Aggregate supply and demand – Yearly performance determined by the pandemic

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- **Aggregate supply and demand (4Q20): -5.1% y/y; Banorte: -5.4%; consensus: -5.3% (range: -7.5% to -2.9%); previous: -11.4%**
- **With these results, aggregate supply and demand fell 10.0% y/y in 2020, strongly impacted by the pandemic. Inside, domestic sectors were weakest, highlighting investment (-18.2%) and consumption (-10.4%). Exports showed a better performance (-7.3%), aided by a recovery in 2H20**
- **In sequential terms, the headline figure in 4Q20 posted a 4.8% q/q expansion. Gains were centered in consumption (5.3%), with a boost from *El Buen Fin* (Mexico's Black Friday), and investment (2.9%). Exports were more modest at +1.6%, albeit only after a whopping 40.3% expansion in the previous quarter. Lastly, imports rose 9.2%**
- **We maintain our expectation of a recovery in 2021, anticipating GDP to grow 5.3% y/y on the back of an additional boost from external demand. However, we remain cautious about performance of domestic-facing sectors, as the business climate remains somewhat subdued**

Aggregate supply and demand posted a 10.0% y/y decline in 2020. This represents the sharpest contraction since the series is available (1994), with dynamics throughout the year impacted by the COVID-19 pandemic and the efforts to combat it. On the supply side, as already known, GDP declined 8.2% y/y, while imports were much weaker at -14.8%. On the latter, we believe the depreciation of the Mexican peso coupled with the hit on employment seriously impacted flows. In this context, services were the weakest at -39.2%, with final and capital goods also low at -14.4% and -16.3%, respectively. Turning to demand, the divide was clear between domestic and external sectors, with the latter managing a more modest decline. In this sense, exports were down 7.3%, with services very low at -41.9%, while goods were stronger at -4.7%. Meanwhile, investment plummeted 18.2%, second weakest in the series, with uncertainty as a key driver behind the contraction. Inside, public GFI declined 7.5%, adding eleven consecutive years down. Meanwhile, the private component fell 19.8%. This sector was the most impacted by the time of the lockdowns, while also having a more challenging base effect, resulting in a deeper contraction. Consumption fell 10.4%. Consistent with the nature of the shock, total services (adding domestic and imported) were the weakest at -14.4%, as social interaction decreased considerably. However, spending in durable and semi-durable goods fell sharply on high uncertainty and job losses, reaching -20.8% and -23.4%, in the same order. However, non-durables were better at -1.8%. These differences are especially evident after breaking down the figures by domestic and imported branches, as seen in Table 1. Lastly, government spending was up 2.3%, in our view aided by a less challenging base effect but also due to additional spending in healthcare and other social programs, which might carry more value added.

Better overall performance in 4Q20. Aggregate supply and demand contracted 5.1% y/y in the quarter, close to consensus (-5.3%) and our 5.4% estimate. This was stronger than the -11.4% seen in 3Q20, which already showed signs of the beginning of the recovery. As we detailed in previous releases, the first months of the period were characterized by efforts to extend the reopening of the economy, with a deceleration towards the end as epidemiological conditions became more complicated. On supply, GDP declined 4.3%, with industry better than services. Meanwhile, imports still lagged at -7.1% (Chart 4), albeit with a relevant boost from intermediate goods (-3.9%), in turn closely related to the manufacturing sector. Turning to demand, consumption stood at -7.2% (Chart 3), in our view benefited by *El Buen Fin* discounts (Mexico's Black Friday) and other seasonal purchases. However, the most impacted categories were still services, both imported (-60.9%) and domestic (-13.9%). Investment remained as the weakest at -12.7%, with the public sector surprising higher at -1.7%, while private GFI was lower at -14.6%. By type, construction outperformed at -12.2%, driven by better prints early in the period, while machinery and equipment stood at -13.3%. Meanwhile, government spending came in at 1.6%. Lastly, and focusing on the external front, exports returned to positive territory at 3.7%, with strong dynamism in goods (6.7%), especially non-oil (6.9%), with services still weak (-38.1%).

Quarterly dynamics kept improving in almost all sectors. Aggregate supply and demand rose 4.8% q/q, building up on the +13.4% of the previous quarter (Table 2). Regarding supply, imports were higher at 9.2% (Chart 8), benefited by a less challenging base, albeit with some dynamism as raw materials were needed to support exports. However, there was also a significant drawdown in inventories at -14.1%, in our view impacted by some delays in customs and other restrictions, such as new labeling laws. Meanwhile, and as previously published, GDP rose 3.3%.

