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FEATURED Q&A

What Forces Are Shaping Mexico's Economic Outlook?

Mexican President Andrés Manuel López Obrador has marked his first 100 days in office with high popularity ratings yet deep suspicions among the country's business sector and investors. // File Photo: Mexican Government.

Q Goldman Sachs last month cut its annual economic growth forecasts for key Latin American countries, with Mexico's economy now expected to grow by 1.5 percent instead of 1.7 percent. The figure is the lowest rate of growth predicted this year among major regional economies covered by the Wall Street bank. What factors are shaping Mexico's economic outlook this year? How much do lowered forecasts have to do with political variables and uncertainty under a new president versus economic trends? Where is the peso currency headed, and what actions might Mexico's central bank take in the months ahead?

A Jaana Remes, member of the Advisor board and partner at the McKinsey Global Institute: "Economic forecasts from Goldman Sachs to the International Monetary Fund suggest Mexico's growth will disappoint this year—again. In January, the IMF cut its 2019 forecast to 2.1 percent, down 0.4 percent from October 2018, and its forecast for 2020 to 2.2 percent, 0.5 percent lower. That is against an expected world average GDP growth rate of 3.5 percent in 2019 and 3.6 percent in 2020. The Achilles' heel for Mexico is weak productivity growth. Fully 70 percent of Mexico's GDP growth since 1990 has come from an expanding pool of workers, and only 30 percent from higher productivity. As expansion in the working-age population declines, Mexico's growth will depend even more on raising the productivity of each worker. What is Mexico's core productivity problem? The answer is a 'missing middle' of firms and consumers. It lacks sufficient modern, globally competitive firms offering high-wage employment that could boost

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United States to Pull All Diplomats Out of Venezuela

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Plans include offering $1 billion of common stock, as well as an agreement with U.S.-based PayPal, which has committed to a $750 million "strategic investment."

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Peru's Vizcarra Swears in Del Solar as New P.M.

Peruvian President Martín Vizcarra has tapped former culture minister and film actor Salvador del Solar as his prime minister. His new cabinet has parity between women and men, with nine each, something that has happened only once before in Peru's history.

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Del Solar // Photo: Peruvian Government.

POLITICAL NEWS

United States to Pull All Diplomats Out of Venezuela

The United States will withdraw all its remaining diplomatic personnel from its embassy in Caracas due to the "deteriorating situation" in Venezuela, Secretary of State Mike Pompeo said late Monday in a tweet. "The presence of U.S. diplomatic staff at the embassy has become a constraint on U.S. policy," he added. Venezuelan President Nicolás Maduro cut diplomatic ties with the United States in January

Pompeo // File Photo: U.S. Government.

and initially ordered all U.S. embassy staff to leave the country within 72 hours following the North American country's recognition of opposition leader Juan Guaidó as Venezuela's interim president. Maduro soon backed off that deadline, avoiding a potential U.S. intervention. Meanwhile, sporadic electricity blackouts continued across the country Monday, BBC News reported. Media reports suggest 17 people have died as hospitals struggle to cope. Photos posted on social media sites showed desperate residents fetching water from polluted rivers and drainage pipes. Other photos show security forces arresting scores of looters who allegedly had broken into closed stores. Maduro blamed the continuing power outages on foreign sabotage. "The United States' imperialist government ordered this attack" on the grid, he said in a televised address, without offering evidence. Pompeo suggested Monday that Cuba, a longtime ally of Venezuela, had a hand in the power grid fiasco. "Cuba is the true imperialist power in Venezuela," Pompeo said, Voice of America reported. The United States expanded sanctions on Monday to include a Moscow-based bank jointly owned by the Venezuelan and Russian governments.

Peru's Vizcarra Picks New Prime Minister

Peruvian President Martín Vizcarra on Monday tapped former culture minister and film actor Salvador del Solar as his new prime minister in a cabinet shuffle, Reuters reported. Del Solar, 48, replaces César Villanueva, who stepped down from the post last week amid falling approval ratings for Vizcarra's government. In addition to a successful career acting in television and movies, del Solar served as former President Pedro Pablo Kuczynski's culture minister for about a year, leaving the post in December 2017. Opposition leader Carlos Tubino, the spokesman for the Fuerza Popular party, said he respected the president's choice in selecting del Solar. "We are willing to dialogue and cease fighting," he said, according to state news agency Andina. Del Solar holds a bachelor's degree in law from the Pontificia Universidad Católica del Perú, as well as a master's degree in international relations from the Maxwell School at Syracuse University in New York. Vizcarra opted to keep Finance Minister Carlos Oliva and Energy and Mines Minister Francisco Ísmodes in their posts, but changed eight other ministers, including the production and agriculture ministers. The new cabinet has parity between women and men, with nine each, something that had only happened in 2013 during the presidency of Ollanta Humala, El Comercio reported.

