LatAm

MEXICO: CHANGE IS AFOOT

Grace Fan

Nearly three months after left-wing populist Andrés Manuel López Obrador (AMLO) and his Morena party won a landslide victory in both the presidential and legislative elections, the President-elect is forging ahead with sweeping plans for his incoming new administration. Those plans largely confirm many of his oft-repeated campaign pledges – both for better and for worse.

If the good news is that markets have thus far responded positively to a relatively smooth political transition – thanks to AMLO's reassurances that he will be fiscally responsible and aided by a preliminary US-Mexico NAFTA agreement announced late last month – Mexico's future leader has nonetheless sent mixed signals on other issues, pointing to storm clouds gathering on the horizon. Should Canada fail to sign up to a new NAFTA deal, other headwinds would emerge.

Key judgments

- On a positive note, the 2019 budget bill appears likely to be fiscally prudent, aiding investor sentiment, even though fiscal erosion remains a growing medium-term risk in our view.
- Investor fears of a big shift in energy policy directives continue to percolate following the nomination of diehard energy nationalists to top posts.
- Other simmering concerns include underlying tensions with Banxico, the new federal salary cap and plans to roll back education reform.
- Key infrastructure projects – notably, the new Mexico City airport, a planned new mega-refinery and the Mayan tourist train – are touchstones to monitor.
- We expect the tug-of-war between AMLO's market-friendly and less market-friendly advisers to continue, leading to divergent interpretations and potential policy clashes.
- Meanwhile, in an astute political move that has sent alarm bells ringing, AMLO has initiated an innovative plan to further concentrate power in his hands.

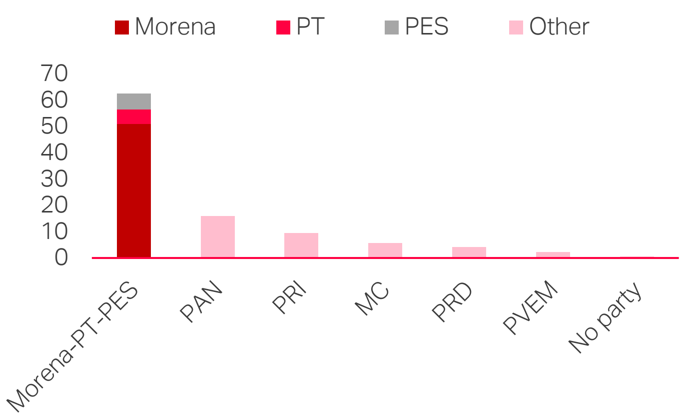
AMLO: Strong on symbolism . . .

Left-wing populist President-elect Andrés Manuel López Obrador (AMLO) is forging ahead with many of his campaign vows, for better and for worse, nearly three months after his landslide victory (see our 6 July 2018 note Power to the left). Following the start of the new legislative session on 1 September. AMLO's young Morena party now holds the reins of the Lower House firmly in its hands, with an absolute majority of 51% (after a post-election deal with the Green Party [PVEM], which ceded five seats to Morena) and 62.6% of the lower legislature when its coalition allies (the Labour Party [PT] and the small conservative Social Encounter Party [PES]) are included. This leaves AMLO just a hair short of the two-thirds majority necessary to pass constitutional reforms in the lower legislature. In the Senate, the President-elect's base is a shade weaker: Morena holds 46% of the seats on its own, while its allied PT-PES base adds an additional 8.6% (see Charts 1 and 2 below).

Not surprisingly, the country's newest political force has sent a clarion sign that change is in the air, starting with a flurry of bills to usher in a new era of "republican austerity". Backed by AMLO's coalition base, the Lower House in its first legislative initiative easily passed a bill on 13 September to cap all federal salaries at the level of the President – a salary that AMLO has promised to slash to MXN108,000/month (US$5,730/month / [MXN18.85/US$]) or 60% less than what outgoing President Enrique Peña Nieto earns – although the legislation does include a provision to allow some select workers to receive up to 150% of his salary. The salary cap bill had originally been passed by the Senate seven years ago but immediately got shunted into the legislative freezer until it was dusted off by Morena a couple weeks ago.

