

## Aggregate supply and demand – Historical decline due to the COVID-19 pandemic

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- **Aggregate supply and demand (1Q20): -21.6% y/y; Banorte: -19.0%; consensus: -19.0% (range: -23.0% to -15.1%); previous: -1.8%**
- **Dynamics in the period were strongly driven by the effects from the COVID-19 pandemic, especially in the first two months of the quarter in which strict lockdown measures were imposed**
- **Weakness was broad, with strong declines in both investment (-34.0% y/y), and consumption (-20.6%), albeit with public spending positive (+2.4%). Regarding the external sector, the impact was stronger, with exports falling sharply due to the stoppage in activity (-30.9%), albeit with imports also in deep contraction (-29.7%)**
- **In sequential terms, we see a similar story, falling 19.8% q/q. We observed significant declines in investment (-29.8% q/q) and exports (-30.5%). Consumption also declined, albeit at a more moderate pace (-19.4%), while government spending edged down 1.0%, although mainly driven by a challenging base effect. Finally, imports were also impacted at -26.6%**
- **We reiterate our expectation of a recovery in 2H20, with the external sector driving the rebound. However, we expect domestic demand to remain somewhat subdued, with uncertainty weighing on investment and consumption**

**Aggregate supply and demand fell 21.6% y/y in 2Q20.** This was lower than consensus (-19.0%), which in this occasion matched our forecast. We should mention that this is the steepest contraction on record (1993), highly impacted by the effects from the COVID-19 pandemic and the measures taken to fight it. On supply, as previously known [GDP fell 18.7% y/y](#), while imports were much weaker at -29.7% ([Chart 4](#)). In a very similar manner and turning to demand, exports fell 30.9%. It should be noted that while the flow of goods was seriously disturbed during the period, both exports and imports of services took the heaviest tolls (see [Table 1](#)). Investment was the hardest hit sector at -34.0%, impacted by both by the stoppage in activities as well as uncertainty clouding capital spending decisions by businesses. In this context, and consistent with the continuation of key projects by the Federal Government, the private component led losses. Consumption was also struck, declining 20.6% ([Chart 3](#)). Once again, the decrease was concentrated in the imported component, consistent with the strong depreciation of the Mexican peso, but also highly influenced by the decline in household income and lockdown measures. Finally, government spending edged-up 2.4%, aided mainly by a less challenging base effect, but also by increased expenditures in healthcare and other social programs, seemingly not compensated by austerity measures in other branches.

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**Quarterly dynamics also reflected the impact of the pandemic.** Aggregate supply and demand declined 19.8% q/q, also a new historical low ([Table 2](#)). Inside, imports declined 26.6% ([Chart 8](#)), already coming from negative territory in 1Q20 as the effects of the pandemic had a toll on trading partners, mainly China and later Europe. However, these came back online in the latter part of 2Q20, also partly supporting this figure. Meanwhile, exports fell more strongly at -30.5%, with a more challenging base effect (as they expanded in the previous quarter), but also with lockdown measures having more of an impact, remembering that on late March they were imposed to try to curb cases down. As a result, there was a mismatch once again in inventories, which after being used in 1Q20, they rose 137.9%, with the build-up taking place mostly in April and May, according to trade balance figures. Going forward, we expect both components to recover, albeit with imports probably lagging behind as non-oil consumption and capital goods remain low as a result of a delay in the recovery of domestic demand. Meanwhile, intermediate imports and overall exports could outperform, with activity abroad supported by stimulus packages –especially in the US–.

In the domestic front, investment plunged 29.8%, now with five consecutive quarters lower. Consistent with economic conditions as well as specific measures taken as part of the lockdown –in which the government continued to develop key infrastructure projects while the rest of construction was stopped–, the private sector was the hardest hit at -33.2%. Meanwhile, public investment only declined 4.4% ([Chart 6](#)). Consumption declined 19.4%, and as already mentioned, with a significant difference between the imported component at -30.0%, relative to the domestic sector at -19.4% ([Chart 5](#)). Within the latter, goods (-18.2%) outperformed services (-21.0%). While we expected the spread among these two to have been greater due to the conditions surrounding the pandemic, the latter is partially benefited by a more favorable base effect. In this sense, more timely data, such as the monthly consumption indicator suggested that people continued to favor purchases of essential goods, with durable and semi-durable goods declining sharply. Lastly, government spending declined 1.0%, which we believe is mainly related to a challenging base effect as this category expanded 3.1% in the previous quarter ([Chart 7](#)).

