

Mexico

Mexico Faces Cloudy 2017 Outlook, Recent Data Mixed

March 23, 2017

Recent data paint a mixed picture of economic growth in Mexico. Employment and industrial production continued expanding, but exports declined. Inflation increased further in February, but the peso recovered some ground against the dollar. A Banco de México policy rate increase in February will likely damp growth; the consensus 2017 gross domestic product (GDP) forecast is for 1.5 percent growth, almost a percentage point below the 2.4 percent in 2016 (as measured on a fourth-quarter-over-fourth-quarter basis).

Output Growth Solid in 2016

The 2.4 percent GDP increase in 2016 matched the previous year (*Chart 1*). Service-related activities (including trade, transportation and business services) rose 3.3 percent. Goods-producing industries (including manufacturing, construction, utilities and mining) were virtually unchanged at -0.04 percent. A 9.7 percent decline in mining activity, which includes oil and gas extraction, more than offset manufacturing growth of 2.1 percent. Agricultural output increased 6.6 percent in 2016. Fourth-quarter GDP grew at a robust 2.9 percent annualized rate—just exceeding initial estimates.

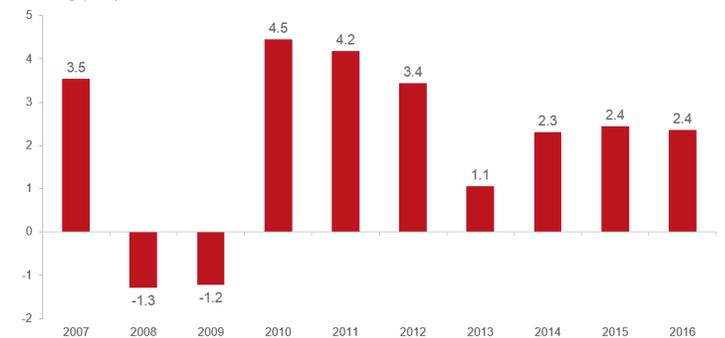
Exports Fall in January After December Increase

Three-month moving averages of total and manufacturing exports indicate consistent growth since mid-2016 despite a 5.4 percent total export decline in January following a 5.3 percent rise in December (*Chart 2*). For 2016 as a whole, total exports were 3.1 percent below 2015 levels, and manufacturing exports trailed the prior year by 2.5 percent. Oil exports turned around earlier in 2016 after a long decline, but the reversal was driven by rising oil prices, not higher volume. Still, the value of oil exports in 2016 was 21 percent below 2015 totals.

Nonmanufacturing Depresses Industrial Production

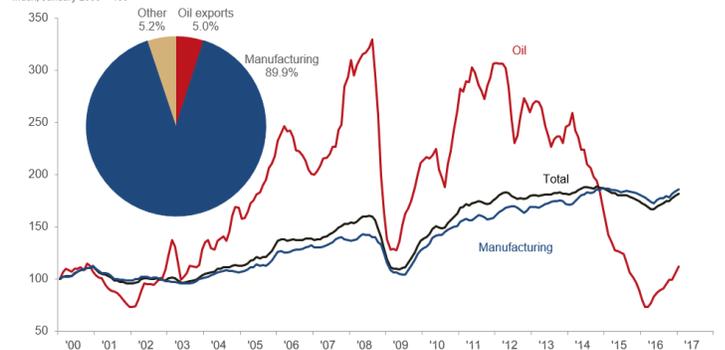
Mexico's industrial production (IP) grew 0.1 percent in January after falling 0.1 percent in December. However, manufacturing production ticked up 0.5 percent in January and has risen steeply since early 2016. U.S. IP fell 0.2 percent in January after growing 0.6 percent in December. Using a three-month moving average, Mexico's manufacturing IP accelerated, while overall IP showed signs of deceleration (*Chart 3*). Total IP, which includes manufacturing, construction, oil and gas extraction, and utilities, has grown more slowly than manufacturing IP since 2014.

Chart 1
Mexico Economic Growth Solid in 2016
Percent change (Q4/Q4)



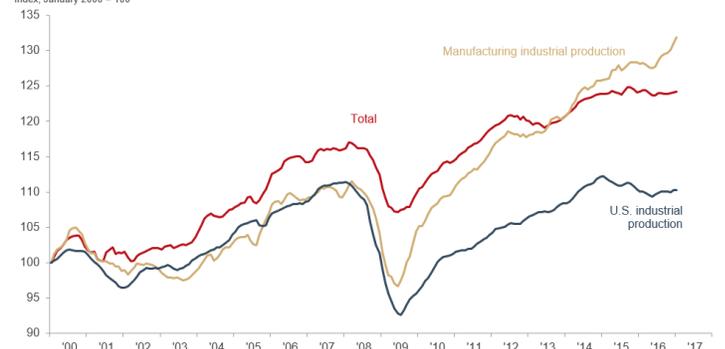
SOURCE: Instituto Nacional de Estadística y Geografía (National Institute of Statistics and Geography).

