



Monarch News

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CEO Executive Summary

The much-anticipated landslide victory for Andrés Manuel López Obrador (AMLO) in the Mexican presidential election dominated the news this past month. His victory translated into large majorities in both houses of the federal legislature, at least five governorships, and majorities in more than half of state legislatures. And it gave him a powerful mandate to remake Mexico economically and politically. This landslide swept away the political party system that had dominated Mexican politics for decades. The ruling PRI party and its erstwhile ally the PAN were savaged at the polls, while the historic face of the Mexican left, the PRD, along with four other parties, are at risk of losing their registration and being eliminated from the political scene. This means that AMLO is well-positioned to build a majority large enough to modify the Mexican constitution, leading some analysts to express fear about the potential erosion of democratic checks and balances. At the same time, this will prevent him from pointing to a lack of political support as an excuse for any shortcomings during his administration.

In true democratic fashion, López Obrador's opponents immediately recognized his election victory, while AMLO's victory speech called for national reconciliation after a hard-fought campaign. Suggesting a smooth transition, AMLO's July 3 meeting with

President Enrique Peña Nieto went very well. Equally reassuring were his post-election pro-democracy statements, which assured his fidelity to the rule of law, his intention to drive reform through democratic and judicial means, and his outright rejection of authoritarianism.

AMLO's relationship with the private sector is likewise off to an encouraging start. In his meetings with business leaders, he has expressed his willingness to collaborate with the private sector. For their part, leaders across industry, in a video message to AMLO have expressed their patriotic willingness to work with the new government.

In U.S.-Mexico relations, the NAFTA talks took a break in June with the expectation that they would begin anew later in July. An experienced trade hand, Jesús Seade, is expected to join the Mexican team during the next round of talks as López Obrador's representative. But we don't expect this to make a marked change in the tone of the negotiations since Seade and AMLO have both expressed support for Mexico's NAFTA stance, and since the main obstacle to success has not been the Mexicans but the Trump Administration. More broadly, we expect Washington's antagonistic attitude toward Mexico and AMLO's focus on human rights, the protection of immigrants and crime prevention, rather than any Mexican hostility to U.S. interests, to lead to somewhat less Mexican cooperation with the United States, especially in the areas of security and immigration.

The Mexican economy in June exhibited signs of slow growth with stable inflation, while the peso went on another wild ride. It plummeted to a 16-month low in the wake of the mid-June U.S. Federal Reserve's decision to raise interest rates, but it strengthened following the Bank of Mexico's decision to follow suit. And despite some volatility surrounding the election, the peso has strengthened while country risk has fallen, an indication that AMLO's effort to calm markets in the wake of his victory has been successful so far.

I. The Mexican Election

AMLO won the Mexican presidential election on July 1 in a true landslide. If the [preliminary election results](#) hold up, he will not only have won 53% of the votes cast but will have defeated his nearest competitor by 30 points and won in every state except Guanajuato. His electoral coalition will have a [solid majority in both houses of the Mexican national legislature, majorities in 17 of the 29 state legislatures and at least five of the nine gubernatorial seats](#) up in this election (with Puebla still too close to call). Not bad for a party that did not even exist four years ago.

This election will give López Obrador a powerful mandate to carry out his policy prescriptions for Mexico. This will include a frontal assault on corruption and impunity and significant modifications to the economic model that has dominated the Mexican economy for over thirty years. Most prominently, this means austerity in government and centralized procurement procedures to produce budgetary savings. These will help fund increased social welfare spending, state investment in the economy, and attention to the rural economy (especially in the South), all beginning with the 2019 budget. It means renewed government leadership in the energy sector, efforts to increase national production of food and fuels, and a new education reform. And it means a new approach to Mexico's security challenge that emphasizes prevention.