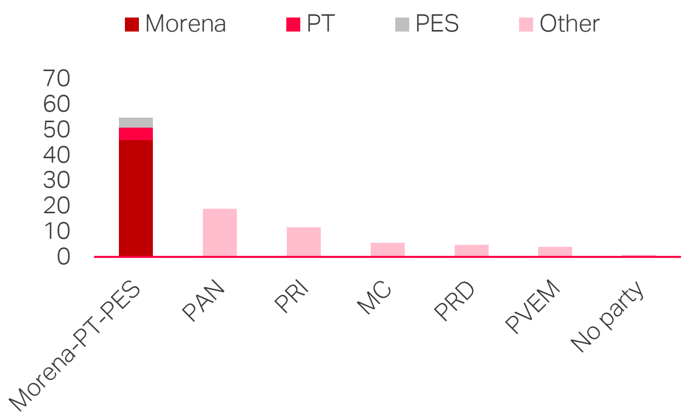
In a corollary move, both houses of the Congress swiftly passed bills to trim the legislative budget for the final four months of 2018 and to slash generous perks for legislators, although some pushback suggests that not all of these cuts will necessarily stay in the 2019 budget.

Chart 1: AMLO's base in the Lower House vs opposition
% of total



Source: Lower House of the Congress.

Chart 2: AMLO's base in the Senate vs opposition
% of total



Source: Mexican Senate.

To further emphasize his differences with the outgoing government, AMLO has proposed strict guidelines for federal employees to cut spending and curb corruption, while pledging that he will ban first-class travel for all federal workers, put the presidential plane up for sale, decentralize the federal government from Mexico City to other states and municipalities and turn the presidential palace into a public space. While some of these measures have merit, others can be debated – starting with the broader efficacy of a salary cap, especially if it is not properly regulated and sparks a big brain drain from the public sector. Yet an important point to highlight is that these populist gestures play well with AMLO's base by foregrounding his determination – if only symbolic – to close the door on the gilded era of government privilege. Moreover, they turn the spotlight on Morena's differences with the country's traditional centre-right parties (PRI, PAN) and have the added political advantage of potentially helping AMLO drive probable opponents to his policies out of office (including senior staff in key ministries, regulatory agencies, state firms and Banxico, not to mention Supreme Court justices). If so, it would be easier for him to bring these organs under his effective control, especially as long-time staffers leave. An estimated 35,000 officials (including nearly 10,000 at Pemex alone) have salaries that exceed the future wage ceiling, although Pemex employees are reportedly excluded from the cap for now because of a legal loophole.

. . . less so on fiscal savings

On a negative fiscal note, the savings generated by such austerity measures appear inadequate to pay for AMLO's ambitious spending plans. As Table 1 below illustrates, AMLO's austerity measures are thus far estimated to save up to MXN132 billion (US$7 billion). However, his campaign promises will cost more than this and include:

- Big-ticket infrastructure projects totalling an estimated MXN500 billion for seven priority projects, notably a planned, new MXN160 billion mega-refinery with a capacity of 400,000 bpd in AMLO's home state of Tabasco;
- A new government-subsidized apprenticeship programme ("Youths Building The Future") – estimated to cost roughly MXN108 billion (or a projected MXN90 billion more than similar programmes in last year's budget) – to train 2.3 million unemployed youths in the workplace, with a guaranteed monthly stipend of MXN3,600 for one year. In addition, university scholarships of roughly MXN2,400/month will be offered to 300,000 students who have a high school diploma;
- Universal pension payouts for senior citizens that will be double the current payout of MXN580 every two months. The annual cost of this pledge has been estimated at between MXN109-185 billion, depending on the rules used; and while incoming Finance Minister Carlos Urzúa has indicated that it may only add an additional MXN35 billion yoy to the 2019 budget (assuming that more stringent rules are adopted), the bigger issue ahead is that this creates a recurring expenditure that will grow every year;
- Monthly scholarships for all high school students and monthly stipends for 1 million children with disabilities;
- A pledge to freeze fuel prices in real terms in the first three years of his term and lower them in the last three years; and
- No new taxes or real tax hikes during his administration.