Turning to demand, consumption was the outperformer at +5.3%. As already explained, we believe there was a boost from seasonal discounts, especially favoring imported goods and services at +16.0% (Chart 5). Still positive, domestic categories extended higher, albeit still noting a relatively large gap between goods and services as conditions continued to dampen the latter. Meanwhile, investment also posted a somewhat large increase at 2.9%, with the public sector edging-out the private one at 3.4% vs 2.4% (Chart 6), respectively. We believe that one driver that may have contributed to this is the beginning of private-public projects announced early in the quarter, while also counting with advances on some of the key infrastructure projects from the Federal Government. However, on non-capital outlays, government spending declined 0.2%, reversing gains in the previous quarter (Chart 7). Lastly, on exports we saw a 1.6% expansion, rather positive considering the 40.3% advance in 3Q20. As a result, this component now stands above pre-pandemic levels, in our view largely supported by massive stimulus from abroad, especially in the US.

We expect a recovery in 2021, with external demand as the main driver. We recently revised our GDP forecast for this year to 5.3% y/y from 4.1% previously. While we already believed the rebound in activity would come from external demand –through higher exports–, the approval of the US$1.9 trillion stimulus plan provided a boost to our previous expectations. This comes on top of our relatively more positive mid-term view, mainly supported by the progress in the vaccination program. However, the short-term scenario remains complex, with available evidence so far supporting our call of a 0.2% q/q sequential decline in 1Q21.

In particular, data so far suggest weak readings due to: (1) Pandemic restrictions throughout January and early February; and (2) Adverse shocks from climate conditions, resulting in blackouts and disruptions to the supply of natural gas. This has been reflected mostly in soft data and other estimates, such as INEGI's *Timely Indicator of Economic Activity* which anticipates a sequential contraction in the second month of the year. More positively, we saw a sharp improvement in epidemiological conditions since the second half of February that has extended to March. Moreover, the normalization in energy supply was relatively fast. Therefore, the economy in March is likely to be stronger following these shocks at the start of the year.

We believe the outlook for 2Q21 and beyond is more favorable despite prevailing risks to the downside. Among the latter we highlight supply-chain issues because of scarcity in semiconductors and other raw materials, obliging production delays on bottlenecks in several sectors. This is most evident in autos, with companies implementing 'technical' stoppages. Industry insiders have stated the situation might normalize until early in the summer. Turning to other positive developments domestically, we note recent news that the US will give our country 2.5 million doses of the AstraZeneca vaccine, which has been supported by several health agencies worldwide after some reports questioning its safety. This should help speed up the process, which so far has been volatile given the availability of vaccines. In turn, this could possibly allow for socially-dependent activities (as well as the economy more broadly) to get back on track sooner.

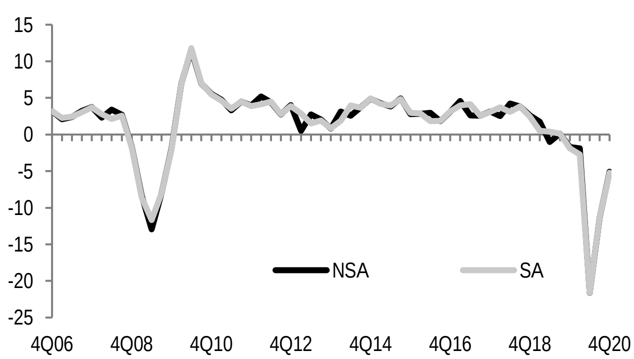
All in all, we expect aggregate supply and demand to continue showing a relevant divide among sectors, with external-facing ones leading the way and domestic ones somewhat subdued. Within the latter, consumption will probably be aided by spillover effects from US stimulus and fatigue about the pandemic. In contrast, we remain more concerned about investment. This is a result of still difficult business climate, especially given recent anti-market legislation proposals out of Congress. In this context, we believe that a necessary condition for a sustainable recovery is the need to see a sharp rebound in investment levels.