In a parallel development, the political party system that had dominated Mexican politics for thirty years collapsed. [Five of the nine parties that participated in this election are on the verge of losing their registration](#), including the Democratic Revolution Party (PRD) which has been the political face of the Mexican left since 1989. The Institutional Revolutionary Party (PRI) and the National Action Party (PAN), meanwhile, are shadows of their former selves. The ruling PRI party suffered its worst defeat in history, leaving it with fewer federal deputies than the *Encuentro Social* party, which will lose its registration. The PAN, meanwhile, [suffered its worst defeat in a generation](#). It will still be the largest opposition party in the national Congress and thus the center of opposition to the López Obrador government. But its capacity to play this role will be hindered by internal divisions and the reduced legitimacy of the party leadership that led the PAN to an embarrassing defeat.

All of this suggests that AMLO is well positioned to construct a constitutional majority – two-thirds of the federal congress and majorities in more than half of Mexican statehouses – needed to modify the Mexican constitution. Orphaned legislators from parties that have lost their registration will be open to allying themselves with one of the four remaining parties, and the gravitational pull of the majority and the benefits this implies will be strong. Meanwhile, the devastating defeat of President Enrique Peña Nieto and his policies will eliminate his influence over the PRI's future. This, combined with the PRI's survival instinct and rumors of conversations between party stalwarts and AMLO during the election campaign, suggest that a good working relationship could develop between the PRI and Morena on a range of issues before the legislature. This has [led some analysts to raise the alarm](#) about the potential for a lack of democratic checks and balances on the AMLO government. But AMLO's massive majority will also prevent him from pointing to a lack of political support as an excuse for any shortcomings during his administration.

Another striking characteristic of this election is the extent of the violence that affected it. While election day was free from violence, no recent Mexican election campaign has been more violent. Although estimates vary, in the past ten months [more than 100 politicians, including at least 40 candidates, have been murdered](#) in circumstances that point to the involvement of organized crime. [Hundreds of other candidates withdrew from electoral races out of fear of being targeted](#). These circumstances emphasize the nature and depth of the security challenge that will face Mexico's next President.

II. The Transition's Early Days

The immediate aftermath of the election was surprisingly anti-climactic. On election night, the PRI's José Antonio Meade and the PAN's Ricardo Anaya gave their concession speeches long before the president of the National Electoral Institute announced the official preliminary results and President Peña Nieto congratulated the victor. López Obrador delivered [conciliatory victory speeches calling for national reconciliation](#) that painted a picture of a pragmatic liberal politician rather than a leftist firebrand. On July 2, [AMLO's economic advisers held a conference call with investors](#) that further calmed market nerves. The following day, AMLO and Peña Nieto held an apparently warm and cordial [meeting that set a collaborative tone for the transition](#), and on July 4 AMLO [met with the Business Coordinating Council](#) where he again delivered a

conciliatory message. AMLO described his meeting with the CCE as one of mutual trust in which the [two agreed to jointly finance AMLO's program to provide job or education opportunities for 2.3 million Mexican young people](#). The next day, the most important leaders of the Mexican private sector delivered [a video message to AMLO](#) expressing their patriotic willingness to work with the new government.

López Obrador also [used his victory speech to announce the key members of his transition team](#), none of whom was a great surprise and all of whom were reassuring. He confirmed that Alfonso Romo will be his chief of staff and, together with future Finance Minister Carlos Urzúa, will lead the economic transition team. He confirmed Olga Sánchez Cordero will be his Interior Minister and, together with campaign chief Tatiana Clouthier, will lead the political transition team. And he tapped a pragmatic politician, Marcelo Ebrard, to work with the more nationalist Héctor Vasconcelos on the foreign policy transition. Four days later AMLO announced that [Ebrard, not Vasconcelos, would be his foreign minister](#).

We will provide insight into the individuals who are apt to hold prominent positions in the AMLO administration and keep tabs on developments in the transition in our new [AMLO Transition Report](#), a subscription-based service that will closely track developments surrounding the transition of power in Mexico.

