Domestic demand moderates in February, but the outlook seems slightly better

- **Gross fixed investment (February): -4.5% y/y (nsa); Banorte: -3.2%; consensus: -4.3% (range: -9.7% to -1.6%); previous: -10.6%**
- **Private consumption (February): -7.5% y/y (nsa); previous: -7.6%**
- **We should mention that annual rates are skewed due to the leap year in 2020, albeit partly offset by the fact that working days remained unchanged**
- **In sequential terms, investment rose 2.4% m/m, boosted by construction (2.5%), with the residential sector leading gains. Machinery and equipment were somewhat mixed (1.5%), with strength in imported and weakness in the domestic branch**
- **Consumption backtracked 0.2% m/m, with all categories down except domestic services, while imported goods were weakest at -1.8%. This suggests some cautiousness among consumers after a relatively strong start of the year**
- **Despite a slight downward surprise, this report and more timely data suggest that domestic demand may be recovering faster than expected, supporting our view of a 5.9% increase in 2021 GDP**

GFI kept improving in February. This came at -4.5% y/y (see Chart 1), close to consensus (-4.3%) but below our -3.2%. The period has a negative calendar effect, with one fewer day in the annual comparison due to the leap year, albeit partly offset by the fact that working days remained unchanged. Correcting for this with seasonally adjusted figures, it fell 3.5% (previous: -9.6%). Meanwhile, data starts to get somewhat distorted by the initial effects from the pandemic. Back to original figures (nsa), construction stood at -5.9% (Chart 2). Following on the trend of previous months, the residential sector outpaced non-residential, at -2.9% and -9.2%, respectively, as flagged by industrial production. Machinery and equipment came in at -2.2%. In annual terms, the imported component climbed 3.4%, which was the main downside surprise relative to our call as transportation equipment plunged 25.4%. Even with this, the domestic one was weaker at -10.3%, dragged also by transportation (-15.8%), with 'other' also down at -2.3%, as shown in Table 1.

Nevertheless, using seasonally adjusted figures, investment rose 2.4% m/m, very positive considering the strong 3.9% expansion seen in January (Chart 3). As a result, activity stands 17.2% below July 2018's historical high (Chart 4), with still a long way ahead for a full recovery. In line with the comment mentioned above, we noted some weakness in domestic machinery and equipment (-1.9%) as both components were negative. In our opinion, these were likely affected by blackouts and the lack of natural gas. This was more evident in transportation (-2.1%). Meanwhile, the imported one climbed 1.9%, consistent –but below– capital goods imports within the trade balance. Construction grew 2.6%, driven by the rebound of 2.5% in the residential sector, after a relatively slow start of the year (Table 2).

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Meanwhile, and in our opinion more relevant, the non-residential came in at 1.6%, extending the move higher after the strong pickup in January. This could be related to increased spending in infrastructure ahead of the elections. Moreover, it is consistent with prevailing signals within public finance data about physical investment spending by the Federal Government.

Private consumption backtracks after a strong performance in January. This component of aggregated demand stood at -7.5% y/y, slightly above the -7.6% of the previous month (Chart 5). As in GFI, calendar effects also distorted the result. With seasonally adjusted figures the contraction was 6.5% y/y (just before the pandemic started), a touch lower than in January (-6.2%). Back to original figures, imported goods stayed stronger (2.1%), particularly durable goods (11.1%), in contrast with semi-durables (-9.7%) (Table 3). Domestic goods were mostly stable and still negative at -1.8%, with non-durables up 1.2% and all others in contraction, along with services which remain as the underperformers as they fell 14.6% (Chart 6), still resenting the effects from the pandemic.

With seasonally adjusted figures, consumption backtracked 0.2% m/m, partially erasing the previous month's advance (Chart 7). In our view, this suggests some cautiousness among consumers after a relatively strong start of the year. In turn, this was probably related to worsening conditions about the pandemic since the end of 2020 and until about the middle of the month. Particularly, and in contrast with annual rates, imported goods plunged 1.8%, likely owing to a very strong result in January (+3.6%). The domestic component was more modest (-0.3%), with services up 0.4% and goods down 0.2%, also with some payback from a strong start of the year.