**We expect a recovery in 2H20, driven by external demand.** As expected, today's figures show that the COVID-19 pandemic had a broad and significant impact across the economy in 2Q20. However, and considering more timely data, activity showed signals of a recovery since June and through August, although with [mixed signals in the latter month](#). In this sense, we still forecast activity to recover in the second half of the year, maintaining our -9.8% y/y estimate for GDP. We note that: (1) Other activities, particularly in services, have been gradually reopening, helping dynamism at the margin; and (2) epidemiological conditions have improved in the last few weeks, a situation which bodes well for the economy. Regarding the latter, we believe containment measures would be more focalized even if we experience a new rise in cases, avoiding a nationwide lockdown. Considering this, as well as the latest signals from data, we believe risks to our estimate are broadly balanced.

Specifically, we expect the rebound to be driven by the external sector, with exports possibly returning to positive territory in the annual comparison by the end of the year. This would be supported by significant stimulus actions taken by several trading partners, mainly in the US, where both monetary and fiscal actions have occurred to support aggregate demand. This would also have a favorable impact on intermediate goods within imports, as they are mostly inputs for the production process. Other sectors that could benefit include transportation services and other industrial sectors indirectly helped by strength in manufacturing.

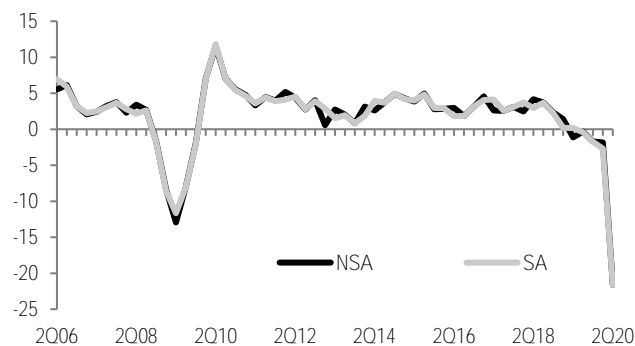
Domestically, we expect the recovery to take longer. We think uncertainty will continue weighing heavily on both investment and consumption. On the former, a significant number of businesses have experienced relevant shocks, compromising their capital allocation decisions in the short-term and with capex probably resuming until the scenario becomes clearer. A similar situation will probably happen on residential investment, with consumers delaying acquisitions big-ticket items, such as property. This will probably extend until a vaccine is readily available, although we do not rule out an earlier recovery once this is announced. On consumption, even after fundamentals recover –showing marginal progress at least [regarding employment](#)–, people will probably remain cautious, building-up at least some savings before resuming the purchase of durable goods. In addition, fear of the virus will continue impacting services the most, especially those more dependent on social interaction or large gatherings (*e.g.* entertainment and tourism). Finally, on government spending, we expect [austerity measures](#) to more than compensate for increased expenditures on healthcare and programs to combat the economic effects of the pandemic, which will probably be a drag going forward.