Friction has also risen between AMLO and Banxico officials in recent days, raising concerns of more fireworks ahead. The President-elect's reportedly belated realization of the big gap between his proposed spending plans and the country's limited budget led to his controversial statement last week that he is inheriting a country "in a situation of bankruptcy" – an assertion that critics immediately rebutted by pointing out that Mexico's investment-grade rating belies his affirmation. AMLO also warned that if the economy worsened, it would not be his fault but rather "due to external circumstances or Banxico's poor handling of financial policy".

Table 1: AMLO's key fiscal proposals and the 2019 budget

Fiscal austerity measures	Preliminary estimates (MXN)
1. Establishing clean, lean government, including:	**Up to 132 bn (in 2019)**
• Slashing salaries for all high-paid public officials and laying off 70% of senior and technical staff in all government departments	Up to 70.4 bn
• Cutting additional benefits	Up to 20.9 bn
• A 28% cut to the total compensation packages of Lower House legislators (the base salary will stay the same, but not the benefits)	409 mn (in 2018) / 1.3 bn (2019)
• Senate budget cut of 30% (luxury travel, fine dining bills, insurance and other expenses of sitting senators will no longer be covered)	599 mn (in 2018) / 1.4 bn (2019)
• Proposed Supreme Court budget cut of 15.1% yoy	1.6 bn (2019)
2. Possible tax amnesty programme	N/A
In 2013, MXN48 bn in extraordinary revenues was raised this way	
3. Streamlining and merging inefficient government programmes	N/A
4. Curbing corruption and freeing up more budgetary funds as a result	N/A
Planned spending initiatives	**Preliminary estimates (MXN)**
1."Youths Building the Future" programme	+90 bn (2019), yoy
2. A universal pension for senior citizens that is double the current payout	+35 bn (2019), yoy
Due to budgetary constraints, the latest plan is to double the pension payout for those aged 68 years and up, not for everyone who has reached the current retirement age of 65	
3. Creating a 30-km free-trade zone in northern border states	N/A
• The value-added tax will be halved to 8% and the corporate income tax trimmed from 30% to 20% starting 1 Jan 2019	40 bn (2019)
• The region's minimum salary will be doubled at the start of 2019	N/A
• Fuel prices will fall to the equivalent of US prices across the border	N/A
4. Decentralization of the federal government to other states	125 bn, plus 2 bn for studies (2019-24)
5. Oil & gas investments	+150-155 bn (2019), yoy; +304 bn (2019-21)
• Modernizing Pemex's six refineries	25 bn
• Beginning the first phase of a new mega-refinery in Tabasco state to refine 400,000 bbl/yr	50-55 bn
• A capital injection into Pemex to improve E&P output	75 bn (2019)
6. Mayan train	16 bn (2019)
While critics are sceptical of the economic viability of the USD6-8 bn project, AMLO reportedly backs a PPP for the project, of which 75% of the funds could come from the private sector	
7 Scholarships totalling MXN2,400/month for all students in high school	N/A (2019)
Estimates suggest this may cost MXN120 bn if given to all students in public high schools and MXN148 bn if private school students are also included	
8. Monthly stipend (MXN1,300) for up to 1 million disabled children	15.8 bn (2019)

Sources: Local press reports.

To add to the sense that Banxico's vaunted independence may be under siege, 200 senior employees are reportedly considering early retirement or leaving to go to the private sector as a result of the new federal salary cap, which is expected to go into effect in January. A key indicator to watch on this front will be AMLO's nominee for a Banxico board seat when the term of Manuel Ramos-Francia, one of five current board members, expires on 31 December. The nomination of a respected technocrat would be a good sign; anything other than this would cause jitters, which could be aggravated if other board members were to resign from their terms earlier than expected. Javier Eduardo Guzmán Calafell's term ends in December 2020, while Banxico Governor Alejandro Díaz de León's term will conclude on December 2021 and that of Roberto del Cueto Legaspi will finish on December 2022.