Despite a slight downward surprise, this report and more timely data suggest that domestic demand may be recovering faster than expected. We think today's results support our call that domestic conditions are turning more positive, especially with investment better than our expectations at the start of the year. Although we recognize this owes a lot to the deep slowdown already seen since mid-2018 (when it reached an historical high), recent data suggests that a bottom may be in the making. Consumption surprised us also lower, although we think fundamentals have been recovering and that its sequential contraction may be related to a difficult base effect given a good start of the year. We still expect these to keep lagging, with more dynamism from the external component. Nevertheless, it seems that differences among them might be narrowing, despite likely remaining weaker.

The latter seems to be supported by timelier data, including March's trade balance. On investment, capital goods imports rose 8.9% m/m, its largest expansion since early 2015 and stringing five months to the upside. As mentioned above, although the initial point is very weak, prevailing uncertainty between the US and China should keep favoring our country. In this context, some experts have pointed out to anecdotal evidence that interest in the opening of industrial parks –especially in northern states of the country– has increased strongly. Apart from China, nearshoring strategies and less reliance on 'just in time' schemes may also be helping, given the problems faced by companies due to the pandemic.

Meanwhile, we have recently had positive news of business investments from private companies. Among them, we highlight: (1) GM's announcement of an investment of over US$1 billion in Ramos Arizpe, Coahuila, oriented to the production of EVs; (2) CAPEX from Bimbo between US$900 million and US$1 billion, which would be the highest in a decade; and (3) Mercado Libre (a LATAM competitor similar to eBay) will invest US$1.1billion in distribution centers. Despite of this, we still think there are important hurdles to attract more FDI. Businesses in the US have raised their concerns more forcefully through official channels within their government about proposed law changes that are in contradiction with USMCA rules –especially in the energy sector. This treaty aims to provide more certainty to foreigners, so the risk is that these proposals undermine some of its benefits. We also add persistent concerns about security and other rule of law issues, as observed in the latest survey from the central bank.

Going to consumption, the outlook also seems more favorable, in our view. In this respect, non-oil consumption goods imports in March surged 8.7% m/m, highest since last November. Other signals point to higher dynamism in non-essential sectors, as suggested by ANTAD sales. Moreover, we are starting to see the first results in tourism for April, accelerating at the margin (probably tied to the *Easter* holiday). More structurally, employment has extended its positive trend, with sizeable gains since February. We believe this is key, given that if this situation keeps improving, confidence among families will rise and the possibility of a resumption of usual consumption patterns will increase. In addition, fiscal stimulus in the US should keep supporting, both due to positive spillover in terms of activity, as well as due to remittances, which registered a new historical high in March.

In this context, and after the release of preliminary GDP for 1Q21, which surprised to the upside, we recently revised our growth estimate for the year to 5.9% from 5.3%. Although part of this change is explained by a better performance of external-facing sectors, it is also motivated by an improvement in our outlook for domestic demand.

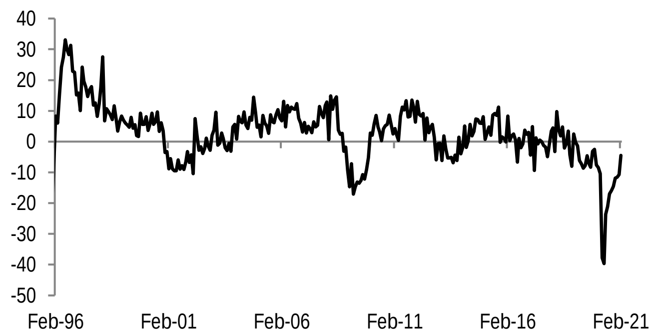
Gross Fixed Investment

Table 1: Gross fixed investment
% y/y nsa

	nsa				sa	
	Feb-21	Feb-20	Jan-**Feb'21**	Jan-**Feb'20**	Feb-21	Feb-20
Total	-4.5	-8.4	-7.7	-8.0	-3.5	-10.5
Construction	-5.9	-7.6	-8.8	-6.8	-6.7	-8.4
Residential	-2.9	-6.8	-5.7	-7.0	-3.5	-7.7
Non-residential	-9.2	-8.5	-11.9	-6.5	-10.1	-9.6
Machinery and equipment	-2.2	-9.7	-6.0	-9.9	1.6	-14.2
Domestic	-10.3	-5.4	-11.7	-5.1	-10.9	-5.8
Transportation Equipment	-15.8	-6.3	-16.8	-7.0	-16.7	-7.9
Other machinery and equipment	-2.3	-4.0	-4.5	-2.4	-2.8	-3.5
Imported	3.4	-12.5	-2.4	-12.7	4.3	-14.0
Transportation Equipment	-25.4	-3.4	-23.9	-13.4	-24.4	-9.3
Other machinery and equipment	9.1	-14.1	1.1	-12.6	10.2	-15.0