III. NAFTA and U.S.-Mexico Relations

The NAFTA negotiations were suspended in June awaiting the outcome of the Mexican election. [The spat](#) between President Trump and Canadian Prime Minister Justin Trudeau at the early June G7 Summit meeting raised questions about the future of the NAFTA talks. An ensuing meeting between Canadian Foreign Minister Chrystia Freeland and U.S. Trade Representative Robert Lighthizer, however, produced [an understanding that the talks should restart this summer](#). No start date was set for the next round, but Mexican Trade Minister [Ildefonso Guajardo suggested they would begin in July](#), an opinion [the Canadians seconded](#) soon after the Mexican election. Meanwhile, President Trump turned up the heat again, stating that he was [not interested in signing any agreement before the U.S. midterm elections](#) and reiterating his [threat to impose steep tariffs on auto exports](#) to the United States in the absence of a revised agreement.

López Obrador has [selected Jesús Seade to be his NAFTA negotiator](#). Seade is a well-respected academic economist who worked at the IMF, the World Bank, and the World Trade Organization, where he was deputy director general. Seade expressed his full support for the efforts of Mexico's current NAFTA negotiating team and [stated that an agreement in principle can be reached "within a couple of months."](#) AMLO has proposed that members of his economic team join the Mexican government's negotiating team during the transition, but precisely how Mexico's new political context will affect the negotiations is unclear. In any event, the main obstacle to reaching an agreement continues to be the United States, which has shown a complete lack of flexibility around some of its more objectionable positions. A failure to complete the talks before December 1 will add another level of uncertainty to the renegotiation process.

Mexico, meanwhile, continues to plan for the worst. The Trade Ministry [is reported to be preparing tariffs on U.S. corn and soy exports](#) should the trade fight with the United States escalate. Trade Minister Guajardo [traveled to Japan in a continuing effort to diversify Mexican exports](#). [Mexico also sponsored a resolution](#) at the Organization of American States, approved by consensus, which expressed the member states' "strong rejection" of the U.S. Administration's policy of separating children from their migrant parents. Foreign Minister Luis Videgaray noted further that this U.S. policy [could impact the NAFTA negotiations](#).

We expect the impact of the election on the bilateral relationship to be real but subtle in the near term. Given the repudiation of President Peña Nieto and his policies that AMLO's landslide represents and given the cordial tone of the first meeting between these two pragmatic politicians, it seems likely that AMLO's foreign policy preferences will seep into U.S.-Mexico affairs during the transition. But AMLO's views on the bilateral relationship suggest this will be far from a radical shift.

We expect a possible reduction in bilateral cooperation, especially in migration and security matters, under an AMLO government. This is not because of any hostility to U.S. interests harbored by AMLO or his foreign policy team but because of AMLO's focus on human rights and crime prevention and the rhetoric and actions that are apt to continue coming from the White House. We do not expect the positive, respectful tone of President Trump's [congratulatory tweet](#) and [ensuing conversation](#) with López Obrador to be a sign of things to come, despite [the decision to dispatch Secretary of](#)

[State Pompeo to Mexico City](#) on July 13 and [AMLO's plan to invite Trump \(and Trudeau of Canada\) to his inauguration](#). To the contrary, in the weeks and months ahead, President-elect López Obrador will likely face the same challenge posed by the Trump Administration as his predecessor, [but he is unlikely to be as willing to bite his tongue](#).

IV. Mexican Economy

[Rising consumer confidence](#), a [12-year low unemployment](#) rate, and [record remittances](#) in May suggest the economy recovered from [its small setback in April](#). [Inflation was stable](#) at 4.5% in the first half of June, but the peso was pilloried. The exchange rate [fell to a 16-month low of 20.7 pesos to the dollar](#) after the [U.S. Federal Reserve raised its benchmark interest rate](#) a quarter point to between 1.75% and 2%.

In the wake of the Fed move, as we expected, the Bank of Mexico [increased its benchmark interest rate another quarter point to 7.75%](#). The peso immediately responded, [strengthening to under 20 per U.S. dollar](#) where it held steady through the last week of June. After stumbling following AMLO's electoral victory, [the peso strengthened to a five-week high](#) on the conciliatory tone of his victory speech and the orderly process with which the presidential transition began. It strengthened further in the ensuing days, reaching 19.4 by July 4. [Mexico's country risk also fell after the election](#). However, the markets remain poised to react either to further positive signals or any missteps López Obrador might make in the coming days and weeks.