Still, the President-elect's economic team – acutely conscious that investors are anxious about the fiscal situation – has taken care to send the right signals on the 2019 draft budget. In one encouraging signal, Morena congressmen – after meeting earlier this month with incoming Deputy Finance Minister Gerardo Esquivel – reported that next year's budget expenditures are projected to rise a nominal 6-7.5% yoy to around MXN5.7 trillion. Assuming the CPI ends the year in the 4-4.5% range, this would mean a modest real increase that is likely to be acceptable to the market, particularly if other budget estimates (GDP, inflation, oil price) remain broadly in line with the Peña Nieto government, as the economic team has signalled. Furthermore, rising oil prices would offer more fiscal margin for extra spending, even though the incoming government will also have to contend next year with higher debt financing costs too.

Equally encouraging, there are some signs that the economic team is quietly working to pare back some of AMLO's populist proposals in a bid to hew to its 2019 budget target. For example, Esquivel has already announced that the minimum age to receive the new, doubled pension payout next year will be set at 68 years, rather than the current retirement age of 65. At the same time, he has reiterated that the government is planning to enact a pension reform in the future (albeit only in the second half of AMLO's *sexenio*). Similarly, while AMLO in late July announced that he would inject MXN175 billion in new energy investments in his first year in office, incoming Energy Minister Norma Rocío Nahle has said more recently that she would be asking for MXN150 billion in new sector investments in the 2019 budget.

In another heartening signal, AMLO's incoming Chief-of-Staff Alfonso Romo has asserted that the government will not subsidize fuel prices next year, contradicting his boss's oft-repeated campaign pledge that he would freeze fuel prices in real terms for the first three years of his administration. While a sustained rise in global oil prices would undoubtedly put such a statement to the test, we see these preliminary signs as positive for the 2019 budget bill – and thus for near-term investor sentiment if and when a fiscally responsible bill is passed. At the same time, however, there are warning signs when it comes to the longer-term outlook, as we discuss below.

Storm clouds over energy reform

Following AMLO's announcement of his nomination of diehard energy nationalists to top energy posts, a cold front has descended on the once red-hot sector. In addition to nominating Norma Rocío Nahle – a longstanding critic of energy reform – as the incoming Energy Minister, the President-elect named her fellow critic, academic Alberto Montoya, as Deputy Energy Minister. As late as April of this year, Montoya publicly argued that energy reform should be reversed, and in a 2014 paper he called the reform "the biggest betrayal of Mexicans in 100 years".

To head the state energy firms, the President-elect has nominated Octavio Romero Oropeza – an agronomist turned AMLO's close political confidante who has no oil & gas background – to be CEO of Pemex, and Senator Manuel Bartlett – an 82-year-old notorious politician who similarly has no energy background and has been a long-time foe of privatizations – to lead power firm CFE. AMLO's tactical decision to put political appointees rather than technocrats in these leadership positions has inevitably fuelled nervousness among sector players that he is preparing to roll back key swathes of energy reform, even if he has sent signals that he would not move to revoke it outright. To add to these fears, notwithstanding a firestorm of criticism about these appointments, AMLO has thus far resisted all pressure to replace his nominees.

While many other key posts still lack nominees, the current frontrunner to head Pemex's E&P division appears to be former Pemex board member Fluvio Ruiz Alarcón, an ally of Rocío Nahle, Although Ruiz has strong technical expertise as a petroleum engineer and physicist, he has argued that Mexico should resign its recently acquired membership at the International Energy Agency (IEA) and align itself with OPEC, in a sign of his policy differences with the current administration.

