



Monarch News

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CEO Executive Summary

U.S.-Mexico Relations hit yet another low in early April after President Trump ordered up to 4,000 National Guard troops to the U.S. southern border. Mexican politicians and citizens uniformly rejected this militarization of the border, with President Peña Nieto roundly denouncing the move, and the rhetoric coming out of the White House, in a nationwide address. This created an inauspicious context for the NAFTA talks, which picked up in intensity in early April. Nevertheless, the three ministers overseeing the negotiations have expressed a renewed sense of optimism, supported in part by apparent U.S. concessions on auto rules of origin in an effort to lay the groundwork for an agreement in principle by the end of the month. Still, an agreement in principle could be a far cry from a completed agreement. Given the number and depth of the disagreements remaining on the table, a May agreement is apt to add up either to relatively small modifications to NAFTA (including a new auto accord), or the promise of a larger deal with many months of hard negotiations still to come. Either way, we are still a long way from knowing whether *any deal* that can be negotiated will be acceptable to President Trump, whose domestic political fortunes appear to be worsening.

Formal campaigning for the Mexican presidency began on March 30, with all four contenders promising to fight corruption, guarantee security, and stand up to the Trump Administration. Heading into the first presidential debate on April 22, the leftist candidate Andrés Manuel López Obrador (AMLO) holds a 13 point lead in the Oraculus poll of polls, although the Federal Electoral Tribunal's April 9 decision to permit a second independent candidate to run for president is apt to pull some votes from AMLO. As private sector concerns about a possible AMLO victory on July 1 grow, the candidate published an open letter to investors laying out what he will and won't do as president to show that he is no threat to them. The letter was widely criticized for its lack of detail, evidence that most investors still do not trust AMLO.

Meanwhile, the Mexican economy continued to plug along with falling inflation and a volatile currency backstopped on the downside by the carry trade. In the energy sector, Pemex was the big winner in round 3.1 of the petroleum auctions even as the country's proven reserves continue to fall. The country's new public-private telecom network, the *Red Compartida*, began operations bringing mobile service to previously unserved areas of the country, and the now 18% completed Mexico City airport project raised \$1.6 billion in new Mexican capital, almost half coming from pension funds, as the Peña Nieto administration pushes to advance the project as far as possible before the end of the "sexenio."

I. U.S.-Mexico Relations

U.S.-Mexico relations hit another low in early April thanks to President Trump's decision to send the National Guard to the border. On April 1, apparently after watching a Fox News report on a caravan of Central American immigrants traveling north through Mexico (an annual event to call attention to the immigrants' plight), [Trump tweeted that Mexico was doing "very little, if not nothing" to stop Central American immigrants](#) from transiting Mexico to reach the United States. He threatened to "stop their cash cow, NAFTA" if they did not act. In making this outrageous assertion, the President seems to have completely ignored several important facts: first, that Mexico in fact closely cooperates with the United States to reduce the flow of Central American immigrants through its territory; second, that migrant [apprehensions are at a historic low](#); third, that the two countries had literally just signed renewed [customs and border security agreements the previous week](#) during Secretary of Homeland Security Kirstjen

Nielson's productive visit to Mexico; and fourth, that his own administration is now urgently seeking to conclude the NAFTA negotiations by the end of April (more on that below).

[Trump then announced](#) that he was "preparing for the military to secure our border" until a wall can be constructed [to protect the United States from "a drastic surge of illegal activity"](#) on the southern border." On April 4, he signed a proclamation ordering Homeland Security to work with border state governors to send National Guard troops to the border. [Arizona and Texas immediately agreed](#) to send several hundred unarmed troops to assist the border patrol with logistics thereby freeing up more CBP agents to patrol the border.

Mexico responded immediately and forcefully to what it sees as a militarization of the border. The [Senate unanimously passed a resolution](#) calling on the government to suspend migration and anticrime cooperation with the United States, and [the Chamber of Deputies unanimously and "energetically" rejected](#) the militarization of the border. All four presidential candidates sharply criticized the American decision. And on April 5, [President Peña Nieto addressed Trump directly in a speech to the Mexican nation](#). He criticized Trump for taking out his frustrations with the U.S. Congress and domestic laws and policy on Mexico, insisting that Trump should "talk to them, and not to Mexicans." He also noted what has already become evident: "If there is one thing all Mexicans agree on, it is that nothing, and no one, is above our dignity as a nation." All four Presidential candidates immediately supported the President's speech, [including AMLO](#). The only criticism came from [the more conservative Ricardo Anaya](#) who called out the government for not matching its words with deeds.