Table 1: Aggregate demand  
% y/y nsa, % y/y sa

	% y/y nsa						% y/y sa	
	2020	1Q20	4Q19	3Q19	Jan-Jun'20	Jan-Jun'19	2020	1Q20
Aggregate supply	-21.6	-1.8	-1.7	-0.3	-11.8	0.1	-21.6	-2.7
GDP	-18.7	-1.3	-0.7	-0.4	-10.1	0.0	-18.7	-2.1
Imports	-29.7	-3.2	-4.3	-0.1	-16.7	0.4	-29.7	-5.0
Goods	-28.6	-2.9	-4.2	-0.3	-16.0	0.7	--	--
Services	-53.7	-10.1	-7.1	2.4	-31.4	-5.1	--	--
Aggregate demand	-21.6	-1.8	-1.7	-0.3	-11.8	0.1	-21.6	-2.7
Private consumption	-20.6	-0.5	0.7	0.5	-10.6	0.2	-20.6	-1.2
Domestic	-20.9	-0.7	0.3	0.3	-10.8	0.6	-20.9	-1.4
Goods	-19.1	0.7	0.6	0.9	-9.2	0.0	-19.2	-0.3
Services	-22.6	-2.0	-0.1	-0.2	-12.3	1.2	-22.6	-1.9
Imported	-31.3	-1.7	5.0	4.6	-16.6	-0.1	-31.3	-1.8
Goods	-30.0	-1.3	5.1	4.8	-15.7	0.9	--	--
Services	-77.5	-14.9	2.0	-2.3	-44.9	-25.5	--	--
Government spending	2.4	3.4	-0.4	-1.7	2.9	-1.7	2.4	3.3
Investment	-34.0	-9.3	-5.3	-6.8	-21.4	-4.1	-34.0	-9.5
Private	-37.3	-9.6	-4.4	-6.7	-23.2	-3.1	-37.4	-9.8
Public	-10.5	-7.0	-10.0	-8.0	-8.7	-10.3	-10.2	-7.2
Exports	-30.9	1.8	-2.2	2.9	-15.3	2.6	-31.1	1.8
Goods	-27.9	2.6	-2.6	2.9	-13.4	2.2	--	--
Services	-74.4	-8.5	2.5	3.4	-39.7	7.5	--	--
Inventories	-17.0	-23.7	-23.1	-17.8	-21.1	-28.7	-16.2	-44.7
Statistical discrepancy	--	--	-39.5	-22.7	736.9	--	--	--