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

	% y/y nsa						% y/y sa	
	4Q20	3Q20	4Q19	3Q19	2020	2019	4Q20	4Q19
Aggregate supply	-5.1	-11.4	-1.7	0.1	-10.0	-0.2	-5.2	-1.9
GDP	-4.3	-8.6	-0.6	0.0	-8.2	-0.1	-4.5	-0.8
Imports	-7.1	-18.5	-4.5	0.6	-14.8	-0.7	-7.3	-4.8
Goods	-5.0	-16.7	-4.2	-0.2	-13.5	-0.7	--	--
Services	-51.3	-48.9	-11.5	15.3	-39.2	-0.4	--	--
Aggregate demand	-5.1	-11.4	-1.7	0.1	-10.0	-0.2	-5.2	-1.9
Private consumption	-7.2	-12.7	0.6	0.8	-10.4	0.6	-7.3	0.6
Domestic	-7.5	-12.2	0.2	0.6	-10.5	0.7	-7.6	0.2
Goods	-1.0	-5.9	0.0	0.1	-6.6	-0.1	-1.0	0.0
Services	-13.9	-18.1	0.4	1.0	-14.1	1.4	-14.0	0.3
Imported	-9.6	-23.0	4.6	4.8	-16.4	2.5	-9.7	4.7
Goods	-8.0	-21.2	5.0	4.9	-15.1	3.1	--	--
Services	-60.9	-68.1	-5.3	2.5	-54.2	-12.9	--	--
Government spending	1.6	2.5	-0.4	-1.6	2.3	-1.3	1.7	-0.2
Investment	-12.7	-18.0	-4.8	-6.4	-18.2	-4.6	-13.0	-4.8
Private	-14.6	-18.9	-3.4	-5.8	-19.8	-3.4	-14.9	-3.6
Public	-1.7	-12.5	-11.6	-10.6	-7.5	-11.9	-2.1	-11.8
Exports	3.7	-2.7	-2.4	2.9	-7.3	1.5	3.8	-2.3
Goods	6.7	0.5	-2.4	2.5	-4.7	1.2	--	--
Services	-38.1	-51.3	-2.3	7.8	-41.9	5.2	--	--
Inventories	-3.5	-7.4	-36.8	-27.4	-10.2	-38.7	-5.0	-31.5
Statistical discrepancy	-76.6	--	-32.6	23.1	-85.1	11.4	--	--

