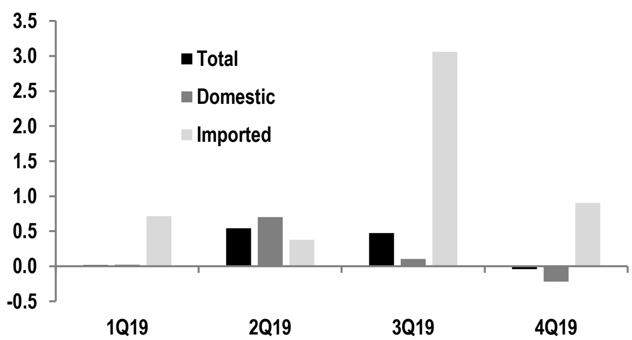
Source: INEGI

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

	% q/q				% q/q saar	
	4Q19	3Q19	2Q19	1Q19	4Q19	3Q19
Aggregate supply	-0.8	-0.1	-0.2	-0.5	-3.0	-0.4
GDP	-0.1	-0.1	-0.1	-0.1	-0.5	-0.3
Imports	-2.4	0.3	-0.3	-2.1	-9.4	1.2
Aggregate demand	-0.8	-0.1	-0.2	-0.5	-3.0	-0.4
Private consumption	0.0	0.5	0.5	0.0	-0.2	1.9
Domestic	-0.2	0.1	0.7	0.0	-0.9	0.4
Goods	-0.5	0.0	0.9	0.6	-1.9	0.1
Services	0.3	0.2	0.1	-0.3	1.2	0.7
Imported	0.9	3.1	0.4	0.7	3.7	12.8
Government spending	0.9	-0.8	-0.3	0.0	3.7	-3.2
Investment	-1.4	-2.2	-3.6	2.5	-5.3	-8.6
Private	-0.6	-2.5	-3.5	3.3	-2.2	-9.7
Public	-5.7	-0.9	-3.2	-3.0	-20.8	-3.6
Exports	-4.6	-0.7	2.3	0.4	-17.1	-2.8
Inventories	-10.3	44.4	33.3	-52.7	-35.2	334.4

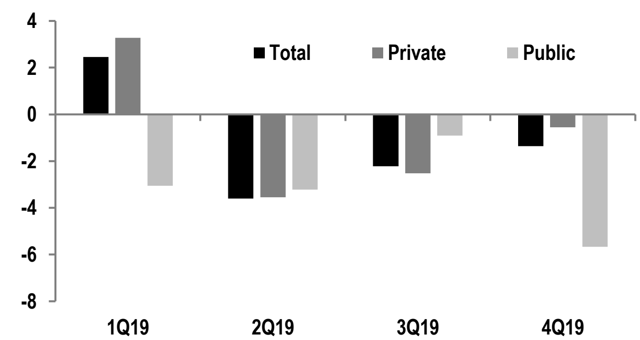
Source: INEGI

Chart 5: Private consumption
% q/q sa



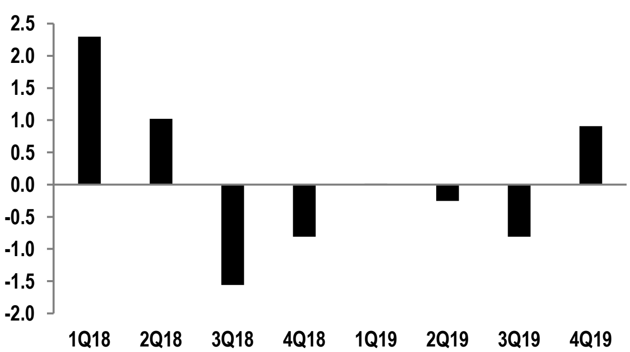
Source: INEGI

Chart 6: Investment
% q/q sa



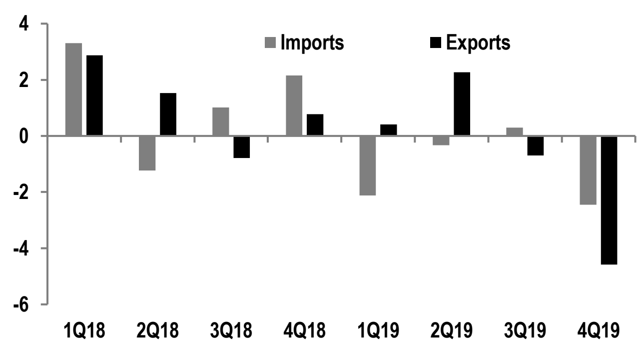
Source: INEGI

Chart 7: Government spending
% q/q sa



Source: INEGI

Chart 8: Exports and imports
% q/q sa



Source: INEGI

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GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Gabriel Casillas Olvera	IRO and Chief Economist	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Economic Research and Financial Market Strategy			
Alejandro Padilla Santana	Executive Director of Economic Research and Financial Markets Strategy	alejandro.padilla@banorte.com	(55) 1103 - 4043
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Economic Research			
Juan Carlos Alderete Macal, CFA	Director of Economic Research	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Senior Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Senior Economist, Global	katia.goya@banorte.com	(55) 1670 - 1821
Luis Leopoldo López Salinas	Economist, Global	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Market Strategy			
Manuel Jiménez Zaldívar	Director of Market Strategy	manuel.jimenez@banorte.com	(55) 5268 - 1671
Fixed income and FX Strategy			
Santiago Leal Singer	Senior Strategist, Fixed Income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Senior Strategist, Equity	valentin.mendoza@banorte.com	(55) 1670 - 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Corporate Debt			
Tania Abdul Massih Jacobo	Director of Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Economic Studies			
Delia María Paredes Mier	Executive Director of Economic Studies	delia.paredes@banorte.com	(55) 5268 - 1694
Miguel Alejandro Calvo Domínguez	Senior Analyst, Economic Studies	miguel.calvo@banorte.com	(55) 1670 - 2220
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.ceballos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Corporate Banking	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454