BUSINESS NEWS

Colombia Signs Oil Contracts With Shell

Colombia's government announced Monday it has signed two exploration and production contracts with Shell in offshore areas of the Caribbean Sea, Reuters reported. The contracts require the U.K.-based company to make

NEWS BRIEFS

Brazil President to Name New Washington Envoy Next Week: Report

Brazilian President Jair Bolsonaro is expected to name a new envoy to the United States when he visits Washington next week, Folha de S.Paulo reported Monday. The top candidates are diplomat Nestor Forster, a reported favorite of Foreign Minister Ernesto Araújo, and attorney Murillo de Aragão, a consultant and analyst with ties to the military wing of Bolsonaro's far-right administration. Meanwhile, the United States has yet to name its ambassador to Brazil, a post that has been open since P. Michael McKinley left in May last year to become senior advisor to the U.S. Secretary of State.

Mexico's CFE to Auction Optical Fiber Contract

Mexican state-owned utility CFE on Monday published the preconditions for an auction that will contract 50,000 kilometers of optical fiber network that will connect 8,535 locations, including schools, hospitals, public parks and federal buildings, to the Internet free of cost, El Universal reported. The auction for the 20-year contract to operate the network is open to international companies. The project is part of President Andrés Manuel López Obrador's goal of free and universal Internet access.

São Paulo Floods Kill at Least 12 People

Intense floods in São Paulo, Brazil's biggest business hub, and nearby cities have killed at least 12 people, the state's security secretariat said Monday, Reuters reported. Heavy rains Sunday into Monday turned roads into rivers and tossed cars atop buildings and into trees. Five people drowned, while others, including at least one infant, were buried alive in mudslides. The damage from Sunday's rains alone will cost an estimated 45 million reais ($11.6 million) to repair, according to Folha de S.Paulo.

initial investments of $100 million, with the potential to grow to $650 million if exploration continues. “The signing of these contracts revalidates the confidence of oil investors in exploration of our offshore resources in the Caribbean,” National Hydrocarbons Agency President Luis Miguel Morelli said in a statement. Colombia has observed several years of declining oil and gas production and weak prices. The administration of conservative President Iván Duque, which took office last year, has sought to increase output. The timing could be good, as prices for its crude oil have risen in the face of an ongoing crisis in neighboring Venezuela. U.S. Gulf refiners have been bidding up prices for Colombian crude due to sanctions on Venezuelan imports, Bloomberg News reported last week. Executives at Ecopetrol, Colombia’s state-controlled oil company, say the company is benefiting, as it is has been able to reliably supply U.S. customers who formerly purchased Venezuelan oil.

MercadoLibre to Raise $1.85 Billion in Equity Offerings

Buenos Aires-based e-commerce giant MercadoLibre said Monday that it intends to raise $1.85 billion in equity offerings in the months ahead. Plans include offering approximately $1 billion of common stock, as well as granting underwriters a 30-day option to purchase up to $150 million of additional shares of common stock. The company also announced that it has entered into an agreement with U.S.-based PayPal, which has committed to a $750 million “strategic investment” through the purchase of common stock. In a separate agreement, San Francisco-based Dragoneer Investment Group has agreed to purchase $100 million of Series A perpetual convertible preferred stock. The PayPal and Dragoneer investments are contingent upon the closing of the public offering. “Digital commerce in Latin America is experiencing tremendous growth and MercadoLibre is well-positioned for continued leadership,” Dan Schulman, PayPal’s president and CEO, said in a statement.

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citizens’ purchasing power and fuel consumption. Disappointingly, growth in employment continues to come mostly from less productive parts of industry. The few large, productive companies are not creating jobs fast enough to absorb workers from small, unproductive and often informal businesses. Over past decades, Mexico has progressed slowly but surely through multiple political transitions and the economic headwinds following the 2007 recession. Its opening up to trade and foreign investment, successful integration of its automotive and aerospace industries in North American value chains, and much improved macroeconomic and fiscal stability are solid foundations for the future. Mexico’s challenge continues to be broadening the pool of modern companies and reigniting domestic demand growth that can create a virtuous growth cycle.”