Chart 2
Moving Average of Exports Continues Rising Despite January Dip
Index, January 2000 = 100*



*Seasonally adjusted, three-month moving average, real dollars.
SOURCE: Instituto Nacional de Estadística y Geografía (National Institute of Statistics and Geography).

Chart 3
Industrial Production Flat as Manufacturing Production Continues Steep Rise
Index, January 2000 = 100*



*Seasonally adjusted, three-month moving average.
SOURCES: Instituto Nacional de Estadística y Geografía (National Institute of Statistics and Geography), Federal Reserve Board.

Retail Sales Strong in 2016 Despite Soft December

Retail sales contracted 1.4 percent in December after growing 0.9 percent in November. Sales rose 9.2 percent in 2016. Smoothed data (three-month moving average) showed sharply accelerating sales revenue throughout 2016 (*Chart 4*). Consumer confidence improved in January after worsening in December.

Solid Job Growth Continues into 2017

Formal-sector employment—jobs with government benefits and pensions—grew at an annualized rate of 4.1 percent in February, following a 4.5 percent expansion in January (*Chart 5*). Employment growth in 2016 was 4.1 percent (December over December) compared with 3.8 percent growth in 2015.

Peso Gains Ground in February

The Mexican currency reversed course in February, averaging 20.3 pesos per dollar, a 5.4 percent gain from January (*Chart 6*). The peso lost 9 percent of its value against the dollar on a year-over-year basis in February. The Mexican currency has weakened largely in anticipation of further increases in U.S. interest rates as well as policy and economic uncertainty following the U.S. presidential election.

Chart 4
Retail Sales Grew Strongly in 2016



Chart 5
Job Growth Robust So Far in 2017

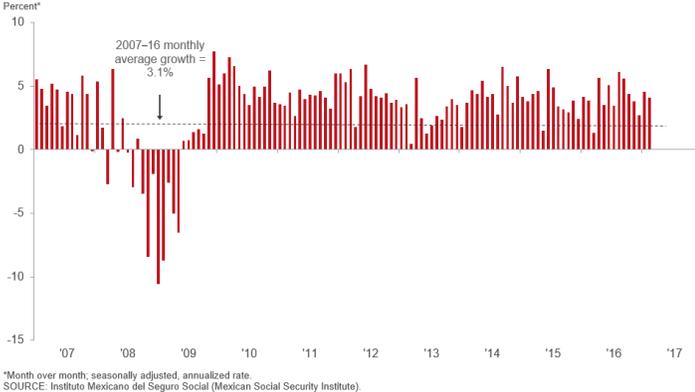


Chart 6
Peso Appreciates Against the Dollar in February



Foreign-Owned Government Debt Stable

Despite recent economic uncertainty and market volatility, the share of peso-denominated government debt held abroad has remained relatively stable at about 35 percent (*Chart 7*). The extent of nonresident holdings of government debt reflects Mexico's exposure to international investors, whose holdings could reverse if they perceive a sudden change in market sentiment toward Mexico.

Inflation Ticks Up in February

Inflation was an annualized 4.9 percent in February compared with 4.7 percent in January. Headline inflation is running significantly above Banco de México's long-term target of 3 percent (*Chart 8*). Core inflation (excluding food and energy) rose 4.3 percent over the 12 months ending in February. Mexico's central bank raised its benchmark interest rate by 50 basis points in February, to 6.25 percent, the seventh increase since December 2015. Banco de México Governor Agustín Carstens has been clear that the central bank will use interest-rate increases and currency interventions as needed to strengthen the peso and stabilize prices.

—Jesus Cañas

About the Author

Cañas is a senior business economist in the Research Department at the Federal Reserve Bank of Dallas.

Chart 7
Nonresident Holdings of Government Debt Stable

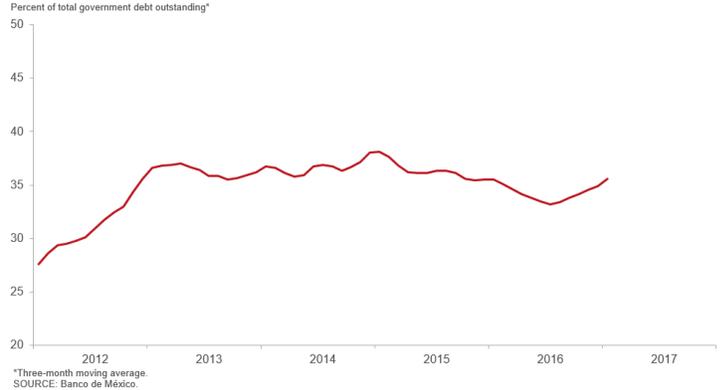


Chart 8
Inflation Jumps in January, Remains High in February