Assuming that there are no big changes to AMLO's energy picks, the top energy priorities of the next government will be very different from those of the current administration. In the upstream segment, there is a vast determination among the new energy team to "make Pemex great again", in stark contrast to the eagerness of the Peña Nieto administration to court foreign oil majors and shrink Pemex's footprint. This mandate could manifest itself in various ways, from more nationalist regulation through higher local content requirements to potentially trying to push out Pemex partners from recently awarded farmout contracts, alongside more preferential policies to favour the oil giant. While such a directive does not automatically exclude future E&P bid rounds that could attract private sector oil players, we note that the biggest priority in the first year of the new government will be to widen Pemex's footprint and to reposition it as the dominant player in Mexico's oil & gas sector, rather than to tender more oil & gas blocks.

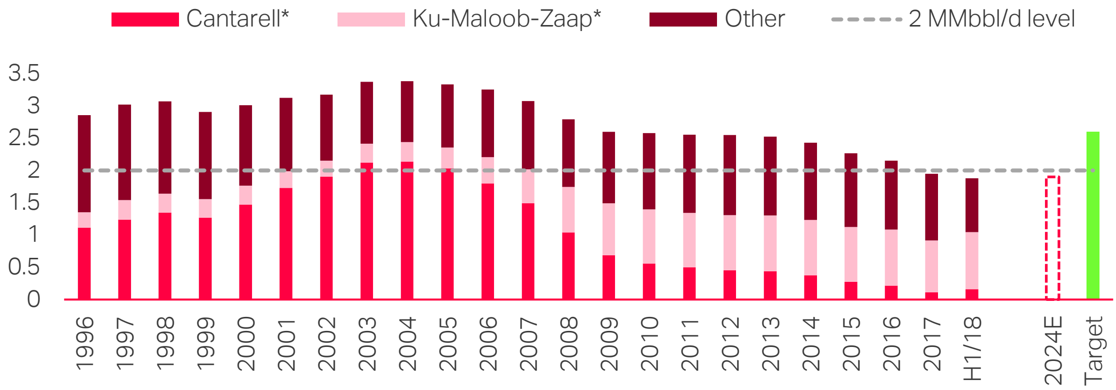
If there is a positive side to the more central role envisioned for Pemex, it is that there is some support for offering the state oil giant full budgetary and operational independence. If so, and if the company's onerous tax burden is also reduced as a consequence, this could improve Pemex's ability to stand on its own two feet. What is less clear, however, is how the Finance Ministry would fix the budgetary hole left by Pemex. Last year, the state oil firm's tax payments accounted for roughly 20% of the federal budget, down from about 40% in 2016. Another problem is that it is likely to take years for additional investments to yield visible results, and if Pemex is propped up in the meantime by the government or takes on more debt, fiscal worries will only increase.

Adding to the challenges, Mexico's oil & gas output continues to fall owing to the inexorable decline of Pemex's top-producing field Ku-Maloob-Zaap – which could see output halve from its average 880,000 bbl/d level in H1/18 by 2025. According to a recent estimate by S&P Global Platts, despite incremental production coming online in other fields, Mexico's oil output may edge down further in the next three years, bottoming out only in 2021 at 1.74 million bbl/d (down 7% from its average output this year) before inching back up to 1.94 million bbl/d by 2030 as deepwater output finally comes online. Outgoing Energy Minister Pedro Joaquín Coldwell has aired a more positive forecast, suggesting the country could reach the 2 million bbl/d level by 2022, albeit only if the next government pushes full-steam ahead with E&P bid rounds and farmouts.

In both cases, this means that while ALMO has recently set a target of reaching 2.6 million bbl/d by the end of his *sexenio* in 2024, he is unlikely to achieve that goal (see Chart 3 below). Yet if he applies the brakes to energy reform, the outlook would only get worse. According to former Pemex E&P director Carlos Morales Gil – who is now CEO of local oil firm Petrobal – the upstream sector will require more than US$20 billion/year to return to the 2 million bbl/d level. By contrast, even with the big injection of funds promised by AMLO, Pemex's E&P budget next year will reach US$11 billion, or nearly half of what is needed to raise output.

For now, the good news is that AMLO continues to appear willing to give the green light to the more than 100 E&P contracts auctioned off under energy reform, barring the discovery of serious irregularities, as we have previously highlighted. Encouraging though this is, there has been chatter that certain contracts have aroused the deep suspicions of the new energy team, particularly the ones in which important oil discoveries were subsequently made by the winning bidders. If even one high-profile contract were to be suspended without strong evidence of corruption, it would send another wave of panic through the sector.