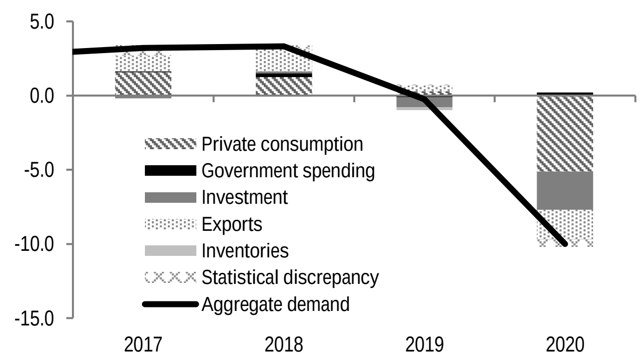
Source: INEGI

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



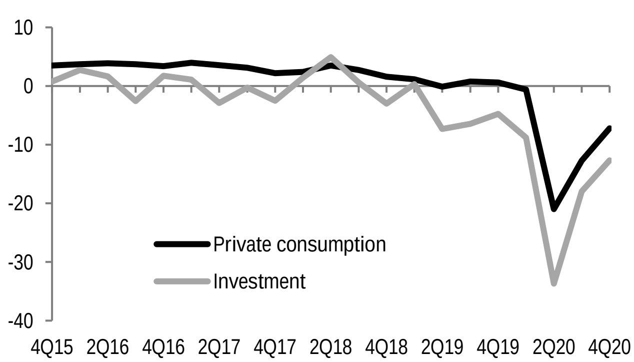
Source: INEGI

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



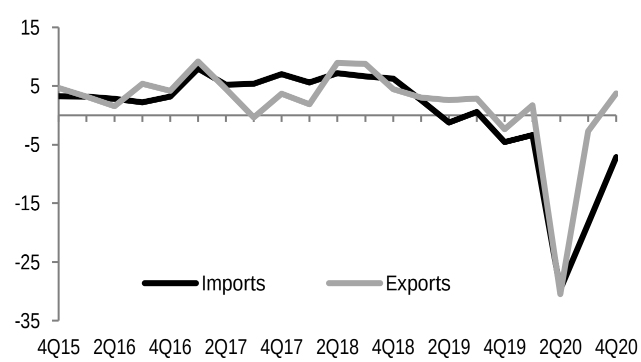
Source: INEGI

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



Source: INEGI

Chart 4: Exports and imports
% y/y nsa



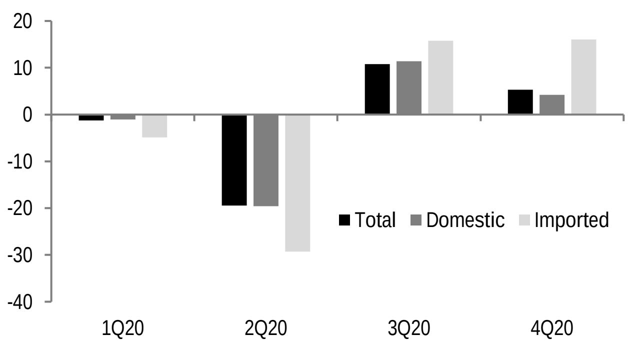
Source: INEGI

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

	% q/q sa				% q/q saar	
	4Q20	3Q20	2Q20	1Q20	4Q20	3Q20
Aggregate supply	4.8	13.4	-19.5	-1.0	20.8	65.5
GDP	3.3	12.4	-16.8	-1.0	13.7	59.6
Imports	9.2	17.1	-26.2	-1.8	42.3	87.8
Aggregate demand	4.8	13.4	-19.5	-1.0	20.8	65.5
Private consumption	5.3	10.8	-19.5	-1.2	22.9	50.5
Domestic	4.2	11.4	-19.6	-1.0	18.1	54.0
Goods	3.9	16.7	-18.1	-0.4	16.7	85.7
Services	4.5	6.5	-21.3	-1.9	19.5	28.8
Imported	16.0	15.8	-29.3	-4.9	81.2	79.8
Government spending	-0.2	0.2	-1.2	2.9	-0.8	0.8
Investment	2.9	21.9	-29.6	-1.5	12.2	120.8
Private	2.4	26.4	-33.0	-1.9	9.8	155.2
Public	3.4	-1.6	-4.0	0.3	14.2	-6.3
Exports	1.6	40.3	-29.6	3.5	6.5	287.6
Inventories	-14.1	34.0	207.3	-73.1	-45.6	222.1

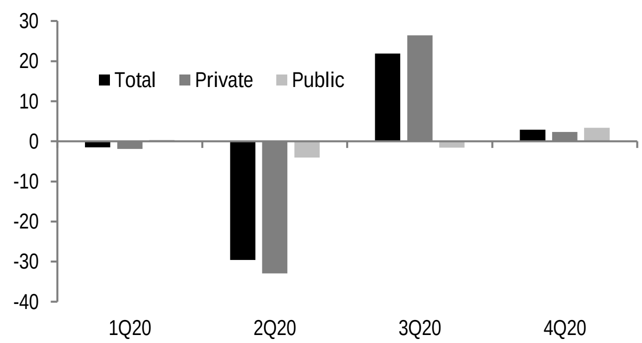
Source: INEGI

Chart 5: Private consumption
% q/q sa



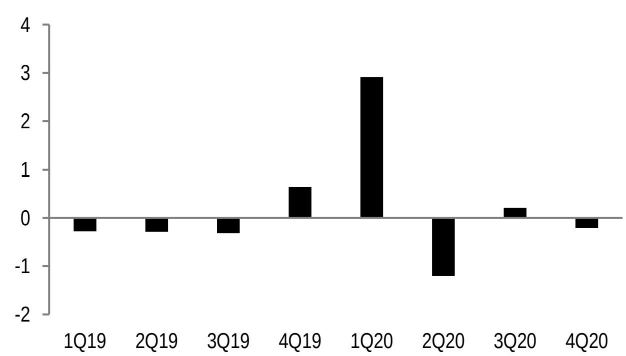
Source: INEGI

Chart 6: Investment
% q/q sa



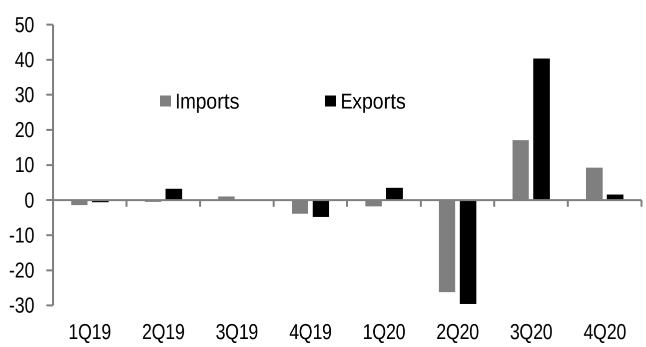
Source: INEGI

Chart 7: Government spending
% q/q sa



Source: INEGI

Chart 8: Exports and imports
% q/q sa



Source: INEGI

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