A **Alfredo Coutiño, director for Latin America at Moody’s Analytics:** “In 2019, the economy is facing two unfavorable factors: the curse of the first year of each new administration and uncertainty regarding the direction of policymaking with the new government. The country is also subject to the external risk coming from a potential deceleration of the global economy, particularly in the United States. In the first case, Mexico’s economy is facing the slowdown typical of the first year of each new government: the deceleration phase of the political cycle. In the past 24 years, the political transition has always introduced a delay in the execution of the federal budget, which has also delayed private decisions of investment. This deceleration phase extends until the middle of the first year, and the economy starts to gain traction when the federal budget normalizes in the second half of the year. The second factor has to do with actions the new government took even before taking office, which introduced uncertainty and affected investor sentiment. Among those measures are the cancellation of the new airport in Mexico City, the reversal of the education reform and revisions of oil contracts already granted to private companies. All this has awakened a sentiment about potential measures that could threaten investment and property rights. In this regard, the deterioration of Mexico’s economic prospects has to do more with domestic factors and less with external tailwinds. If the new leftist government implements measures that directly affect investors or actions that could put macroeconomic discipline at risk, financial markets will be shaken strongly, investment will fall and the economy’s performance will be even worse this year. Under this scenario, the central bank will be left with no option other than turning to more restrictive monetary policy in order to restore stability. Unfortunately, once again, the economy has not been able to escape the curse of the first year’s deceleration.”

A **Amanda Mattingly, senior director at The Arkin Group in New York:** “The financial institutions and the larger business community have been concerned about a softening Mexican economy ever since President Andrés Manuel López Obrador was elected last July. While it seemed López Obrador might have turned over a pragmatic leaf in giving his tacit blessing to the re-negotiated NAFTA deal, he is at heart a leftist and a nationalist skeptical of corporate interests. Recall that he was willing to throw out the $13 billion airport project, much to the dismay of the corporate community and the Mexican peso, which experienced volatility immediately following the decision. Since López Obrador was elected, Mexico’s economy has slowed. Industrial output decreased, and services slowed in the fourth quarter of 2018. Oil production fell 6.9 percent last year to 1.8 million barrels per day, leading the rating agencies to downgrade Pemex in January upon hearing this news. Complicating matters further, López Obrador recently announced an end to oil joint ventures

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between private companies and the state-owned Pemex—the hallmark of the 2013 energy reforms. Another variable is the U.S. economy, given that the two economies are inextricably linked. The combined effect has left economists less than optimistic, and they have lowered their forecasts for Mexico in 2019 as a result. The decline in industrial output, services and oil production did not happen entirely on López Obrador's watch, but his current policies and political rhetoric are not helping to assuage jittery investors or to build confidence in the Mexican economy. In fact, they are doing the opposite."

A **Amy Glover, CEO for Mexico at Speyside Corporate Relations:** "The main factor influencing the Mexican economy at this moment is uncertainty. Despite the long transition, the government of Andrés Manuel López Obrador has taken time to coalesce, and with an approval rating of approximately 80 percent, the government is concentrating on its core social mission. His popularity means that the views of the private sector—and certainly foreign investors—have taken a back seat on the list of priorities. AMLO sees the domestic economy as separate from global economic dynamics and has taken personally the fact that rating agencies like Fitch have called into question the financial health of Pemex and the economic vibrancy of the country (S&P recently downgraded long-term growth prospects from stable to negative). The uncertainty related to the U.S. economy certainly does not help Mexico. Elevated political risk in Washington and President Trump's protectionism have done nothing to encourage greater economic growth globally. When the U.S. economy slows down as the year progresses, Mexico's economy will follow suit given the strong interdependence. As long as there are no negative short-term surprises, the peso will continue to trade in the range of 19 pesos to the dollar in the coming months. Despite mixed signals on the public policy front, there is still significant interest in the Mexican market coming from technology companies and consumer-focused startups. Mexico's economy still has a lot to gain from efficiencies related to the introduction of new technologies, and while this could potentially mean the loss of some manufacturing jobs, it could also introduce greater dynamism, innovation and productivity."

A **Alma Caballero, director for Mexico at McLarty Associates:** "Mexico's economic outlook for 2019 is conditioned by the level of uncertainty surrounding the lack of clarity over the economic policies that the López Obrador administration will pursue. External factors that strongly influence the future of Mexico's economic outlook include a stronger U.S. dollar, a slowdown in the global industrial and manufacturing sectors, escalating global trade tensions and the tightening of financial conditions. President López Obrador has vowed to combat poverty and corruption by putting forth an aggressive economic agenda that aims to center on addressing income distribution through a much more progressive fiscal policy and empowering the role of the state in key economic sectors—particularly in the energy sector. All of this while seeking to calm markets by promising business-friendly policies and respecting the autonomy of the central bank. Uncertainty remains, however, over whether AMLO's economic agenda will be motivated by ideology or technically sound proposals."

> **"The main factor influencing the Mexican economy at this moment is uncertainty."**
> **— Amy Glover**

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at **gkuleta@thedialogue.org**.

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