Chart 3: Mexico's crude output



*Cantarell was Mexico's top-producing oil field for three decades; Ku-Maloob-Zaap eclipsed it in 2009 but its output is also starting to decline.
Sources: Pemex, S&P Global Platts, local press reports.

That said, AMLO's market-friendly incoming Chief-of-Staff Alfonso Romo has been a voice of reason on this front; and in our base case, we continue to expect the bulk of these contracts to be allowed to proceed, especially with nearly 400,000 bbl/d estimated to come online by 2025 from the first blocks tendered under energy reform. Should AMLO fail to adopt a pragmatic stance on encouraging private sector investment in the upstream sector, output will plunge. Despite this binary equation, we note that there is real concern among some sector investors that we have spoken to that the new government could yet move in the wrong direction if the nationalists have their way, before it learns the hard way that it must reverse course.

In the downstream sector, AMLO has long dreamed of building more domestic refineries and making Mexico energy self-sufficient – a vision shared by incoming Energy Minister Rocío Nahle. Although this goal is a laudable one given the unpredictable whims of US President Trump and Mexico's own energy security issues, it remains patently unclear how the new government will make its planned new expensive mega-refinery profitable, especially with extremely efficient refineries operating just north of the border and AMLO's oft-repeated campaign pledge never to introduce big fuel price increases. It is also unclear whether it will be Pemex that will ultimately be saddled with the brunt of the construction costs or whether the government will inject funds into the refinery project via another route. Either way, ratings agencies have already warned that they could downgrade the firm and/or the country should big capital outlays in the downstream sector occur, especially if upstream bid rounds are indefinitely suspended or fail to attract investor interest. Either way, we view the downstream part of AMLO's energy plan with extreme scepticism, and it is a major reason why fiscal erosion appears as a growing risk over the medium term, particularly if this part of AMLO's programme continues to gain traction.

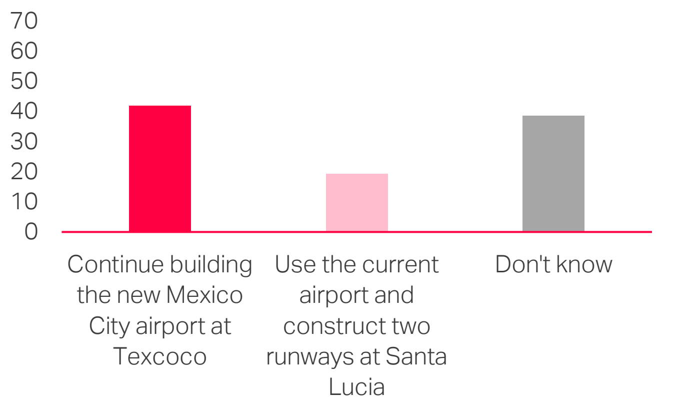
Other touchstones to monitor

Apart from the new mega-refinery in Tabasco, another planned big-ticket infrastructure project to track is the USD6-8 billion Mayan train project. First proposed in 2012 by President Peña Nieto for roughly half the cost, the project was scrapped in 2015, only to be revived again after AMLO became enamoured of the idea of a high-speed train line that would cross the Yucatán Peninsula, connect some of the most significant archeological sites of the Mayan civilization and bring tourist revenues to poorer southeastern states. The 830-km rail line is projected to start in Cancún in northeast Quintana Roo, with stops in popular tourist destinations such as Tulum and Campeche, before ending in Palenque, Chiapas. Owing to the lack of funds in the government's budget, however, the President-elect reportedly backs a PPP for this project, with hopes that 75% of the funds might come from the private sector. Still, with strong political winds behind this project, Morena legislators recently said that it would indeed be included in the 2019 budget, with a preliminary investment of MXN16 billion.