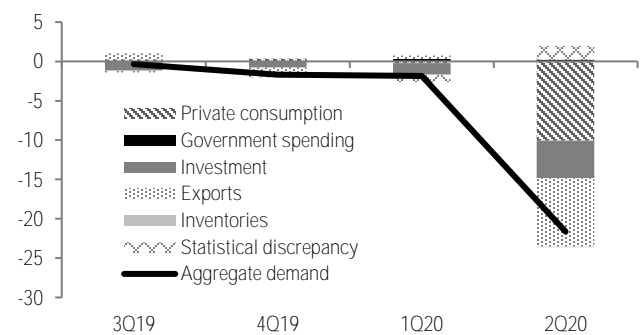
Source: INEGI

Chart 1: Aggregate demand  
% y/y nsa, % y/y sa



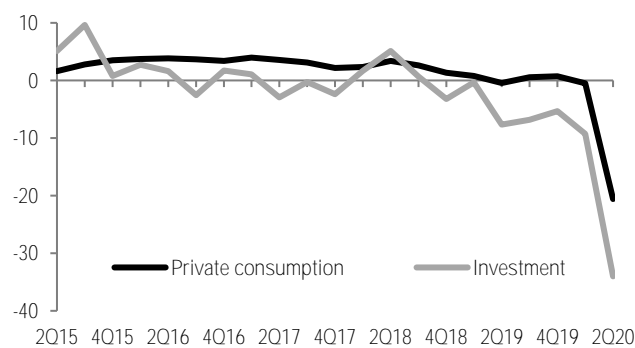
Source: INEGI

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



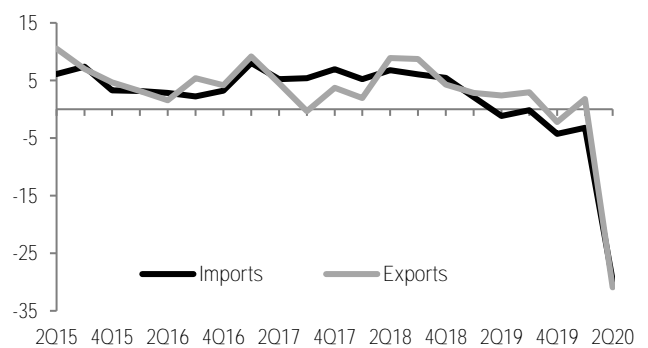
Source: INEGI

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



Source: INEGI

Chart 4: Exports and imports  
% y/y nsa



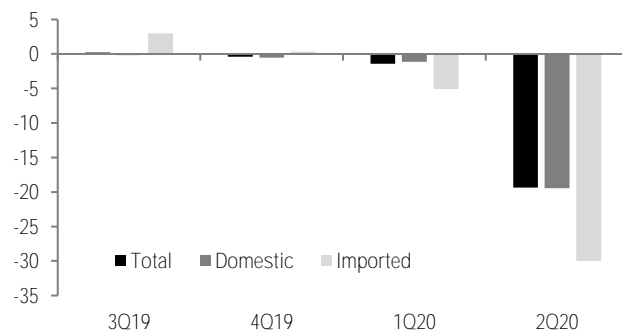
Source: INEGI

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

	% q/q sa				% q/q saar	
	2020	1Q20	4Q19	3Q19	2020	1Q20
Aggregate supply	-19.8	-1.1	-1.1	-0.2	-58.5	-4.3
GDP	-17.1	-1.2	-0.6	-0.2	-52.7	-4.6
Imports	-26.6	-1.7	-2.7	0.1	-70.9	-6.6
Aggregate demand	-19.8	-1.1	-1.1	-0.2	-58.5	-4.3
Private consumption	-19.4	-1.4	-0.4	0.2	-57.7	-5.5
Domestic	-19.4	-1.1	-0.5	-0.2	-57.9	-4.5
Goods	-18.2	-0.3	-0.8	-0.1	-55.3	-1.1
Services	-21.0	-2.3	0.3	0.0	-61.0	-9.0
Imported	-30.0	-5.1	0.4	3.0	-76.0	-18.8
Government spending	-1.0	3.1	0.6	-0.3	-4.1	12.9
Investment	-29.8	-2.2	-1.7	-2.4	-75.7	-8.5
Private	-33.2	-2.3	-1.2	-2.8	-80.1	-8.7
Public	-4.4	-1.9	-4.1	-0.2	-16.6	-7.3
Exports	-30.5	3.1	-3.9	0.0	-76.6	13.1
Inventories	137.9	-64.7	-17.8	21.6	3,101.5	-98.5

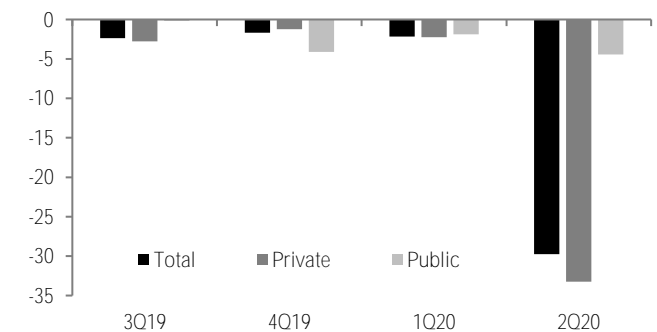
Source: INEGI

Chart 5: Private consumption  
% q/q sa



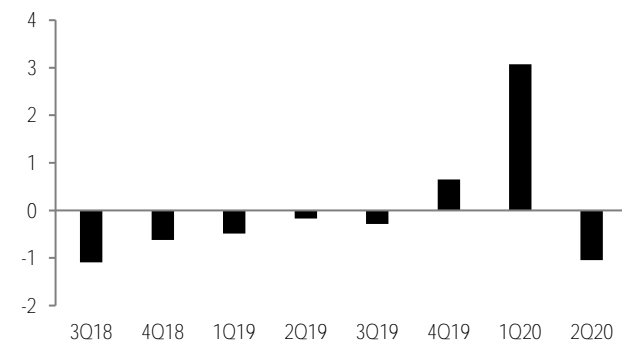
Source: INEGI

Chart 6: Investment  
% q/q sa



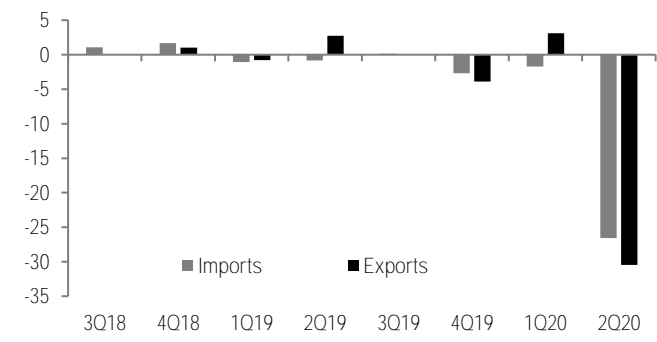
Source: INEGI

Chart 7: Government spending  
% q/q sa



Source: INEGI

Chart 8: Exports and imports  
% q/q sa



Source: INEGI

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