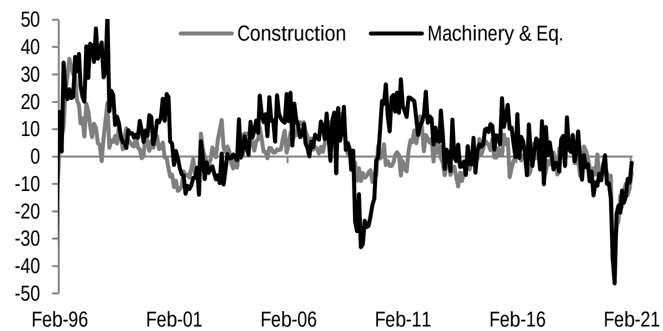
Source: INEGI

Chart 1: Gross fixed investment
% y/y



Source: INEGI

Chart 2: Gross fixed investment by sector
% y/y



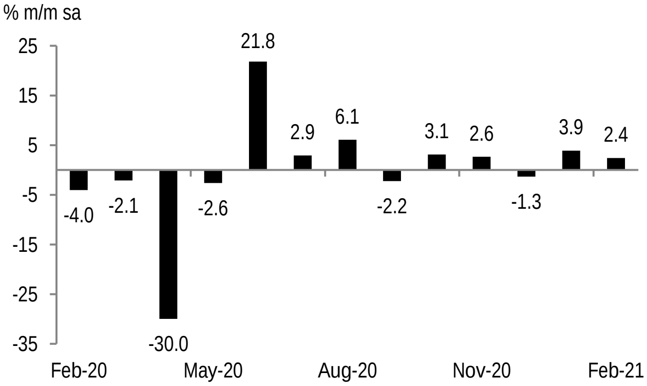
Source: INEGI

Table 2: Gross fixed investment
% m/m sa; % 3m/3m sa

	% m/m			% 3m/3m	
	Feb-21	Jan-21	Dec-20	**Dec'20**-**Feb'21**	**Nov'20**-**Jan'21**
Total	2.4	3.9	-1.3	21.0	18.7
Construction	2.6	3.6	-2.2	19.0	14.4
Residential	2.5	1.2	-6.7	7.1	21.0
Non-residential	1.6	8.2	-2.8	19.4	9.8
Machinery and equipment	1.5	4.3	-1.7	17.8	20.7
Domestic	-1.9	3.5	-1.5	7.0	14.7
Transportation Equipment	-2.1	8.0	0.9	22.3	8.1
Other machinery and equipment	-1.5	0.6	-0.7	-2.9	12.4
Imported	1.9	4.3	0.2	24.2	21.5
Transportation Equipment	5.1	3.7	-3.9	9.6	31.2
Other machinery and equipment	1.6	4.9	0.9	29.1	22.5