The fate of the new Mexico City airport now hinges on a popular referendum, but two recent polls suggest a favourable outcome, offering hope to investors. In the weeks since his victory, AMLO has also moved ahead on his late-stage campaign pledge to let the Mexican population decide whether to let the new US$13 billion airport – the biggest infrastructure project of the Peña Nieto administration and a frequent target of his campaign – to continue at its current site (Texcoco) or to abandon it and construct two runways at a nearby military airfield (Santa Lucia), which most experts agree would be a less optimal solution. The referendum is currently projected to be held on 28 October.

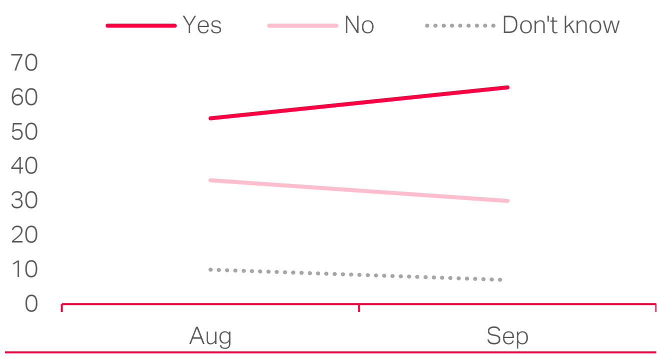
In a nationwide poll of 1,000 people interviewed in their homes earlier this month by Consulta Mitofsky, an estimated 42% of those surveyed said that they were in favour of maintaining the current project, while just 19.4% said they were against it. In a more recent telephone poll conducted by local financial daily *El Financiero* last week, an even more significant 63% of those surveyed said they backed keeping the airport at Texcoco, up 9pp from the same poll conducted by the newspaper a month ago. However, the *El Financiero* poll comprised just 420 people, making its results less reliable (see Charts 4-5 below).

Chart 4: First airport poll: Which statement do you agree with more?
% / Poll dates: 7-9 Sept



Source: Consulta Mitofsky.

Chart 5: Second airport poll: Should work on the new Mexico City airport be continued at Texcoco?
% / Poll dates: 20-22 Sept



Source: *El Financiero*.

While much will hinge on the actual question asked of voters in the referendum, there appears to be a quiet acknowledgement among key members of the AMLO team that it is easier for all concerned to keep the current airport project where it is, although one potential foe remains incoming Communications and Transport Minister Javier Jiménez Espriú. As the clock ticks down to the referendum, the incoming government has started to review and audit airport contracts, with an eye to cutting costs. As part of this process, it has already ratcheted up its demand for more local content in these contracts, in what could be a harbinger to watch for future oil & gas contracts. On a side note, critics have pointed out that the President-elect's plans to use more popular referendums as a way to guide his decisions could inject more unpredictability into future government policy.

A planned rollback of education reform has also been listed as one of AMLO's top priorities. Thus far, however, it is unclear what would replace it. To date, proposals by Morena congressmen and allied parties have included: 1) the complete rollback of education reform; 2) allowing teachers suspended from work for failing to meet minimum standards to be reinstated; and 3) calls for the Education Ministry to immediately halt all teacher evaluations indefinitely. However, AMLO himself has yet to weigh in on the new model to be proposed. The passage of this seminal reform under the Peña Nieto administration was hailed by the market as a big achievement; a wholesale return to the pre-reform days would undeniably be a setback. Key to monitor will be whether the teacher evaluation process survives in some form and how much power will be ceded back to the teachers' unions which supplied many Morena foot soldiers in the recent elections.

AMLO moves to consolidate power

On a corollary battlefield, the President-elect's initiative to dismantle traditional structures linking the federal government and the states – further aggregating power in his hands – is also worth watching. Notwithstanding his coalition's large Congressional majority, AMLO has not been content to rest on his recent political laurels. Instead, in a move that has alarmed many, particularly opposition governors of key states, the President-elect has announced a plan to eliminate all federal delegations to the 32 state governments via the appointment of one federal political coordinator in each state who would be in charge of all the various social and economic programmes. The 32 new delegates will also be given the power to control federal fund transfers to the states, which on average account for roughly 80% of state budgets. Not surprisingly, state governors fear that their traditional powers will be significantly eroded as a result of this move, as they will now have to negotiate with the new federal coordinators for funds. Moreover, in several of the states – including the state of Mexico – the new appointees ran (and lost) in recent gubernatorial races, further highlighting the partisan nature of this gambit.