Sector Focus: Energy

With [107 contracts signed between the government and 73 companies](#) over the past three years, the National Hydrocarbons Commission announced [terms for the next petroleum bid round, scheduled for September](#), in which 37 onshore blocks and three joint ventures with Pemex will be in play. [Pemex, meanwhile, announced that it aims to sign 20 joint ventures before the end of 2018](#), a goal that oil sector analysts see as overly ambitious in the midst of the political transition. Indeed, Rocío Nahle, the woman flagged by AMLO to potentially be Mexico's next energy minister, has opposed any additional farm-outs until the new administration assumes power. It is worth noting, however, that Nahle may never take office at SENER. She also won a Senate seat, and her legislative experience might prove to be more useful to AMLO than having her lead

the energy ministry. Should this come to pass, many will view this as positive for the sector as she has been a vocal critic of the energy reform.

Overall, uncertainty hangs over the energy sector following the election of AMLO, [despite reassuring statements by Alfonso Romo](#), one of AMLO's closest advisers and the nominee to be his chief of staff. As we noted previously, our sense is that AMLO will slow down, not terminate, the auction process while focusing more policy attention on reviving Pemex and on the construction of an oil refinery. He will also review all energy (oil and power) contracts signed with the private sector during the Peña Nieto Administration to verify there was no corruption in the auction and contracting process. While still early, we do not believe that AMLO intends to interfere with any contracts legitimately awarded.

Sector Focus: Infrastructure

During the campaign, López Obrador called for the cancellation of the new airport project, suggested it could be finished through a private sector concession, and [proposed a referendum](#) to determine the fate of the project. Following his election win, he and his surrogates took a more conciliatory stance. [Now they say that all alternatives will be considered](#), including continuing the current project, while playing down the possibility of canceling it altogether. AMLO's designate for Transportation Minister, Javier Jiménez Espriú, [said nothing would happen for a month](#) while the López Obrador and Peña Nieto teams jointly discuss the future of the project. In the meantime, construction will continue.

Beyond the airport, aggressive plans for infrastructure expansion during the AMLO administration are already being discussed. The Trans-Isthmian railway that would connect the Atlantic to the Pacific is AMLO's central project, and Peña Nieto's canceled Mexico City-Queretaro railway is being revived. We believe that the new administration's infrastructure spending will be heavily focused in southern Mexico in an effort to close the development gap between the South and the North, perhaps AMLO's most ambitious economic campaign promise.

V. Monarch Events, Speeches, Publications

June 28: Monarch published [NAFTA News – Volume 8](#), a periodic newsletter from MGS, Manatt, Phelps & Phillips, and TACTIX, jointly offering information and insight on NAFTA renegotiations from experts in the three NAFTA national capitals. For this edition of NAFTA NEWS, our partners in Ottawa, Mexico City, and Washington provided a snapshot of the political pressures facing an agreement in each of the three NAFTA nations.

July 2: MGS Chairman Amb. James R. Jones published an op-ed in [The Washington Post](#) arguing that Andrés Manuel López Obrador’s nationalism does not equate to anti-Americanism.

July 2: MGS President and CEO Michael Camuñez was interviewed on Fox 11 Los Angeles’s [Good Day LA](#) discussing the outcome of the Mexican election and consequences for the U.S.

July 2: Michael Camuñez was quoted in the [Financial Times](#) on the likely impact of AMLO’s victory on U.S.-Mexico relations.

July 2: MGS Senior Adviser Pamela Starr published an op-ed in [The New York Times](#) analyzing the paradoxical character of Andrés Manuel López Obrador.

July 3: Michael Camuñez was quoted in [POLITICO](#) arguing that the United States, not Mexico, is apt to be the main obstacle to concluding the NAFTA talks in the AMLO era.