The result is a less than auspicious Mexican environment for the NAFTA talks, even after [Trump tweeted a thank you to the Mexican government for supposedly stopping the caravan](#) in southern Mexico. Concerned that it would look like it was doing the bidding of the United States in an increasingly nationalist domestic political context, the Peña Nieto administration quickly corrected President Trump noting that this outcome was due to a decision by the caravan's organizers and not any action by the Mexican government.

II. NAFTA

Despite the charged political atmospherics attendant with Trump's Tweeting tirades, the NAFTA talks picked up in intensity and seemed to change tone in early April. U.S. Trade Representative Robert Lighthizer eschewed a formal negotiating round (once rumored for the week of April 8) to allow negotiators and working groups to focus on substantive progress that could result in an agreement in principle toward the end of April. The three principals – USTR Robert Lighthizer, Canadian Foreign Minister Chrystina Freeland, and Mexican Economy Minister Ildefonso Guajardo – met in Washington April 5-6. While the [ministers were unable to strike an agreement](#), their respective technical teams met during the following week. Guajardo recently [gave 80% odds that an agreement will be reached by the first week of May](#). Chances for success rest on nailing down rules of origin in the auto sector. Meanwhile, the principals have agreed to meet again in what Secretary Guajardo has characterized as a “permanent round” of final discussions.

The optimism surrounding the negotiations [reflects reports that the U.S. had dropped its demand for a minimum 50% U.S. content](#) for automobiles and light trucks and [lowered its regional content demand from 85% to 75%](#) (from the current 62.5%). It also reflects an agreement among the three parties on how to measure regional content. [According to Inside U.S. Trade](#) (subscription required), under this regional content plan (originally proposed by the Canadians in round six), the contribution of different vehicle parts to regional content will be weighted according to their importance to the final car or light truck. Engines, for example, would count more than seats. But the United States has [proposed an added requirement](#) that the most critical components of each vehicle be produced where worker wages are at least \$15 per hour. The Mexicans unsurprisingly oppose this proposal, but it has the advantage of being acceptable to the Canadians and pleasing to U.S. labor and their democratic supporters.

The upbeat mood surrounding this informal eighth round of talks persists despite the fact that there has been no reported movement toward an agreement on government procurement or dispute resolution, and only 6 of 30 chapters are completed. [Mexico's Guajardo has long identified April 30 as the deadline](#) after which the Mexican

presidential campaign will force the Mexican government to step away from the negotiations. What caught analysts' attention, however, were the early April statements from White House advisor and free trade skeptic Peter Navarro, President Trump himself, and Canadian Prime Minister Justin Trudeau. [Navarro noted](#) that "whether [the conclusion of negotiations is] two weeks or 30 days, it's got to be soon." President Trump followed his advisor's lead and [stated: "We'll have something. I think fairly soon."](#) And [Trudeau hoped](#) that "there will be some good news coming" because the negotiations are having a "very productive moment."

That being said, any agreement reached by late April or early May could end up being either a small modification of NAFTA focused on the auto sector, not unlike [the recent agreement with South Korea](#), or a far cry from a completed agreement. While an agreement in principle will allow the three governments to declare an intermediate victory, this will likely come with a number of key areas of disagreement still outstanding. Any agreement reached in the coming days and weeks will either sweep these under the rug in the interest of expediency or leave ahead many months of hard negotiations before a final agreement can be reached.

The truth is, no one really knows what will happen. While all indicators suggest that a deal is now increasingly possible, the "decider in chief" remains President Trump. As his political fortunes wane, and as he faces more discontent from his base (that is already disappointed with his failure to deliver on his promise to build a wall, combined with significant frustration over the spending bill he recently signed), the President, we suspect, will want something to hold onto to rile up his base heading into the November mid-terms. Given that Mexico has always been his favorite piñata, it seems, at least to some of us, unlikely that Trump will agree to a new NAFTA deal that he can't sell *politically* to his base. That said, his unfortunate decision to pick a trade war with China, which is threatening substantial retaliation that will hurt many sectors, but especially farmers, could force Trump to embrace a NAFTA deal that he would otherwise be disinclined to support. The jury remains out.