In another sign that AMLO is planning to centralize power via this route, he has created a new cabinet position specifically to liaise with the 32 new coordinators and has appointed a close ally, Morena's General Secretary of Organization Gabriel García Hernández, to the post of general coordinator. We see this move – in tandem with the federal salary cap – as a sign of AMLO's drive to sweep what is left of the old "mafia of power" out of office and to establish Morena as the "new PRI" – and the country's dominant political power for the next generation. Furthermore, at this very moment when the country's traditional parties are debilitated after a bruising election and his party will control the purse strings in the Congress, the President-elect has a priceless opportunity to do so. Yet as brilliant as this move is as a political stratagem for the purposes of consolidating power and for disrupting previously established networks of corruption, it is unclear whether it is good for institutions in Mexico. More likely, it will set up parallel and competing power structures in opposition-controlled states, which will give AMLO's allies an edge in upcoming state elections as well as in the all-important mid-term legislative elections in 2021.

Conclusion

In the nearly three months since AMLO's election, markets have largely reacted well, aided by a smooth political transition and the preliminary US-Mexico agreement on NAFTA. As we have previously highlighted, we continue to see the President-elect as a pragmatic politician in many ways and the post-electoral stance he has adopted on key issues has largely been in line with our expectations. The big surprise on the downside has been the absence of moderates nominated to the top energy posts. Although AMLO's reassurances that he will not use his new legislative majority to revoke energy reform outright has helped to temporarily allay worries, how he sets energy policy going forward will only grow in importance after the presidential inauguration on 1 December.

Looking ahead, investor sentiment in Q4 will likely be dictated by two major issues. These are: 1) progress (or lack thereof) on NAFTA, particularly in regards to Canada signing onto the preliminary US-Mexico agreement (with the November US mid-term elections an important potential inflection point to watch on this front); and 2) the final 2019 budget proposal, which must be submitted by 15 December by the new government and passed before yearend. We will be taking a closer look at the NAFTA deal in a forthcoming note; and as for the 2019 budget, our base case is that a fiscally responsible budget will be passed, especially given the encouraging signs sent thus far by AMLO's economic team. The fact that there are few penalties in store for the government should it spend more than its allotted budget, as the Peña Nieto administration has shown, is an additional incentive.

Mixed messages from the incoming government will likely continue, owing to the tug-of-war between AMLO's market-friendly advisers and less market-friendly cabinet members. Similar to his US counterpart north of the border, a key reason for ongoing investor uncertainty about the new President-elect is not only his penchant for making controversial statements, but also the fact that conflicting messages are coming from different parts of his core team. On one side of the divide, his more investor-friendly advisers (incoming Finance Minister Urzúa and his team, incoming Chief-of-Staff Alfonso Romo) are pulling policy one way, while on the other side, his more nationalistic advisers (notably the new energy team) have other plans. Policy differences and even zig-zags could erupt as a result of this ongoing clash.

Yet the key driver for AMLO may be less dependent on economic ideology than on core political imperatives, with his decisions likely to be shaped by a broader sense of his mission in Mexican history and his plan to install Morena as the country's preeminent political force for decades to come. When it is politically expedient to be market-friendly we expect him to adopt investor-friendly policies; but if it interferes with another more pressing political goal, conflicts could rise. It is for this reason that we are less worried about his administration and its fiscal policies in the first year of office (particularly as he has good reasons to court investors at this stage), and more concerned about AMLO's eventual stance in 2020-21 when he will be increasingly focused on winning the mid-term legislative elections. Should the economy fail to react as he hopes, he could not only resort to opening up the fiscal taps but also look for scapegoats. In the absence of a real opposition, easy targets at hand could be Banxico and foreign oil majors.

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