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The Company Newsletter for Supply Chain Finance.

E FACTOR NETWORK NEWSLETTER

eFactor network

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Sociedad Financiera Objeto Múltiple E.N.R.

Company News and Highlights

Supply Chain Finance Solutions for Cash Requirement.

Fintech products and market development based on Fundamentals of Economic Theory and Financial Risk.

COMPLICATED START OF THE SIX-TERM: REVIEW OF THE EXPECTATION BASE OF GDP.

Written by Edgardo A. Ayala G.

Negative supply Shocks. The beginning of the administration has been framed in three problems that affect production in the short term. These are the following

- *Petrol shortage*. Framed in the fight against the illegal theft of petrol, called Huachicoleo, the federal government closed ducts and decided to transport the petrol in pipes. The instrumentation was made in hasty form, during December, which is the month with the highest consumption of the energy and with only a couple of days of inventory. In this way, there was a serious shortage of fuel mainly in the Bajio area and the west of the country. Currently, the situation is under control in most parts of the country, the government claims to have significantly increased PEMEX's sales revenue.
- *Maquiladora strikes*. Between January and February of this year were placed on strike or there were blockades in about 50 maquiladoras in Matamoros, in most cases the workers requested a salary increase of 20% and an annual bond of 32000 pesos. It must be recognized that, in many cases, labor contracts established equal or greater wage adjustments to minimum wage increases, so that by increasing the latter by 100% at the border, labor relations would be tightened. It is estimated that the problems affected 5% of the maquiladora production of Tamaulipas in an average duration of 17 days. Most of the cases have been resolved in favor of the workers and only some maquiladoras have chosen to close operations.
- *Blockade of railway lines in Michoacán.* Due to the lack of payment of salaries and benefits, the teachers of the CNTE in Michoacán took the railroads of the state. The blockades lasted for more than six weeks, and it is estimated that they affected business operations in at least 13 states of the Republic.

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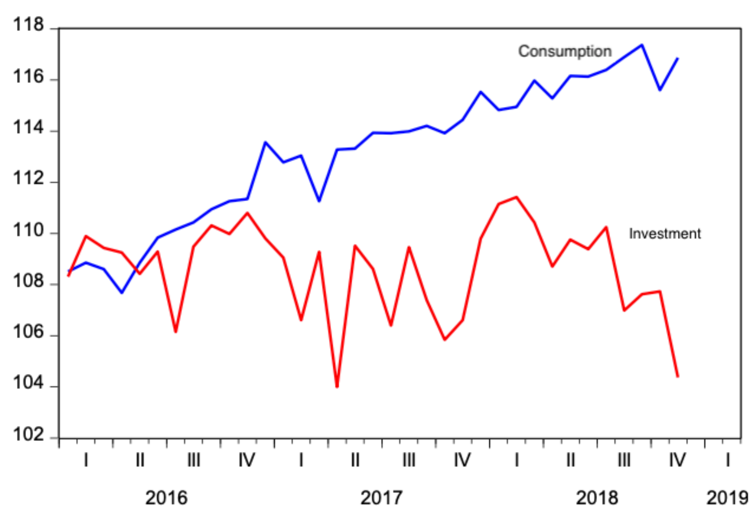
Some analysts, such as Banorte and IMEF economists, have estimated that interruptions in production and supply caused by these problems could mean losses of 0.3% to the estimated GDP growth during 2019. In our case, we believe that these shocks will have a negative impact on the growth of the first quarter, but to the extent that these events have only been transient and do not become systemic, then the effect must be softened throughout the year.

However, the dynamics of aggregate demand and industrial activity revealed during the closing of 2018, and the severity of the financial problems of PEMEX, force us to review the estimated growth during 2019.

Slowdown of aggregate demand. Monthly aggregate demand indicators show a significant slowdown in consumption and a faster weakening in investment, as shown in graph 1.