III. Mexican Politics

The three-month-long presidential campaign formally began on March 30 with all four candidates at the time promising to fight corruption and insecurity and to stand up to the Trump Administration.

At 12:01 am on March 30 the PAN/PRD candidate, Ricardo Anaya, [kicked off his campaign with a 'hackathon'](#) designed to increase his appeal with millennial voters who make up 48% of the Mexican electorate, [half of whom currently back the left-leaning Andrés Manuel López Obrador](#). Mexico's lone independent candidate, Margarita Zavala, also began campaigning in the first possible minute with a rally at the Independence Angel in Mexico City, the historic rallying point for PAN politicians fighting for democracy in the late 20th century.

PRI candidate José Antonio Meade and AMLO symbolically decided against initiating their campaigns on Good Friday and instead waited until April 1 to begin campaigning, and both [kicked off with a traditional campaign speech](#). In Merida, Yucatan, [Meade laid out the proposals that will define the core of his campaign](#) – improve education, healthcare, and security, eliminate poverty, and end corruption – the first four of which are indistinguishable from the promises made by Enrique Peña Nieto when he ran for president six years ago.

AMLO spoke in the politically significant city of Ciudad Juarez: It is named for AMLO's political hero, Benito Juarez, and is the site where another AMLO hero, Francisco I. Madero, crossed into Mexico to start the Mexican Revolution; it has a difficult security context; and it is situated on the border during a difficult period in U.S.-Mexico relations. Speaking for a full 45 minutes, AMLO laid out the history and policy challenges that motivated his candidacy and explained his policy proposals. He promised to end corruption and impunity, ensure austerity in governance, invest in Mexico's youth, and defend the country. [Regarding the United States, he insisted that](#) "no threat, no wall, no overbearing attitude of any foreign government" will prevent Mexico from improving itself. He also promised to convince President Trump that his security policy and

disrespectful attitude toward Mexicans are mistaken, and most memorably he insisted that “neither Mexico nor its people will be the piñata of any foreign government.”

The so-called “nationalist” candidate was not alone in his broadsides. Meade tweeted that he is the only candidate with the experience to deal with the United States. [In a March 7, 2017, Washington Post op-ed](#), Margarita Zavala referred to Trump as the “bad hombre” who makes Mexico question whether the United States is a reliable partner. And Ricardo Anaya [called for an end to security, immigration, and anti-terrorism cooperation](#) until the National Guard is withdrawn from the border. In a country where [just 39% of Mexicans have a favorable view of the United States](#) and virtually none trust President Trump, nationalism is good politics regardless of political persuasion.

Heading into the first presidential debate on April 22, polls are measuring AMLO’s lead from five to 18 points. Given that, we rely on a poll of polls to measure each candidate’s standing. According to [the most recent numbers from Oraculus](#), support for López Obrador averages 43%, Anaya 29%, Meade 23%, and Zavala 6%. This will change soon, however, owing to the [April 9 decision of the Federal Electoral Tribunal](#) to overturn the Federal Electoral Institute’s decision and allow former Nuevo Leon Governor, Jaime “El Bronco” Rodríguez, to participate in the presidential election as an independent candidate. The highly questioned decision is expected to pull anti-PRI votes away from AMLO.

Finally, in response to rising concern in the private sector over the possibility of an AMLO victory, the candidate sent [an open letter to investors](#) on April 4 laying out his diagnosis of the situation and planned policy responses. In it, AMLO promised zero budget deficits and no tax increases while increasing social spending, public investment, and the role of the state in the economy more generally. He expressed his willingness to renegotiate NAFTA and, in the process, to protect Mexican producers and establish just salaries and migration rules. He promised to preserve democracy, establish an authentic rule of law, deal with crime and violence, and protect the independence of the central bank. And he promised to keep his word, so investors should not be frightened. The letter was not well-received and was instead met with demands for more detail to support the promises. The problem continues to be that most investors do not trust AMLO and thus take his promises with a hefty grain of salt.

IV. Mexican Economy

Growth in the Mexican economy continued steady, with the [OECD increasing its 2018 growth forecast](#) from 2.2% to 2.5% while the [finance ministry held its projections steady](#) at 2-3%. Inflation continued its gradual decline, reaching [its lowest level in over a year in the first half of March](#) at 5.2%, on a trajectory that is still [expected to deliver 3% inflation](#) by the first quarter of next year. As part of its inflation targeting strategy, and in the wake of the Fed's recent interest rate increase, the Bank of Mexico is expected to raise interest rates another 25 basis points to 7.5% in the second quarter, although it held rates steady in April.