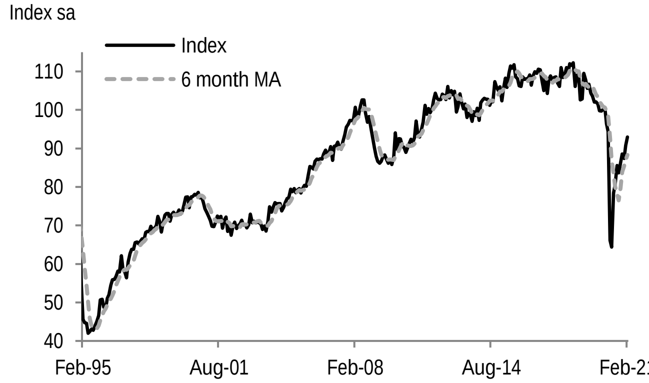
Source: INEGI

Chart 3: Gross fixed investment
% m/m sa



Source: INEGI

Chart 4: Gross fixed investment
Index sa



Source: INEGI

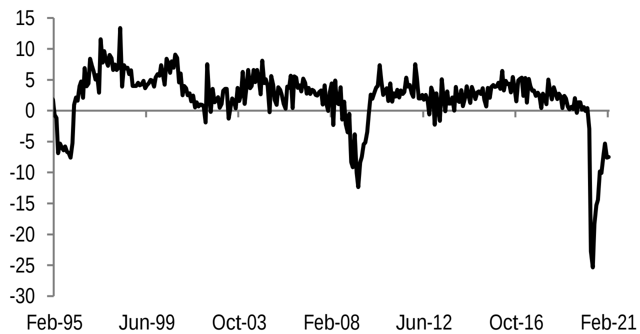
Private consumption

Table 3: Private consumption
% y/y nsa

	nsa				sa	
	Feb-21	Feb-20	Jan-**Feb'21**	Jan-**Feb'20**	Feb-21	Feb-20
Total	-7.5	0.4	-7.5	0.2	-6.5	-0.8
Domestic	-8.6	0.5	-8.4	0.1	-7.6	-0.7
Goods	-1.8	0.2	-2.0	-0.2	-0.5	-1.3
Durables	-7.9	6.5	-8.0	5.2	--	--
Semi-durables	-13.1	-4.2	-11.4	-1.6	--	--
Non-durables	1.2	0.3	0.4	-0.6	--	--
Services	-14.6	0.7	-14.5	0.4	-14.1	0.3
Imported goods	2.1	-0.1	0.1	0.7	2.9	-1.3
Durables	11.1	-8.1	4.4	-7.1	--	--
Semi-durables	-9.7	-1.2	-13.1	-0.7	--	--
Non-durables	2.0	7.1	3.8	8.4	--	--

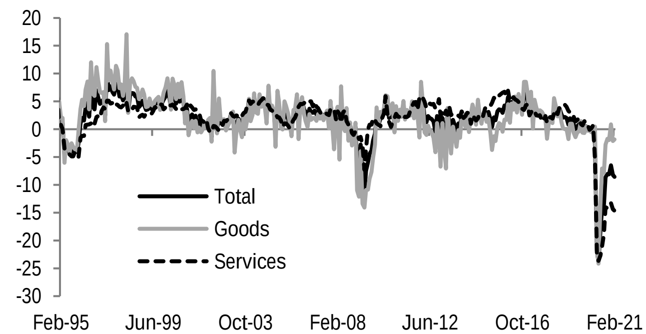
Source: INEGI

Chart 5: Private consumption
% y/y



Source: INEGI

Chart 6: Domestic consumption: Goods and services
% y/y



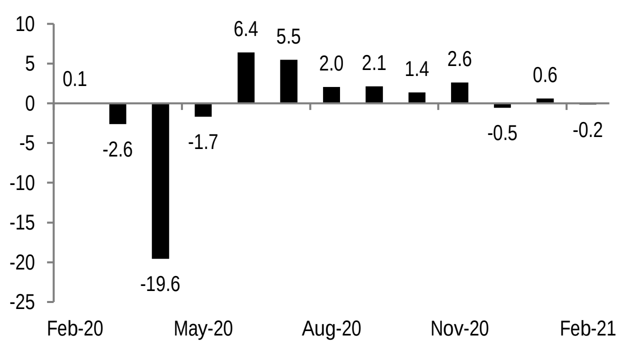
Source: INEGI

Table 4: Private consumption
% m/m sa; % 3m/3m sa

	% m/m			% 3m/3m	
	Feb-21	Jan-21	Dec-20	**Dec'20**-Feb'**21**	**Nov'20**-Jan'**21**
Total	-0.2	0.6	-0.5	2.0	4.1
Domestic	-0.3	0.4	-0.3	0.6	2.1
Goods	-0.2	1.0	-0.5	1.5	2.7
Services	0.4	-0.2	0.6	0.7	1.9
Imported goods	-1.8	3.6	0.0	15.7	23.2

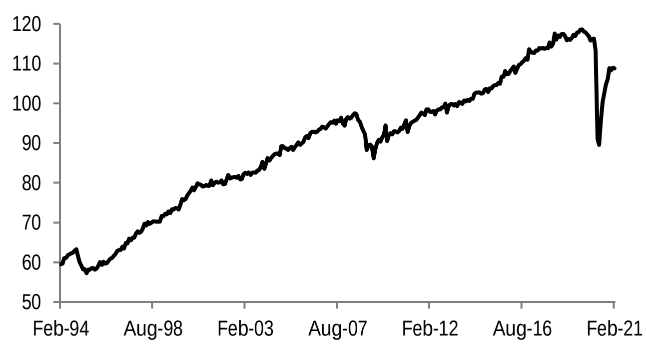
Source: INEGI

Chart 7: Private consumption
% m/m sa



Source: INEGI

Chart 8: Private consumption
Index sa



Source: INEGI

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