In November 2018, the last available data, the growth of private consumption was of the order of 2%, below the peak that was given in March of that year when it grew to 4%. Indeed, the growth trend from April 2017 is clearly downward. The gross fixed investment has a very erratic dynamic, month by month, but clearly moved from the expansion zone to the contraction area in 2017, very possibly due to uncertainty about the Trump administration's actions and the renegotiation of the Free Trade agreement. But the expansion that was given at the end of 2017 and 2018, last year of an outgoing administration, loses vigor in the first third of the year and descends quickly since July of 2018, at annual rate the contraction was at the end of the year of the order of 2.1%.

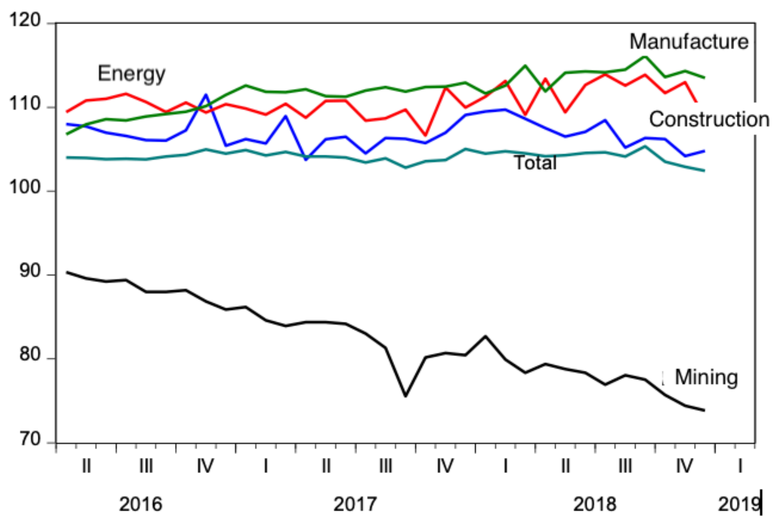
Graph 1
Annual growth rates of the consumption index and gross fixed investment



Source: Prepared by the author, based on information from INEGI

The industrial activity indexes that INEGI estimates also present important signs of deceleration as evidenced in graph 2. Only manufactures maintain a moderate annual expansion, although in December it was only 0.5%. In contrast, mining is still in freefall because of the problem of oil production, electric power, water and Gas and construction begin to present contractions between October and December 2018. In December 2018, Industrial activity decreased 2.5% per annum, carried by annual falls of the order of 8% in mining, 1% in energy, water and Gas and 4% in construction.

Graphic 2
Industrial activity Indexes in Mexico
(Seasonally Indexes 2013=100)



Source: Prepared by the author, based on information from INEGI

Austerity of spending and problems of PEMEX. Although there are no definitive figures of the magnitude of the cut to the operating expenses of the federal government, anecdotal evidence makes us think that it will be of more depth than that was made at the beginning of the administration Peña Nieto, when the consumption of government Only increase 0.5% in real terms. Most likely, it is more like the contractions that were presented in the first year of the Zedillo administration (-1.1%) Or Fox's (-2.7%). To austerity we must add the additional pressure that will cause on public finances the financial weakness of PEMEX, which is now requiring to reduce the tax burden of the company in the equivalent of 3 percentage points, a tax sacrifice of Order of 15 billion pesos (BP). It would be no surprise that the capitalization of PEMEX has to increase during the year.

Revision to the growth scenario. The trend in aggregate demand and industrial activity components only presents the framework at the end of 2018. Unlike the negative supply shocks of petrol shortages, strikes and rail blockades, the trend in investment and government consumption does not seem to be reversed in 2018. In table 1 we estimate GDP growth during 2019 by comparing the average scenario of the general policy criteria (CGP) which assumed a real stagnation of government consumption as of the gross fixed investment, a growth of 2% for the Private consumption and imports and 4% for exports. Maintaining the latter but anticipating a 1% drop in government consumption and 2% in investment, which are consistent with recent trends, the result is expected growth of 1.5% instead of 2% and 1.8% that we proposed in the January newsletter.

Table 1
Growth expectation review

	CGP	New projection
Private Consumption	0.020	0.020
Government Consumption	0.000	-0.010
Total Consumption	0.017	0.015
Investment	0.000	-0.020
Exports	0.040	0.040
Imports	0.020	0.020
Gross Domestic Product	0.020	0.015

Source: Prepared by the author, based on information from INEGI and CGP

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