This interest rate strategy has helped to keep a volatile peso in the range of 18-19 pesos per U.S. dollar in the past month. Even as AMLO's position in the polls strengthens and the NAFTA negotiations swing from near collapse to a supposed near agreement, the [peso was the best performing currency relative to the dollar during the first quarter of 2018](#). Downward pressure on the Mexican currency created by election and trade uncertainty is constrained by at least three factors. First is [the carry trade](#), taking advantage of low U.S. interest rates to borrow funds to invest in Mexican [bonds that currently earn a 7.3% interest rate](#), which has helped sustain a strong portfolio investment flow into Mexico. Second, [record high remittances](#) apparently driven by fears of deportation, and third, [Mexico's healthy supply of international reserves](#).

In trade policy, the Mexican government signed the [Comprehensive and Progressive Agreement for Trans-Pacific Partnership](#), or TPP11, without the United States and [sent the treaty to the Senate for confirmation](#). And Mexican trade [negotiators are trying to finish up an updated free trade agreement with the European Union](#) before President Peña Nieto's European trip later this month.

Sector Focus: Energy

In the last bid round before the July 1 presidential election, Round 3.1 of the petroleum auctions held on March 27 [awarded 16 of the 35 blocks tendered](#), bringing the total to over 100 contracts signed thus far. In this auction, [Pemex was the big winner](#), obtaining

the rights to develop seven shallow water fields either alone or in a consortium. Overall this round generated an expected investment of \$8.6 billion.

Rushing to meet its ambitious energy reform goals, the Energy Ministry [announced a plan to schedule a fifth auction round](#) for shallow water heavy crude fields before the end of the current administration. This announcement came in the wake of data published on the National Hydrocarbon Commission (CNH) website showing [another reduction in Mexican oil reserves](#) despite the first ever private reserves added to the total.

In the electricity sector, the Energy Regulatory Commission announced [Mexico's fourth long-term power auction](#), whose results will be announced November 2 and the contracts signed in February 2019.

Sector Focus: Telecom

On March 21, [the Red Compartida went live](#). This public-private wide-band mobile network was authorized by the telecommunications reform and is designed to serve the 46 million Mexicans who still do not have access to mobile telecom services. The new network currently covers about a third of the Mexican population and is expected to scale up to cover half the population by 2020 and 92% by 2024. And in the private telecom market, the [Telmex union announced its opposition](#) to the division of the firm into two companies as ordered last month by the Federal Telecommunications Institute. Additionally, [over the past three years Telmex has lost 8.6% of the fixed line telephone market](#) as cable operators gradually chip away at Telmex's monopoly position.

Sector Focus: Infrastructure

In the shadow of AMLO's oft-stated promise to stop construction on Mexico City's new airport, the [project raised \\$1.6 billion](#) by selling shares in the Fibra E infrastructure investment trust. All of these funds came from Mexican investors with almost half coming from pension funds. This money will help ramp up construction on a [project that, according to public sources, is already 18% complete](#), making it more costly for the next administration to cancel the project.

V. Monarch Events, Speeches, Publications

March 15: MGS Senior Advisor Pamela K. Starr discussed trade, drugs, and the presidential election in Mexico on [35 West](#), the podcast of the Americas Program at the Center for Strategic & International Studies.

March 29: MGS CEO & President Michael C. Camuñez appeared on [MSNBC](#) to discuss the firing of Veterans Affairs Secretary David Shulkin specifically and the White House cabinet appointments process generally.

March 29: MGS Chairman Amb. James R. Jones commented in the Inter-American Dialogue's [Latin America Advisor](#) on the implications on U.S.-Latin America relations of Mike Pompeo replacing Rex Tillerson as Secretary of State.

April 4: MGS Chairman Amb. James R. Jones appeared on Fox News Channel's [The Story](#) to discuss the need to modernize NAFTA while underscoring the existing cooperation between Mexican and U.S. authorities in securing the border.

April 13: MGS Chairman Amb. James R. Jones and Senior Advisor Pamela K. Starr each commented on the status of U.S.-Mexico relations in the Inter-American Dialogue's [Latin America Advisor](#).