Economic Analysis

# Economic stagnation in 2019 affects current account and net foreign direct investment

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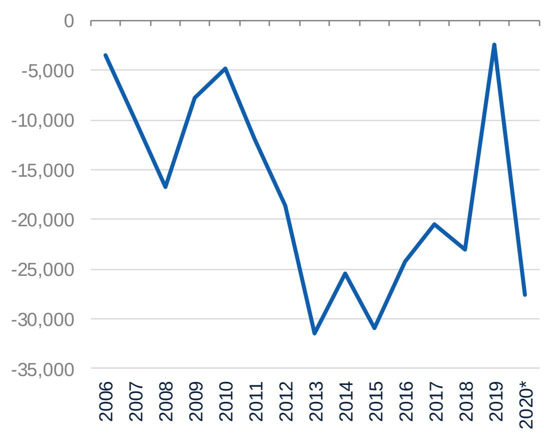
- **Annual drop of 16.1% in net foreign direct investment in 2019**
- **The current account deficit decreased by USD 20.6 billion in 2019 vs. 2018, mainly due to the trade balance on non-oil goods posting a higher surplus**

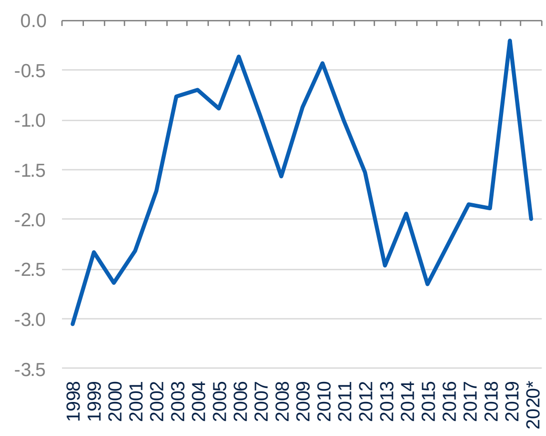
After having stood at USD 23.0 billion in 2018, the current account deficit decreased to USD 2.4 billion in 2019 (Figure 1). In terms of GDP, the current account deficit stood at 0.2% (Figure 2). For 2020, we predict that the current account deficit will be roughly USD 27.6 billion (2.0% of GDP).

Figure 1. **Current account** (USD millions)




*/Forecast
Source: BBVA Research with Banxico data

Figure 2. **Current account** (% of GDP)




*/Forecast
Source: BBVA Research with Banxico data

Analysis of the behavior of the current account in the fourth quarter of 2019 shows that a higher surplus was registered when compared to the third quarter of 2019 (Table 1). This can mainly be attributed to the higher surplus posted in the trade balance on non-oil goods, which was partially offset by the higher deficit in the primary income balance. When we compare how the current account deficit performed in 2019 vs. 2018, we can see that its USD 20.6 billion decrease is mainly due to the trade balance on non-oil goods posting a higher surplus and, to a lesser extent, to the lower deficit in the balance on services (Table 2). In our opinion, the main factor underlying the current account behavior in 2019 was the weakness in aggregate demand.

Table 1. **The current account and its components in the third and fourth quarters of 2019**
(USD millions)

| | Jul–Sep 19 (A) | Oct–Dec 19 (B) | Difference (B–A) |
|---|---|---|---|
| **Current account** | 820 | 2,487 | 1,667 |
| Bal. on goods and services | -3,407 | 1,965 | 5,372 |
| Balance on goods | -518 | 3,085 | 3,603 |
| Bal. on oil products | -5,294 | -5,342 | -48 |
| Bal. on non-oil goods | 4,836 | 8,475 | 3,639 |
| Bal. on goods procured in ports by carriers | -60 | -48 | 12 |
| Balance on services | -2,889 | -1,120 | 1,769 |
| Bal. on primary income | -5,253 | -8,383 | -3,130 |
| Bal. on secondary income | 9,480 | 8,905 | -575 |

Source: BBVA Research with Banxico data

Table 2. **The current account and its components in 2018 and 2019**
(USD millions)

| | 2018 (A) | 2019 (B) | Difference (B–A) |
|---|---|---|---|
| **Current account** | -23,005 | -2,443 | 20,562 |
| Bal. on goods and services | -22,721 | -547 | 22,174 |
| Balance on goods | -13,796 | 5,624 | 19,420 |
| Bal. on oil products | -23,160 | -21,222 | 1,938 |
| Bal. on non-oil goods | 9,542 | 27,042 | 17,500 |
| Bal. on goods procured in ports by carriers | -178 | -196 | -18 |
| Balance on services | -8,924 | -6,171 | 2,753 |
| Bal. on primary income | -33,168 | -37,175 | -4,007 |
| Bal. on secondary income | 32,884 | 35,279 | 2,395 |

Source: BBVA Research with Banxico data

In terms of Net Foreign Direct Investment (NFDI), this indicator posted USD 22.7 billion in 2019 vs. USD 27.0 billion in the previous year. In other words, NFDI showed a year-on-year contraction of 16.1%. By looking at the annual historical information (since 2006) of NFDI, it is important to note that this contraction is the highest of the last three years. In 2018 and 2017, NFDI showed a negative annual variation of 10.6% and 0.9%, respectively.

The much lower current account deficit in 2019 compared to 2018, as well as the double-digit annual contraction in NFDI, are indicative of the economic stagnation the country experienced in 2019. We expect that both the anticipated economic recovery in 2020 and the eventual entry into force of the United States–Mexico–Canada Agreement (USMCA) to boost NFDI.

## Conclusions

Our forecast of 2.0% of GDP for the current account deficit implies that the country will enter a phase of economic recovery after a real GDP annual contraction of 0.1% in 2019. The magnitude we expect for this deficit suggests that the country is not vulnerable to external shocks and even conveys the message that a sizable share of the current account deficit could be financed with net FDI and in full with the amount we estimate the country will receive for international remittances. In addition, we estimate that net portfolio investment flows will continue at positive levels due to the high differential of risk-adjusted rates the country has and the perception that public finances will remain stable. In regard to the relatively low performance of NFDI in 2019, this could be due to both internal factors associated with the uncertainty of public policies, the cancellation of the new airport, as well as the controversy surrounding the gas pipeline contracts contributed, in our opinion, to the less dynamism of the NFDI, and external factors related to the ratification process of the USMCA and the lower growth of global manufacturing. To help increase FDI flows into

Mexico in the coming years, it will be necessary to send signals of increased certainty to investors through improved public policies, particularly, signs that the contracts will be respected and that the rules of the game will not be changed since the match has begun, and that global manufacturing recover its growth path.

We do not believe there is a structural problem to finance the current account deficit. If said deficit returns to the levels we estimate, of around 2%, it will be due to a recovery in economic activity that in turn will be accompanied by higher levels of NFDI and portfolio investment. In the event that the recovery is not achieved, we will continue to see reduced levels of current account deficits that can be financed with current amounts of NFDI and international remittances.